

IN THE HIGH COURT OF KARNATAKA AT BENGALURU

DATED THIS THE 19TH DAY OF JUNE 2020

PRESENT

THE HON'BLE MR. JUSTICE ALOK ARADHE

AND

THE HON'BLE MR. JUSTICE M.NAGAPRASANNA

I.T.A. NO.555 OF 2018

BETWEEN:

M/S. HAJEE A.P. BAVA AND COMPANY
CONSTRUCTIONS PVT. LTD.
HAPBCO TOWER, #32, 9TH MAIN ROAD
RPC LAYOUT, HAMPINAGAR
VIJAYANAGAR, BENGALURU-560104
PAN: AACCH 1218 C
(REPRESENTED BY ITS VICE PRESIDENT
FINANCE, MR. SUNDARAM VENKATARAMAN
AGED ABOUT 49 YEARS
S/O M. VENKATARAMAN)

... APPELLANT

(BY SRI. CHYTHANYA K.K. ADV.,)

AND:

THE ASSISTANT COMMISSIONER OF INCOME TAX
CIRCLE - 3(1)(2), ROOM NO.228
2ND FLOOR, BMTc BUILDING
80 FT. ROAD, 6TH BLOCK
KORAMANGALA, BANGALORE-560095.

... RESPONDENT

(BY SRI. K.V. ARAVIND, ADV.,)

THIS ITA IS FILED UNDER SECTION 260-A OF I.T. ACT,
1961, ARISING OUT OF ORDER DATED 20/04/2018 PASSED IN ITA

NO.2153/BANG/2017, FOR THE ASSESSMENT YEAR 2014-15, PRAYING TO:

(I) FORMULATE THE SUBSTANTIAL QUESTION OF LAW STATED ABOVE.

(II) ALLOW THE APPEAL AND SET ASIDE THE IMPUGNED ORDER OF THE INCOME TAX APPELLATE TRIBUNAL, BENGALURU 'A' BENCH, BEARING IN ITA NO.2153/BANG/2017 FOR THE AY 2014-15, AS ENCLOSED IN ANNEXURE-A & ETC.

THIS ITA COMING ON FOR ORDERS, THIS DAY, ALOK ARADHE J., DELIVERED THE FOLLOWING:

JUDGMENT

This appeal under Section 260A of the Income Tax Act, 1961 (hereinafter referred to as the Act for short) has been preferred by the assessee. The subject matter of the appeal pertains to the Assessment year 2014-15. The appeal was admitted by a bench of this Court vide order dated 20.11.2018 on the following substantial questions of law:

- (i) *Whether in the facts and circumstances of the case, the tribunal is right in law in upholding disallowance of the bad debts written off under Section-36(1)(vii) of IT Act read with Section-36(2)?*
- (ii) *Whether, in the facts and circumstances of the case, is not the finding of the*

Tribunal that the relevant income was not offered to tax and there was no subsisting debt perverse?

2. Facts leading to filing of the appeal briefly stated are that the assessee is a private limited company, which is engaged in the business of fabrication, erection, commissioning, maintenance of mechanical plants and machineries. The assessee filed its return of income for the Assessment year 2014-15 by declaring total income of Rs.7,71,76,700/- on 30.11.2014. The assessee filed the revised return of income on 28.11.2015 by declaring total income of Rs.20,83,75,020/-. The original return of the assessee was processed under Section 143(1) of the Act and the case of the appellant was selected for scrutiny. Notices under Section 143(2) of the Act dated 28.08.2015 and under Section 142(1) of the Act were issued. The assessing officer by an order dated 29.11.2016 passed under Section 143(2) of the Act inter alia held that from

perusal of the ledger extracts, it is evident that no credit entry on the account of bad debts has been made in the debtors account during or at the end of financial year 2013-14. It was further held that account has not been squared off and closed at the year end and the assessee continued to have transactions with the debtor in the subsequent financial year also. It was also held that amount claimed in the profit and loss account as bad debts had not actually been written off from the debtors account and has merely been transferred to account making provision for doubtful debts. By placing reliance on decision of the Supreme Court in '**SOUTHERN TECHNOLOGIES LTD., VS. JCIT**', (2010) 320 ITR 577 (SC) and by taking into account explanation to 36(1)(vii) it was held that mere provision for doubtful debts cannot be allowed as deduction and in the instant case the assessee has failed to credit the account of individual debtor and has merely reduced the gross sundry debtor account in the balance sheet which does

not amount to writing off the debt in the assessee's books of account. The assessing officer further held that decision rendered by Supreme Court in case of '**VIJAYA BANK VS. CIT', (2010) 323 ITR 166 (SC)** is not applicable to the in the fact situation of the case as the assessee is a non-banking and non-finance company and the main issue involved in the case of **VIJAYA BANK** supra was the apprehension that if the assessee failed to close each and every individual account of its debtors it might result in assessee claiming deduction twice over whereas, the case of the assessee in the instant case is deferment of tax liability to subsequent years. Accordingly, the bad debts written off to the extent of Rs.11,45,33,140/- were disallowed.

3. The appellant filed an appeal before the Commissioner of Income Tax (Appeals). The Commissioner of Income Tax (Appeals) by an order dated 20.09.2017 inter alia held that assessee has only created a provision for doubtful entry in the books of

accounts and since it is following a double entry system of accounting, corresponding entries have been made in the profit and loss and the balance sheet, without actually writing off the bad debts. Thus, it was held that the claim of assessee for allowing the bad debts is not sustainable. In the result, the appeal was dismissed.

4. Being aggrieved, the assessee filed an appeal before the Income Tax Appellate Tribunal. The tribunal by an order dated 20.04.2018 inter alia held that on mere perusal of the ledger account of the company in books of account extracted in the order of assessment it is clear that opening balance of Rs.8,91,12,550.61/- was shown as due from the debtor and during the course of year under consideration the debtor had debited the account of recoveries made towards statutory levies such as cess, sales tax and TDS recoveries. It was further held that as on the end of the accounting year ending on 31.03.2014 a sum of Rs.3,79,64,917.38/- was debited by passing a journal entry and therefore, it

is not clear whether the aforesaid amount was offered to tax. It was also held that mere wrong entry in the books of account does not constitute debt which can be written off. The aforesaid amounts are not due from the party and are not in the nature of subsisting debt and the requisite condition for allowance as bad debts that the debt should have been offered to tax in the earlier Assessment year is also not satisfied. In the result, the appeal was dismissed. The assessee thereafter filed a miscellaneous petition against the order of the tribunal, which is pending consideration before the tribunal. In the aforesaid factual background, this appeal has been filed.

5. Learned counsel for the assessee submitted that the sole issue which arises for consideration in this appeal is whether the assessee has written off the debt as bad debt as required under Section 36(1)(vii) read with Section 36(2) of the Act. It is further submitted that assessee has debited the amount of doubtful debt

to the profit and loss account and has credited the asset account like sundry debtors account and therefore, has complied with the provisions in Section 36(1)(vii) of the Act. It is further submitted that the assessee has made a provision for bad debt and the debtor is under liquidation and a claim has been made before the official liquidator by the assessee. It is further submitted that it is not necessary for the assessee to demonstrate that it has taken action for recovery of the debt and Section 36(1)(vii) of the Act applies to banking as well as non banking companies. It is also urged that merely on the basis of apprehension that if the assessee failed to close each and every individual account of its debtor, it might result in assessee claiming deduction twice over, the benefit of writing off the debt under Section 36(1)(vii) of the Act cannot be denied to the assessee. It is pointed out that Section 41(4) is incorporated in the statute book to deal with an assessee who may claim the deduction twice over as under the aforesaid provision,

an action for recovery of the amount can be initiated. It is also urged that the finding recorded by the authorities that the assessee has failed to actually write off the debt in the books of accounts is perverse. It is also urged that the revenue has not referred to any material on record to prove that the assessee has abused the provision of law. Alternatively it is submitted that the matter be remitted to the assessing officer for determining the question whether the debt written off during the year in question was offered to income in Previous year. In support of aforesaid submissions, reference has been made only to decisions in cases hereinafter referred even though the compilation contains the list of as many as 36 judgments, viz., **'VIJAYA BANK VS. CIT', (2010) 323 ITR 166 (SC), 'T.R.F. LTD. VS. CIT', (2010) 323 ITR 397 (SC), 'CIT VS. YOKOGAWA INDIA LTD.,', (2012) 17 TAXMANN.COM 15 (KAR), ' CIT VS. KIRLOSKAR SYSTEMS LTD.,', (2013) 220 TAXMAN 1 (KAR), 'CIT**

VS. VODAFONE ESSAR GUJARAT LTD.,', (2017) 397 ITR 55 (GUJ), 'CIT VS. TAINWALA CHEMICALS & PLASTICS INDIA LTD.,', (2013) 215 TAXMAN 153 (BOM.), CIRCULAR NO.516 DATED 15.06.1988.

6. On the other hand, learned counsel for the revenue submitted that assessee is required to make a provision for debiting the amount from the profit and loss account and same has to be reduced from the asset side of the balance sheet. It is also urged that the assessee in the instant case has not complied with the requirement under Section 36(1)(vii) of the Act and the facts that whether or not the debt which was written off during the relevant year was offered to income in previous years and whether the assessee has complied with the requirement of writing off the debt as prescribed in **VIJAYA BANK** supra need to be examined.

7. We have considered the submissions made on both the sides and have perused the record. Section 36(1)(vii) of the Act was amended with effect from 01.04.1989 which is reproduced below for the facility of reference:

36. Other deductions : (1) the deductions provided for in the following clauses shall be allowed in respect of the matters dealt with therein, in computing the income referred to in S.28-

(i) to (vi).....

(vii) subject to the provisions of sub-s,(2), the amount of any bad debt or part thereof which is written off as irrecoverable in the accounts of the assessee for the previous year.

8. Thus, it is evident that after 01.04.1989 it is not necessary for the assessee to establish the fact that the debt in fact had become irrecoverable and it is sufficient if the bad debt is written off as irrecoverable in the books of accounts of the assessee.

9. In the facts of the case, twin issues viz., (i) whether debt which was written off during the relevant year was offered to income in Previous year or earlier years, (ii) whether the assessee has debited the amount of doubtful debt to profit and loss account and has reduced the same from the asset side of the balance sheet require determination to decide the claim of the assessee with regard to writing off the bad debt. The Supreme Court dealt with Section 36(1)(vii) of the Act, which was amended with effect from 01.04.1989 in '**SOUTHERN TECHNOLOGIES LTD. VS. JT. CIT**', **(2010) 320 ITR 577**. It was inter alia held that after 01.04.1989, a mere provision for bad debt would not be entitled to deduction under Section 36(1)(vii) of the Act. It was further held that if an assessee debits an amount of doubtful debt to profit and loss account and credits the asset account like sundry debtors account, it would constitute a right of an actual debt. However, if an assessee debits 'provision for doubtful debit' to profit

and loss account and makes a corresponding credit to current liabilities and provisions on the liabilities side of the balance sheet then it would constitute a provision for doubtful debt. It was thus held that in the latter case the assessee would not be entitled to deduction after 01.04.1989. The aforesaid decision was referred to with approval in **VIJAYA BANK** supra.

10. However, from the close scrutiny of the orders passed by the assessing officer, Commissioner of Income Tax (Appeals) as well as Income Tax Appellate Tribunal, we find that aforesaid aspect of the matter has not been examined. Therefore, the impugned orders are quashed and the matter is remitted to the assessing officer to ascertain twin questions viz., (i) whether debt which was written off during the relevant year was offered to income in Previous year or earlier years, (ii) whether the assessee has debited the amount of doubtful debt to profit and loss account and has reduced the same from the asset side of the balance sheet. The

matter is remitted to the assessing officer for *de novo* consideration of the aforementioned aspect.

In view of the preceding analysis, it is not necessary to answer the substantial questions of law framed by this court. In the result, the appeal is disposed of.

**Sd/-
JUDGE**

**Sd/-
JUDGE**

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