IN THE HIGH COURT OF DELHI AT NEW DELHI

+I.T.A. No. 269/2009

Date of Decision: 27.08.2009

#Commissioner of Income Tax .....Appellant
!
Through: Ms.Suruchi Aggarwal with Mr.Ashish Kumar

Versus

$M/s. Bonanza Portfolio Limited .....Respondents

Through Dr. Rakesh Gupta with Ms.Mahima Agarwal

CORAM :-
*THE HON'BLE MR.JUSTICE A.K.SIKRI
THE HON'BLE MR. JUSTICE VALMIKI J. MEHTA

1.Whether Reporters of Local papers may be allowed to see the Judgment?
2.To be referred to the Reporter or not?
3.Whether the judgment should be reported in the Digest?

A.K. SIKRI, J.

:

1. Admit.

2. Following question of law arises for consideration:-

"Whether in view of the provisions of Section 36(1)(viii), the total debit balance including the consideration collectible by the assessee company for the sale purchase of share can be claimed by the assessee as bad debts when the assessee company had only credited brokerage in the P&L A/c?"

3. With the consent of the parties the matter is heard at this stage itself on the paper-book filed. Learned counsel for both the parties have advanced their arguments in detail and we proceed to decide the question of law framed in the following manner:-

4. In the income tax return filed by the assessee for the assessment year 2001-2002 the assessee declared income of Rs. 33,25,404/-. This return was processed under section 143(1) of the Income Tax act. Statutory notice under Section 143(2) of the Act was given and the assessment completed under Section 143(3) of the year. During the assessment Assessing Officer found that the assessee had claimed bad debt in the sum of Rs. 50,30,491/-. According to the A.O. conditions for allowability of this amount as bad debt as stipulated in Section 36(1)(vii) of the Income Tax Act read with Section 36(2) thereof were not satisfied and, therefore, he disallowed the said claim of bad debt. The order of the Assessing Officer was confirmed in appeal by the CIT (Appeal). However, in further appeal preferred by the assessee before the Income Tax appellate Tribunal, the Tribunal has allowed the appeal and held that aforesaid amount should have been allowed as bad debt by the Assessing Officer as conditions stipulated in section 36(1)(vii) and

section 36(2) has been satisfied. Against the order of the Tribunal the present appeal is preferred by the Revenue.

5. The only question which falls for consideration is as to whether the conditions laid down in the aforesaid revisions has been satisfied or not. Section 36(1)(vii) and Section 36(2) of the Act which are relevant for our purpose may be first taken note of:-

> "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- subject to the provisions of sub-sec. (2), the amount of any bad debt or part thereon which is written off as irrecoverable in the accounts of the assessee for the previous year"
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> Section 36(2)(i) imposes restrictions on the scope of such deduction, which reads as under:
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> "No such deduction shall be allowed unless such debt or part thereof has been taken into account in computing the income of the assessee of the previous year in which the amount of such debt or part thereof is written off or of an earlier previous year, or represents money lent in the ordinary of the business of banking of money-lending which is carried on by the assessee."

6. The Assessing Officer in his assessment order has also reproduced the aforesaid provision and on that basis he observed that following conditions for allowability of deduction of bad debt are to be satisfied:-

   i. If the assessee is not in the business of money lending or

income of Assessee (offered for taxation) in the current previous year or earlier years. It means that the debt claims must have been a revenue receivable.

ii. If the assessee is in the business of money lending ~~and~~ or banking, such debt should have been money lent in the ordinary course of such business.

7. It is not in dispute that the assessee is in the business of shares broking. The assessee has purchased the shares in question on behalf of one of his clients and against the purchase of the said shares, he had paid the money from his pocket. The brokerage received by the assessee was shown as income in his books of accounts of the immediate previous year. Since the balance amount to the extent of Rs. 50,30,491/- could not be received from the client on whose behalf the aforesaid shares were purchased, the assessee during the year had written off the said sum as a bad debt. It is not disputed by the learned counsel for the Revenue that the aforesaid amount which could not be recovered had become bad. The two fold submission was, however, as under:-

(i) It was not a 'debt'. This flowed from the ~~agreement~~ argument

of the shares himself, it should have been treated as investment by the assessee and thus, no debt' was to be recovered.

(ii) Second submission, which is based upon the first one, was that the loss thereon should have been treated as capital loss.

8. On this premise, it is sought to be argued that provisions of Section 36(1)(vii) read with Section 36(2) of the Act has not been satisfied.

9. Before we proceed to deal with this contention of the learned counsel for the Revenue, it would be apposite to take note of the discussion contained in the order of the Tribunal to understand the manner in which the Tribunal has dealt with this aspect.

> "2.2Before us, the Ed. A.R. for the assessee at the very outset pointed out that in view of the judgment of Hon'ble jurisdictional High Court of Delhi in case of Morgan Securities and Credits Pvt. Ltd. (292 ITR 339) burden was no longer on the assessee to establish that the debt had become bad before claiming the same as deduction u/s 36(1)(vii) in view of the amendments to the relevant provisions w.e.f. 1.4.1989. As regards the claim of bad debt in relation to the payment made by the assessee for purchase/sale of shares on behalf of the clients, it was submitted that this issue was also covered by the decision of Delhi bench of the Tribunal in case of Madhup Jam in I.T.A. No. 3950/Del/2004 for Assessment year 2001-2002 and the decision of the Mumbai Bench of the tribunal in case of Olympia Securities Ltd. in L.T.A. No. 4053/MumJ02. Reference was also made to the decision of Hyderabad Bench of

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170) in support of the claim. The ld. Sr. DR appearing for the revenue on the other hand placed reliance on the orders of authorities below.

2.3 We have perused the records and considered the rival contentions carefully. The dispute raised is regarding claim of bad debt, which had been disallowed on the ground that the assessee had failed to establish that the debt had become bad during the year and also on the ground that the debt had not been taken into account in the computation of income of the earlier year. The issue whether the assessee is required to establish that the debt had become irrecoverable during the year even after the amendments w.e.f. 1.4.1989 had been recently considered by the Hon'ble High Court of Delhi in case of Morgan Securities and Credits Pvt. Ltd. (292 ITR 339), in which the Hon'ble High Court after considering the circular No. 551 of CBDT noted that the amendments had been made with a view to ending litigation in relation to the practice that the assessee had to establish that the debt had become bad and held that there was no longer any burden on the assessee to establish that the debt had become bad. Therefore, the first limb of the issue raised in ground is covered by the judgment of Hon'ble High Court of Delhi (supra). As for the second aspect as to whether payment made by the assessee on behalf of the clients as a broker for purchase/sale of shares could be considered to have been taken into account in the computation of income of earlier years, we find that this such has also been considered by the Delhi bench of the tribunal in case of Madhup jain vide their order dated 31.5.2007 in I.T.A. No. 3950/Del/2004. In the said case, the tribunal held that the brokerage payable by the clients is a part of the debt and since the part of the debt had been taken into account in the computation of income, the entire debt including the purchase/ sale price paid by the assessee broker has to be taken as considered in computation of income and the conditions prescribed in Section 36(2)(i) were satisfied. The same view was taken by the Mumbai Bench of the tribunal in case Olympia Securities Ltd. in their order dated 21.12.2006 in I.T.A. No. 4053/M/2002. This aspect had also been considered by the Hyderabad bench of the Tribunal in case of ITW Singnode India Ltd. (110 TTJ 170). In that case, the bad debt had been claimed on account of inter corporate deposits (ICD) along with the interest due thereon. The tribunal noted that the words used in the Section 36(1)(vii) were "any bad debt or part thereof, and since

> entire debt including ICD had to be taken as having been considered in the computation of income. Accordingly, the tribunal held that the bad debt on account of ICD was allowable as deduction. The case of the assessee is thus covered by the decisions of the tribunal (supra) and, therefore, respectfully following these decisions and the judgment of Hon'ble jurisdictional High Court in case of Morgan Securities and Credits Pvt. Ltd. (supra), we set aside the order of Cit (A) and allow the claim of the assessee."

10. In so far as question of burden is concerned, learned counsel for Revenue did not dispute that the aforesaid aspect stands settled by the judgment of this case in Morgan Securities Credits Pvt. Ltd. (supra), note whereof has been taken of by the Tribunal. We are, thus, left with only this aspect as to whether payment made by the assessee on behalf of his client was the payment for purchase to sale of shares and therefore, non realization is to be treated as bad debt or it was to be treated as investment. As mentioned above, the assessee is carrying on business of shares and stock broking. He is member of National Stock Exchange. The shares were purchased by him on behalf of his clients. Merely because he made payments against those shares would not make it an investment by the assessee on his own behalf. We are of the opinion that the very basis of this argument is mis-conceived, namely, that the particular purchase should be treated as investment by the assessee only

has shown the income in his books of accounts as income from the brokerage. That itself shows that in so far as transaction in question is concerned, it was treated as a transaction of brokerage for purchase/sale of shares on behalf of his clients and it was not a transaction which was entered into by the assessee on his own behalf. This Court had occasion to deal with somewhat similar issue in ITA No. 415/2007 which appeal was decided against the Revenue by taking note of the following aspects:

> "ITA No. 415/2007
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> The admitted facts are that the assessee/respondent herein is a member of the Delhi Stock Exchange and is carrying on the business of shares and stock broking along with the allied activities such as broker/sub-broker, underwriters to new issues of shares, debentures and securities of all kinds, brokers and fixed deposit of companies, trading in shares, investment consultants, etc. The assessee had purchased shares of M/s. Mannu Finlease Ltd. in January and February 1996 on behalf of and on instructions from its sub-broker M/s. Glory Securities Ltd. Total value of these shares purchased by the assessee was Rs.1,06,10,247/- at an average price of Rs.55/- per share. The said sub-broker had made payment to the extent of Rs.64 lacs only. As remaining amount of Rs.41,37,881/- was not paid, the assessee did not deliver those shares to the sub-broker. However, in the said year, brokerage was shown as income in the Income-Tax Return, which was assessed as well. Since balance payment was not made in the next year also, presumably because of the reason that the price of shares fell from Rs.55/- per share to Rs.5/- per share, the assessee in its Income-Tax Return for the assessment year 2001-02 claimed deduction of Rs.41,37,881/- as 'bad debt' under Section 36(1)(7) of the Income Tax Act,

was affirmed by the Commissioner of Income-Tax in appeal, but the Income-Tax Appellate Tribunal, in the appeal preferred by the assessee, has allowed the said deduction vide its impugned orders dated 8.9.2006.

Learned counsel for the Revenue, in this appeal filed against the aforesaid order, has canvassed two submissions:-

(1) The aforesaid amount could not be treated as 'debt' at all under the provisions of Section 36(2) of the Act and, therefore, the question of treating it as 'bad debt' does not arise. (2) The assessee had not sold the shares to anybody else in the market and in the absence of such a sale, the assessee could not claim the aforesaid amount as 'bad debt'.

Insofar as the first submission of learned counsel for the Revenue is concerned, we do not find any force therein. As pointed out in the aforesaid admitted facts, the assessee had purchased the aforesaid shares on behalf of the sub-broker and, in fact, paid the amount of Rs.1,06,10,247/-. As against this amount, he received only a sum of Rs.64 lacs. The brokerage which was received in the aforesaid transaction was shown as income by the assessee in the previous year, which was taxed as such as well by the Assessing Authority. Under these circumstances, only because shares were not delivered for want of full payment, which was to be made by the sub-broker to the assessee, it cannot be said that there was no transaction between the parties. Once we proceed on the basis that there was a valid transaction between the assessee and the sub-broker and the assessee had to make payment on behalf of the sub-broker, which he could not recover to the extent of Rs.41,37,881/-, that sum has to be treated as 'debt'."

11. Following the aforesaid order we hold that the money receivable from the client has to be treated as 'debt' and since it became bad, it was rightly considered as 'bad debt' and claimed as such by the

the year in question, it was shown by the assessee in that manner. Since the brokerage payable by the client is a part of the debt and that debt had been taken into account in the computation of the income, the conditions stipulated in Sub-Section (2) of Section 36 read with Section 36(1)(vii) stand satisfied in this case. Hence, the question of law stands decided against the Revenue and in favour of the assessee. This appeal is accordingly dismissed.

(A.K. SIKRI)
JUDGE

(VALMIKI J. MEHTA)
JUDGE

August 27, 2009
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