IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 06.07.2005

CORAM

THE HON'BLE MR.MARKANDEY KATJU, CHIEF JUSTICE
and
THE HON'BLE MR.JUSTICE F.M.IBRAHIM KALIFULLA

T.C.No.157 of 2003

Commissioner of Income Tax,
Tiruchirapalli. ..Appellant.

Vs.

M/s.Micromax Systems (P) Ltd.,
Tiruchirapalli. ..Respondent.

PRAYER: Appeal preferred against the order of the Income-tax Appellate Tribunal Madras 'C' Bench dated 19.03.2003 passed in ITA No.513/Mds/1999. Assessment year 1997 - 98 and PAN/GI.No.M-60 order dated 30.7.98 on the file of Asst Commissioner of Income Tax Campany Circle, Tiruchi and IT/WT/GT/ Appeal No.152/98-99 order dated 31.12.98 on the file of Commissioner of Income Tax (Appeals) XIII (I/C), 121 Mahatma Gandhi Road, Chennai 34.

For Appellant :: Mrs.Pushya Sitaraman Senior Counsel for IT

For Respondent :: Mr.V.S.Jayakumar

JUDGMENT

THE HON'BLE THE CHIEF JUSTICE

This appeal under Section 260(A) of the Income-tax Act has been filed by the department challenging the order of the Income-tax Appellate Tribunal dated 19.03.2003 by which the appeal of the revenue has been dismissed by the Tribunal.

2. The appeal was admitted by the Court on the following substantial questions of law:-

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" 1. Whether in the facts and circumstances of the case, the Tribunal was right in allowing the assessee's claim for a bad debt, when the bad debt had not actually been written off in the books of account?

2. Whether in the facts and circumstances of the case, the Tribunal was right in allowing the claim for bad debt on the ground that the provision had been shown under the head expenditure in the annual report of the assessee company?

3. Whether in the facts and circumstances of the case, and in view of the provisions of Section 36(vii), an assessee other than a banking company can be allowed a claim for a bad debt on the basis of a mere provision?"

3. We have heard learned counsel for the parties and perused the record. The relevant assessment year is 1997-98. For this year the assessee claimed bad debt of Rs.3 lakhs. The Assessing Officer disallowed it on the ground that it was shown as a provision for bad and doubtful debts in the books of the assessee, but the assessee had not actually written off the bad debt of Rs.3 lakhs as irrecoverable in its books of account.

4. The assessee is a limited liability company, manufacturing control systems and equipments. It received three orders from M/s. Ignifluid Boilers India Limited for Rs.15 lakhs, Rs.16,17,000/- and Rs.1,50,000/- respectively. The orders were completed on 03.02.1996 and invoices were raised. The customer thereafter made part-payment and confirmed the balance of Rs.9,93,350/- as on 29.07.1996.

5. The assessee tried to realise the balance from the customer by follow-up letters, fax messages and telephone calls on several occasions, but despite its efforts the entire balance could not be collected. Thus, though the assessee was able to collect some amounts there was a balance sum of Rs.5,43,350/- of which Rs.3 lakhs was written off in the previous year relevant to the assessment year 1997-98 and the balance of Rs.2,43,250/- in the next previous year relevant to the subsequent assessment year. Though the amount of Rs.3 lakhs was debited with the noting "provision for bad debts" it was alleged by the assessee that the debt had in fact become bad.

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6. The assessee appealed to the Commissioner of Income-tax (Appeals), who by his order dated 31.12.1998 allowed the appeal and decided in favour of the assessee. Aggrieved against that order the department preferred an appeal before the Tribunal which has been dismissed by the impugned order.

7. The Tribunal has observed in paragraph – 4 of its order as follows:-

> "From the facts, it is seen that the assessee had taken lot of efforts to collect the debt. While debiting a sum of Rs.3 lakhs the assessee had claimed entire bad debt during this year and the next year. Though the nomenclature used is 'provision', it is seen that the claim of bad debt had to be allowed. At the time of hearing, the learned counsel for the assessee filed Sixth Annual Report (1997-98) wherein at page No.9, the provision for bad debts had been clearly stated under the head 'Expenditure'. Therefore, I do not find any infirmity in the order of the learned CIT(A) directing the A.O. to allow the bad debts as claimed by the assessee. The order of the learned CIT(A) is confirmed. It is ordered accordingly".

8. The relevant portions of Section 36 of the Income-Tax Act after the amendment w.e.f. 01.04.1989 reads as follows:-

> "Sec-36(1): The Deductions provided for in the following clauses shall be allowed in respect of 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
>
> (viia) in respect of any provision for bad and doubtful debts may be –
>
> (a) a scheduled bank…
>
> (b) a bank being a bank incorporated by or under the laws of a country outside India….
>
> (c) a public financial institution…..

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36(2) – In making any deduction for a bad debt or part thereof, the following provisions shall apply –

(iv) where any such debt or part of debt is written off as irrecoverable in the accounts of the previous year, being a previous year relevant to the assessment year commencing on the 1st day of April, 1988 or any earlier assessment year, and the Assessing Officer is satisfied that such debt or part became a bad debt in any earlier previous year not falling beyond a period of four previous years immediately preceding the previous year in which such debt or part is written off, the provisions of sub Section (6) of Section 155 shall apply".

9. The learned counsel for the department submitted that a mere provision of bad debt is not sufficient to get the benefit of the above provision and it is only when the debt is actually written off as irrecoverable in the books of account that a claim for bad debt can be allowed as a deduction.

10. On the other hand, the submission of the learned counsel for the assessee is that it was only by an inadvertent mistake committed by the assessee that a narration was made in the profit and loss account as "provision for bad debt".

11. On the facts of the case, we are of the opinion that this appeal has to be allowed.

12. In this case, the provisions of Section 36(vii a) of the Act are not attracted, since the assessee is admittedly not a bank or a public financial institution. It is only a company manufacturing control systems and equipments. Hence only Section 36 (vii) of the Act would apply and not Section 36(vii a) of the Act.

13. The difference between clause (vii) and clause (vii a) of Section 36(1) of the Act (after the amendment with effect from 01.04.89) is significant. Clause (vii) clearly mentions that the bad debt or part thereof can be allowed only if it is written off as irrecoverable in the accounts of the assessee for the previous year.

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14. No doubt prior to 01.04.89, even if the debt had not been written off, it could be allowed as a "bad debt" if the assessee could establish that the debt had in fact become bad. However, after the amendment with effect from 01.04.89, there is an additional requirement in Section 36(1)(vii) namely that the "bad debt" should be written off as irrecoverable in the accounts of the assessee for the previous year. Hence unless it is written off as irrecoverable in the accounts, it cannot be allowed as a "bad debt".

15. It may be mentioned that prior to the amendment of Section 36(1)(vii) with effect from 01.04.89, clause (vii) of Section 36(1) reads as follows:-

> " subject to the provisions of sub-section(2), the amount of any debt or part thereof which is established to have become a bad debt in the previous year."

16. Thus prior to 01.04.89, even if the debt has not been written off as irrecoverable in the accounts of the assessee, it could still be allowed as a bad debt if the assessee could establish that in fact it had become a debt in the previous year. After the amendment by Act 4 of 88 with effect from 01.04.89, the essential requirement for a claim of 'bad debt' to be allowed is that it should have been written off as irrecoverable in the accounts of the assessee for the previous year. Thus for and from the assessment year 1989-90, the requirement as to the writing off of the debt as irrecoverable has become essential for a claim of 'bad debt' to be allowed.

17. Thus, it is now a mandatory condition that deductions can be allowed as bad debts only when it is actually written off as irrecoverable in the accounts and not on the basis of a mere provision.

18. Learned counsel for the assessee has relied on the decision of the Supreme Court reported in C.I.T v. ASEA Ltd, 258 ITR 407 where deduction of a bad debt was allowed on the basis of a provision. However, the above decision was rendered in the context of Section 36(1)(vii) as it stood prior to 1989. Hence the said decision is clearly distinguishable.

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19. Learned counsel for the assessee then contended that the revenue never objected to the fact of the debt becoming bad in the year of account, but only objected to the fact that it has not been written off as irrecoverable in the assessee's accounts.

20. In our opinion, the principle of plain or literal interpretation has to be applied in interpreting a taxing statute. As observed by Lord Cairns in Partington v. Attorney General, (1869) LR 4HL 100 : -

> " If the person sought to be taxed comes within the letter of the law he must be taxed, however great the hardship may appear to the judicial mind. On the other hand if the Court seeking to recover the tax cannot bring the subject within the letter of the law, the subject is free, however apparently within the spirit of the law the case might otherwise appear to be.

21. Thus, in interpreting a taxing statute one cannot go by the notion as to what is just and expedient vide CIT v. Shahzada Nand, AIR 1966 SC 1342). In IRC v. Hinchy, (1960) AC 748 the House of Lords held that a provision in the Income Tax Act, 1952 for a statutory penalty (for making an incorrect return of income) of 20 pounds and trebling 'the tax which he ought to be charged under this Act' referred not to the tax on the amount which the taxpayer had failed to declare, but to the whole tax which he ought to be charged for the relevant year, notwithstanding the extravagant consequences which flowed from giving the words their natural meaning.

22. The Supreme Court of India has held that equity is out of place in tax laws (vide CIT v. Firm Muar , AIR 1965 SC 1216). In CIT v. Madho Prasad Jatia, (1976) 4 SCC 92, it held that there could be no consideration of equity if the language of the provision was plain and clear, but where it was not, and two interpretations were possible, the one in consonance with equity and fairness should be preferred."

23. The principle of strict interpretation of taxing statutes was best enunciated by Rowlatt, J in his classic statement (vide Cape Brady Syndicate v. IRC, (1921) 1 KB 64 cited with approval in AIR 1968 SC 623): -

> "In a taxing statute one has to look merely at what is clearly said. There is no room for any intendment. There is no equity about a tax. There is no presumption as to a tax. Nothing is to be read in, nothing is to be implied. One can look fairly at the language used."

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24. In AV Fernandez v. State of Kerala, AIR 1957 SC 657 the Supreme Court of India stated the principle as follows: -

> " If the Revenue satisfies the Court that the case falls strictly within the provisions of the law, the subject can be taxed. If, on the other hand, the case is not covered within the four corners of the taxing statute no tax can be imposed by inference or by analogy or by trying to probe into the intentions of the legislature and by considering what was the substance of the matter."

25. In CIT v. G.Hyatt, AIR 1971 SC 725 the question was whether under Section 17(3) of the Income Tax Act, 1961, the interest on the assessee's own contribution to an unrecognized provident fund could be treated as salary. The Supreme Court of India held that the language of Section 17(3) was plain and unambiguous, and hence the said amount was not salary but income from other sources and taxable under Section 56.

26. In Polester & Co. Ltd v. Addl.Comm. of Sales Tax, AIR 1978 SC 897 the question was whether sales outside Delhi would also be included in taxable income. The Supreme Court held that the section used the word 'resale' simpliciter, and hence it referred to all resales and could not be limited to resales within Delhi alone. Thus the Supreme Court went by the plain language of the statute, and did not speculate on the intention of the legislature.

27. In Hemraj Gordhandas v. HH Dave, Asst.Collector, (1978) 2 ELT 350, the Supreme Court of India considered the language of a notification under the Central Excise Tariff and held that all that was required for claiming an exemption was that the cotton fabric must be produced on power looms owned by the co-operative society. There was no further requirement in the language of the notification that the cotton fabric must be produced by the society for itself. The Supreme Court refused to go into the question of the intention behind the exemption since the language of the notification was clear.

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28. In Assessing Authority v. East India Cotton Mfg Co Ltd., (1981) 48 STC 239 the concessional rate under the Punjab Sales Tax was payable if certain raw materials were used in the manufacture of goods for sale. The contention of the assessee was that the word used in the Act was ' for sale' and not 'for sale by him' and hence the goods sold by a third party were also covered by the provision.

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This contention was accepted by the Supreme Court which followed the literal rule of interpretation.

29. In CWT v. Ellis Bridge Gymkhana, AIR 1988 SC 120 the Supreme Court held that the word 'individual' in the charging section could not be stretched to include an association of persons. The Court held that the charging section had to be construed strictly, and if a person could not be brought within the ambit of the charging section by clear words, he could not be taxed at all.

30. In the present case, it can be seen that the assessee did not write off the debt in question as irrecoverable in his accounts for the previous year. Hence on the plain language of Section 36(1)(vii) of the Act the debt cannot be allowed as a 'bad debt'. It may be that the assessee committed an inadvertent mistake, but we cannot go by notions of equity in tax matters. Making a provision is not the same thing as writing off a debt as irrecoverable.

31. For the reasons given above, the impugned judgment of the Income Tax Tribunal, and of the CIT (Appeals) with respect to the claim of the assessee regarding bad debts are set aside, and the order of the Assessing Officer is restored. The appeal is allowed.

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Sd/
Asst.Registrar

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Sub Asst.Registrar

Copy to:

1. The Commissioner of Income Tax,
Tiruchirapalli.

2. The Asst Registrar,
Income Tax Appellate Tribunal,
Rajaji Bhavan, 3rd Floor,
Besant Nagar, Chennai 90.

3. The Asst Commissioner of Income Tax,
Company Circle, Tiruchy.

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4. The Commissioner of Income Tax,
Appeals XIII (I/C),
121, Mahatma Gandhi Road,
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+ 1 cc to M/s Pushya Sitaraman, Advocate SR No.28346

+ 1 cc to Mr.V.S. Jayakumar, Advocate SR 28370

JE(CO)
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Pre-delivery Judgment
in T.C.(A) No.157 of 2003

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