

## **Compensation paid to family on death of freelance sea divers in marine accident was business exp.**

**Summary – The Mumbai ITAT in a recent case of Adsun Offshore Diving Contractors (P.) Ltd., (the Assessee) held that where freelance divers of assessee-company died in ship accident and their family members threatened to file suit and assessee paid compensation, same was to be allowed as business expenditure**

### **Facts**

- The assessee-company was engaged in business of sub-sea diving, job work and equipment hiring. It was executing the work of diving support services for its AE on a ship in international water. Due to bad weather, an accident occurred where ship sunk and the freelance divers of assessee died.
- Assessee with the help of UAE company paid a certain sum immediately to the families of these divers and the said expenditure was debited to 'Compensation for Accident' under Project Expenses.
- The Assessing Officer declined to allow expenditure as business expenditure on ground that there was no specific clause in the agreement entered into by the assessee with the said freelance divers for providing compensation in the event of damages of loss of life in a marine accident and, that it was liability of other company.
- Family members of divers had threatened to file suit in international court.
- The Commissioner deleted the disallowance observing that since the expenditure was incurred by the assessee with an intention to protect its business interest, it was purely a commercial decision to avoid further litigation in the international court where the legal cost must have exceeded the compensation paid.
- On appeal:

### **Held**

- Expenses incurred was in the course of business, and in order to safeguard the business interest and avoid unwanted litigation and decision to settle the matter and pay compensation was a commercial decision taken by the company to safeguard the business interest of the assessee. It was with view to maintain co-ordial relations and goodwill amongst freelance divers who were regularly being employed by assessee for execution of the sub-sea projects. Without the support of these freelance divers, it would not be possible for the assessee to execute contracts it signs up and honour its commercial commitments. Hence, as a need of the business to maintain good relations and gain the confidence amongst diving community.
- The remark of the Assessing Officer that 'liability of some other company' was taken up by assessee, which is not the fact. Assessing Officer did not realise that entire compensation amount was a liability of assessee and even then only small amount was claimed as expenditure. The contract with divers was entered into by the assessee-company. And another aspect that the Assessing Officer

disallowed the said compensation paid for accident treating it as 'application of income' of the assessee. As can be observed from the facts narrated above, the said expenditure was a genuine business expenditure of the assessee and it never formed part of the income of the assessee. Income is to be arrived at after deducting business expenditure from the gross revenue earned by the business. Hence, this payout never formed part of the income and was not the "application of the income" as treated by the Assessing Officer. The concept of application of income is wrongly invoked by the Assessing Officer. There is no diversion of income as alleged by Assessing Officer.

- Whatever test may be applied in deciding whether any expenditure is allowable as a deduction under section 37, the essential requirement must in every case be as to whether the expenditure was either in reality or as a measure of business expediency necessary for the purpose of earning profit or for protecting and safeguarding the business assets of the assessee including goodwill or in connection with some transaction or activity which is directly and substantially connected with the running of the business of the assessee or is intimately connected with the assessee business activities. Such expense must necessarily pertain to the business itself and must not be an expenditure merely connected with any activity, however remote or ancillary. It has to be shown in every case that not only the expenditure was wholly and exclusively laid out, but it was so laid out for the purpose of the business of the assessee, that is, some purpose directly connected with or attributable to the assessee normal business activities or the protection of its business interest. In the instant case the expenses incurred in connection with the accident occurred in course of the business where 7 lives of divers were lost, expenditure incurred was wholly and exclusively for the purpose of the company's business. In view of the above legal and factual position, compensation paid by the assessee to the family members of deceased divers being in course of the assessee business, and the assessee had rightly considered the business expediency and thereafter incurred the said legitimate business expenses. Accordingly, the order of Commissioner (Appeals) and dismiss the appeal of the revenue.