



* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

+ **{ITA No.1153 OF 2008}**

% *Judgment reserved on:27.01.2011*
Judgment delivered on:31.01.2011

THE COMMISSIONER OF INCOME TAX . . . **APPELLANT**
Through : Mr. N.P. Sahni, Advocate

VERSUS

WHIRLPOOL OF INDIA LTD. . . . **RESPONDENT**
Through: Mr. Ajay Vohra, Advocate with
Ms. Kavita Jha, Mr. Somnath
Shukla,, Advocates.

CORAM :-

HON'BLE MR. JUSTICE A.K. SIKRI
HON'BLE MR. JUSTICE M.L. MEHTA

1. Whether Reporters of Local newspapers 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. This appeal pertains to assessment year 1996-97. In this year, in the return filed by the respondent assessee, it had *inter alia* claimed write off of ₹ 13,64,000/- as bad debt. According to the assessee this was the interest which had accrued in earlier assessment year and was payable by one M/s Harita Stock Ltd. (hereinafter referred to as 'HSL') on the loans advanced to the said company. Since the amount of interest became unrecoverable, the



assessee had treated it as bad debt written off. The Assessing Officer, however, disallowed the aforesaid amount and made additions to the extent of ₹ 13,64,000/-. The order of the Assessing Officer reveals that he had asked the assessee to explain the nature of the loan and also as to whether this loan pertains to the business carried on by the assessee. Since the assessee could not give any satisfactory explanation, the Assessing Officer added back this amount holding that it was not covered by provisions of Section 36(1) (a) of the Income Tax Act with reference to the write off of bad debts.

2. The assessee preferred appeal against order made by the Assessing Officer. Before the CIT (A), the assessee explained that it had entered into an agreement with HSL under which the assessee had advanced a short term loans of ₹ 6 crores and ₹ 23.34 crores to the said company on 8.2.1995 and 24.3.1995. As a security for the said amount, the assessee took possession of 5,84,500/- equity shares of TVS Whirlpool Ltd. (later renamed as Whirlpool Washing Machines Ltd.). Under these loan agreements HSL was to pay an interest at the rate of 10% on the aforesaid loans. According to the assessee, for the previous year ending 31.3.1995 interest to the tune of ₹ 13,64,219/- had accrued which was shown as income on which tax was paid. However, as the HSL could not repay the loan



within the time prescribed for the loan agreement, the assessee liquidated the shares given to it by way of security by the HSL. In this manner the loan amount was appropriated by the sale of those shares. However, since the interest amount remained unpaid and could not be realized the assessee had treated the same as bad debt written off in the year in question.

3. Accepting the aforesaid explanation, the CIT(A) held the view that conditions specified in Section 36(1)(vii) read with Section 36 (2) of the Act were fulfilled and the assessee was entitled to write off all the aforesaid amount. He, thus, deleted disallowance made by the Assessing Officer. Relevant portion of the order of the CIT (A) is as under :

“Having considered the submission of the appellant and finding from the facts of the case there is no doubt that the appellant pursuant to the agreement was entitled to payment of interest on the loan given. Thus according to the system of accounting adopted by the appellant mainly mercantile the amount of interest due for the concerned year was credited in the P & L account of the previous year i.e. for Assessment Year 1995-96. When subsequently such dues are not realized it would only be fair to allow deduction or write off of such amounts in the following year. The claim of the appellant in this regard is quite justified. Incomes accrued but which was never actually realized cannot really be taxed. **The disallowance made by the A.O. is therefore to be deleted.**”



4. The ITAT has accepted the aforesaid view taken by the CIT (A). While doing so, however, the reason given by the ITAT was that written off interest formed part of arrears and referring to the decisions of this court, it is held that there was compliance for claiming deductions under Section 36(1)(vii) of the Act.

5. In the aforesaid factual backdrop this appeal was admitted on the following question of law:

“Whether the ITAT was correct in law in confirming the order or CIT(Appeals) who deleted the addition of Rs.13,64,000/- made by the Assessing Officer by disallowance of the amount under the head interest written off?”

6. In opposing the aforesaid approach adopted by the ITAT as well as the CIT (A), submission of learned counsel appearing for the Revenue is that both the authorities below have not looked the matter in a proper perspective. He emphasized that the main reason because of which the Assessing Officer disallowed the interest written off was that the assessee had not been able to show that it was the activity of the assessee company to advance loans or the loan was given for business purposes. He pointed out that the CIT(A) did not discuss this aspect at all and in so far as ITAT is concerned, it went into altogether alien/irrelevant consideration viz it was not necessary for the assessee to prove that the debt had



become bad during the period. He thus, argued that unless it is proved that the loan was advanced for business purposes and therefore it was a debt which had become bad, the conditions stipulated in Section 36(1)(vii) read with Section 36(2) had not been fulfilled and therefore, the approach of the authorities was clearly erroneous.

7. On the other hand, in order to show that the loan given by the assessee to HSL was business loan and interest received thereon was treated as business income, Mr. Vohra, learned counsel appearing for the assessee had produced the copy of the balance sheet as on 31st March, 1996 which reflects the figures as on 31st March, 1995 as well. On the basis of entries made in this balance sheet, he has tried to demonstrate that the assessee was in fact into the business of advancing loan as well and substantial income by way of interest from loans was shown in these two years. He also produced copy of the assessment orders passed by the AO in respect of assessment year 1995-96 (i.e. immediately preceding year) when only income from interest was shown and accepted as business income. Learned counsel also produced copy of Memorandum of Association of the assessee in support of his submission that the advancing of loan is one of the objects objectives of the assessee.



8. Refuting the contention of Mr. Vohra, based upon the aforesaid documents, Mr. Sahni argued that neither CIT(A) nor ITAT have based their decision on these documents. There is not even any reference/discussion of these documents in the impugned orders. He has drawn out attention to the orders passed by the Assessing Officer wherein the Assessing Officer recorded as under:-

“The assessee has written off ₹ 13,64,000/- as outstanding against M/s Harita Stock Ltd. The assessee was asked to explain as to why this write off should not be disallowed. Vide its letter dated 05.10.1998, the assessee submitted that this amount represented interest owned by M/s Harita Stock Ltd. However the assessee has not explained the nature of the loan and also as to whether this loan pertained to the business carried on by the assessee, hence this amount is added back as being not covered by the provisions of Section 36 (1) (viii) with reference to the write off of bad debts.”

9. He thus submitted that it appears that these documents were not produced before the Assessing Officer and the CIT (A) as well as ITAT did not discuss the import of these documents. His further submission was that one cannot straightaway jump to the conclusion that the interest income or business income much can be said either way about these documents. His argument in this behalf was that from the documents produced it cannot be conclusively said that the assessee is engaged in the business of lending and borrowing when it's main business was of manufacturing of household gadgets and sale thereof. There was no finding either that the interest income was



assessed under the head “business income” in so far as two loan agreements dated 7th February, 1995 and 24th March, 1995 with M/s HSL are concerned, his comments were as under:-

Agreement dated 07.02.1995

This agreement is for giving short term loan to M/s HSL amounting to ₹ 600 lakhs without any interest to be repaid in 6 months and M/s HSL pledged 12 lakh equity shares of M/s TVS Whirlpool Ltd. (TWL) with signed blank transfer forms. No interest was payable on this loan.

Agreement dated 24.03.1995

As per this agreement a loan of ₹ 23,24,25,000/- was advanced to M/s HSL to be repaid in 12 months and interest @ 10% was to be charged. M/s HSL pledged 46,48,500 equity shares of TWL alongwith signed blank transfer forms. The assessee credited the interest of ₹ 13,64,000/- on this loan amount.

10. Another aspect which Mr.Sahni tried to highlight from these documents was that the assessee did not attempt to recover the amount. Instead it appropriated these shares and handed over it to its holding company M/s Whirlpool Corp., USA who in turn paid the amount of ₹ 29,24,25,000/- i.e. only the principal amount to the assessee. This shows that the transaction is a collusive transaction between the assessee and its holding company based in USA. Had this transaction taken place with an entity other than assessee’s holding company then the assessee would have sold these shares and the proceeds would have been appropriated towards the interest amount and principal amount leading to capital gain or capital loss. Mr. Vohra



tried to explain the aforesaid aspects and reiterated his submission that the interest income was the business income.

11. However, having considered the aforesaid submissions of both the counsel, we are of the view that the matter has not been examined by any of the authorities below in proper perspective. In fact, the documents which have surfaced now before us, have not been considered by these authorities. In order to arrive at a conclusion as to whether the interest income was business income or not, a deep scrutiny of these documents alongwith other evidence would be required. We are in agreement with the submissions of learned counsel for the Revenue to this effect.

12. We accordingly set aside these orders and remit the case back to the Assessing Officer who shall, on the basis of evidence produced, will record a specific finding as to whether advancing of loan is the business activity of the assessee or not and the loans advanced to M/s HSL was its business income or not. The Assessing Officer shall also be entitled to scrutinize and analyze the loan agreements with M/s HSL and will examine as to whether the sale of shares by the assessee to its parent company had arm length or not. Bases on the findings on these issues, the AO shall determine as to whether the bad debt written is to be allowed under Section 37 of the Act or not.



13. This appeal is disposed of in the aforesaid terms.

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(A.K. SIKRI)
JUDGE

A handwritten signature in cursive script, appearing to read 'M.L. Mehta', positioned above the printed name.
(M.L. MEHTA)
JUDGE

January 31, 2011
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