

# CALCUTTA HIGH COURT

Commissioner of Income Tax

Vs

Hindustan Motors Ltd

(Sahas Chandra Sen, J.)

07.06.1994

## JUDGEMENT

**Sahas Chandra Sen, J.:**

( 1. ) The Tribunal has referred the following question of law under s. 256(2) of the IT Act, 1961, to this Court : "Whether, on the facts and in the circumstances of the case, the Tribunal was right in fact and in law in holding that the provision for leave pay liability should be treated as 'reserve' for the purpose of computation of capital under the provisions of the Companies (Profits) Surtax Act, 1964 ?"

( 2. ) THE assessment years involved are 1982-83, 1983-84 and 1984-85, for which the corresponding previous years were the financial years 1981-82, 1982-83 and 1983-84. The facts as stated by the Tribunal in the statement of facts were as under: The AO in the course of assessment, while computing "capital" relevant to the respective surtax assessment, did not consider leave pay liability as "reserve" inasmuch as this liability was provided for meeting a known liability arising in future and, as such, it was only a provision and not a reserve. Being aggrieved, the assessee went up in appeal before the CIT (A), and urged that in income- tax assessment, provision for leave salary was disallowed on the ground that the liability concerned was of the nature of contingent liability and could not be considered to have arisen exactly. Therefore, in surtax assessment, the amount representing such liability should be treated as reserve. The assessee in support of the contention relied on the decision of the Supreme Court in the case of *CIT vs. Saran Engineering Co. Ltd*<sup>1</sup>.

( 3. ) THE CIT (A), however, to arrive at the distinction between "provision" and "reserve", relied on the decisions of the Supreme Court in the case of *Vazir Sultan Tobacco Co. Ltd. vs. CIT*<sup>2</sup> *Metal Box Co. of India Ltd. vs. Their Workmen*<sup>3</sup> and *CIT vs. Elgin Mills Ltd*<sup>4</sup>. and viewed that the Court held that whereas a "provision" is a charge against the profits to be taken into account against gross receipts in the P&L a/c, a "reserve" is an appropriation of profits, the asset or assets by which it is represented being retained to form part of the capital employed in the

business. The Court also held that merely because a particular liability is not a provision that would not make it a "reserve" automatically. But in the present case, the liability has been anticipated legitimately by the assessee and a fund to meet such liability cannot be treated as reserve. The liability has been created by making a debit to the operating (sic) account and not by way of appropriation or charge on the profits. Thus, the CIT (A) confirmed the order of the AO. ;

#### Cases Referred.

1(1986) 161 ITR 741 (SC)

2(1981) 132 ITR 559 (SC)

3(1969) 73 ITR 53

4(1986) 161 ITR 733 (SC)