IT : Where assessee had not written back sundry creditors in his profit and loss account and had shown balance outstanding towards those creditors even in next assessment year, it could not be said that there was any cessation of liability under section 41(1)

IT : Where assessee had claimed an expenditure towards labour & fabrication charges paid by it and furnished requisite evidences to prove that payee had duly considered such charges paid by assessee in its return of income, no disallowance under section 40(a)(ia) could be inflicted in respect of such charges in hands of assessee payer

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IN THE ITAT KOLKATA BENCH 'A'

Jashojit Mukherjee

v.

Assistant Commissioner of Income-tax, Circle- 50, Kolkata*

S.S. GODARA, JUDICIAL MEMBER
AND M. BALAGANESH, ACCOUNTANT MEMBER
IT APPEAL NO. 403 (KOL.) OF 2017
[ASSESSMENT YEAR 2012-13]
MAY 4, 2018

I. Section 41(1) of the Income-tax Act, 1961 - Remission and cessation of trading liability (Cessation of liability) - Assessment year 2012-13 - Assessee had shown provision for sundry creditors - Assessing Officer held that since present whereabouts of creditors were not known to assessee, sum claimed towards sundry creditors were to be treated as deemed income of assessee under section 41(1) on account of cessation of liability - It was noted that assessee had shown balances outstanding towards sundry creditors even in next assessment year - Assessee had not written back these creditors in his profit and loss account as liabilities no longer payable - Hence, there was no unilateral write back of creditors to his profit and loss account by assessee and from same it could be safely concluded that assessee had proved that liabilities had not ceased to exist - Whether since assessee had duly acknowledged his debt by accepting creditors liability to be discharged in future, there could not be any cessation of liability under section 41(1), thus impugned, additions to income of assessee was unjustified - Held, yes [Para 5] [In favour of assessee]

II. Section 40(a)(ia) of the Income-tax Act, 1961 - Business disallowance - Interest, etc., paid to a resident without deduction of tax at source (General/principles) - Assessee had claimed an expenditure under head 'labour & fabrication charges' paid to several parties - Assessing Officer noticed that assessee had short deducted tax at source on labour and fabrication charges paid to one, AKM and, accordingly, disallowed same under section 40(a)(ia) for short deduction of tax at source - It was noted that assessee had provided Chartered Accountant's certificate to prove fact that payee (i.e. AKM) had duly taken into account such sum in its return of income filed under section 139 for computing income and had paid taxes due on income declared by him in return of

income - Whether since assessee had furnished requisite evidence to prove that payee had considered subject mentioned receipt in his return of income, no disallowance under section 40(a)(ia) could be inflicted in respect of same in hands of assessee payer - Held, yes - Whether, further, in case of short deduction of tax at source, no disallowance under section 40(a)(ia) could be made in hands of assessee and in such cases proceedings could be initiated against assessee only under section 201 - Held, yes [Paras 7.2 and 7.3] [In favour of assessee]

FACTS-I

- The assessee had shown sundry creditors. The assessee furnished the balances of each creditor having outstanding balance. The Assessing Officer from same picked up 11 parties to examine these creditors and accordingly issued notices under section 133(6) to them. Out of 11 parties, the notices could be served only on 3 parties from whom no replies were received by the Assessing Officer. The remaining notices sent to 8 parties returned unserved. Since the present whereabouts of the creditors were not known to the assessee, the Assessing Officer treated the sundry creditors as deemed income under section 41(1) on account of cessation of liabilities. The Assessing Officer observed that out of the other sundry creditors for labour and materials the assessee had provided the list of creditors along with addresses showing opening balance, total of supplies made during the year (credit), payments made thereon (debits) including debits towards debit notes and TDS and closing balance of each of the creditors. From the same, the Assessing Officer issued notice under section 133(6) to 4 parties, out of which 2 notices returned unserved; 1 notice was served but no reply was received from the party and balance 1 notice was served and reply was received from the said supplier. The Assessing Officer observed that MJ who had filed the reply wherein it had confirmed the transaction executed during the year but did not confirm the balance of receivable amount at the starting and at the end of the year. Based on this, the Assessing Officer treated the said creditor, *i.e.* M.J. as a bogus creditor. Accordingly, he treated the balance outstanding in respect of aforesaid 4 parties as bogus sundry creditors.
- On appeal, the Commissioner (Appeals) also upheld the addition made by the Assessing Officer under section 41(1) as well as in respect of bogus creditors.
- On second appeal:

HELD-I

- It is not in dispute that the assessee had claimed deduction at the time of creation of these trading liabilities in the earlier years. The only dispute is whether the same could be brought to tax under section 41(1) on account of cessation of liabilities. The assessee had shown the same balances as outstanding towards the sundry creditors even in next assessment year. It was not in dispute that the assessee had not written back these creditors in his profit and loss account as liabilities no longer payable. Hence there was no unilateral write back of the creditors to his profit and loss account by the assessee. From this it could be safely concluded that the assessee had proved that the liabilities had not ceased to exist. The very fact, that the liabilities are continued to be shown in the books of the assessee even in the next financial year ended 31-3-2013 relevant to assessment year 2013-14, goes to prove that the assessee had duly acknowledged his debt by accepting the creditors liability to be

discharged in future, hence, there could not be any cessation of liability as on 31-3-2012. Moreover, in order to invoke the provisions of section 41(1) there should be a clear finding to prove that the liabilities had ceased to exist during the previous year relevant to assessment year 2012-13 (*i.e.* the year under appeal). No such finding is recorded by both the authorities below. In the absence of such crucial finding, invocation of provisions of section 41(1) as deemed income did not arise in the hands of the assessee. Moreover, the assessee had not obtained any benefit in respect of these trading liabilities in view of the fact that he had duly acknowledged the debt payable to these creditors in his books. [Para 5]

- In view of the aforesaid observations in the facts and circumstances of the case the Assessing Officer is directed to delete the addition made under section 41(1). [Para 5.2]
- With regard to the addition sustained by the Commissioner (Appeals) towards bogus creditors, it was found that out of the 3 parties, one party MJ had duly responded to the notice under section 133(6) before the Assessing Officer confirming the transactions with the assessee. From the ledger accounts it is seen that the following payments were made after due deduction of tax at source during the year by the assessee which has been accepted as genuine by the Assessing Officer. When the payments made during the year by account payee cheque had been examined and accepted by the Assessing Officer which was also partly subjected to due deduction of tax at source and especially in view of the fact that one of the parties MJ had duly responded to notice under section 133(6) before the Assessing Officer by confirming the transactions the notice under section 133(6) was duly served on the said supplier, it cannot be said that those suppliers are non-existent and bogus. The assessee had placed all the relevant materials before the lower authorities to drive home the point that the sundry creditors shown in the name of these three parties are indeed genuine and transactions were done during the year with them. These facts were not appreciated by the Assessing Officer while treating these creditors as bogus. It is not in dispute that these 3 creditors balances were brought forward from previous year and during the year, only small payments were made to them and hence the balance outstanding in these accounts cannot be the subject matter of addition during the year under appeal. [Para 6]

FACTS-II

- The assessee had claimed an expenditure under the head 'labour & fabrication charges'. The assessee submitted party wise details of labour and fabrication expenses and party wise details of TDS in all the four quarters.
- While comparing the party wise details with TDS details, the Assessing Officer noticed that the assessee had short deducted tax at source in respect of amount paid to one, AKM. The Assessing Officer disallowed the same under section 40(a)(ia) for short deduction of tax at source.
- On appeal, the Commissioner (Appeals) observed that the assessee had submitted a certificate from the Chartered Accountant that AKM had considered the subject mentioned payment in his return and accordingly in view of the second proviso to section 40(a)(ia) read with section 201, which was held to be retrospective in operation, the assessee should not be treated as assessee-in-default. Consequentially no disallowance under section 40(a)(ia) could be inflicted on him. The Commissioner

(Appeals) observed that since AKM had filed the return of income beyond the due date under section 139(1) the conditions laid down in proviso to section 201(1) were not satisfied and, accordingly, upheld the disallowance made by the Assessing Officer.

- On appeal:

HELD-II

- At the outset, the disallowance under section 40(a)(ia) has been made due to short deduction of tax at source on labour and fabrication charges paid to AKM. The Commissioner (Appeals) had considered the assessee (payer) as assessee-in-default despite the chartered accountant's certificate proving the fact that AKM had duly considered the payments made by the assessee in his return of income filed. The Commissioner (Appeals) had held that since the return was filed belatedly under section 139(4) by payee (*i.e.* AKM), the conditions prescribed in proviso to section 201(1) were not satisfied and accordingly the assessee was to be treated as assessee-in-default. In this regard, the conditions prescribed in proviso to section 201(1) are to be considered. From the bare reading of the conditions prescribed in proviso to section 201(1) it is found that the legislature had no where provided that the payee should furnish his return of income under section 139(1). The condition only says section 139. It does not mention about section 139(1). The return filed within the time limit prescribed under section 139(4) is also a valid return as that leeway has been provided in the statute itself. It was not in dispute that the payee (*i.e* AKM) had duly considered the subject mentioned payment made by the assessee in the return of income filed under section 139 and had taken into account such sum for computing the income and had paid the taxes due on the income declared by him in the return of income. All the three conditions are duly satisfied. These facts were evident from the chartered accountant certificate issued in terms of first proviso to section 201(1), which was part of records and which fact remain uncontroverted by the revenue. The Commissioner (Appeals) had taken cognizance of this CA certificate but had not given weightage of the same due to his interpretation that section 139 referred to in the proviso to section 201(1) need to be construed only as section 139(1) and not otherwise. In these facts and circumstances, the assessee had furnished requisite evidences to prove that the payee had duly considered the subject mentioned receipt in his return of income, no disallowance under section 40(a)(ia) could be inflicted on the same in the hands of the assessee payer. [Para 7.2]
- Yet another point that arises for consideration in the instant case is as to whether the provisions of section 40(a)(ia) could be invoked for short deduction of tax at source. This issue has been held in favour of the assessee by the co-ordinate bench decision of this Tribunal in the case of *Dy. CIT* v. *S. K. Tekriwal* [2011] 48 SOT 515/15 taxmann.com 289 wherein it was held that in the case of short deduction of tax at source, no disallowance under section 40(a)(ia) could be made in the hands of the assessee and the assessee could be proceeded against only under section 201 in such cases. Respectfully following the same, no disallowance under section 40(a)(ia) could be made in the hands of the assessee payer herein. [Para 7.3]

CASE REVIEW-I

CIT v. *Alvares & Thomas* [2016] 239 Taxman 456/69 taxmann.com 257 (Kar.) (para 5) *followed.*

Kesoram Industries & Cotton Mills Ltd. v. *CIT* [1992] 196 ITR 845 (Cal.) (para 5.1) *distinguished*.

CASE REVIEW-II

Dy. CIT v. *S.K. Tekriwal* [2011] 48 SOT 515/15 taxmann.com 289 (para 7.3) *distinguished*.

CASES REFERRED TO

CIT v. *Alvares & Thomas* [2016] 239 Taxman 456/69 taxmann.com 257 (Kar.) (para 5), *Kesoram Industries & Cotton Mills Ltd.* v. *CIT* [1992] 196 ITR 845 (Cal.) (para 5.1) and *CIT* v. *S.K. Tekriwal* [2011] 48 SOT 515/15 taxmann.com 289 (Kal.) (para 7.3).

P.K. Himmatsinghka, AR *for the Appellant.* **Sallong Yaden**, Addl. CIT *for the Respondent.*

ORDER

M. Balaganesh, Accountant Member - This appeal by the assessee arises out of the order of the Learned Commissioner of Income Tax(Appeals)-15, Kolkata [in short the ld CIT (A)] in Appeal No. 285/CIT (A)-15/14-15/Cir-50/Kol dated 12.01.2017 against the order passed by the ACIT, Circle-50, Kolkata [in short the ld AO] under section 143(3) of the Income Tax Act, 1961 (in short "the Act") dated 23.02.2015 for the Assessment Year 2012-13.

2. The first issue to be decided in this appeal is as to whether the ld CITA was justified in upholding the addition made by the ld AO u/s. 41(1) of the Act in the sum of Rs. 1,08,65,202/- in the facts and circumstances of the case. The interconnected issue to be decided thereon is as to whether the ld CITA was justified in confirming the addition of Rs. 29,49,535/- as bogus sundry creditors in the facts and circumstances of the case.

3. The brief facts of this case are that the assessee is an individual and is an Interior Decorator and Contractor in the name and style of M/s. VIBGYOR. The return of income for the Asst Year 2012-13 was filed by the assessee on 23.3.2013 (belated return but within time specified u/s. 139(4) of the Act) declaring total income at Rs. 15,48,850/-. The ld AO observed that in response to notices issued u/s. 143(2) and 142(1) of the Act, the authorized representative of the assessee attended and submitted details, which were examined with annexure, reports etc along with the return of income and kept on record. The total turnover declared by the assessee was Rs. 1.66 crore from M/s. VIBGYOR. In addition to business income, the assessee is a partner is M/s. D.M.Constructors and has remuneration income of Rs. 7,20,000/- during the year under consideration.

3.1 The ld AO on perusal of the balance sheet as on 31.3.2011 observed that the assessee had shown sundry creditors as under:—

Sundry Creditors	- Rs. 1,08,65,202/-
Sundry Creditors Labour	- Rs. 25,60,398/-
Sundry Creditors Materials	- Rs. 30,82,491/-

The details of the same were called for and the assessee in response thereto furnished the balances of each creditor having outstanding balance over Rs. 25,000/- as on 31.3.2009, 31.3.2010, 31.3.2011, 31.3.2012 and 31.3.2013. He also furnished the balance of creditors below Rs. 25,000/- for the same period. All these details were furnished in tabular form. The total of these creditors as on 31.3.2012 was Rs. 1,08,65,202/-. The ld AO from the same picked up 11 parties sought to examine these creditors and accordingly issued notices u/s. 133(6) of the Act to them. Out of 11 parties, the notices could be served only on 3 parties from whom no replies were received by the ld AO. The remaining notices sent to 8 parties returned unserved. The ld AO show caused the assessee as to why the entire creditors balance outstanding in the sum of Rs. 1,08,65,202/- be not treated as deemed income u/s. 41(1) of the Act on

account of cessation of liabilities as there is no movement in the said parties account from 31.3.2009 onwards. The assessee replied that he is in the business of interior decorating and other similar types of job and for that purpose he wants sub-constract some other person for carrying out the job within West Bengal and outside the state. In the books of the assessee, some old creditors balances are outstanding and lying unadjusted due to non-aware of the present whereabouts of such creditors after a lapse of 4 to 5 years and whatever address are available with the assessee had been given by the suppliers at the time when the assessee had purchased material and / or taken labour from them. It was specifically brought to the notice of the ld AO that the assessee had not written back the sundry creditors to his profit and loss account as liabilities no longer payable and hence the liability had ceased to exist. Accordingly it was pleaded that there is no cessation of liability within the meaning of section 41(1) of the Act as the liabilities are continued to be retained in the books of the assessee. The ld AO observed that the assessee had made payments in financial year 2012-13 relevant to Asst Year 2013-14 to some of the creditors to the tune of Rs. 29,09,787/- and hence the reason stated by the assessee that the present whereabouts of the creditors were not known to the assessee. The ld AO accordingly proceeded to treat the sundry creditors in the sum of Rs. 1,08,65,202/- as deemed income u/s. 41(1) of the Act on account of cessation of liabilities.

3.2 The ld AO observed that out of the other sundry creditors for labour and materials in the sums of Rs. 25,60,398/- and Rs. 30,82,491/- respectively, the assessee had provided the list of creditors along with addresses showing opening balance, total of supplies made during the year (credit), payments made thereon (debits) including debits towards debit notes and TDS and closing balance of each of the creditors. From the same, the ld AO issued notice u/s. 133(6) of the Act to 4 parties, out of which 2 notices returned unserved ; 1 notice was served but no reply was received from the party and balance 1 notice was served and reply was received from the said supplier. The details of these 4 parties are as under:—

Sl. No.	*Name of Creditor party*	*Op. Balance*	*Cl. Balance*	*Remarks*
1.	Shri Brahmadeb Das	7,21,962/-	5,96,962/-	No Reply received
2.	M/s. Intex	8,81,094	9,73,673.-	Received Un-served
3.	M/s. M.J. Contractor	18,38,395	18,34,395	Reply Received
4.	Shri Sarvjit Kumar Tiwary	5,26,178/-	5,18,178	Received Un-served
		39,67,629	39,23,208	

The ld AO observed that M/s. M.J. Contractor who had filed the reply on 16.1.2015 wherein it had confirmed the transaction of Rs. 4,000/- executed during the year but did not confirm the balance of receivable amount at the starting and at the end of the year. Based on this, the ld AO treated the said creditor i.e M/s. M.J. Contractor as a bogus creditor.

3.2.1 The assessee was also granted opportunity to produce the remaining three parties namely (i) Shri Brahmadeb Das ; (ii) M/s. Intrex and (iii) Shri Sarvjit Kumar Tiwary along with the details / documents from which the genuineness of the closing balance could be proved. The ld AO showcaused the assessee as to why the balances outstanding in their accounts be not treated as bogus liabilities.

3.3 The assessee submitted reply to this effect by furnishing few copies of the bills raised by M/s. M.J. Contractor to the assessee and also the ledger copies of all the 4 parties before the ld AO. Regarding other 3 creditors, the assessee expressed his inability to produce the parties before the ld AO as the present whereabouts of such creditors are not known to the assessee. It was also specifically pointed out that the assessee had not written back the sundry creditors to his profit and loss account as liabilities no longer payable and accordingly there was no cessation of liabilities warranting invocation of deeming provisions of section 41(1) of the Act.

3.4 The ld AO observed from the copy of account of M/s. M.J. Contractor from assessee's books, that during the financial year 2009-10, the total amount of labour and fabrication work shown of Rs.

28,75,064/- out of which TDS was Rs. 7,25,392/- and the assessee had made payment of Rs. 9,75,392/- against the total amount, and balance amount of Rs. 19,10,320/- shown to be payable at the end of the financial year 2009-10. Since the said party did not confirm the balance outstanding at the end of the year as shown by the assessee, the ld AO treated the same as a bogus creditor. The ld AO further observed that the balance of sundry creditors as shown in the balance sheet did not tally with the creditors as per accounts submitted before him. Based on this, he concluded that the assessee had introduced certain bogus creditors into his books. Accordingly, he treated the balance outstanding in respect of aforesaid 4 parties in the sum of Rs. 39,23,208/- as bogus sundry creditors.

4. The addition made in the sum of Rs. 1,08,65,202/- u/s. 41(1) of the Act was upheld by the ld CITA for the same reasons stated by the ld AO. With regard to addition made towards bogus creditors, the ld CITA observed that the balance outstanding in the sum of Rs. 9,73,673/- with M/s. Intrex, was not creditors outstanding, rather it was debtors outstanding (i.e receivable by the assessee). Hence he held that the same cannot be added as bogus creditors in the hands of the assessee. However, he upheld the balance portion of bogus creditors in the sum of Rs. 29,49,535/- made in the assessment. Aggrieved, the assessee is in appeal before us on the following grounds:—

1. That under the facts and circumstances of the case, Ld. CIT (A) erred in confirming the addition of Rs. 1,08,65,202/- u/s. 41(1) as cessation of liability despite there is no change in closing balance of creditors liability, the addition therefore arbitrary, unjustified, illegal and uncalled for.
2. For that on facts of the case, Ld. CIT (A) erred in not considering the facts that unilaterally no cessation of liability can take place, therefore, the addition so made by the AO and confirmed by the Ld. CIT (A) is bad in law and liable to be cancelled.
3. That under the facts and circumstances of the case, Ld. CIT (A) was wrong in confirming the addition of Rs. 29,49,535/- as bogus sundry creditors u/s. 41(1) of IT Act despite there is no cessation of liability, which is completely wrong, arbitrary, unjustified and illegal.

5. We have heard the rival submissions and perused the materials available on record. The addition in the sum of Rs. 1,08,65,202/- has been made u/s. 41(1) of the Act by the ld AO. For the sake of convenience, the provisions of section 41(1) of the Act are reproduced below:—

> "Where an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee and subsequently during any previous year,—
>
> (*a*) the first-mentioned person has obtained, whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained by such person or the value of benefit accruing to him, shall be deemed to be profits and gains of business or profession and accordingly chargeable to income-tax as the income of that previous year, whether the business or profession in respect of which the allowances or deduction has been made is in existence in that year or not;
>
> (*b*) the successor in business has obtained, whether in cash or in any other manner whatsoever, any amount in respect of which loss or expenditure was incurred by the first-mentioned person or some benefit in respect of the trading liability referred to in clause (a) by way of remission or cessation

thereof, the amount obtained by the successor in business or the value of benefit accruing to the successor in business shall be deemed to be profits and gains of the business or profession, and accordingly chargeable to income tax as the income of that previous year.

[Explanation 1- For the purposes of this sub-section, the expression "loss or expenditure or some benefit in respect of any such trading liability by way of remission or cessation thereof" shall include the remission or cessation of any liability by a unilateral act by the first mentioned person under clause (a) or the successor in business under clause (b) of that sub-section by way of writing off such liability in his accounts.]

It is not in dispute that the assessee had claimed deduction towards at the time of creation of these trading liabilities in the earlier years. The only dispute is whether the same could be brought to tax u/s. 41(1) of the Act on account of cessation of liabilities. We find that the assessee had shown the same balances as outstanding towards the sundry creditors even as on 31.3.2013 (i.e the next assessment year). It is not in dispute that the assessee had not written back these creditors in the sum of Rs. 1,08,65,202/- to his profit and loss account as liabilities no longer payable. Hence there is no unilateral write back of the creditors to his profit and loss account by the assessee. From this it could be safely concluded that the assessee had proved that the liabilities had not ceased to exist. The very fact, that the liabilities are continued to be shown in the books of the assessee even in the next financial year ended 31.3.2013 relevant to Asst Year 2013-14, goes to prove that the assessee had duly acknowledged his debt by accepting the creditors liability to be discharged in future. Hence there cannot be any cessation of liability as on 31.3.2012. Moreover, in order to invoke the provisions of section 41(1) of the Act, there should be a clear finding to prove that the liabilities had ceased to exist during the previous year relevant to Asst Year 2012-13 (i.e the year under appeal). We find that no such finding is recorded by both the authorities below. In the absence of such crucial finding, invocation of provisions of section 41(1) of the Act as deemed income does not arise in the hands of the assessee. Moreover, the assessee had not obtained any benefit in respect of these trading liabilities in view of the fact that he had duly acknowledged the debt payable to these creditors in his books. In this regard, we find that the reliance has been rightly placed by the ld AR on the decision of the Hon'ble Karnataka High Court in the case of *CIT* v. *Alvares & Thomas* [2016] 239 Taxman 456/69 taxmann.com 257 (Kar.) on similar set of facts and circumstances had held as under:—

The appellant-Revenue has preferred the present appeal by raising the following substantial question of law:

"Whether under the facts and in the circumstances of the case, the Tribunal was right in law deleting the addition of Rs. 81,40,232 on account of cessation of liability under Section 41(1) being outstanding liability towards M/s. Durga Traders as claimed by the assessee when the assessee failed to prove the existence of the creditor and that the credit had insisted for the payment at pay point of time or initiated any legal action against the assessee, although the entry has been appearing in the books of the assessee for past 7 to 8 years and assessing authority rightly invoked provisions of sections 41(1) as all the conditions are fulfilled in the case of assessee?"

2. We may record that the relevant discussion of the Tribunal is at paragraphs 11 to 14 which reads as under:—

'11. We have given a careful consideration to the rival submissions. On almost identical facts, the Hon'ble Delhi High Court in the case of *Shri Vardhaman Overseas Ltd.* (*supra*), has clearly laid down that neither section 41(1) nor section 68 of the Act can be applied. On the applicability of section 68, we are of the view that those provisions will not apply as the balances shown in the creditors account do not arise out of any transaction during the previous year relevant to AY

2009-10. The provisions of sec. 68 are clear inasmuch as they refer to "sum found credited in the books of account of an assessee maintained for any previous year". Since the credit entries in question do not relate to previous year relevant to AY 2009-10, the same cannot be brought to tax u/s. 68 of the Act. The proper course in such cases for the Revenue would be to find out the year in which the credits in question were credited in the books of account and thereafter make an enquiry in that year and make an addition in that year, if other conditions for applicability of section 68 are satisfied.'

12. As far as applicability of section 41(1) of the Act is concerned, the question before us is limited to the applicability of Section 41(1) of the Act. The section insofar as it is relevant for our purpose is as below:

"Profits chargeable to tax.

41. (1) Where an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee (hereinafter referred to as the first-mentioned person) and subsequently during any previous year, —

(*a*) the first-mentioned person has obtained, whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained by such person or the value of benefit accruing to him shall be deemed to be profits and gains of business or profession and accordingly chargeable to income-tax as the income of that previous year, whether the business or profession in respect of which the allowance or deduction has been made is in existence in that year or not; or

** ** **"

[Explanation 1 - For the purposes of this sub-section, the expression— loss or expenditure or some benefit in respect of any such trading liability by way of remission or cessation thereof shall include the remission or cessation of any liability by a unilateral act by the first mentioned person under clause (a) or the successor in business under clause (b) of that sub-section by way of writing off such liability in his accounts." (Underlining Ours)

13. Explanation 1 which was inserted w.e.f. 1.4.1997 is not attracted to the present case since there was no writing off of the liability to pay the sundry creditors in the assessee's accounts. The question has to be considered de hors Explanation 1 to Section 41(1). In order to invoke clause (a) of Sec. 41(1) of the Act, it must be first established that the assessee had obtained some benefit in respect of the trading liability which was earlier allowed as a deduction. There is no dispute in the present case that the amounts due to the sundry creditors had been allowed in the earlier assessment years as purchase price in computing the business income of the assessee. The second question is whether by not paying them for a period of four years and above the assessee had obtained some benefit in respect of the trading liability allowed in the earlier years. The words "remission" and "cessation" are legal terms and have to be interpreted accordingly. In the present case, there is nothing on record to show that there was either remission or cessation of liability of the assessee. In fact, there is no reference either in the order of the AO or CIT (A) to the expression "remission or cessation of liability". In such circumstances, we are of the view that the provisions of section 41(1) of the Act could not be invoked by the Revenue. In fact the decision of the Hon'ble Delhi High Court in the case of *Vardhaman Overseas Ltd.* (*supra*) clearly supports the plea of the Assessee in this regard. On identical facts, the Hon'ble Delhi High Court on the applicability of Sec. 41(1) of the Act, held:—

12. That takes us to the next question as to what constitutes remission or cessation of the liability. It

cannot be disputed that the words "remission" and "cessation" are legal terms and have to be interpreted accordingly. In *State of Madras* v. *Gannon Dunkerley & Co.* AIR 1958 SC 560 Venkatarama Aiyyar J. explained the general rule of construction that words used in statutes must be taken in their legal sense and observed :

"The ratio of the rule of interpretation that words of legal import occurring in a statute should be construed in their legal sense is that those words have, in law, acquired a definite and precise sense and that, accordingly, the legislation must be taken to have intended that they should be understood in that sense. In interpreting an expression used in a legal sense, therefore, we have only to ascertain the precise connotation which it possesses in law".

In our opinion, this rule should be applied to the interpretation and understanding of the words "remission" and "cessation" used in the section.

13. In Bombay *Dyeing & Mfg. Co. Ltd.* v. *State of Bombay* AIR 1958 SC 328 the legal position was summarized by T.L. Venkatarama Aiyar, J., in the following manner :

"It has been already mentioned that when a debt becomes time-barred, it does not become extinguished but only unenforceable in a Court of law. Indeed, it is on that footing that there can be statutory transfer of the debts due to the employees, and that is how the board gets title to them. If then a debt subsists even after it is barred by limitation, the employer does not get, in law, a discharge therefrom. The modes in which an obligation under a contract becomes discharged are well-defined, and the bar of limitation is not one of them. The following passages in Anson's Law of Contract, 19th Edition, p. 383, are directly in point :

"At Common Law lapse of time does not affect contractual rights. Such a right is of a permanent and indestructible character, unless either from the nature of the contract, or from its terms, it be limited in point of duration."

But though the right possesses this permanent character, the remedies arising from its violation are withdrawn after a certain lapse of time; interest reipublicaeut si finis litium. The remedies are barred, though the right is not extinguished."

And if the law requires that a debtor should get a discharge before he can be compelled to pay, that requirement is not satisfied if he is merely told that requirement is the normal course he is not likely to be exposed to action by the creditor." (Underlining, italicised in print, Ours)

This was also the view taken by the Supreme Court in *CIT* v. *Sugauli Sugar Works (P.) Ltd.* 236 ITR 518 (SC) (*supra*).

14. Since the Tribunal has relied on the judgment of the Supreme Court in the case of *CIT* v. *Sugauli Sugar Works (P.) Ltd.* (*supra*) we may usefully refer to the decision in order to appreciate the controversy therein and the ratio laid down. That was a case of a private limited company. In respect of the asst. yr. 1965-66, it transferred a sum of 3,45,000 from the suspense account running from 1946-47 to 1948-49 to the capital reserve account. The ITO found that a sum of 1,29,000 out of the above amount repaymented deposits and advances which were paid back by the assessee. He, therefore, deducted this amount from the amount of 3,45,000 and the balance of 2,56,529 was brought to assessment under s. 41(1) of the Act. The assessee appealed unsuccessfully to the AAC and thereafter carried the matter in further appeal to the Tribunal. Its contention before the Tribunal was that the unilateral entry of transferring the amount from the suspense account to the capital reserve account would not bring the said amount within s. 41(1). The contention was accepted by the Tribunal whose decision was affirmed by the Calcutta High Court in *CIT* v. *Sugauli Sugar Works (P.) Ltd.* (1981) 23 CTR (Cal) 226 : (1983) 140 ITR 286 (Cal). The Revenue carried the

matter in the appeal to the Supreme Court. The contention of the Revenue (as noted at p. 520 of 236 ITR) was that on the facts of the case, the liability came to an end as a period of more than 20 years had elapsed and the creditors had not taken any steps to recover the amount and consequently there was a cessation of the debt which would bring the matter within the scope of s. 41(1). It may be noted that the contention of the Revenue in the case before us is precisely the same. To recapitulate, the learned standing counsel contended before us that since a period of more than 4 years has admittedly elapsed from the debt on which the debts were incurred and since the creditors had not taken any steps to recover the amount, there was a cessation of the debts which brought the matter under s. 41(1). Turning back to the judgment of the Supreme Court, we find that the judgment of the Calcutta High Court under appeal was affirmed for two reasons. The first reason was based on a judgment of the Full Bench of the Gujarat High Court in *CIT* v. *Bharat Iron & Steel Industries* (1992) 105 CTR (Guj.) (FB) 331 : (1993) 199 ITR 67 (Guj.)(FB). It was held by the Supreme Court that the Gujarat High Court was right in saying that in order to attract taxability under s. 41(1) the assessee should have obtained, whether in cash or in any other manner whatsoever, any amount in respect of the loss or expenditure earlier allowed as a deduction. This part of the reasoning, in the light of the amended cl. (a) of sub-s. (1) of s. 41 may not be relevant after substitution of the said clause by the Finance Act, 1992 w.e.f. 1st April, 1993, by which the words "some benefit in respect of such trading liability by way of remission or cessation thereof" were inserted. After the amendment, therefore, it is not necessary that in respect of a trading liability earlier allowed as a deduction, the assessee should have received any amount, in cash or otherwise, but it is necessary that the assessee should have received "some benefit" in respect of such trading liability. However, we have already seen that this benefit in respect of trading liability should be "by way of remission or cessation of the liability", after the amendment made to the clause w.e.f. 1st April, 1993. The second part of the reasoning of the Supreme Court in *CIT* v. *Sugauli Sugar Works (P.) Ltd.* (*supra*) is based on the interpretation of the words "cessation or remission" of the trading liability. The Supreme Court noticed a judgment of the Bombay High Court in *J.K. Chemicals Ltd.* v. *CIT* (1996) 62 ITR 34 (Bom.) in which it was explained as to what could bring out a cessation or remission of the assessee's liability. The observations of the Bombay High Court in the judgment cited above are as under :

"The question to be considered is whether the transfer of these entries brings about a remission or cessation of its liability. The transfer of an entry is a unilateral act of the assessee, who is a debtor to its employees. We fail to see how a debtor, by his own unilateral act, can bring about the cessation or remission of his liability. Remission has to be granted by the creditor. It is not in dispute, and it indeed cannot be disputed, that it is not a case of remission of liability. Similarly, a unilateral act on the part of the debtor cannot bring about a cessation of his liability. The cessation of the liability may occur either by reason of the operation of law, i.e., on the liability becoming unenforceable at law by the creditor and the debtor declaring unequivocally his intention not to Honour his liability when payment is demanded by the creditor, or a contract between the parties, or by discharge of the debt the debtor making payment thereof to his creditor. Transfer of an entry is neither an agreement between the parties nor payment of the liability. We have already held in *Kohinoor Mills Co. Ltd.* v. *CIT* (1963) 49 ITR 578 (Bom.) that the mere fact of the expiry of the period of limitation to enforce it, does not by itself constitute cessation of the liability. In the instant case, the liability being one relating to wages, salaries and bonus due by an employer to his employees in an industry, the provisions of the Industrial Disputes Act also are attracted and for the recovery of the dues from the employer, under s. 33C(2) of the Industrial Disputes Act, no bar of limitation comes in the way of the employees."

15. The Supreme Court noticed that the above observations of the Bombay High Court were quoted by the Calcutta High Court in the judgment under appeal before them, and observed as under while

upholding the judgment of the Calcutta High Court :

"This judgment has been quoted by the High Court in the present case and followed. We have no hesitation to say that the reasoning is correct and we agree with the same. To reinforce the conclusion, the Supreme Court also noticed its earlier judgment in *Bombay Dyeing & Mfg. Co. Ltd.* v. *State of Bombay* AIR 1958 SC 328 wherein it was held that the expiry of the period of limitation prescribed under the Limitation Act could not extinguish the debt but it would only prevent the creditor from enforcing the debt.

16. In our opinion, the judgment of the Supreme Court in *CIT* v. *Sugauli Sugar Works (P.) Ltd.* (*supra*) is a complete answer to the contention of the learned standing counsel. In the case before the Supreme Court for a period of almost 20 years the liability remained unpaid and this fact formed the basis of the contention of the Revenue before the Supreme Court to the effect that having regard to the long lapse of time and in the absence of any steps taken by the creditors to recover the amount, it must be held that there was a cessation of the debts bringing the case within the scope of s. 41(1). In the case before us, the identical contention has been taken on behalf of the Revenue, though the period for which the amount remained unpaid to the creditors is much less. It was held by the Supreme Court that a unilateral action cannot bring about a cessation or remission of the liability because a remission can be granted only by the creditor and a cessation of the liability can only occur either by reason of operation of law or the debtor unequivocally declaring his intention not to honour his liability when payment is demanded by the creditor, or by a contract between the parties, or by discharge of the debt."

14. From the ratio laid down in the aforesaid decision, we are of the view that there is nothing on record to show any cessation or remission of liability by the creditor or even an unilateral act by the Assessee in this regard. In view of the above, we are of the view that the impugned addition cannot be sustained and the same was rightly directed to be deleted by the CIT (A). The order of the CIT (A) is therefore confirmed.

3. The aforesaid shows that, the Tribunal has considered that the issue is already covered by the decision of Delhi High Court that Section 41(1) cannot be invoked and based on the decision of Delhi High Court, the Tribunal held that unless there is no material on record either for cessation or remission of liability by the creditor, Section 41(1) of the Income Tax Act cannot be invoked and the addition made cannot be sustained. Consequently, the Tribunal has directed the deletion made by the assessing officer.

4. However, Mr. Arvind, learned counsel appearing for the revenue relied upon the decisions of Rajasthan and Punjab & Haryana High Courts in *Rama Steel Rolling Mills & General Engg. Works* v. *ITO* [2013] 35 taxmann.com 262 and *Mrs. Adarsh Sood* v. *CIT* [2014] 47 taxmann.com 268/225 Taxman 67 respectively. He also relied upon the provisions of Section 41 of the Income Tax Act.

5. The principal contention is that unless the burden is discharged with regard to the existence of the liability by the assessee, it is open for the Revenue to invoke the provisions of Section 41(1) of the Act and to make addition on the premise that, the liability has ceased to pay the amount of the creditor.

6. In his submission, the decision of Delhi High Court which has been referred to by the Tribunal in case of *CIT* v. *Shri Vardhman Overseas Ltd.* [2011] 16 taxmann.com 350/[2012] 204 Taxman 524/343 ITR 408 cannot be applied to the facts of the present case since in the said decision, it was not a case where the party/creditor was not verifiable or that the address was not changed. He therefore, submitted that Court may consider the present appeal.

7. As in the above referred order of the Tribunal, the relevant portion of Section 41 is reproduced, we may not reproduce the same. But, the relevant aspect is that, there are two requirements for invoking the provision of Section 41. The Sine qua non is, the remission or cessation of the trading liability and the additional requirement is, some benefit in respect of such trade liability is taken by the Assessee. If the aforesaid conditions are satisfied, then only Section 41(1) could be invoked by the Assessing Officer.

8. Examining of the facts of the present case reveals that, it is not the case of the Department that, any benefit in respect of such trading liability was taken by the assessee but, the Revenue contends that since the burden was not discharged of existence of the liability, it be treated as cessation of the liability and therefore, Section 41(1) could be invoked. Further, stand of the Revenue is that, when in respect of debt in question, confirmation was called for, a letter was produced of the creditor with its address but, when the same was verified, the report was that, party could not be traced and therefore, it was not verifiable.

9. In our view, even if we accept the contention of the Revenue that the party could not be traced and therefore debt could not be verified then also, by no stretch of imagination can it be held that it would satisfy the requirement of cessation of liability. In legal parlance, merely because the creditor could not be traced on the date when the verification was made, same is not a ground to conclude that there was cessation of the liability. Cessation of the liability has to be cessation in law, of the debt to be paid by the assessee to the creditor. The debt is recoverable even if the creditor has expired, by the legal heirs of the deceased creditor. Under the circumstances, in the present case, it can hardly be said that the liability had ceased. If the liability had not ceased or the benefit was not taken by the assessee in respect of such trade liability, in our view, the conditions precedent were not satisfied for invoking Section 41(1) of the Act in the instant case.

10. The Tribunal has rightly relied upon the decision of Delhi High Court in case of *Shri Vardhman Overseas Ltd.* (*supra*). The discussion of the decision of Delhi High Court was relevant, for consideration of the facts of the case in order to find out as to under what circumstances it could be said that there is cessation of liability. Further, the decision of Delhi High Court is after considering the view taken by the Apex Court in case of *CIT* v. *Sugauli Sugar Works (P.) Ltd.* [1999] 236 ITR 518/102 Taxman 713.

11. In the decision of Rajasthan High Court in the case of *Rama Steel Rolling Mills & General Engg. Works* (*supra*), the question examined was with regard to discharge of the liability, whether by remission or cessation was not concluded but was rather referred to the assessing authority for fresh assessment. In the decision of High Court of Punjab and Haryana in case of *Mrs. Adarsh Sood* (*supra*), there were entries shown in the books of account of the assessee as not in the nature of debts but as credits. Such are not the fact situations in the present case.

12. Under the circumstances, the aforesaid decisions of High Court of Rajasthan and High Court of Punjab and Haryana cannot be applied to the facts of the case.

13. In view of the aforesaid, we find that when the issue is already covered by the decision of Delhi High Court, read with the reasons recorded by us hereinabove, it cannot be said that any substantial question of law would arise for consideration as sought to be canvassed.

Hence, the present appeal is dismissed."

(Bold letters provided by us)

5.1 Moreover, we find that in the decision of the Hon'ble Jurisdictional High Court in the case of *Kesoram Industries & Cotton Mills Ltd.* v. *CIT* [1992] 196 ITR 845 (Cal.) which was heavily relied

upon by the ld DR, the facts in that case were that the assessee had written back the unclaimed wages to its profit and loss account by an unilateral act on its part, which the Hon'ble Court held that the very unilateral act of writing back tantamounts to cessation of liability and accordingly the provisions of section 41(1) of the Act are attracted. But in the instant case, the assessee before us had not written back the sundry creditors in the sum of Rs. 1,08,65,202/- to its profit and loss account and had continued to show the same in its balance sheet. Hence the decision relied upon by the ld DR is factually distinguishable.

5.2 In view of the aforesaid observations in the facts and circumstances of the case and respectfully following the judicial precedent relied upon hereinabove, we have no hesitation in directing the ld AO to delete the addition made in the sum of Rs. 1,08,65,202/- u/s. 41(1) of the Act. Accordingly, the Grounds 1 & 2 raised by the assessee are allowed.

6. With regard to the addition sustained by the ld CITA in the sum of Rs. 29,49,535/- towards bogus creditors, we find that out of the 3 parties, one party M/s. M.J. Contractor (outstanding of Rs. 18,34,395/-) had duly responded to the notice u/s. 133(6) of the Act before the ld AO confirming the transactions with the assessee. We find from the ledger accounts enclosed in pages 20 to 22 of the paper book that the following payments were made after due deduction of tax at source during the year by the assessee which has been accepted as genuine by the ld AO :—

Name of the Supplier	*Net Amt Paid*	*TDS portion*	*Nature of Paymt*
Shri Brahmadeb Das	Rs. 1,23,750/-	Rs 1,250/-	Sub contractor payment
M.J. Contractor	Rs. 3,960/-	Rs. 40/-	Sub contractor payment
Sarvjit Kumar Tiwary	Rs. 8,000/-	Rs. Nil	Supplier payment

We find that when the payments made during the year by account payee cheque had been examined and accepted by the ld AO which was also partly subjected to due deduction of tax at source and especially in view of the fact that one of the parties M/s. M.J. Contractor had duly responded to notice u/s. 133(6) of the Act before the ld AO by confirming the transactions and in respect of Shri Brahmadeb Das, the notice u/s. 133(6) of the Act was duly served on the said supplier, it cannot be said that those suppliers are non-existent and bogus. We find that the assessee had placed all the relevant materials before the lower authorities to drive home the point that the sundry creditors shown in the name of these three parties are indeed genuine and transactions were done during the year with them. These facts were not appreciated by the ld AO while treating these creditors as bogus. It is not in dispute that these 3 creditors balances were brought forward from previous year and during the year, only small payments were made to them as detailed *supra* and hence the balance outstanding in these accounts cannot be the subject matter of addition during the year under appeal. Accordingly, the Ground No. 3 raised by the assessee is allowed.

7. The last issue to be decided in this appeal is as to whether the ld CITA was justified in upholding the disallowance made u/s. 40(a)(ia) of the Act in the sum of Rs. 1,15,716/- relating to Adhir Kumar Mondal upon payment of labour and fabrication charges in the facts and circumstances of the case.

7.1 The brief facts of this issue is that the assessee had claimed an expenditure of Rs. 63,59,500/- under the head 'Labour & Fabrication Charges' during the year under consideration. The assessee submitted party wise details of labour and fabrication expenses and party wise details of TDS in all the four quarters. While comparing the party wise details with the TDS details, the ld AO noticed that the assessee had short deducted tax at source in respect of amount paid to Adhir Kumar Mondal to the tune of Rs. 1,15,716/-. The ld AO disallowed the same u/s. 40(a)(ia) of the Act for short deduction of tax at source. In appeal, the ld CITA observed that the assessee had submitted a certificate from the chartered accountant that Adhir Kumar Mondal had considered the subject mentioned payment in his return filed on 23.3.2013 and accordingly in view of the second proviso to section 40(a)(ia) read with section 201, which has been held to be retrospective in operation, the assessee should not be treated as assessee in

default and consequentially no disallowance u/s. 40(a)(ia) of the Act could be inflicted on him. The ld CITA observed that since Adhir Kumar Mondal had filed the return of income on 23.3.2013 (i.e beyond the due date u/s. 139(1) of the Act), the conditions laid down in proviso to section 201(1) of the Act are not satisfied and accordingly upheld the disallowance of Rs. 1,15,716/- made by the ld AO. Aggrieved, the assessee is in appeal before us on the following ground:—

> 4. That under the facts and circumstances of the case, Ld. CIT (A) was wrong in confirming the disallowances of Rs. 1,15,716/- relating to Adhir Kumar Mondal upon payment of labour & fabrication charges u/s. 40(a)(ia), therefore, the addition so made is liable to be cancelled.

7.2 We have heard the rival submissions. At the outset, we find that the disallowance u/s. 40(a)(ia) of the Act has been made due to short deduction of tax at source on labour and fabrication charges paid to Adhir Kumar Mondal. We find that the ld CIT (A) had considered the assessee (payer) as assessee in default despite the chartered accountant's certificate proving the fact that Adhir Kumar Mondal had duly considered the payments made by the assessee in his return of income filed on 23.3.2013. The ld CITA had held that since the return was filed belatedly u/s. 139(4) of the Act by the payee (i.e Adhir Kumar Mondal), the conditions prescribed in proviso to section 201(1) of the Act were not satisfied and accordingly the assessee is to be treated as assessee in default. In this regard, the conditions prescribed in proviso to section 201(1) of the Act are reproduced below for the sake of convenience:—

> Section 201 - Consequences of failure to deduct or pay
>
> (1)** ** **
>
> [18][Provided that any person, including the principal officer of a company, who fails to deduct the whole or any part of the tax in accordance with the provisions of this Chapter on the sum paid to a resident or on the sum credited to the account of a resident shall not be deemed to be an assessee in default in respect of such tax if such resident—
>
> (*i*) has furnished his return of income under section 139;
>
> (*ii*) has taken into account such sum for computing income in such return of income; and
>
> (*iii*) has paid the tax due on the income declared by him in such return of income, and the person furnishes a certificate to this effect from an accountant in such form as may be prescribed[19]:]

From the bare reading of the conditions prescribed in proviso to section 201(1) of the Act above, we find that the legislature had no where provided that the payee should furnish his return of income u/s. 139(1) of the Act. The condition only says section 139. It does not mention about section 139(1) of the Act. The return filed within the time limit prescribed u/s. 139(4) of the Act is also a valid return as that leeway has been provided in the statute itself. It is not in dispute that the payee (i.e Adhir Kumar Mondal) had duly considered the subject mentioned payment made by the assessee in the return of income filed u/s. 139 of the Act and had taken into account such sum for computing the income and had paid the taxes due on the income declared by him in the return of income. All the three conditions are duly satisfied. These facts are evident from the chartered accountant certificate issued in terms of first proviso to section 201(1) of the Act, which is part of records before us, and which fact remain uncontroverted by the revenue before us. We find that the ld CITA had taken cognizance of this CA certificate but had not given weightage of the same due to his interpretation that section 139 referred to in the proviso to section 201(1) of the Act need to be construed only as section 139(1) of the Act and not otherwise. In these facts and circumstances, we hold that the assessee had furnished requisite evidences to prove that the payee had duly considered the subject mentioned receipt in his return of income and hence no disallowance u/s. 40(a)(ia) of the Act could be inflicted on the same in the hands of the assessee payer.

Accordingly, the Ground No. 4 raised by the assessee is allowed.

7.3 Yet another point that arises for our consideration in the instant case is as to whether the provisions of section 40(a)(ia) of the Act could be invoked for short deduction of tax at source. We find that this issue has been held in favour of the assessee by the co-ordinate bench decision of this tribunal in the case of *CIT* v. *S.K. Tekriwal* [2011] 48 SOT 515/15 taxmann.com 289 (Kol.) wherein it was held that in the case of short deduction of tax at source, no disallowance u/s. 40(a)(ia) of the Act could be made in the hands of the assessee and the assessee could be proceeded against only under section 201 of the Act in such cases. This decision was admittedly approved by the *Hon'ble Jurisdictional High Court in the same case in ITAT NO. 183 of 2012 G.A.No. 2069 of 2012 dated 3.12.2012*. Respectfully following the same, we hold that no disallowance u/s. 40(a)(ia) of the Act could be made in the hands of the assessee payer herein. Accordingly, the Ground No. 4 raised by the assessee deserves to be allowed on this aspect also.

8. The Ground No. 5 raised by the assessee is general in nature and does not require any specific adjudication.

9. In the result, the appeal of the assessee is allowed.

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*In favour of assessee.