IN THE HIGH COURT OF HIMACHAL PRADESH, SHIMLA

ITA No.21 of 2004

Date of decision: September 1, 2009

Commissioner of Income Tax **..Appellant**

Versus

H.P. Financial Corporation **..Respondent**

Coram

The Hon'ble Mr. Justice Deepak Gupta, Judge.

The Hon'ble Mr. Justice V.K.Ahuja, Judge.

Whether approved for reporting?[1] No

For the Appellant.: ***Mr.Vinay Kuthiala, Advocate.***

For the Respondent: **Mr.Vishal Mohan, Advocate.**

Deepak Gupta, J.(oral)

This appeal by the Revenue has been admitted on the following questions of law:

> "1.Whether the Ld. ITAT was right in law in holding that the bad debts of Rs.19,04,000/- had been written off in the books of account, even though no corresponding entries to this effect had been made in the individual accounts of the loanees and thus the mandatory condition laid down in Section 36(1)(vii) of the Income-tax Act, was not satisfied?
>
> 2.Whether in the facts and in the circumstances of the case, the ld.ITAT failed to consider the amended provision of Section 36(1)(viia)(c) of the Income-tax Act, effective from 1.4.1992 vide which the claim for deduction of bad debts has to be restricted to 5%?"

The brief facts giving rise to the present appeal are that admittedly the assessee M/s.Himachal

---

[1] ***Whether the reporters of the local papers may be allowed to see the Judgment? yes***

Pradesh Financial Corporation (HPFC) is a financial institution which grants loans to Industries and Businessmen. In this case we are concerned with the assessment year 1994-95. In the return filed for the year in question the assessee claimed deduction of Rs.26.47 lakhs for the bad debts and written off debts.

The Assessing Officer came to the conclusion that the assessee was not entitled to claim deduction in respect of rs.19.04 lakhs. According to the Assessing Officer these debts had not been written off in the individual loans of the Company. An Appeal was filed by the assessee before the CIT (Appeals) who came to the conclusion that the HPFC was maintaining accounts under the cash system of accounting and had undertaken that in case recoveries are made from the defaulters on filing of civil suits then the amounts recovered shall be credited to the income under Section 41 of the Income Tax Act, 1961. Following the orders passed for the assessment years 1992-93 and 1993-94, the Commissioner, Income-tax allowed the appeal of the assessee. The Revenue filed an appeal before the ITAT which has been rejected. Hence, the present appeal.

The ITAT decided the matter in favour of the assessee. Admittedly, the Financial Corporation is following the cash system and has written off the bad

debts in according with the accounting system following by the Company. There is no error in the order of the ITAT. The first question is accordingly decided in favour of the assessee and against the Revenue.

With regard to the second question, Section 36(vii-a)(c) of the Income Tax Act at the relevant time read as follows:

> "36(vii-a) in respect of provision for bad and doubtful debts made by –
>
> c) a public financial institution of a State Financial Corporation or a State Industrial Investment Corporation, an amount not exceeding 5% of the total income (computed before making any deduction under this clause and chapter VI-A)"

This section was inserted by the Financial Act No.2 of 1991 w.e.f. 1.4.1992 and therefore applies to the assessment year in question. This section clearly provides that a financial corporation cannot make a provision for a bad debt exceeding 5% of its total income computed before making any deduction under Section 36(vii-a) and Chapter VI-A. Admittedly this section was not taken into consideration by any of the authorities i.e. the Assessing Officer, CITA or the learned Tribunal. It appears that since this section had just then been introduced the income tax authorities were not aware of the same. Even if the Financial Corporation had correctly written off the bad debts, as held by us above, it could

only claim deduction in terms of the aforesaid section. Therefore, the authorities were bound to take note of this section while considering the case of the assessee. Since this has not been done we have no other option but to set-aside the assessment orders passed by the authorities and remand the case to the Assessing Officer who shall decide the same in the light of the observations made hereinabove and after taking into consideration the provisions of Section 36(vii-a) of the Act.

Question No.1 is answered in favour of the assessee and against the revenue, Question No.2 is answered in favour of the Revenue and the case is remanded to the Assessing Officer.

(Deepak Gupta), J.

September 1, 2009 (V. K. Ahuja), J.
PV