
(1990) 03 MAD CK 0045

In the Madras High Court

Case No : Tax Case No. 32 of 1980 (Reference No. 32 of 1980)

Commissioner of Income Tax

APPELLANT

Vs

Devi Chit Fund

RESPONDENT

Date of Decision : 22-03-1990

Acts Referred:

Income Tax Act, 1961 — Section 36(1)

Citation : (1990) 186 ITR 738

Hon'ble Judges : V Ratnam, J; K.A. Thanikkachalam, J

Bench : Division Bench

Advocate : C.V. Rajan, for the Appellant;

Judgement

Ratnam, J.—At the instance of the Revenue, u/s 256(2) of the Income Tax Act, 1961 (hereinafter referred to as "the Act"), the following

questions of law have been referred to this court for its opinion :

(1) Whether, on the facts and circumstances of the case, the Appellate Tribunal's finding that debts to the tune of Rs. 40,254 due from C. L.

Badrinarayanan and C. B. Lakshminarayanan Chettiar have become irrecoverable during the year of account and the same should be allowed as

"bad debts" in the assessment for the year 1971-72 is sustainable in law ?

(2) Whether the Appellate Tribunal's above finding is based on relevant materials and is a reasonable view to take on the facts obtaining in this

case ?

2. The assessee is a firm carrying on business in money-lending and conducting chits. While filing the return for the assessment year 1971-72 for

the accounting period ending March 31, 1971, the assessee claimed allowance for bad debts in the accounts of C. L. Badrinarayanan, and C. B.

Lakshminarayanan and others, amounting to Rs. 40,254. The total amount due from the debtors referred to above was Rs. 62,000 and 50% of

this amount, i.e., Rs. 31,000, along with court costs of Rs. 9,254, totalling Rs. 40,254 was written off in the books of account of the assessee.

According to the assessee, the debtor had incurred heavy losses and had closed down their business and their properties had also vested in the

official receiver owing to their adjudication as insolvents. The Income Tax Officer took the view that the write-off was premature, as the official

receiver had not declared any dividend and disallowed the claim of the assessee for the write-off of this amount. On appeal by the assessee, the

Appellate Assistant Commissioner also upheld the disallowance on the ground that there was no communication regarding the total assets and

liabilities of the debtors and that the insolvency proceedings had also not become final. On further appeal by the assessee to the Tribunal, it took

into account the several steps taken by the assessee in securing decrees by institution of suits and the execution proceedings levied therein as well

as the affidavit of assets and liabilities filed by the insolvents and concluded that all the properties of the debtors were under attachment at the

instance of several creditors and the insolvents had also inflated the value of the assets and as the liabilities exceeded the value of the assets, there

was no reasonable prospect of the assessee recovering any amount from the debtors and in that view, upheld the claim for write off of the bad

debt. That is how the two questions of law set out earlier have come up before this court for its opinion and the assessee, though served with

notice, has not appeared in person or through counsel.

3. Learned counsel for the Revenue submitted that merely because the debtors had been adjudicated as insolvents, the debt cannot be considered

to be irrecoverable and that it has to be established that the debt has become irrecoverable and in cases of insolvency, a debt can be stated to

have become bad, only when the official receiver declares a final dividend and not till then. Reference in this connection was also made to the

decisions reported in ALAGANANDA MUDALIAR Vs. COMMISSIONER OF INCOME TAX, MADRAS., , (1941) 9 ITR 202; NANAK

CHAND MAMRAJ MAL Vs. COMMISSIONER OF Income Tax, SIMLA., and Chettinad Company Pvt. Ltd. Vs. Commissioner of Income

Tax, Tamil Nadu-IV, .

4. We find from the record of the proceedings that the assessee had advanced to C. B. Lakshminarayanan and C. L. Badrinarayanan amounts of

Rs. 5,000, Rs. 6,500 and Rs. 19,500. For the recovery of the amounts so advanced, the assessee had also instituted three suits and obtained

decrees therein. In execution of those decrees, the assessee also attached three items of properties belonging to the debtors and it was during the

pendency of the execution proceedings, at the instance of another creditor, that the debtors were adjudicated as insolvents. In the course of the

insolvency proceedings, the debtors filed an affidavit of their assets and liabilities and according to that, the three items of immovable properties

attached by the assessee were valued at Rs. 4,00,000, Rs. 2,00,000 and Rs. 22,500. The movable properties disclosed were all book debts

amounting to Rs. 1,30,141 and all of them were barred debts. The total liabilities inclusive of the amounts due to the assessee were shown as Rs.

6,00,255 and according to the affidavit of the assets and liabilities filed by the insolvents, there was an excess of assets over liabilities in a sum of

Rs. 1,52,386. The first item of property valued by insolvents at Rs. 4,00,000 had been let on an annual rental of Rs. 1,650 and the Tribunal rightly

took the view that the valuation given by the debtors was exorbitant. The second item of property, it was noticed by the Tribunal, had been sold in

the execution of a mortgage decree obtained in O.S. No 397 of 1971 for Rs. 80,125 which was just sufficient to satisfy the claim of the mortgage

- decreeholder. The third item of property valued by the debtors at Rs. 22,500 was originally sold in court auction in O.S. No. 191 of 1970 for a

sum of Rs. 10,000, though the court sale was subsequently set aside. On the basis of the materials so made available by the assessee relating to the

assets and liabilities of the insolvents, as per their affidavit of assets and liabilities filed in the course of the insolvency proceedings, the Tribunal

found that the value of the first and the third items of properties, as given, could not be accepted, as the value had been exaggerated and that the

liabilities exceeded the assets and there was no reasonable prospect of the assessee recovering any amount from the debtors. The Tribunal had

taken into account the institution of suits and the obtaining of decrees by the assessee, the resort to execution proceedings, the adjudication of the

debtors as insolvents, the value of the available assets as disclosed in the affidavit of assets and liabilities as well as the sale of one of the items of properties in satisfaction of the mortgage decree to conclude that the liabilities exceeded the assets and there was, therefore, no reasonable prospect of the assessee recovering any amount from the debtors. We thus find that the Tribunal had taken into account the properties available with the insolvents as well as the liabilities to be discharged and had come to the conclusion that the assessee had really no hope of recovering any amount from the debtors. It is true that merely because the debtors are adjudicated as insolvents, it cannot be said that the debt becomes irrecoverable, but the irrecoverability of a debt turns upon a variety of circumstances, particularly, the amount of property at the disposal of the insolvents and how bleak or bright are the chances of recovery of the amount by the creditors out of the properties so available. We find from a careful perusal of the order of the Tribunal that it had considered all the relevant circumstances to ascertain the properties available and also the chance of recovery of the amounts from the debtors by the assessee and had found that there were no chances and that view so taken by the Tribunal, on the facts and circumstances of this case, cannot, in any manner, be assailed.

5. We may now refer to the decisions relied on by counsel for the Revenue. In ALAGANANDA MUDALIAR Vs. COMMISSIONER OF

INCOME TAX, MADRAS., , a firm, which owned the assessee substantial amounts, became insolvent in 1929 and the preferential payments

were ultimately decided by the Privy Council in 1934 and on receiving a letter in 1936 from the official assignee to the effect that there was no

prospect of any dividend being declared, the assessee wrote off the debt, as a bad debt, in 1936-37. The Income Tax authorities took the view

that it was possible for the assessee even in 1929 to know from the schedule filed by the insolvents that the debt was irrecoverable and, therefore,

the assessee should have written off a major portion of the debt even in 1929. It was held that there was no material to support the finding of the

Income Tax authorities that the debt had become bad even in 1929 and should have been written off in that year, but that on the materials, there

was no justification whatever to hold that the assessee should have written off the debt, at any rate in 1934 and that the authorities were not

justified in refusing to allow the assessee to write off the debt in 1936-37. This conclusion was arrived at on the view that the official assignee informed the assessee that there was no hope of any dividend and it was, therefore, not possible to say that the assessee should have written off the debt at an earlier stage. We are unable to understand the ratio of this decision as laying down that in every case, only after the receipt of an intimation from the official assignee to the effect that there is no chance of payment of any dividend, the assessee could proceed to write off and not before. We may point out that the question of write off has to be decided not solely on the basis of the impossibility of declaration of dividend, but also on a cumulative consideration of the facts and circumstances. The decision turned more upon the year in which the write-off should be permitted and cannot be understood as laying down that a communication from the official assignee regarding the non-availability of evidence for declaring a dividend would, in all cases, be a condition to be fulfilled. We are, therefore, of the view that the principle of this decision cannot be pressed into service by the Revenue. In (1941) 9 ITR 202 it was held that, on the materials on record, the debt became finally a bad debt only when the official receiver declared a final dividend and stated that no more was expected to be declared and, therefore, the assessee was entitled to deduct the amount as a bad debt in the accounting year 1936-37, as the communication from the official receiver was received on June 11, 1936. It is thus seen that the decision rested on the materials available with reference to the point of time when the debt became bad as per the communication of the official receiver. Even this decision does not lay down that only when there is a declaration of the inability of the official receiver to declare further dividends, the creditor can proceed to write off and not till then. This decision cannot in any manner advance the case of the Revenue. NANAK CHAND MAMRAJ MAL Vs. COMMISSIONER OF Income Tax, SIMLA., , dealt with a case where on the adjudication of the debtor as an insolvent, a first dividend was received and there was a lull for a period of almost twelve years thereafter after which the assessee received a further sum. However, the assessee claimed even in the year 1949-50, the benefit of a write-off and the Tribunal took the view that the debt had become irrecoverable after 1941 and in any case long before the relevant accounting year 1948-49. It was on

these facts that the court held that there was no material to justify the finding of the Tribunal that the bulk of the debt had become irrecoverable

long before 1948-49, as the receiver completed the administration of the estate of the insolvent only in 1950. We are unable to find anything in this

decision which would advance the contention of the Revenue. It is true that this decision had proceeded on the footing that so long as there was a

faint ray of hope, however dim that ray may be, and so long as the debt was in the process of realisation, it cannot be said that it has become

irrecoverable. Even so, the ultimate conclusion in that decision was rendered with reference to the non-availability of materials on record to sustain

the view taken by the Tribunal that there was no hope of recovery of the amounts after 1941. Thus even this decision cannot assist the Revenue. In

Chettinad Company Pvt. Ltd. Vs. Commissioner of Income Tax, Tamil Nadu-IV, , in the course of the money-lending business carried on by the

assessee, in respect of an advance made by the assessee, it obtained a decree and the debtor paid a small amount leaving a large outstanding. The

first mortgagee of the debtor had instituted a suit for the recovery of the amounts due and the debtor had also gone into liquidation and the

assessee-company wrote off in its books, in the accounting year relevant to the assessment year 1966-67, the entire amount due from the debtor

and claimed the same as a deduction in the course of the assessment. That claim, however, was not countenanced by the Income Tax Officer and

the assessee reiterated the same claim in the next two years, but this was also rejected by the Income Tax Officer and the rejection was also

confirmed by the Tribunal as, in its view, even as late as 1973, there was no clear information of the liquidation proceedings and as to the stage at

which the matter stood and there was, therefore, no evidence to show that there was no chance of recovery of any portion of the amount during

the years in question. It was held that the disallowance having been confirmed by the Tribunal and there being no evidence or material to support

the assessee's plea that the debt had become bad, the Tribunal cannot be said to have come to a wrong conclusion. It is thus seen that the view of

the Tribunal was upheld on the basis that support the plea of the assessee that the debt had become bad in the sense that the debtor's properties

had gone in for discharge of debts of secured creditors, who were entitled to payment in preference to the assessee, and there was also no material

whatever to show the value of the debtor's properties and the amount payable by the debtor. It was in the context of the absence of these

particulars, it was held that it would be improper to act on the ipse dixit of the assessee that there was no chance of recovery. In this case, the

materials available on record clearly establish that there is not even a slightest hope of recovery of the amounts from the debtors, whose properties,

on a fair and proper valuation, are inadequate to permit any distribution, as the liabilities far exceed the value of assets. Under those circumstances,

the decision in Chettinad Company Pvt. Ltd. Vs. Commissioner of Income Tax, Tamil Nadu-IV, , also would not be of any assistance to support

the contention of the Revenue. We may now refer to two decisions which would be relevant for the disposal of this reference. In the first of these

decisions reported in Bank of Bihar Ltd., Patna Vs. Commissioner of Income Tax, Bihar and Orissa, , the Supreme Court laid down that the

question whether a debt is a bad debt is one of fact and if there is some evidence to justify that conclusion, it is not open to the High Court in a

reference u/s 66 of the Indian Income Tax Act to reappraise the evidence. In doing so, the Supreme Court referred to the following observations

of the Privy Council in CIT v. S. M. Chitnavis [1932] 2 Comp Cas 464; [1932] 6 ITC 453(at p. 429 of 45 ITR) :

Whether a debt is a bad debt, and, if so, at what point of time it became a bad debt, are questions which in their Lordships' view are questions of

fact, to be decided in the event of dispute by the appropriate Tribunal, and not by the ipse dixit of anyone else. The assessee has no option of

declaring a debt as bad.... In every case it is a question of fact, to be determined after consideration of all relevant circumstances".

6. The above passage referred to in the decision of the Supreme Court also clearly establishes that the question whether a debt is a bad debt and if

so at what point of time, are essentially and purely questions of fact. Again, in T. S. PL. P. Chidambaram Chettiar (By Legal Representatives) Vs.

Commissioner of Income Tax, Madras., , after referring to the decisions in CIT v. Chitnavis [1932] 6 ITC 453; [1932] 2 Comp Cas 464 Bank of

Bihar Ltd., Patna Vs. Commissioner of Income Tax, Bihar and Orissa, and NANAK CHAND MAMRAJ MAL Vs. COMMISSIONER OF

Income Tax, SIMLA., it was held that a debt became bad not because the assessee was minded to treat it so at a particular time but because at

and from a particular point of time, it was no longer possible to recover, as the debtor had no means or assets to repay and the circumstances made it plain that recovery would not be possible and that if the official assignee had no assets of the insolvents in his hands, there was no reason why a creditor should wait until three years after he had knowledge of that position and only then treat the debt due to him as a bad debt. It has also been clearly laid down that whether a debt is a bad debt or a doubtful debt, in either case is purely a factual matter depending on actual facts having a bearing on that and not merely the hopes, fears or judgment of the creditor himself and it is for the assessee who claims it to be a bad or doubtful debt to prove that it had become bad in the accounting year, by relevant and proper evidence. In this case, the Tribunal, as noticed earlier, had adverted to all the relevant considerations relating to the availability of assets and liabilities of the insolvents and had found that the assessee had not been left even with a dim or remote ray of hope of recovery of the amounts from the insolvents and, therefore, the write-off, as claimed by the assessee, should be allowed. The conclusion so arrived at by the Tribunal is essentially one of fact and is more than amply supported by the available materials on record. We, therefore, answer the questions referred to us in the affirmative and against the Revenue. There will be no order as to costs.