No disallowance of foreign travel exp. of partners who travelled to Countries from which sizeable business generated

Summary – The Mumbai ITAT in a recent case of Allied Gems Corporation (Bombay)., (the Assessee) held that where assessee was following mercantile system of accounting, it was justified in claiming loss incurred on account of short realisation of export proceeds at end of relevant year even though realisation of said proceeds took place in subsequent assessment year

Expenditure incurred by partners of assessee-firm on foreign travel to countries from which substantial business was generated, was to allowed as deduction under section 37(1)

Facts

- The assessee was a partnership firm engaged in the business of dealing in cut & polished diamonds. In the course of assessment proceedings, assessee claimed a loss of Rs. 49.64 lakhs on account of realization of export proceeds, which was outstanding at the end of relevant year *i.e.* 31-3-2009.
- The Assessing Officer disallowed said claim of loss on the ground that the realization of outstanding export receivables was an event which took place in the subsequent assessment year and, therefore, such loss could not be allowed while computing the income for the relevant assessment year.
- The Commissioner (Appeals) noted that the Assessing Officer had not doubted the short realization of the debtors and, hence, it could not be said that it was an improper claim. The Commissioner (Appeals), thus, allowed assessee's claim.
- On revenue's appeal:

Held

- It is quite well understood that section 4, charges tax in respect of the total income of a previous year relevant to the concerned assessment year. Section 5, prescribes the scope of total income and so far as instant case is concerned, the dispute relates to the income chargeable under the head 'profits and gains of business or profession'; which is liable to be computed in accordance with the methodology prescribed in section 145(1) *i.e.* either in terms of cash or mercantile system of accounting regularly employed by the assessee. Sub-section (2) of section 145 empowers the Central Government to notify Accounting Standards for any class of assessees or in respect of any class of income.
- In the present case, assessee firm has maintained its accounts on mercantile system and while computing income for the year under consideration, it claimed deduction for a sum representing loss on short realization of export proceeds, which were outstanding as on 31-3-2009, of course,

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short realization having taken place in the subsequent period. The claim of the assessee is that the mercantile system of accounting adopted by the assessee justifies such adjustment and for that matter, reference is made to the principle of prudence, which has been emphasized in the Accounting Standard -1 notified under section 145(2)

- The principle of prudence seeks to ensure that provision ought to be made for all known liabilities and losses even though there may remain some uncertainty with its determination. So however, it has to be appreciated that what the principle of prudence signifies is that the probable losses should be immediately recognized. In the present context, the stand of the assessee is that though realization of export receivables took place in the subsequent period, but the loss could be accounted for in the instant year itself as it would be prudent in order to reflect the correct financial results.
- Factually speaking, revenue did not dispute the short realization from debtors to the extent of Rs. 49.64 lakhs and, therefore, insofar as the quantification of the loss was concerned, the claim of the assessee could not be assailed on grounds of uncertainty. Therefore, assessee was justified in determination of such loss on the basis of actual figures which were available while assessing its income in the instant assessment year.
- In the present case, short realization of export proceeds to the extent of Rs. 49,64,937/-, took place in next year but it related to export receivable for the instant year, and at the time of finalization of accounts for the instant year, the actual figure was available, and therefore, assessee made no mistake in considering it for the purposes of arriving at the taxable income.
- Even otherwise, it has to be appreciated that tax is a levy on income and that what is liable to be assessed is real income and while computing such real income, substance of the matter ought to be appreciated. Quite clearly, the assessee was aware while drawing up its accounts for the previous year relevant to the assessment year under consideration that the export receivables, outstanding as at the year-end were short recovered by a sum of Rs. 49,64,937/- and, therefore, the real income for the instant year could only be deduced after deduction of such loss. Therefore, considering the entirety of facts and circumstances, the Commissioner (Appeals) made no mistake in allowing the claim of the assessee.
- In the result, revenue's appeal is dismissed.

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