

Oxygen Pvt. Ltd. and interest earned in the earlier years has been taxed as business income and following the ratio of that judgement, the loss on account of writing off these debts should have been allowed as business deduction.

3) *That the disallowance of Rs.2,10,28,688/- confirmed by the CIT(A) is bad in law.*

4) *That the aforesaid grounds are without prejudice to one another.”*

3. Facts of the case, in brief, are that the assessee had given certain amounts as advance to M/s H. Lon Hosiery Ltd. and M/s Mahadev Leasing Ltd., in 1998-99. The assessee had given this advance as Inter Corporate Deposit and earned interest on the advance given. The assessee stated that the interest was declared as business income. During the relevant year, the amount was written off along with unpaid interest and claimed as a bad debt. The AO stated that the company was not an NBFC and the advance and interest was not incidental to the business of the company as nowhere was it stated that the company was giving advances to earn interest. The AO therefore disallowed interest and the amount claimed as a bad debt by observing as under:-

“4.2 From the reply submitted as above, it has been perused that the assessee company is not an NBFC and the amount of advances made and interest accrued thereon was not incidental to the business of the company. To claim any amount as a bad debt, it is primary condition that the amount must be incidental to the business operations of the assessee company and in the case of assessee company the same are not in pursuance to the business of assessee company as it has been admitted that the amount was given as advance to earn interest which is not covered as business activity of the assessee company. The nature of advance given by the assessee company are considered as non performing asset NPA for which no deduction is available to an

assessee which is not a banking company so much so the same is not available to even an NBFC as held by the Hon'ble Supreme Court in the case of Southern Technologies Limited vs. CIT (2010) 187 Taxmann 346. Hence, in view of the above discussion amount claimed as bad debts and interest to the tune of Rs. 15000000 + 6028688/- is not allowed written off as bad debts and disallowed while computing income for the assessment year 2010-11. I am satisfied that the assessee company furnished inaccurate particulars of income to the tune of Rs. 21028688/- on account of wrong claim of bad debts for which penalty proceedings under section 271(1)(c) of the Act are initiated.”

4. Before the CIT(A), the assessee submitted that the assessee was being regularly assessed and had advanced the loans in the regular course of business. The advanced amounts were all reflected in the regular accounts of the assessee. The Id.CIT(A) confirmed the addition made by the AO by observing as under:-

“7.4 The appellant stated that it had taken all measures for recovery and then the advances were written off. The appellant has quoted several case laws to support its contentions. The appellant has relied on the decision of M/s Poysha Oxygen Ltd. vs. ACIT, Circle 14(1), New Delhi. However, I have noted in this case the amounts were lent by the appellant whose business was also of money lending. The appellant's business is not of money lending or giving of loans & advances.

(i) In order to claim deduction in respect of bad debt, the bad debt must be debited to the P&L A/c and correspondingly/simultaneously the aforesaid bad debt should be obliterated or reduced from loans and advances/debtors on the assets side of the balance-sheet and consequently at the end of the year, the figure of the loans and advances or the debts on the assets side of the balance sheet is shown as net of the provisions for the impugned bad debt.

(ii) For the deduction in relation to bad debts u/s 36(1)(vii) of the Act, it is not necessary for the assessee to establish that the debt has,

in fact, become irrecoverable, it is enough if the bad debt is written off as irrecoverable in the accounts of the assessee.

7.5. In order to eliminate the disputes in the matter of determining the year in which a bad debt can be allowed and also to rationalize the provisions, the Amending Act, 1987 has amended clause (vii) of sub-section (1) and clause (i) of sub-section (2) of section 36 to provide that the claim for the bad debt will be allowed in the year in which such a bad debt has been written off as irrecoverable in the accounts of the appellant.

7.6. In the case of Bank of Bihar Ltd. vs. CIT, the Supreme Court has held that, if a debt has become bad in a particular year, the appellant cannot, by purporting to amalgamate it with other debts due but not yet irrecoverable, revive it so as to claim it in a later year when the other debts also become bad.

7.7. A bad debt can be written off and allowed only in the course of a business that was being carried on during the relevant previous year. Bad debts in respect of a business that was closed down or discontinued before the commencement of the previous year cannot be allowed.

7.8. There are three important elements in the concept of a bad or doubtful debt which qualifies for deduction under clause (vii) of sub-section (1) of section 36 read with sub-section (2) thereof. The first is that there should be a debt, properly speaking and should be one which, when good, would have come into the balance sheet as a trading debt to swell the profits of the business. The second requirement is that the debt should be established to have become bad in the previous year. The expression earlier used in the statute and also in accountancy parlance was that the debts in question are "bad and doubtful" but the adjective "doubtful" does not qualify, add to or detract from the true meaning of the expression, viz., that there are no chances of recovery of the whole or concerned part of the debt at the end of the previous years in which it has become bad, in as much as it is doubtful of recovery. The third element is that it should have been written off by the appellant in the relevant previous year in respect of which the claim for deduction is made by the appellant.

7.9. A debt proper is that which one owes to another; any money, goods or services that one is bound to pay another; a pecuniary due; a liquidated demand; a sum of money due by certain and express

agreement. It includes any claim or demand upon which a judgement for a sum of money or directing the payment of money can be recovered in an action. Where it was held by a competent court that an appellant was not entitled to recover an amount claimed on the basis of transaction apparently unauthorized and illegal, such amount cannot be described as a debt.

7.10. A bad debt presupposes the existence of a debt and relationship of creditor and debtor. The mere fact that the appellant has lost some moneys on which he has been taxed will not be sufficient to justify a deduction under this section, particularly when the loss is of a capital nature.

7.11. Therefore debts incurred by an appellant should be on revenue account. They must have been taken into account in computing the profits of the appellant for an earlier year and so should naturally be allowed when they turn out to be irrecoverable or they should represent the irrecoverable loans of a money lending business carried on by the appellant in which the money lent constitutes the appellant's stock-in-trade. The appellant has been able to prove that the debts incurred were on revenue account.

7.12. In view of the above discussion, it is held that the AO had rightly disallowed Rs.2,10,28,688/-. The appellant cannot claim this as a deduction from its income. The amount may be claimed as a capital loss. The addition made by the AO of Rs.2,10,28,688/- is confirmed. The grounds of appeal are ruled against the appellant.”

5. The Id. Counsel for the assessee, at the outset, submitted that the issue involved in the instant appeal is squarely covered by the order of the Hon'ble Bombay High Court in the case CIT-V, Pune vs. Pudumjee Pulp & Paper Mills Ltd., dated 5th August, 2015 in ITA No.1590 of 2013 for AY 2004-05.

6. The Id. Sr. DR could not controvert the above submissions of the Id. Counsel of the assessee.

7. On careful consideration of the rival submissions, we find the issue involved in the instant appeal is squarely covered by the order of the Hon'ble Bombay High Court in the case CIT-V, Pune vs. Pudumjee Pulp & Paper Mills Ltd., dated 5th August, 2015 in ITA No.1590 of 2013 for AY 2004-05. The relevant observations of the Hon'ble High Court of Mumbai read as under:-

“12. So far as first part of Section 36(2)(i) of the Act is concerned, i.e., (a) above, we find that the Respondent-Assesee had during the earlier Assessment Years offered to tax an amount of Rs.42.65 lakhs received as interest on the deposit made with M/s. GSB Capital Market Ltd. The Appellant had since Assessment Year 1998-99 claimed an amount of Rs.49.82 lakhs as doubtful debts from M/s. GSB Capital Market Ltd. This consisted of the aggregate of principal and interest payable by M/s. GSB Capital Market Ltd. It was in the subject Assessment Year that a settlement was arrived at between the parties and the Assesee received Rs.15 lakhs from M/s. GSB Capital Market Ltd. and the balance amount of Rs.34.82 lakhs being non recoverable was being claimed as bad debts by writing off the same in its books of account. It would thus be noticed the amount of Rs.34.82 lakhs which constitutes partly the principal amount of the inter corporate deposits and partly the interest which is unpaid on the principal debt. The Assessing Officer's contention that amount of Rs.34.82 lakhs was not offered to tax earlier and, therefore, deduction under Section 36(2)(i) of the Act is not available, is no longer res integra. This very issue came up for consideration before this Court in Shreyas S. Morakhia (supra) wherein the assessee was a stock broker and engaged in the business of sale and purchase of shares. The brokerage payable by the client was offered for tax. Subsequently, it was found that the principal amount which was to be received from its clients would not be received. The assessee sought to claim as bad debts not only the brokerage amounts not received but the aggregate of principal and brokerage amounts not received in respect of the shares transacted. This Court held that the debt comprises not only the brokerage which was offered to tax but also principal value of shares which was not received. Therefore, even if a part of debt is offered to tax, Section 36(2)(i) of the Act, stands satisfied. The test under the first part of Section 36(2)(i) of the Act is that where the debt or a part thereof has been taken into account for computing the profits for earlier Assessment Year, it would satisfy a claim to deduction under Section

36(1)(vii) read with Section 36(2)(i) of the Act. In fact, the Revenue also does not dispute the above provisions as no submission in that regard were made during the course of hearing before us.

13. Therefore, in view of the above self evident position in Section 36(2)(i) of the Act as well as decision of this Court in Shreya Morakhia (supra), no substantial question of law arises for our consideration.”

8. The Hon’ble Supreme Court has relied and referred to its own judgement in the case of CIT vs. Shreyas Morakhia, 342 ITR 285 (SC) wherein their Lordships held that the assessee being entitled to deduction in view of First Part of Section 36(2)(i) of the Act. On being asked by the Bench the ld. Sr. DR could not show us any different facts and circumstances, from said judgement of the Hon’ble Supreme Court in the case of CIT vs. Pudumjee Pulp & Paper Mills Ltd. (supra). Therefore, respectfully following the same, we hold that the issue of amounts written off pertaining to the inter-corporate deposits/advances to certain entities is squarely covered in favour of the assessee by the order of the Hon’ble Supreme Court in the case of CIT vs. Shreyas Morakhia (supra). Hence, the sole ground of the assessee is allowed. The AO is directed to delete the impugned disallowance.

9. In the result, the appeal filed by the assessee is allowed.

Order pronounced in the open court on 31.08.2022.

Sd/-

(PRADIP KUMAR KEDIA)
ACCOUNTANT MEMBER

Sd/-

(C.M. GARG)
JUDICIAL MEMBER

Dated: 31st August, 2022.

dk

Copy forwarded to :

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR

Asstt. Registrar, ITAT, New Delhi