(2005) 07 MAD CK 0046

In the Madras High Court

Case No : T.C. No. 157 of 2003

Commissioner of Income Tax	APPELLANT
Vs	
Micromax Systems P. Ltd.	RESPONDENT

Date of Decision : 06-07-2005

Acts Referred:
Income Tax Act, 1961 — Section 155(6), 17(3), 260A, 28, 36

Citation : (2005) 198 CTR 578 : (2005) 277 ITR 409

Hon'ble Judges : Markandey Katju, C.J;F.M. Ibrahim Kalifulla, J

Bench : Division Bench

Final Decision : Allowed

Judgement

Markandey Katju, C.J.—This appeal u/s 260A of the Income Tax Act, 1961, has been filed by the Department challenging the order of the

Income Tax Appellate Tribunal dated March 19, 2003, by which the appeal of the Revenue has been dismissed by the Tribunal.

2. The appeal was admitted by the court on the following substantial questions of law :

1. Whether, on the facts and circumstances of the case, the Tribunal was right in allowing the assessee''s claim for a bad debt, when the bad debt

had not actually been written off in the books of account ?

2. Whether, on the facts and circumstances of the case, the Tribunal was right in allowing the claim for bad debt on the ground that the provision

had been shown under the head ''Expenditure'' in the annual report of the assessee-company ?

3. Whether, on the facts and circumstances of the case, and in view of the provisions of Section 36(1)(vii), an assessee other than a banking

company can be allowed a claim for a bad debt on the basis of a mere provision ?

3. We have heard learned counsel for the parties and perused the record. The relevant assessment year is 1997-98. For this year the assessee

claimed bad debt of Rs. 3 lakhs. The Assessing Officer disallowed it on the ground that it was shown as a provision for bad and doubtful debts in

the books of the assessee, but the assessee had not actually written off the bad debt of Rs. 3 lakhs as irrecoverable in its books of account.

4. The assessee is a limited liability company, manufacturing control systems and equipment. It received three orders from M/s. Ignifluid Boilers

India Limited for Rs. 15 lakhs, Rs. 16,17,000 and Rs. 1,50,000 respectively. The orders were completed on February 3, 1996, and invoices

were raised. The customer thereafter made part payment and confirmed the balance of Rs. 9,93,350 as on July 29, 1996.

5. The assessee tried to realise the balance from the customer by follow-up letters, fax messages and telephone calls on several occasions, but

despite its efforts the entire balance could not be collected. Thus, though the assessee was able to collect some amounts there was a balance sum

of Rs. 5,43,350 of which Rs. 3 lakhs was written off in the previous year relevant to the assessment year 1997-98 and the balance of Rs.

2,43,250 in the next previous year relevant to the subsequent assessment year. Though the amount of Rs. 3 lakhs was debited with the noting

provision for bad debts"" it was alleged by the assessee that the debt had in fact become bad. The assessee appealed to the Commissioner of

Income Tax (Appeals), who by his order dated September 30, 1998, allowed the appeal and decided in favour of the assessee. Aggrieved against

that order the Department preferred an appeal before the Tribunal which has been dismissed by the impugned order.

6. The Tribunal has observed in paragraph 4 of its order as follows :

From the facts, it is seen that the assessee had taken lot of efforts to collect the debt. While debiting a sum of Rs. 3 lakhs the assessee had

claimed entire bad debt during this year and the next year. Though the nomenclature used is ''provision'', it is seen that the claim of bad debt had to

be allowed. At the time of hearing, learned counsel for the assessee filed sixth annual report (1997-98) wherein at page No. 9, the provision for

bad debts had been clearly stated under the head ''Expenditure''. Therefore, I do not find any infirmity in the order of the learned Commissioner of

Income Tax (Appeals) directing the Assessing Officer to allow the bad debts as claimed by the assessee. The order of the learned Commissioner

of Income Tax (Appeals) is confirmed. It is ordered accordingly.

7. The relevant portions of Section 36 of the Income Tax Act after the amendment with effect from April 1, 1989, read as follows :

(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 Section 28--...

(vii) subject to the provisions of Sub-section (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 ; . . .

(viia) in respect of any provision for bad and doubtful debts made by--

a) a scheduled bank...

(b) a bank being a bank incorporated by or under the laws of a country outside India . . .

(c) a public financial institution ...

(2) In making any deduction for a bad debt or part thereof, the following provisions shall apply -

(iv) where any such debt or part of debt is written off as irrecoverable in the accounts of the previous year (being a previous year relevant to the

assessment year commencing on the 1st day of April, 1988 or any earlier assessment year), and the Assessing Officer is satisfied that such debt or

part became a bad debt in any earlier previous year not falling beyond a period of four previous years immediately preceding the previous year in

which such debt or part is written off, the provisions of Sub-section (6) of Section 155 shall apply"". Learned counsel for the Department submitted

that a mere provision of bad debt is not sufficient to get the benefit of the above provision and it is only when the debt is actually written off as

irrecoverable in the books of account that a claim for bad debt can be allowed as a deduction.

8. On the other hand, the submission of learned counsel for the assessee is that it was only by an inadvertent mistake committed by the assessee

that a narration was made in the profit and loss account as ""provision for bad debt"".

9. On the facts of the case, we are of the opinion that this appeal has to be allowed.

10. In this case, the provisions of Section 36(1)(viia) of the Act are not attracted, since the assessee is admittedly not a bank or a public financial

institution. It is only a company manufacturing control systems and equipment. Hence only Section 36(1)(vii) of the Act would apply and not

Section 36(1)(viia) of the Act.

11. The difference between Clause (vii) and Clause (viia) of Section 36(1) of the Act (after the amendment with effect from April 1, 1989) is

significant. Clause (vii) clearly mentions that the bad debt or part thereof can be allowed only if it is written off as irrecoverable in the accounts of

the asses-see for the previous year.

12. No doubt prior to April 1, 1989, even if the debt had not been written off, it could be allowed as a ""bad debt"" if the assessee could establish

that the debt had in fact become bad. However, after the amendment with effect from April 1, 1989, there is an additional requirement in Section

36(1)(vii), namely, that the ""bad debt"" should be written off as irrecoverable in the accounts of the assessee for the previous year. Hence unless it is

written off as irrecoverable in the accounts, it cannot be allowed as a ""bad debt"".

13. It may be mentioned that prior to the amendment of Section 36(1)(vii) with effect from April 1, 1989, Clause (vii) of Section 36(1) reads as

follows :

subject to the provisions of Sub-section (2), the amount of any debt or part thereof, which is established to have become a bad debt in the

previous year.

14. Thus prior to April 1, 1989, even if the debt has not been written off as irrecoverable in the accounts of the assessee, it could still be allowed

as a bad debt if the assessee could establish that in fact it had become a debt in the previous year. After the amendment by Act 4 of 88 with effect

from April 1, 1989, the essential requirement for a claim of ""bad debt"" to be allowed is that it should have been written off as irrecoverable in the

accounts of the assessee for the previous year. Thus for and from the assessment year 1989-90, the requirement as to the writing off of the debt as irrecoverable has become essential for a claim of ""bad debt"" to be allowed.

15. Thus, it is now a mandatory condition that deductions can be allowed as bad debts only when it is actually written off as irrecoverable in the

accounts and not on the basis of a mere provision.

16. Learned counsel for the assessee has relied on the decision of the Supreme Court reported in Commissioner of Income Tax Vs. Asea Ltd.

(now known as Asea Brown Boveri Ltd.), where deduction of a bad debt was allowed on the basis of a provision, However, the above decision

was rendered in the context of Section 36(1)(vii) as it stood prior to 1989. Hence the said decision is clearly distinguishable.

17. Learned counsel for the assessee then contended that the Revenue never objected to the fact of the debt becoming bad in the year of account,

but only objected to the fact that it has not been written off as irrecoverable in the assessee''s accounts.

18. In our opinion, the principle of plain or literal interpretation has to be applied in interpreting a taxing statute. As observed by Lord Cairns in

Partington v. Attorney General [1869] LR 4 HL 100 :

If the person sought to be taxed comes within the letter of the law he must be taxed, however great the hardship may appear to the judicial mind.

On the other hand if the court seeking to recover the tax cannot bring the subject within the letter of the law, the subject is free, however

apparently within the spirit of the law the case might otherwise appear to be.

19. Thus, in interpreting a taxing statute one cannot go by the notion as to what is just and expedient vide Commissioner of Income Tax, Patiala

and Others Vs. Shahzada Nand and Sons and Others, . In IRC v. Hinchy [1960] AC 748 (HL) the House of Lords held that a provision in the

Income Tax Act, 1952 for a statutory penalty (for making an incorrect return of income) of 20 pounds and trebling ""the tax which he ought to be

charged under this Act"" referred not to the tax on the amount which the taxpayer had failed to declare, but to the whole tax which he ought to be

charged for the relevant year, notwithstanding the extravagant consequences which flowed from giving the words their natural meaning.

20. The Supreme Court of India has held that equity is out of place in tax laws (vide Commissioner of Income Tax, Madras Vs. V. Mr. P. Firm,

Muar, . In CITv. Madho Pd. Jatia , it held that there could be no consideration of equity if the language of the provision was plain and clear, but

where it was not, and two interpretations were possible, the one in consonance with equity and fairness should be preferred.

21. The principle of strict interpretation of taxing statutes was best enunciated by Rowlatt J. in his classic statement (vide Cape Brandy Syndicate

v. IRC [1921] 1 KB 64 cited with approval in Income Tax Officer, Tuticorin Vs. T.S. Devinath Nadar and Others,) :

In a taxing Act one has to look merely at what is clearly said. There is no room for any intendment. There is no equity about a tax. There is no

presumption as to a tax. Nothing is to be read in, nothing is to be implied. One can only look fairly at the language used.

22. In A.V. Fernandez Vs. The State of Kerala, , the Supreme Court of India stated the principle as follows (page 661 of AIR 1957) :

If the Revenue satisfies the court that the case falls strictly within the provisions of the law, the subject can be taxed. If, on the other hand, the case

is not covered within the four corners of the provisions of the taxing statute no tax can be imposed by inference or by analogy or by trying to probe

into the intentions of the Legislature and by considering what was the substance of the matter.

23. In Commissioner of Income Tax, Assam and Nagaland etc. Vs. Shri G. Hyatt, , the question was whether u/s 17(3) of the Income Tax Act,

1961, the interest on the assessee''s own contribution to an unrecognized provident fund could be treated as salary. The Supreme Court of India

held that the language of Section 17(3) was plain and unambiguous, and hence the said amount was not salary but income from other sources and

taxable u/s 56.

24. In Polestar Electronic (Pvt.) Ltd. Vs. Additional Commissioner, Sales Tax and Another, , the question was whether sales outside Delhi would

also be included in taxable income. The Supreme Court held that the section used the word ""resale"" simpliciter, and hence it referred to all resales

and could not be limited to resales within Delhi alone. Thus the Supreme Court went by the plain language of the statute, and did not speculate on

the intention of the Legislature.

25. In Hansraj Gordhandas v. H. H. Dave, Asst. Collector [1978] 2 ELT 350, the Supreme Court of India considered the language of a

notification under the Central Excise Tariff and held that all that was required for claiming an exemption was that the cotton fabric must be

produced on power looms owned by the co-operative society. There was no further requirement in the language of the notification that the cotton

fabric must be produced by the society for itself. The Supreme Court refused to go into the question of the intention behind the exemption since the

language of the notification was clear.

26. In Assessing Authority-cum-excise and Taxation Officer, Gurgaon and Another Vs. East India Cotton Mfg. Co. Ltd., Faridabad, the

concessional rate under the Punjab sales tax was payable if certain raw materials were used in the manufacture of goods for sale. The contention of

the assessee was that the word used in the Act was ""for sale"" and not ""for sale by him"" and hence the goods sold by a third party were also

covered by the provision. This contention was accepted by the Supreme Court which followed the literal rule of interpretation.

27. In Commissioner of Wealth Tax, Gujarat-III, Ahmedabad Vs. Ellis Bridge Gymkhana, , the Supreme Court held that the word ""individual"" in

the charging section could not be stretched to include an association of persons. The court held that the charging section had to be construed

strictly, and if a person could not be brought within the ambit of the charging section by clear words, he could not be taxed at all.

28. In the present case, it can be seen that the assessee did not write off the debt in question as irrecoverable in his accounts for the previous year.

Hence on the plain language of Section 36(1)(vii) of the Act the debt cannot be allowed as a ""bad debt"". It may be that the assessee committed an

inadvertent mistake, but we cannot go by notions of equity in tax matters. Making a provision is not the same thing as writing off a debt as

irrecoverable.

29. For the reasons given above, the impugned judgment of the Income Tax Tribunal, and of the Commissioner of Income Tax (Appeals) with

respect to the claim of the assessee regarding bad debts are set aside, and the order of the Assessing Officer is restored. The appeal is allowed.

