



Mum ITAT: OCI-Based Notional Actuarial Gain On Gratuity Not 'Income'

Facts

The assessee filed return of income declaring loss. The return was processed u/s 143(1) and an addition in respect of mismatch in the tax audit report (TAR) and return of income was made. The mismatch was on account of notional gain on the valuation of gratuity, which was credited to the Profit & Loss account (below the net profit before tax) under the head other comprehensive income (OCI). However, the tax auditor reported the notional amount of gratuity under clause 16d of the TAR. The assessee preferred an appeal before the CIT(A).

The CIT(A) dismissed the assessee's appeal and noted that the assessee in the earlier year has considered and offered the reversal of gratuity provision for the purpose of MAT Liability u/s.115JB. Furthermore, the same was also disclosed under the heading 'Amount not credited to Profit & Loss account-any other item of income'.

Consequently, the assessee preferred an appeal before the Hon. ITAT.

Contentions of the assessee

The Ld. AR submitted that, the addition was merely a notional gain on account of actuarial valuation of gratuity routed through "other Comprehensive income" which was shown below the net profit before tax. Accordingly, it had no impact on the computation of income since the starting point for computation of income under the head profit and gains from business and profession is net profit before tax.

As per section 43B of the Act the assessee had claimed deduction of gratuity on actual payment. No deduction of the gratuity provision was claimed in earlier years.

Even in the earlier years, upon increase in the provision of gratuity under OCI, the assessee had not claimed any deduction despite the fact that the same was paid to the gratuity fund. Therefore, upon the reversal of the provision in OCI, the same ought not be taxable.

Observations of the Hon. ITAT

The ITAT noted that on perusal of AS-19, the changes to actuarial valuation could be because of changes in the assumption for such valuation like average age of the employees, period of service etc and is show OCI. The ITAT also noted that the OCI did not impact the real income of the assessee. In any event, the assessee had claimed deduction on payment basis only, thus, any increase or decrease in the amount of gratuity as per actuarial valuation, which is not routed through P&L A/c, cannot have any impact on the taxable income. Accordingly, the addition of notional gain in valuation of OCI was deleted.

Citation

Reliance Commercial Dealers Limited [TS-1560-ITAT-2025(Mum)]

**Our Comments**

The employee benefit (gratuity) made in accordance with the INDAS classified as OCI is notional and is not debited to profit & loss account (above profit before tax). Being a notional gain, it can never assume the character of income just as notional loss can never be claimed as deductible. The adjustments under OCI are notional in nature, arising out of valuation assumptions and therefore do not, even in accounting parlance, impact the operational results of the year.

So far as gratuity is concerned, for tax purposes, deduction is allowed for actual amount of gratuity paid to employees or provision for contribution payable to an approved gratuity fund, subject to such payment being made within the time provided for in section 43B. Debit for such liability is to the P&L Account itself unlike notional valuation changes in liability which are mandated to be routed through OCI. Such notional gains, not being income chargeable to tax, should not be reported in the tax audit report under the head 'Income not credited to P & L account' else it will give the tax department a handle to bring the same to tax, as was done in this case.