IN THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD BENCH 'B', HYDERABAD

BEFORE SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER
AND SMT. ASHA VIJAYARAGHAVAN, JUDICIAL MEMBER

ITA NO. 1106/Hyd/2011
Asst. Year: 2007-08

M/s Electronics Corporation of India Ltd., ***… Appellant***
Hyderabad
(PAN - AAACE 4809 L)

Vs.

Asst. Commissioner of Income-tax, ***… Respondent***
Circle 2(2), Hyderabad

ITA NO. 895/Hyd/2011
Asst. Year: 2007-08

Asst. Commissioner of Income-tax, ***… Appellant***
Circle 2(2), Hyderabad

Vs.

M/s Electronics Corporation of India Ltd., ***… Respondent***
Appellant
Hyderabad
(PAN - AAACE 4809 L)

Assessee by **:** *Shri C.P. Ramaswamy*
Respondent by : *Smt. Alka R. Jain*

Date of Hearing	25.7.2012
Date of Pronouncement	25/09/2012

O R D E R

Per Asha Vijayaraghavan, Judicial Member:

Both these appeals are cross appeals directed against the order of the CIT(A) dated 23.3.2011 for the assessment year 2007-08.

ITA NO. 1106/Hyd/2011 – appeal by the assessee

2. Facts of the case in relation to the issue in brief are that the assessee-company is a Central Public Sector Undertaking and is engaged in business of manufacture and sale of electronic goods and components. It also derives income from maintenance services and from computer educational services. For the assessment year 2007-08, it has filed return of income on 29.10.2007, declaring an income of Rs.1,89,78,55,064. During the course of assessment proceedings, the assessing officer while verifying the details of miscellaneous expenses noticed that the assessee has debited an amount of Rs.2,62,42,012/- towards 'Provision for CISF security expenses'. He noted that such amount is a mere provision. On query raised by him for justifying such claim, the assessee while stating that the said amount pertained to the proportionate expenses at 32% of the total cost incurred by Nuclear Fuel Complex on CISF personnel, for providing security to their complexes and premises, has submitted that they are required to make such provision in the accounts for the financial year 2006-07, as per the approval of their parent department, Department of Atomic Energy(DAE), to the proposal in that regard submitted by NFC. The assessing officer was not satisfied with the explanation of the assessee. Referring to the letter of the department of Atomic Energy dated 16.4.2003, the assessing officer noted that the approval of competent authority has not been taken for finalizing the Memorandum of Understanding. He therefore, noted that such

liability in this case is in the nature of a contingent liability and the same cannot be allowed as a deduction for the assessment year 2007-08.

3. The assessing officer, further, on verification of Form Nos.3CM and 3CL issued by the Ministry of Science & Technology, Department of Scientific and Industrial Research, the assessing officer noticed that as per such certificates issued by the said authority, the R&D expenditure was only Rs.3126.02 lakhs. Based on this fact, on query raised by the assessing officer for justifying the claim of deduction, the assessing officer submitted that the said authority has not considered certain expenditure in that regard. However, the assessing officer did not accept the said submission of the assessee, and since the said certificate issued by the competent authority in form No.3CM and 3CL only an amount of Rs.3126.02 lakhs was shown as expenditure incurred by the assessee on Research & Development, the assessing officer held that the assessee is eligible for deduction of an amount of Rs.46879.03 lakhs only being 150% of Rs.3126.02 lakhs. The assessing officer accordingly disallowed the excess claim of the assessee for deduction under S.35(2AB), which resulted in an addition of Rs.1,69,73,987.

4. The assessing officer made certain other additions like Rs.10,764,00,000 on account of provision made towards wage revision arrears and disallowance of depreciation to the extent of Rs.16,79,224 on software capitalized during the assessment year 2003-04, and also allowing further depreciation for the said amounts of Ra.16,79,224, the

assessing officer completed the assessment on a total income of Rs.2,04,57,91,840, vide order of assessment dated 10.12.2009 passed under S.143(3) of the Act.

5. On appeal before the CIT(A), on the issue disallowance out of security expenses, it was pleaded that once the proposal for sharing of expenditure for deployment of CISF personnel on proportionate basis put forward by NFC was 'found to be reasonable, realistic and practical and therefore approved in the department and further ECIL was directed to "take immediate action to finalize the MOU and settle the pending dues on the expenditure incurred by NFC on deployment of CISF…" vide DAE's letter dated 16.4.2003. Thereafter, the sharing of expenditure on deployment of CISF on an annual basis, has become a routine exercise requiring no further approval from the Department. It was stated that the provision in question of Rs.2,62,42,012/- relates to the share of security charges for the previous year relevant to assessment year 2007-08 only. It was clarified before the CIT(A) that the question of obtaining approval on year to year basis does not arise. Reliance in this behalf was also placed on the decision of this Tribunal in assessee's own case for assessment year 2006-07, wherein the Tribunal allowed the assessee's claim on the basis of the one time approval granted by the controlling department, viz. DAE. It was further submitted that NFC has been raising demand towards share on security expenses on provisions of CISF personnel, on quarterly basis and the ECIL has been making payments after adjusting NFC's share of private security expenses borne by ECIL, and thus, as against demands of Rs.57,81,333 and

Rs.70,77,460 received from NFC for the first two quarters of financial years 2006-07, actual payments to NFAC amounted to Rs.55,67,529 and Rs.68,74,4893 respectively, which worked out to a total of Rs.128.42 lakhs. Since demand letters for the last two quarters were not received from NFC before the close of the accounts, ECIL made a provision of Rs.138 lakhs for these two quarters since it is mandatory to follow actual basis of accounting, and thus, the total expenditure including provision of Rs.138 lakhs amounted to Rs.262.42 lakhs, which has been claimed by the assessee. It was further submitted that on receipt of demand letters from NFC for the last two quarters, vide their letters dated 21.4.2007 and 12.6.2007, ECIL made the payments on 31.5.2007 and 21.8.2007.

6. The CIT(A), after detailed consideration of these submissions and taking into account the letter of the CMD of the assessee-company dated 20.12.2010 filed before him, to assert that the assessee, having obtained the permission for sharing of security expenses on proportionate basis with NFC in the first instance there is no need subsequently to obtain such approvals periodically time and again thereafter, and also following the decision of the Tribunal in assessee's own case for the immediately preceding year, viz. assessment year 2006-07 noted above, held that the amount incurred towards expenditure for deployment of CISF personnel for providing security to the premises of the assessee company during the assessment year 2006-07 is allowable in this case.

7. However, the CIT(A) granted only part relief to the assessee and restricted the disallowance of Rs.2,62,42,012

made by the assessing officer to Rs.69,00,000, with the following observations-

> *"5.4. …….It has been stated that against the demand raised for the first two quarters during the F.Y. 2006-07, the appellant has made necessary payment. However, the invoices/bills towards such expenses for the last two quarters of the current financial year has not been received during the year. However, I am unable to agree with the contention of the appellant. Even if, it is stated that the bill for the third quarter has not been received from NFC, the appellant could have obtained the same from the said authority, after December, 2006. It is only the demand for the last quarter which the appellant might not have received before 31st March, 2007. Under the circumstances, the provision made by the appellant towards security expenses for that quarter only is allowable on basis of such provision made by them. However, since the appellant was making payment of its dues on that account on quarterly basis, the amount claimed towards provision of for the third quarter during the year, in my view, cannot be allowed as deduction in this case. Since the appellant has not furnished the amount of such provision pertaining to the said third quarter, 50% o the said amount of Rs.138 lakhs claimed as provision for the last two quarters, shall be considered as the provision pertaining to such third quarter. Hence, excluding an amount of Rs.69 lakhs out of such amount of Rs.262.42 lakhs, the balance amount is allowable as deduction in this case. Thus, out of such disallowance of Rs.2,62,42,012/- towards provision of CISF security expenses made in the assessment, disallowance to the extent of Rs.69,00,000/- is confirmed and the balance amount is deleted. "*

8. As for the other disallowances, disputed in the first appeal before him, of Rs.1,69,73,787/- on account of excess claim made for weighted deduction under S.35(2AB) of the Act, and the disallowance of Rs.10,64,l00,000/- towards provision

for wage revision arrears, the CIT(A) confirmed the disallowances made by the assessing officer, rejecting the grounds of the assessee in that behalf, and in that process ultimately partly allowed the appeal of the assessee before him.

9. Aggrieved by the relief granted by the CIT(A) the assessee preferred the present appeal before us and has raised the following grounds of appeal:

> "*The order of the CIT(A) in so far as it is prejudicial to the interests of the appellant, is against law, weight of evidence and probabilities of the case.*
>
> *Security Expenses*
>
> *a) The learned CIT(A) erred in confirming an addition of Rs. 69,00,000/- out of expenditure incurred for deployment of security personnel jointly with NFC. He ought to have allowed the full amount on accrual basis.*
>
> *b) The learned CIT(A) failed to appreciate that accrual of liability on this account for the third quarter did not depend on receipt of invoice from NFC, especially when the decision of this Hon'ble "B" Bench for the assessment year 2004-05 in ITA No. 1056/Hyd/08 specifically upheld the claim of the appellant on accrual basis.*
>
> *Weighted deduction u/s 35(2AB)*
>
> *a) The learned CIT(A) erred in confirming the disallowance of claim u/s 35(2AB) for a sum of Rs. 1,69,73,987/-. He ought to have allowed the claim fully.*
>
> *b) The learned CIT(A) failed to appreciate that the weighted deduction available in terms of section 35(2AB) is in respect of the expenditure incurred on in-house research and development facility and that Form No. 3CM does not specify the amount of expenditure to be allowed. Nor the provisions of section 352AB) restrict the claim in such manner.*
>
> *c) The learned CIT(A) failed to appreciate the arithmetical error committed by the DSIR while issuing Form No.*

3CL and consequently erred in confirming the disallowance.

Wage Revision arrears

a) *The learned CIT(A) in confirming the disallowance of arrears of wage revision despite the fact that such provision was made in tune with similar claim allowed by the Hon'ble Tribunal in the case of NMDC.*
b) *For the above grounds and such other grounds that may be urged at the time of hearing, the appellant prays that the appeal be allowed.*
c) *The appellant craves leave to add to, amend or modify the above grounds of appeal either before or at the time of hearing of the appeal, it if is considered necessary.*

10. We have heard the arguments of both the parties, perused the record and gone through the orders of the authorities below. We are of the opinion that the liability to share the expenses for the security provided by NFC is an accrued liability. In fact, NFC had raised bills and assessee paid for the same for the first two quarters for the relevant previous year but for the last two quarters, for whatever reason, the NFC has not raised bills and assessee therefore had to make a provision for the said expenditure. Similar expenditure has been claimed and allowed by the ITAT in assessee's own case for the AY 2003-04. The Tribunal in ITA 1056//08 dt.10.10.09 has held considering the various correspondence that the liability of ECIL to pay its dues on account of security expenses to NFC definitely accrued during the AY 2003-04 relevant to the AY 2004-05.

11. The Tribunal, following the decision of the Apex Court in case of Bharath Earth Movers Ltd 245 ITR 428 upheld the claim of the assessee that the liability to pay security expenses

to NFC accrued during the financial year and it was not contingent upon any other happening. Hence, the ITAT had allowed the claim of the assessee towards their share of security expenses. As held by the Tribunal in the assessee's own case for the assessment year 2004-05 the liability to pay their share to the security expenses to NFC is a defined and accrued liability. The mere fact that it was not quantified during the year by way of raising of bills by NFC could not alter the fact that such liability even though on an estimated basis is an accrued and allowable liability. The Supreme Court in the case of Rotor Control Pvt Ltd vs CIT 314 ITR 62 had held that a provision made for warranty expenses, even though will be actually expended at a later point of time, is an allowable expenditure in the year of sale of product for which such warranty has been given. Similarly, the Apex Court in the case of Bharat Earth Movers Ltd 245 ITR 428 has held that once a liability has accrued, then even if such liability can be quantified and settled only at future point of time, is allowable deduction in the year in which the liability has accrued. In the present case there is no dispute that the liability to share the expenses for security provided by NFC has accrued and pertains to the year under appeal. Therefore, the estimated liability for such expenses provided for in the books of accounts by the assessee is an allowable expenditure in view of the decision of Apex Court as cited above as well as the decisions of the Tribunal in the assessee's own case for the assessment year 2004-05.

12. In the circumstances the appeal of the Assessee regarding disallowance of Rs.69 lakhs out of the provision made for their share of security expenses is allowed.

13. With respect to the issue of Weighted deduction u/s.35(2AB), the assessee had claimed a deduction of Rs.48,58,76,987/- u/s.35(2AB) of the Act. However, the Ministry of Science & Technology, the Department of Scientific and Industrial Research had vide their certificate in form 3CL dt.20.3.09 had approved of Research & Development expenditure of Rs.3,126.02 lakhs as eligible for weighted deduction. Accordingly the AO granted weighted deduction of Rs.4,689.03 lakhs (150% of Rs.3,126.02 lakhs). Therefore, he disallowed the excess claim of deduction made by the Assessee to the extent of Rs.1,69,73,97/-. The Assessing Officer and CIT(A) rejected the claim of the assessee for a higher deduction u/s.35(2AB).

14. Aggrieved the assessee is on appeal before us.

15. It is the contention of the assessee that the DSIR in giving certificate in form 3CL had committed a mistake by excluding certain amount of capital expenditure while at the same time reducing the total amount of expenditure by the grant given by the Government which included the very same capital expenditure which was not taken into account in determining the R&D expenditure. According to assessee this would amount to double deduction and hence it is a prima facie mistake in the certificate given by DSIR Therefore the

Assessee submitted that their entire claim of Rs.48,58,76,987 u/s.35(2AB) should be granted.

16. Section 35(2AB) reads as under:

1. Where a company engaged in the business of ["bio-technology or in any business of manufacture or production of any article or thing, not being an article or thing specified in the list of the Eleventh Schedule] incurs any expenditure on scientific research (not being expenditure in the nature of cost of any land or building) on in-house research and development facility as approved by the prescribed authority, then, there shall be allowed a deduction of [a sum equal to [two] times of the expenditure] so incurred.

[Explanation – For the purposes of this clause, "expenditure on scientific research", in relation to drugs and pharmaceuticals, shall include expenditure incurred on clinical drug trial, obtaining approval from any regulatory authority under any Central, State or Provincial Act and filing an application for a patent under the Patents Act, 1970 (39 of 1970).]

2. No deduction shall be allowed in respect of the expenditure mentioned in clause(I0 under any other provision of this Act.

3. No company shall be entitled for deduction under clause (I) unless it enters into an agreement with the prescribed authority for co-operation in such research and development facility and for audit of the accounts maintained for that facility.

4. The prescribed authority shall submit its report in relation to the approval of the said facility to the Director General in such form and within such time as may be prescribed.]

5. No deduction shall be allowed in respect of the expenditure referred to in clause (I) which is incurred after the 31st day of March.[2012].

6. No deduction shall be allowed to a company approved under sub-clause © of clause (iia) of sub-section (1) in respect of the expenditure referred to in clause (I) which is incurred after the 31st day of March, 2008.

17. As per the provisions of sec 35(2AB) of Act as applicable to the relevant Assessment year , the expenditure incurred by the assessee in any approved in-house research facility, to the extent of approved by the prescribed authority, is entitled to weighted deduction of 150% of such approved expenditure. Therefore, the expenditure as approved by the DSIR in the certificate given by them in Form 3CL alone is to be granted weighted deduction. The DSIR in their certificate has certified expenditure eligible for weighted deduction as Rs.3,126.02 lakhs. Therefore, it is not for either the assessing authority or the appellate authority to decide on the expenditure which will be entitled to weighted deduction u/s.35(2AB). In fact, U/s.35(2AB)(3) if any question arises u/s.35 as to whether and if so, what extent any activities constitutes or constituted or any asset was used for scientific research, the matter should be referred to the appropriate authority whose decision will be final. In this case the appropriate Authority is the DSIR. Therefore once the DSIR has certified the quantum of eligible R&D expenditure for the purposes of weighted deduction u/s 35(2AB) the figure cannot be tampered with by ITAT. Even if the assessee is right in that the there is a mistake in the certificate issued by the DSIR, which we don't know, the same can only be rectified by DSIR and not the ITAT in appellate proceedings. We, therefore, uphold the decision of lower authorities in restricting the weighted deduction u/s.35(2AB)

to Rs.46,89,03 lakhs and disallowing sum of Rs.1,69,73,987 out of the claim made by the assessee. We, however, direct that in case DSIR corrects the amount of research and development expenditure on which the assessee is entitled weighted deduction for the assessment year under appeal, corresponding weighted deduction u/s.35(2AB) shall be granted on receipt of the clarification from DSIR. Consequentially if the assessee is able to prove that any amount of expenditure in their in-house research and development facilities was omitted to be considered by the DSIR for weighted deduction the same may be allowed as a deduction u/s.35/ 37 of the Act. With this observation we dismiss the appeal of the assessee on this issue.

18. With respect to the Provision for Wage revision , the Assessing Officer and the CIT(A) disallowed Rs.10.64 Crores towards provision for wage revision arrears. From the facts furnished to us the assessee entered into wage agreement for a period of 10 years from 1.1.97 to 31.12.2006. Therefore the due date for revision of wages and salaries were from 1.1.07. The workmen had submitted their charter of demands on 30.6.06 during the previous year relevant assessment year under appeal. Even though final memorandum of settlement was reached on 24.9.09 the increase in salary was effective from 1.1.07. The enhanced salary is an accrued and crystallized liability from 1.1.07 to 31.3.07. Merely because the same was quantified later would not alter the fact that the amount is a crystallized liability. As held by the Apex Court in the case of Bharat Earth Movers Ltd vs. CIT 245 ITR 428 and Rotor Control India Pvt Ltd 314 ITR 62 and the accounting

standard issued by the CBDT u/s.145 any liability which has accrued during any financial year is to be allowed in that year notwithstanding the fact that the actual quantification and settlement of the liability is made at a later point of time.

19. In fact, in the case of Bharat Earth Movers Ltd, the company had made provision for leave salary which had accrued every year. The Apex Court held that such liability is a allowable deduction notwithstanding the fact that an employee may avail of the leave and hence will not be entitled to any amount towards leave salary. It will not alter the accrual and allowability of liability in the year in which it accrued.

20. The Tribunal in the case of National Mineral Development Corporation Ltd in ITA 12,705/H/02 and ITA 1035/H/103 for assessment year 2000-01 dt.11.7.05 has held as under:

> "*It is an undisputed legal principle that salary and wages accrue either daily, weekly, fortnightly or monthly as per the contract of appointment. This is so as service is rendered in praesenti. As soon as the service i9s rendered right to compensation for the service rendered accrues. However, the right to receive the payment arise as per the contract of employment. Also for the employer liability to compensate the employees for the service rendered accrues in praesenti. Such services have been incurred for earning the income which the employer reflects in his accounts. In the present case the right to receive compensation for the services rendered by the employees arise out of the contract on employment. The contract of employment in the instant case is not in dispute. What is in dispute is quantification of compensation. In this case the charter of demands by the employees covered under IDA scheme for salary was available as early as 1.1.97. for these employees the revised wages/salary was to be given w.e.f. 1.1.97.*

Thus, it can be said that the appellant was reasonably certain of its increased liability on this account. As the Personnel Department of the appellant had knowledge of dealing with suh pay hikes in the past, the assessee could estimate the quantum of such enhanced liability. The liability was certain. What was not certain is the quantum of such liability. Also, the entries taken in the books of account towards provision of enhanced salary/wages cannot be said to be unilateral entry made by the appellant. The appellant accepted its liability to the extent provision was made in the books of account based on the demands from its employees. It may also be noted that the accounting standards were also made part of the Act. Taking into account principle of prudence and the definition of accrual as given therein, as also the principle of real income, we are of the opinion that in the facts of the present case, the provision made towards additional liability on account of enhanced wages and salary are allowable in the year of making such provision. In this view of the matter, this ground of the assessee is allowed."

21. The CIT(A) has referred to the decision in the assessee's own case in ITA 875/H/06 dt.9.5.08 for the AY 2003-04. We find that the issue on appeal for that year is allowability of the provision of Rs.82,57,45,377 being arrears payable on account of pay/wage revision referable to earlier years, i.e. from 1.1.97. In that case, the Tribunal concluded that the provision for arrears arising on account of wage revision relating to the earlier years is not an admissible deduction for the AY 2003-04 because the assessee did not obtain the approval of the competent authority and hence the provision made was merely a contingent liability. However, in the instant case the provision made is for the year under appeal itself and not arrears relating to earlier years and hence distinguishable on facts. Therefore the provision made by the assessee for estimated liability of provision of wages for the period 1.1.07

to 31.3.07 applying the ratio of the Apex Court in the case of Bharat Earth Movers Ltd and Rotor Control India Pvt Ltd (supra) is an allowable deduction.

22. Accordingly we allow the appeal of the assessee on this issue.

ITA 895/H/11 - revenue's appeal:

23. The effective grounds of the Revenue in this appeal read as follows-

"1) The learned CIT(A) ought to have upheld the order of Assessing officer.

2) The learned CIT(A) erred in law.

3) The learned CIT(A) ought not to have restricted the disallowance of security expenses to Rs.69,00,000/- on estimate basis having confirmed the disallowance made by the A.O. towards weighted deduction u/s. 35(2AB) of the Act. "

24. Thus, the only effective grievance of the Revenue in this appeal relates to the relief granted by the CIT(A) in the matter of the assessee's claim for security expenses.

25. The facts relating to this ground is identical with a similar ground raised by the Assessee in their appeal in ITA No 1106/Hyd/2011 and are dealt with in that appeal supra. The security for the Assessee's facilities was provided by Nuclear Fuel Complex (NFC) which is a unit of DAE is located adjacent to ECIL's manufacturing and other facilities. It has been agreed between the Assessee and NFC that the latter will charge 32% of total cost incurred by NFC for CISF personnel,

as Assessee's share of security expenses. Accordingly the Assessee claimed Rs.2,62,42,012 as their share of security expenses. The Assessing Officer rejected the same on the grounds that it is only contingent expenditure. On appeal, it was submitted before the CIT(A) that the provision of Rs.2,62,42,012 relates to the share of security charges for the previous year relevant to the Assessment Year 2007-08 only. The CIT(A) found that NFC had raised bills towards ECIL's share of security expenses on provision of CISF personnel for the first two quarters of the FY 2006-07 and the assessee had made necessary payments. However, for the last two quarters the assessee had not received the bills before 31.3.07. CIT(A) found that the provision made for the last two quarters amounted to Rs.138 lakhs and on adhoc basis disallowed Rs.69 lakhs i.e. out of the claim of Rs.2,62,42,012 the CIT(A) had restricted the disallowance to Rs.69 lakhs.

26. Aggrieved the revenue is on appeal.

27. As held by us in the assessee's appeal(supra) the liability to share the expenses for the security provided by NFC is an accrued liability. Hence we held that the entire amount of Rs.2,62,42,012 claimed by the Assessee is an allowable expenditure. In line with our decision in the Assessee's appeal on this issue, the appeal of the revenue regarding disallowance of Rs.69 lakhs out of the provision made for security expenses is dismissed.

28. In the result, appeal of the assessee is allowed and the appeal of the revenue is dismissed.

Order pronounced in the court on 25/09/2012.

Sd/-	Sd/-
(CHANDRA POOJARI)	**(ASHA VIJAYARAGHAVAN)**
Judicial Member.	**Accountant Member.**

Hyderabad, Dt/- 25th September, 2012

Copy forwarded to:

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4. Commissioner of Income-tax II, Hyderabad
5. Departmental Representative ITAT, Hyderabad

B.V.S./KV