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

+ ITA 500/2009

COMMISSIONER OF INCOME TAX Appellant
Through Mr. Sanjeev Sabharwal, sr. standing
counsel.

versus

AUTO PINS INDIA LTD. Respondent
Through Mr. Ved Jain and Mr. Ashish
Aggarwal, Advocates.

CORAM:
HON'BLE MR. JUSTICE SANJIV KHANNA
HON'BLE MR. JUSTICE R.V.EASWAR

ORDER
09.04.2012

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By order dated 8th November, 2010, this appeal under Section 260A of the Income Tax Act, 1961 (Act, for short) filed by the Revenue impugning order of the Income Tax Appellate Tribunal dated 21st August, 2008 was admitted and the following two substantial questions of law were framed:-

- “1. Whether ITAT was correct in law in allowing the claim of assessee as bad debts written off amounting to 5.12 crores u/s 36(1)(vii) of the Act?
2. Whether provisions of Section 36(1) are at all applicable to the present case?



2. The aforesaid appeal relates to the assessment year 2003-04 and arises in the case of Auto Pin India Ltd., the respondent-assessee.

3. The respondent-assessee is engaged in manufacture and sale of automobile parts. For the assessment year in question, the assessee on 21st November, 2003, had filed its return of income declaring a loss of Rs.19,88,20,459/-. By assessment order dated 10th March, 2006, the total income of the assessee was assessed at loss of Rs.7,94,51,570/-. One of the major additions made by the Assessing Officer was disallowance of bad debt of Rs.5,12,78,675/- written off by the assessee. The entire amount was disallowed by the Assessing Officer after noticing that the bad debts were substantial and almost 50% of the turnover during the current year. It was observed that bad debts related to parties, to whom supplies were made, but had refused to make payment on the ground that the material supplied was defective. These supplies were made over a period of seven years, prior to the assessment year in question. It was observed that the assessee had earlier claimed bad debt of Rs.18,11,242/- in the assessment year 2000-01 and thereafter bad debt of Rs.5,12,78,675/- was claimed in the assessment year in question. The Assessing Officer observed that the assessee had not furnished year wise analysis of the bad debts claimed or



invoices year wise details. The documents furnished by the appellant were regarding the material supplied in the previous financial years, other than the financial year under consideration. He held that the assessee had also not furnished details of efforts made to recover the bad debt. The Assessing Officer concluded that the deduction towards bad debt cannot be allowed as it would give a distorted picture of business in the year in question. Accordingly, an amount of Rs.5,12,78,675/- was disallowed and added back to the income of the assessee.

4. The CIT (Appeals) deleted the said addition after referring to the case law on the subject and observed that the Assessing Officer had not disputed the factum that bad debts written off, relate to trading transactions. The case of the assessee was that the transportation cost and cost of lifting the rejected goods itself was prohibitive. The contention of the assessee was accepted.

5. The appeal preferred by the Revenue has been dismissed by the tribunal. The tribunal went into the factual matrix of the case and observed that full details of bad debt along with the dates on which invoice for sale was raised, copy of bill and copy of accounts for earlier years with efforts made by the assessee for recovery, were filed before the Assessing Officer,



but these were ignored. The assessee had given full details of the transactions with the respective parties with copy of ledger account, copy of vouchers etc. It was held that bad debt written off in the books of accounts was a bona fide claim and was allowable under Section 36(1)(vii) of the Act.

6. Learned counsel for the Revenue does not dispute that the bad debts were written off in the year in question. He, however, contends that the writing off bad debts of Rs.5.12 crores in one year itself would distort the income of the said year and this aspect has been ignored by the tribunal. It is submitted that allowing the claim would result in anomalies and distortion of the profit and loss account of the year in question.

7. The question, which arises for consideration, is whether bad debt should be allowed under Section 36(1)(vii) read with Section 36(2)(i) of the Act. The two provisions read as under:-

“36(1) Other deductions.-(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.”

“36(2) In making any deduction for a bad debt or part



thereof the following provisions shall apply-

(i) 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 course of the business of banking or money-lending which is carried on by the assessee.”

8. A combined reading of the aforesaid two clauses shows that two conditions are stipulated. (i) The amount should be written off as irrecoverable in the accounts of the assessee for the previous year. (ii) The amount, which is sought to be written off, should have been taken into account as income of the assessee in the previous year relevant to the assessment year or in the earlier previous years.

9. The tribunal has noticed that the assessee had made sales of Rs.231.57 crores to the parties in the seven previous years. In some cases, sale proceeds were not received on the ground that the material supplied was defective. Learned counsel for the Revenue has not been able to dispute and show that the provisions of Section 36(1)(vii) read with Section 36(2)(i) are not satisfied in the present case. We may only record that in the case of *TRF Ltd. Vs. Commissioner of Income Tax (2010) 323 ITR 397 (SC)*, it has been held that after 1st April, 1989, it is not necessary for



the assessee to establish that the debt, in fact, had become irrecoverable. It is enough if the assessee has been able to show that the bad debt is written off as irrecoverable in the profit and loss account of the assessee. The fact that these conditions are satisfied is not disputed by the Revenue.

10. The contention of the Revenue that writing off bad debts of Rs.5.12 crores in one assessment year would result in distortion of the profit and loss accounts of the year in question, is an attractive contention. But in the present case we are not inclined to examine the same. We may record here that there have been several instances where Revenue has disallowed warranty claims on the ground that it was merely presumptive and unascertained liability and could be only allowed when the claim was actually made. However, in view of the decision of the courts, warranty claims are now allowed if made on scientific and on rational basis/data. As noticed, the income returned in the year in question was at loss and the income assessed by the Assessing Officer is at a loss of more than Rs.7.94 crores. Writing off of bad debts would result in increase in the loss figure. There is no evidence or material on record to show that there was deliberate attempt by the assessee to delay writing off the bad debts in the earlier assessment years, which has resulted in understatement of income or



short recovery of tax. The Assessing Officer on the contrary had recorded that the assessee was unable to establish/show the efforts made to recover the amounts. We do not have before us and the Assessing Officer has not referred to the income returned by the assessee in the earlier assessment years or in the subsequent years. In a given case, if we have full facts and necessary details, we may examine the aforesaid contention, but in absence of factual details, we do not think that the said aspect should be examined in vacuum. We may only note that the learned counsel for the assessee has stated that in most of the earlier years, the assessee had shown taxable income and if bad debts were written off in the said years, it would have resulted in lower taxation or nil taxation.

10. With the aforesaid observation, we answer the aforesaid two questions of law in affirmative i.e. in favour of the assessee and against the Revenue. The appeal is disposed of without any order as to costs.

SANJIV KHANNA, J

R.V.EASWAR, J

APRIL 09, 2012
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