IN THE INCOME TAX APPELLATE TRIBUNAL, BENCH 'A' KOLKATA

[Before Hon'ble Shri N.V.Vasudevan, JM & Shri Waseem Ahmed, AM]

ITA No.1010/Kol/2014
Assessment Year : **2010-11**

M/s. Aparna Agency Ltd. Kolkata (PAN:AACCA 1096 K) (Appellant)	-versus-	I.T.O., Ward-12(3), Kolkata (Respondent)

For the Appellant: Shri Subash Agarwal, Advocate
For the Respondent: Shri A.K.Sinha, JCIT

Date of Hearing : 16.02.2017.
Date of Pronouncement : 01.03.2017.

ORDER

PER N.V.VASUDEVAN, JM:

This is an appeal by the Revenue against the order dated 28.03.2014 of CIT(A)-XII, Kolkata relating to A.Y.2010-11.

2. Ground no.1 raised by the assesee reads as follows :-

"1. For that on the facts and in the circumstances of the case, the Ld. CIT(A) was not justified in confirming the addition to the extent of Rs.1,70,7801- out of the total addition of Rs.7,32,771/- made by the A.O. on account of Distribution Charges. "

3. The assessee is a company. It is engaged in the business of trading and acting as acquiring and forwarding agents. While computing the income under the head "income from business" the assessee claimed a sum of Rs.17,07,826/- as distribution charges. The assessee was acting as distributor of FMCG products. The AO called upon the assessee to furnish vouchers in support of the expenses. Since the vouchers in support of the claim was voluminous, the assessee produced vouchers to the extent of Rs.75,000/- which was verified on a test check basis by the AO. On such test checking, the AO found the following discrepancy in four of the vouchers produced by the assessee :-

Sl.No.	Amount (in Rs.)	Date	Discrepancies
1.	3,000/-	21.04.2009	The payments were made to the Govt. Of West Bengal for violation of Law, which is not an allowable expenditure.
2.	13,680/-	07.04.2009	No information about who received the amount.
3.	1,500/-	30.03.2010	No information about who received the amount.
4.	14,000/-	30.03.2010	No information about who received the amount.
Total	32,180		

4. The AO was of the view that out of the vouchers produced evidencing expenditure of Rs.75,000/-, Rs.32,180/- was liable to be allowed for the reasons given in the chart given above. According to the AO, the remaining expenditure under this head would also be of the same pattern as the expenditure whose vouchers were verified on a test check basis. According to the AO therefore the same ratio of disallowance of expenses as were made on expenditure verified on test check basis should be made. Applying the same ratio, the disallowance out of the distribution charges of Rs.17,07,826/- would be Rs.7,32,771/-. The AO issued a show cause notice proposing to disallow a sum of rs.7,32,771/-.

5. The assessee in reply to the aforesaid show cause notice submitted that the payment of Rs. 3,000/- is against 26 slips of Rs. 100/- each (plus incidental expenses of Rs.400/-) issued by the Govt. of West Bengal MTV Cell Department for the alleged minor traffic violations in respect of the delivery vans of the assessee. The Assessee submitted that these payments were not against any proved violation/infraction of law but were merely a payment in settlement of a contemplated action charging the assessee with an offence. It was submitted that the payment of fine was not equivalent to proof of guilt. The payment was made purely with a view to avoid prolonged litigation, save time and litigation cost. Therefore the payment in question cannot be said to be a payment which is hit by Explanation to Sec.37(1) of the Act which reads as follows:

> **"General.**
>
> **37.** (1) Any expenditure (not being expenditure of the nature described in sections 30 to 36 and not being in the nature of capital expenditure or personal expenses of the assessee), laid out or expended wholly and exclusively for the purposes of the

> business or profession shall be allowed in computing the income chargeable under the head "Profits and gains of business or profession".
>
> *Explanation 1*.—For the removal of doubts, it is hereby declared that any expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law shall not be deemed to have been incurred for the purpose of business or profession and no deduction or allowance shall be made in respect of such expenditure."

Reliance was placed on the decision of the Hon'ble Madras High Court in the case of CIT vs. Parthasarathy (Mad) 212 ITR 105 (Mad.), wherein it was held that for deciding the question whether an expenditure is hit by explanation1 to Sec.37(1) on has to examine the scheme of the provisions of the relevant statute, providing for payment of such imposts notwithstanding the nomenclature of the impost as given by the statute, to find out whether it is compensatory or penal in nature. The authority has to allow deduction under section 37(1) of the Income-tax Act, whenever such examination reveals the concerned impost to the purely compensatory in nature. Whenever such impost is found to be of composite nature, that is, partly of compensatory nature and partly of penal nature, the authorities are obliged to bifurcate the two components of the impost and give deduction to that component which is compensatory in nature and refuse to give deduction to that component which is penal in nature.

6. With regard to the other three vouchers of Rs. 13,680/-, Rs. 1,500/- and Rs. 14,000/- which, according to the AO did not contain any information as to who received the amount, it was submitted that these vouchers pertained to payments in respect of hire charges paid for the carriage of goods to the outside vehicles taken on hire when Assessee's own vehicles were not sufficient due to pressure of work. The Vehicles were summoned from the road side parking in such emergent situations. The vehicles in question operate in the unorganized sector and do not have any office address. It was pointed out that the vehicle number are duly mentioned in the vouchers and the recipient of hire charges has also duly signed the voucher at the back. It was submitted it would be impossible for the Assessee to keep the name and address proof

of each and every person with whom Business transaction is being made. Business Practice is to be considered before questioning any business expense. So, all the three Vouchers as mentioned above are for the business purpose and genuine in nature. In the circumstances, no disallowance is called for.

7. The AO however did not deal with the above objections specifically and he disallowed a sum of Rs.7,32,771/- observing as follows:

> "The submission of the assessee has been considered carefully. In respect of payment to Govt: is it seen that the payment was in the nature of Penalty and therefore, it is not allowable. The vouchers were verified on test check basis and it is found that these are self made vouchers and it is not known who received the payments. The onus is on the assessee to substantiate its claim of expenditures and the assessee has failed to discharge its onus. Therefore, a sum of Rs.7,32,771/-, as mentioned above is disallowed and added back to the total income of the assessee."

8. Aggrieved by the order of AO the assessee preferred appeal before CIT(A). The CIT(A) was of the view that the disallowance of Rs.3,000/- for minor traffic violations had to be disallowed for the reasons given by the AO. With regard to the remaining disallowance CIT(A) was of the view that the sample chosen by the AO was a very small sample and on that basis the quantum of expenses disallowed by the AO was on the higher side. The CIT(A) was of the view that in the given circumstances of the case it would be just and proper to disallow 10% of the distribution charges of Rs.17,07,826/-.The addition made by AO was accordingly restricted to Rs.1,17,718/-. Aggrieved by the order of CIT(A) the assessee has raised ground no.1 before the Tribunal.

9. We have heard the submissions of the ld. Counsel for the assesee, who reiterated the submissions made by the assessee before AO. The ld. DR relied on the order of CIT(A).

10. We have considered the rival submissions. As far as the disallowance of penalty of Rs.3000 imposed for minor violations is concerned, it is necessary to see the provisions of Sec.119 of the Motor Vehicles Act, 1988 (MV Act), in the light of the

various violations for which the payment in question was made by the Assessee. Some of the Sections of the MV Act which have been quoted in the bills evidencing payment of the aforesaid sums reads thus:

"119. Duty to obey traffic signs.—

(1) Every driver of a motor vehicle shall drive the vehicle in conformity with any indication given by mandatory traffic sign and in conformity with the driving regulations made by the Central Government, and shall comply with all directions given to him by any police officer for the time being engaged in the regulation of traffic in any public place.
(2) In this section "mandatory traffic sign" means a traffic sign included in Part A of the First Schedule, or any traffic sign of similar form (that is to say, consisting of or including a circular disc displaying a device, word or figure and having a red ground or border) placed or erected for the purpose of regulating motor vehicle traffic under sub-section (1) of section 116."

"Section 177 in The Motor Vehicles Act, 1988

177. General provision for punishment of offences.—Whoever contravenes any provision of this Act or of any rule, regulation or notification made thereunder shall, if no penalty is provided for the offence be punishable for the first offence with fine which may extend to one hundred rupees, and for any second or subsequent offence with fine which may extend to three hundred rupees."

"Section 122 in The Motor Vehicles Act, 1988

122. Leaving vehicle in dangerous position.—No person in charge of a motor vehicle shall cause or allow the vehicle or any trailer to be abandoned or to remain at rest on any public place in such a position or in such a condition or in such circumstances as to cause or likely to cause danger, obstruction or undue inconvenience to other users of the public place or to the passengers."

"Section 129 in The Motor Vehicles Act, 1988

129. Wearing of protective headgear.—Every person driving or riding (otherwise than in a side car, on a motor cycle of any class or description) shall, while in a public place, wear 1[protective headgear conforming to the standards of Bureau of Indian Standards]: Provided that the provision of this sections shall not apply to a person who is a Sikh, if he is, while driving or riding on the motor cycle, in a public place, wearing a turban: Provided further that the State Government may, by such rules, provide for such exceptions as it may think fit. Explanation.—"Protective headgear" means a helmet which,—
(a) by virtue of its shape, material and construction, could reasonably be expected to afford to the person driving or riding on a motor cycle a degree of protection from injury in the event of an accident; and
(b) is securely fastened to the head of the wearer by means of straps or other fastenings provided on the headgear."

Explanation to Sec.37(1) of the Act use the expression expenditure incurred "for any purpose which is an offence or which is prohibited by law" The word "offence" is not defined in the Income Tax Act. However, it is defined in Section 3(38) of the General Clauses Act, 1887 as follows: *"offence" shall mean any act or omission made punishable by any law for the time being in force;*". The expression "prohibited by law" , too, is not defined in the Income Tax Act. It may be viewed either as an act arising from a contract which is expressly or impliedly prohibited by statute, or contracts entered into with the object of committing an illegal act. The Hon'ble Supreme Court in **Haji Aziz and Abdul Shakoor Bros. v CIT Bombay City II** (1961) 41 ITR 350, it was held that '*In our opinion, no expense which is paid by way of penalty for a breach of the law can be said to be an amount wholly and exclusively laid for the purpose of the business. The distinction sought to be drawn between a personal liability and a liability of the kind now before us is not sustainable because anything done which is an infraction of the law and is visited with a penalty cannot on grounds of public policy be said to be a commercial expense for the purpose of a business or a disbursement made for the purposes of earning the profits of such business'.*

11. It is clear from the statutory provisions of the MV Act as well as the law laid down in judicial pronouncements that payments made for any purpose which is an offence or which is prohibited by law and which are not compensatory in nature cannot be allowed as a deduction u/s.37(1) read with Explanation thereto. Perusal of the various statutory provisions of the MV Act under which the payment in question were made were for offences committed by the employees of the Assessee for which the Assessee was vicariously liable. These payments were not compensatory in nature. Therefore these sums cannot be allowed as a deduction. We uphold the order of the CIT(A) to this extent.

12. As far as the disallowance of the remaining sum sustained by the CIT(A), the disallowance sustained by CIT(A) deserves to be deleted. Admittedly the sample vouchers in which the AO found defects had registered vehicle numbers that were

hired by the assessee for carriage of goods. This provided enough information for the AO to make further enquiries. In the circumstances under which the carriage was hired by the assesee it is not possible to insist on all details being given in the voucher. The explanation of the assessee has not been found to be incorrect by the AO or CIT(A). We therefore direct that the addition sustained by CIT(A) to the extent it relates to disallowance of 10% of total expenditure of Rs.17,07,826/- excluding the sums paid by way of penalty, be deleted. Ground no.1 raised by the assessee is partly allowed.

13. Ground No.2 raised by the assessee reads as follows :-

"2. For that on the facts and in the circumstances of the case, the Ld. CIT(A) erred in confirming the addition of Rs.5,17,093/- made by the A.O. under the head "Cash Destroyed by Fire".

14. The assessee had debited Rs. 5,17,093.09 under the head "Cash destroyed by fire" in the Profit & Loss account and claimed the same as deduction while computing income from business. A fire broke out on 13/02/2010 (late night) at Strand Road Warehouse of the Assessee. It is the plea of the Assessee that Strand Road Warehouse had a small office wherein cash used to be given by customers. It was the plea of the Assessee that two of its customers had given cash of Rs. 5,17,093.09 on 13.2.2010 and the same was kept in the office attached to the warehouse for onward transmission to the head office. In the fire that broke out in the late night of 13.2.2010, the said cash realization as well as huge stock was destroyed. The entry for receipt of cash was made in the cash book on 15.2.2010. The entry for loss of cash by destruction by fire was however made only on 31.3.2010, the last date of the previous year. According to the AO there was no documentary evidence produced in support of cash destruction. The AO also found from the copy of the letter addressed by the Assessee to the Directorate of Fire Service on 16.02.2010 that there was no mention about destruction of cash on that date. According to the AO, therefore, a sum of Rs. 5,17,093/- was liable to be disallowed.

15. The AO issued a show cause notice and called upon the Assessee to explain how loss due to alleged destruction of cash was allowable as deduction. The Assessee submitted that in the letter dated 16.02.2010 addressed by the Assessee to the Directorate of Fire Service, there is reference to loss of stock and market credit bills amounting to about Rs. 5 crores but no reference about the cash loss due to the simple reason that only the stock was insured with the National Insurance Co. Ltd. and the rules of the insurance co. require reports from the Fire Department and the Police Department. The Assessee brought to the notice of the AO that it had in support of the claim for loss of cash on account of fire, all the relevant pages of Cash Book and that entry in Cash Book dt. 15.2.10 wherein the entry reflects that the Assessee collected cash against dues from customer, as detailed below:

Customer of	Amount (Rs)
i) Reckitt Benckiser Product	1,72,413.00
ii) Glaxo Smithline Product	3,44,662.00
	5,17,093.00

The Assessee also brought to the notice of the AO that it had filed a writ petition in the High Court of Calcutta on 27.07.2010 praying for direction to the landlord and the Police and Fire Department to permit the Assessee and or their agents, authorised men entry into the tenanted warehouse premises. The Assessee highlighted the fact that in the said writ petition, it was clearly mentioned that three companies of the group viz., Aparna Agency Ltd., Aparna Distributors (P) Ltd. and Sales & Services were transacting business from the said premises and there was loss of stocks and market credit bill was to the tune of Rs. 5 crores and cash received from market sales and credit collections to the tune of Rs. 16 lakhs of the three companies. Though the petitioner before the Hon'ble Court was the assessee, two of the Assessee's group companies were also tenant in respect of different portions of the same premises and in order to avoid multiple proceedings a single writ petition was filed wherein the figures pertaining to the three companies of the group were provided. The Assessee pointed out that loss on account of cash was duly reflected in the final accounts of all the three companies, which totals upto Rs. 16 lakhs. With regard to entry relating to

the loss of cash being made only 31/03/2010 when fire broke out on 13.02.2010, it was submitted that the Assessee was making endeavour to get ingress into the premises to ascertain the extent of loss, which was denied to the Assessee by the police authorities. This ultimately led filing of writ petition in July, 2010 i.e., after the close of the accounting year. However, at the end of the year i.e., on 31.03.2010, the Assessee was reasonably sure of the loss considering the extent of damage and hence the entries in the books of accounts were made on the last date of the previous year. It was argued that as per the principles of mercantile system of accounting, which the Assessee was following, the loss / liability which can be ascertained with reasonable certainty should be provided for in the accounts as at the end of the relevant financial year and the Assessee's claim was well within the mercantile system of accounting.

16. The AO however held that assessee filed some documentary evidence with regard to its claim for deduction on account of destruction of cash in fire but in none of the documents it could be discerned that such amount of cash was destroyed by fire. The AO also held that the reason for making entry in cash book only on 31.03.2010 was also not known. The AO therefore held that the claim of the Assessee for deduction of the sum in question was as afterthought only and not acceptable. Therefore, a sum of Rs. 5,17,093/- was disallowed and added back to the total income of the assessee.

17. On appeal by the assessee the CIT(A) confirmed the order of AO observing as follows :-

> "I have carefully considered the submission of the appellant along with the supporting evidences furnished, perused the facts of the case including the observation /finding of the AO in the assessment order and the other materials brought on record. I do not find any merit in the argument put forth by the appellant. It is noted that in the documentary evidences filed by the appellant, no where it was mentioned that cash was destroyed by fire in the case of the appellant. I also find force in the contention of the AO. that if the cash was destroyed by fire on 13.02.2010, then the entry passed on 31.03.2010 on account of such loss did not reflect the correct position of cash. Further, it is not the case of the appellant that a separate cash book was maintained in respect of the said premises. Therefore, it is seen that the appellant has failed to prove by sufficient documentary evidences the loss claimed in respect of fire.

> In the light of the above discussion and observation, I hold that the action of the A.O. in making the disallowance of Rs.5,17,093.09 was correct and thus the disallowance so made is upheld. Hence, this ground of appeal of the appellant is dismissed."

18. Aggrieved by the order of CIT(A) the assessee has raised ground no.2 before the Tribunal. We have heard the submissions of the ld. Counsel for the assessee, who reiterated the stand taken of the assessee as put forth before AO. The ld. DR relied on the order of CIT(A).

19. We have heard the rival submissions. It is clear from the facts available on record that there was a fire in the assessee's warehouse at Strand Road on 13.02.2010 late night. The warehouse also has an office attached to it in which the assessee had kept receipt in cash from two customers against the dues. The name of the customers and the sum which they had paid to the Assessee in cash was duly furnished by the assessee before the AO. The cash book was maintained at the Head office which is in a different premises. The entry in the cash book regarding receipt of cash was made only on 15.02.2010. It is because of the delay in communication of the receipt of cash by the godown cum office at Strand Road to the head office of the assesee which was at Shambu nath Pandit Road. It is clear from the copy of the writ petition filed before the Hon'ble Calcutta High Court in connection with the assessee's right to enter the warehouse after the incident of fire that the assessee has clearly set out the fact that it had kept cash collections also in the godown that suffered fire accident though the writ petition had been filed by the assessee in the month of July, 2010. In the given circumstances the best evidence that the AO could have obtained regarding the correctness of the claim of the assessee for destruction of cash in fire would have been to make enquiries from the persons from whom the assessee claimed to have received cash. Admittedly the AO did not take recourse to such an action but merely rejected the explanation offered by the assessee. This approach of the AO in our view was not proper. The entry relating to the loss of cash having been made in the books of account of the assessee only on 31.03.2010, in our view, is not a very vital

circumstance. We are therefore of the view that in the given facts and circumstances of the case, the claim of the assessee for loss on account of cash destroyed by fire ought to have been allowed as deduction. We hold accordingly and direct the AO to allow deduction claimed by the assesee. Ground No.2 raised by the assessee is allowed.

20. In the result the appeal by the assessee is allowed.

Order pronounced in the Court on 01.03.2017.

Sd/- Sd/-

[Waseem Ahmed] [N.V.Vasudevan]
Accountant Member Judicial Member

Dated : 01.03.2017.

[RG PS]

Copy of the order forwarded to:

1.M/s. Aparna Agency Ltd., 82A, S.N.Pandit Street, Kolkata-700020.
2.I.T.O., Ward-12(3), Kolkata..
3. CIT(A)-XII, Kolkata.
4. CIT-IV, Kolkata.
5. CIT(DR), Kolkata Benches, Kolkata.

True Copy

By order,

Asst. Registrar, ITAT, Kolkata Benches