(2005) 07 MAD CK 0024

In the Madras High Court

Case No : T.C. (A) No. 394 of 2001

Narayanan Chettiar Industries — APPELLANT

Vs

The Income Tax Officer — RESPONDENT

Date of Decision : 11-07-2005

Acts Referred:
Income Tax Act, 1961 — Section 260A, 41(1)

Citation : (2005) 199 CTR 148 : (2005) 277 ITR 426

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

Bench : Division Bench

Advocate : P.P.S. Janardhana Raja, for the Appellant; Pushya Sitaraman, Senior Standing Counsel for I.T., for the Respondent

Final Decision : Allowed

Judgement

Markandey Katju, C.J.—This is an appeal u/s 260A of the Income Tax Act which was admitted on the following substantial question of

law:-

Whether the Tribunal was right in treating the amount of Rs. 23,66,695/- (the amount which was written off by the sister concern of the assessee)

as the income in the hands of the assessee and on that count liable to be taxed u/s 41(1) of the Income Tax Act?

2. We have heard the learned counsel for the parties and perused the records, including orders of the Income Tax authorities. All the authorities

have decided on the above point against the assessee.

3. The question is as to whether the amount in question can be added as income in the hands of the assessee u/s 41(1) of the Income Tax Act.

4. It is well settled that the revenue can add a sum to the assessee''s income u/s 41(1) of the Income Tax Act only if it can prove that the allowance

or deduction has been made in the assessment in the previous year in respect of the loss, expenditure or trading liability.

5. As observed by the Supreme Court in Tirunelveli Motor Bus Service Co. Vs. Commissioner of Income Tax, Madras, , unless it is established

that a deduction of liability was allowed while making the assessment in the earlier year, the addition as deemed profits u/s 41(1) in respect thereof

would not be permissible.

6. The same view was taken in Commissioner of Income Tax Vs. Thakurdas, , CIT Vs. Kharaiti Lal & Co. (1989) 175 ITR 265 , Commissioner

of Income Tax Vs. Lal Textile Finishing Mills (P.) Ltd., , Commissioner of Income Tax Vs. Pranlal P. Doshi, , CIT Vs. Western Rolling Mills,

(1994) 72 Taxman 15, etc.

7. The learned counsel for the appellant/assessee has submitted that in this case there is no deduction or allowance made in the assessment of any

year and there is no finding to this effect.

8. On the other hand, the learned counsel for the department has contended that the assessee had not raised this issue before the Income Tax

Tribunal, as can be seen from the grounds of appeal before the Tribunal.

9. We have perused the grounds of appeal filed before the Tribunal. We find that there is no such ground which was raised before the Tribunal

which is being sought to be raised before us now. However, there is a general ground being ground No.1 which was raised before the Tribunal:-

The Commissioner of Income Tax (A) erred, both in law and on the facts of the case, in determining the profit u/s.41(1) of the Act"".

10. In the order of the Assessing Officer it has been stated (in page - 3):-

ii) No deduction had been allowed in respect of the above amounts received from India Leather Corporation (P) Ltd., and the assessee did not

derive any benefit in respect of the above liability"".

11. In the order of the CIT (Appeals) also it has been stated at page -2:-

It was also pleaded that no deduction had been allowed in respect of the above amount and the appellant firm did not derive any benefit in respect

of the above liability"".

12. No doubt, before the Tribunal this ground which is sought to be taken now before us was not taken in clear cut terms (though it is included in

the general ground No.1 before the Tribunal). However, in our opinion, this ground goes to the root of the matter since unless an allowance or

deduction has been made in the computation of profit or gains of the business or profession in respect of loss, expenditure or trading liability

incurred by the assessee no addition can be made u/s 41(1), vide Juggilal Kamlapat, Bankers Vs. Commissioner of Income Tax, , Sharma and Co.

Vs. Income Tax Officer, B-Ward, , Indian Motor Transport Co. Vs. CIT, (1978) 114 ITR 677, etc.

13. Section 41(1) of the Income Tax Act creates a legal fiction, and hence has to be strictly complied with if any addition in the income is sought to

be made by the revenue.

14. Thus, the question sought to be raised before us goes to the root of the matter because unless an allowance or deduction has been made in the

previous year in respect of loss, expenditure or trading liability there can be no addition u/s 41(1) of the Income tax Act.

15. A perusal of the impugned order of the Income Tax Appellate Tribunal shows that there was no finding of the Tribunal that any deduction or

allowance was made in the assessment of the assessee in an earlier year. In the circumstances, we set aside the impugned order of the Tribunal and

remand the matter to the Tribunal for a fresh decision in accordance with law after hearing the parties concerned in which a clear finding should be

given whether any deduction has been allowed in the assessment of the assessee in an earlier year so as to comply with Section 41(1) of the

Income Tax Act. This appeal is allowed, the impugned order of the Tribunal is set aside, and the matter is remanded to the Tribunal for a fresh

decision in accordance with law.