

Court No. - 35**Case :-** INCOME TAX APPEAL No. - 168 of 2011**Appellant :-** The Commissioner Of Income Tax Muzaffarnagar And Another**Respondent :-** Muzaffarnagar District Co-Operative Bank Ltd.**Counsel for Appellant :-** S.S.C. I.T., Krishna Agrawal, Subham Agarwal**Counsel for Respondent :-** Ashish Agarwal**Hon'ble Bharati Sapru,J.****Hon'ble Saumitra Dayal Singh,J.**

Heard Sri Subham Agarwal, learned counsel for the department.

This appeal has been filed against the order of the Income Tax Appellate Tribunal for the assessment year 2007-08 in case of assessee a district cooperative bank engaged amongst others in granting advances in rural areas. Learned counsel for the appellant has raised two substantial questions of law quoted as below:-

"(1) Whether on the facts and in the circumstances of the case, the Tribunal is justified in law in confirming the order of the CIT (A) deleting the disallowance of bad debts of Rs. 2,84,42,000/- claimed by the assessee by completely ignoring the fact that the assessee had not credited the amount of bad debt in the individual account of the debtors?"

"(2) Whether on the facts and in the circumstances of the case, the Tribunal is justified in law in confirming the order of the CIT (A) agreeing in principle that exemption u/s 10 (34) of the Act is available to the assessee in respect of dividend income of Rs. 20,03,000/- despite the admitted fact that the assessee had neither claimed exemption of dividend income u/s 10 (34) of the Act in its return of income nor at the time of assessment proceedings and this dividend income was not even reflected in the profit & loss account submitted/filed by the assessee alongwith its return of income?"

During the assessment proceedings, the Assessing Authority disallowed the provision on account of bad debts -

Rs. 2,84,42,000/- under clause (vii) of Section 36(1) of the Income Tax Act, 1961 (hereinafter referred as to the Act). Also, in view of the fact that the assessee had himself offered to tax dividend income of Rs. 20,03,000/-, the Assessing Officer proceeded to tax the same.

In first appeal from assessment, besides disputing the disallowance made under Section 36(1)(vii), the assessee raised an additional ground to question the action of Assessing Officer to tax dividend income.

The first appellate authority vide his order dated 07.07.2010 allowed the appeal on both counts. In respect of disallowance of bad debts he found that the assessee being a District Cooperative Bank having made advances in rural areas, provisions of clause (viiia) of Section 36(1) were applicable and it was therefore entitled to the allowance on account of 'provision' of bad debts without actually writing off such a bad debt.

As to the second aspect, the first appellate authority found that the amount of Rs. 20,03,000/- was dividend income received in the hands of the assessee and therefore prima facie, it was exempt from tax. At the same time, since there was no evidence to establish that the same had been subjected to tax in the hands of the company, the CIT remitted the matter to the Assessing Officer to verify that factual aspect.

Being aggrieved, the department preferred an appeal before the Tribunal. The Tribunal took note of the provisions of Section 36(1)(viiia) and found that under the said provision

to allow an expenditure it is not the requirement that the bad debt should be actually written off by the assessee. Thus, in view of the Tribunal, such allowance could be claimed and allowed even upon a provision being made for that purpose by the assessee as it was a district cooperative bank that had made advances in rural areas.

Disputing the correctness of the finding recorded by the Tribunal, learned counsel for the department submits, that proviso to Section 36(1)(vii) mandates that the debts should actually be written off before allowance be claimed on that count.

This issue has been specifically considered in the decision of the Supreme Court in ***Catholic Syrian Bank Vs. Commissioner of Income Tax*** reported in ***(2012) 248 CTR (SC) 1*** wherein, in similar circumstance, the Supreme Court considered the provision of Section 36(1)(vii) and 36(1)(viiia). It was thereafter held that for the purpose of sub-section (viiia) which applied to district cooperative bank that had made rural advances, it is not a requirement of law that the debt should have been written off before an allowance could be made. It was thus held that in such cases even it appears that an allowance has been made to write off a bad debt the assessee could claim such expenditure. In paragraph 25 of that judgment, it was held as below:-

"25. The language of Section 36(1)(vii) of the Act is unambiguous and does not admit of two interpretations. It applies to all banks, commercial or rural, scheduled or unscheduled. It gives a benefit to the assessee to claim a deduction on any bad debt or part thereof, which is written off as irrecoverable in the accounts of the assessee for the previous year. This benefit is subject only to Section 36(2) of the Act. It is obligatory upon the assessee to prove to

the assessing officer that the case satisfies the ingredients of Section 36(1)(vii) on the one hand and that it satisfies the requirements stated in Section 36(2) of the Act on the other.

The proviso to Section 36(1)(vii) does not, in absolute terms, control the application of this provision as it comes into operation only when the case of the assessee is one which falls squarely under Section 36(1)(viiia) of the Act. We may also notice that the explanation to Section 36(1)(vii), introduced by the Finance Act, 2001, has to be examined in conjunction with the principal section. The explanation specifically excluded any provision for bad and doubtful debts made in the account of the assessee from the ambit and scope of 'any bad debt, or part thereof, written off as irrecoverable in the accounts of the assessee'. Thus, the concept of making a provision for bad and doubtful debts will fall outside the scope of Section 36(1)(vii) simplicitor. The proviso, as already noticed, will have to be read with the provisions of Section 36(1)(viiia) of the Act. Once the bad debt is actually written off as irrecoverable and the requirements of Section 36(2) satisfied, then, it will not be permissible to deny such deduction on the apprehension of double deduction under the provisions of Section 36(1)(viiia) and proviso to Section 36(1)(vii). This does not appear to be the intention of the framers of law. The scheduled and non-scheduled commercial banks would continue to get the full benefit of write off of the irrecoverable debts under Section 36(1)(vii) in addition to the benefit of deduction of bad and doubtful debts under Section 36(1)(viiia).

Mere provision for bad and doubtful debts may not be allowable, but in the case of a rural advance, the same, in terms of Section 36(1)(viiia)(a), may be allowable without insisting on an actual write off."

That being the position in law, the argument raised by learned counsel for the department cannot be accepted and the question is therefore to be answered in favour of the assessee and against the revenue.

As to the second question raised in the appeal we find that the Tribunal CIT has not allowed the claim of the assessee but has only settled the principle that to be applied. The department does not dispute that the source of income of Rs. 20,03,000/- was dividend income received by the

assessee. Principally, therefore the amount was exempted. Merely because, the assessee did not claim that exemption at the time of filing of the return could not make the said receipt taxable in nature. This Court in the case of ***Commissioner of Income Tax Vs. Lucknow Public Educational Society*** reported in ***(2010) 231 CTR (All) 407*** had in similar circumstance followed the principle that the department should not take advantage of the ignorance of the assessee.

In so far as it is not disputed to the department that the assessee received Rs. 2,03,000/- as dividend income, it cannot be said that the same would become taxable at the hands of the assessee. It was also open to the Assessing Officer to have examined the correct aspect himself and to grant the benefit, if the said amount was not taxable.

Merely because the assessee did not raise the claim at the time of his assessment it did not stop him from raising the claim before first appellate authority. In that regard it is not disputed that as a fact an additional ground was raised in the first appeal and that was allowed. Even at present, the department had been required to verify the correctness of the claim and to grant benefit to the assessee if the claim is found to be verified.

In view of the above, the second question is also answered in favour of the assessee and against the revenue. Accordingly, the instant appeal lacks merit and is **dismissed**. No order as to costs.

Order Date :- 21.11.2017
A. Singh