(2009) 12 MAD CK 0112

Madras High Court

Case No: T.C. (A) No. 490 of 2004

Commissioner of Income Tax	APPELLANT
Vs	
V. Ramakrishna and Sons Ltd.	RESPONDENT

Date of Decision: Dec. 23, 2009

Acts Referred:

- Income Tax Act, 1961 - Section 143(3), 251, 36(1), 36(2), 41(1)

Citation: (2010) 236 CTR 433 : (2010) 326 ITR 315

Hon'ble Judges: M.M. Sundresh, J; K. Raviraja Pandian, J

Bench: Division Bench

Advocate: J. Narayanaswamy, for the Appellant; R. Venkatanarayanan, for Subbaraya Aiyar, for the Respondent

Final Decision: Dismissed

Judgement

M.M. Sundresh, J.
The Revenue has come on appeal against the order passed by the Income Tax Appellate Tribunal, Chennai "B" Bench in I. T. A. No. 2272/Mds/1994 dated September 23, 2003 for the assessment year 1989-90 by raising the following substantial questions of law:

(1) Whether on the facts and in the circumstances of the case the Income Tax Appellate Tribunal was right in holding that the claim of bad debts to the tune of Rs. 25,98,579 made by the assessee-company in respect of money lent to its subsidiary company should be allowed as a deduction ?

(2) Whether on the facts and in the circumstances of the case the Income Tax Appellate Tribunal was right in law in holding that the bad debt amounted to Rs. 25,98,579 was deductible as a trading loss, since the writing off of the said amount was made in the course of the assessee''s business ?"

2. The facts of the case in a nut-shell are as follows:

The assessee has been involved in money-lending business. The assessee''s memorandum and articles of association permitted money-lending business. The assessee also had a subsidiary company. Prom the year 1969 onwards, the assessee had been financing monies to its subsidiary company apart from financing various other concerns and interest was charged on the amount financed by the assessee to its subsidiary company from the assessment years 1970-71 to 1977-78. The said interest offered by the subsidiary company has been assessed as business income. Thereafter, due to commercial expediency, the assessee did not charge the interest. The subsidiary company became weak and, therefore, in order to prop-up financial business interest, the assessee paid further amounts totalling Rs. 26,08,278.79 which was due as on September 30, 1988, after collecting a sum of Rs. 10,000 a sum of Rs. 25,98,278.79 was written off as bad debt.

3. The subsidiary company paid back the outstanding principal amount of Rs. 7,50,000 but there was an outstanding interest of Rs. 4,13,567.22. The assessee also had shares in the subsidiary company which were sold after the subsidiary company faced difficulties. The assessee also stood as a guarantor for the credit facilities granted by the bank to the subsidiary company. In view of the transfer of the shares belonging to the assessee in the subsidiary company, the said company thereafter ceased to be a subsidiary company. In spite of the fact that the advances have been made by the assessee in favour of the subsidiary company to prop-up the sagging business, the same could not be run.

4. Therefore, under those circumstances, the assessee has written off the loans advanced to the subsidiary company in its books of account as bad debts for the assessment year 1989-90. The Assessing Officer in the assessment passed u/s 143(3) read with Section 251 of the Income Tax Act, 1961, has disallowed the bad debts claims for a sum of Rs. 25,98,579. The Assessing Officer has held that when the interest was not received from the assessment year 1978-79, the payment of further advances by the assessee in favour of the subsidiary company cannot be construed as an advancement of loans during the course of business and, therefore, the assessee was not entitled to claim bad debt. The Assessing Officer has also held that the amount having been given only to tide over the financial difficulties of the subsidiary company, the same cannot be construed as a loan or advance made in the course of business.

5. Being aggrieved by the order passed by the Assessing Officer, the assessee filed an appeal to the Commissioner of Income Tax (Appeals) in Appeal No. 491/92-93. The first appellate authority has allowed the appeal by holding that there is no dispute regarding the genuineness or bona fides of the transactions, the fact that for the subsequent advances no interest was received by itself cannot be a ground for disallowance as bad debt and the amount having been given towards commercial expediency in order to protect the interest of the assessee to prop-up the sagging business of the subsidiary company, the same would amount to a bad

debt allowable u/s 36(1)(vii) of the Income Tax Act. The appellate authority also held that at the time of writing off the debt, the subsidiary had huge accumulated loss. It is further held by the appellate authority that the amount lent by the assessee was also assessed to tax u/s 41(1) of the Income Tax Act, 1961, in the case of the subsidiary company. It was further observed that in any case, the debt will have to be construed as trade debt in the course of the appellant''s business. Accordingly, the first appellate authority has allowed the appeal filed by the assessee in so far as the disallowance of the bad debt is concerned.

6. Not being satisfied with the same, the Revenue filed a further appeal to the Tribunal and the Tribunal also confirmed the order of the first appellate authority by holding that inasmuch as the debts having become irrecoverable, the same have been rightly written off as bad debts. Challenging the said order, the Revenue has filed the present appeal.

7. The contentions of the learned Counsel appearing for the Revenue:

Mr. J. Narayanaswamy, learned Counsel appearing for the Revenue, submitted that the advances have been made by the assessee to the subsidiary company not in the course of its business. The assessee after knowing that interest was not paid by the subsidiary company periodically has given further amounts only in order to tide over the difficulties of the subsidiary company and, therefore, the same cannot be construed as a business transaction of the assessee. The learned Counsel further submitted that though the assessee is entitled to the outstanding amount from 1977-78, the advances made by the assessee after the same cannot be written off as bad debts. It is a further submission of the learned Counsel that when no interest is charged on the money advanced, it cannot be considered as a debt incurred in the course of the business and, therefore, the same cannot be construed as a bad debt. Hence, the learned Counsel sought for the appeal to be allowed.

8. The submissions of the learned Counsel appearing for the assessee:

Shri R. Venkatanarayanan learned Counsel for M/s. Subbaraya Aiyar appearing for the assessee submitted that in the present case on hand there is no dispute to the fact about the money-lending business of the assessee. There is also no dispute about the advancing of money by the assessee in favour of the sister concern from 1969 onwards. The mere fact that no income was received subsequent to 1978 alone cannot be a ground to disallow the claim of bad debt. The Assessing Officer has not doubted the genuineness or bona fides of the transactions. Further, the assessee has made the payment in order to protect its interest which is by way of recovering the amount due to the assessee, to sustain the value of its share and to get over the liability as a guarantor. Moreover, the subsidiary company has suffered huge loss and, therefore, under those circumstances, the first appellate authority as well as the Tribunal have correctly concluded that the bad debts claimed by the assessee are allowable.

9. We have heard the learned Counsel appearing for the Revenue as well as the assessee.

10. The facts involved in the present case are not in dispute. The assessee is doing the business in financing. The memorandum and articles of the association of the assessee also clearly indicate the said fact of money-lending. The assessee has lent money in favour of the subsidiary company right from 1969 onwards. The assessee also stood as a guarantor to the credit facilities obtained by the subsidiary company from the bank and also held shares. It is also not in dispute that the subsidiary company paid the principal amount in favour of the assessee for a sum of Rs. 7,50,000. However, what was not paid was the interest from 1978 onwards. The assessee made further payment thereafter. The said payments have been made during the course of the business and also due to commercial expediency, since the business of the subsidiary company was sagging requiring to be propped-up. Thereafter, the amount became irrecoverable and the assessee also suffered a loss towards the sale of the shares which resulted in losing the subsidiary company. Hence, under those circumstances, the assessee was constrained to write off the money advanced in favour of the subsidiary company as irrecoverable amounting to bad debts.

11. The above said facts would clearly show that the transaction of the assessee being the financing company with the subsidiary company is genuine and bona fide. The subsidiary company has been paying the interest earlier and thereafter paid the principal amount. The assessee paid further advances in its own interest with a view to recover the amount given earlier, to sustain a share and to avoid the guarantee being invoked. The mere fact that the payment of money after the stoppage of interest from the subsidiary company by itself cannot be a ground to hold that the transactions are not in the course of the business. There is no bar in law for financing any amount by the assessee in favour of the subsidiary company.

12. It is also to be seen the income received by the assessee from the subsidiary company by way of interest was subjected to tax and the advance made by the assessee to the said company was also subjected to tax. It is also an admitted fact that at the time of writing off the debt, the subsidiary company has accumulated huge loss which was twice the amount due as the paid up capital. The assessee also suffered a loss while selling the shares of the subsidiary which resulted in the subsidiary company ceasing to be the subsidiary of the assessee.

13. Therefore, the abovesaid circumstances would clearly show that the money advanced by the assessee has become irrecoverable and the same was given during the course of the business. Further, admittedly, the subsidiary company was paying the interest regularly earlier and thereafter paid the principal as well. What was not paid by the subsidiary company was only the interest and there was no principal amount due at the time of advancing the amount thereafter. The advances made by the assessee were also utilised by the subsidiary company for the purpose for which

the same was obtained which is to run the foundry. The abovesaid facts would also indicate that the amount has been given out of commercial expediency as well.

14. An identical issue was considered by the Calcutta High Court in Commissioner of Income Tax Vs. Gillanders Arbuthnot and Co. Ltd., wherein, it has been observed as follows (page 766):

The Appellate Assistant Commissioner held, on appeal, that the amount was not allowable u/s 36(2) as the amount could not be said to have been advanced in the course of any money-lending business in a normal or prudent manner. There was an appeal before the Tribunal and the Tribunal considered the rival contentions and the authorities cited before the Tribunal and thereafter observed as follows:

We have given careful and anxious thought to the rival submissions made by both the sides. In our opinion, the assessee''s case is well founded. From the facts as narrated in the earlier portion of this order, it would be clear that the assessee-company was engaged in various business activities, one of which was to guide the destinies of the subsidiaries by financing them or advancing loans to them in a sustained fashion and over a period of time. The loans advanced to the subsidiary concerned in this case were not an isolated instance but were a part of the formidable list of such advances made by the assessee-company to its subsidiaries, some of which were managed by it as managing agent. It may be repeated here that the employees of the assessee-company were on the board of directors of the subsidiary company concerned and it is also a fact that the income of the subsidiary showed an upward trend after the share capital of the subsidiary company was taken over by the assessee-company. No doubt, the balance-sheet of the subsidiary as on December 31, 1965, does not inspire much confidence. However, the subsidiary was engaged in the business of consulting engineers and, by its very nature, the share capital and the assets were not formidable. The financial position was undoubtedly weak but the assessee did its very best to prop up the sagging finances of the subsidiary and bolster up its declining business. The assessee was intimately connected with the various subsidiaries and the interests of the subsidiaries were, therefore, vitally connected with the assessee''s business interests which were diverse. The memorandum of association permitted the assessee-company to advance the loans and the fact that the assessee did not charge any interest to this particular subsidiary, in fact, speaks well of the business prudence of the assessee-company and does not indicate any mala fides. It was only when the subsidiary concern went into liquidation and when the liquidator clearly wrote on March 31,1965, to the assessee-company that there were absolutely no chance of effecting any recovery from the subsidiary that the assessee chose to write off this debt and claim it in its assessment.

Since we have held that the assessee was engaged in the business as a holding company of financing its subsidiaries, the other arguments of the Departmental representative that the assessee''s claim cannot be allowed against the dividend

income, if at all, loses its significance. Even if the amount cannot be treated as a bad debt in the sense that it was not an advance in the course of money-lending business, it can certainly be allowed as a trading loss incurred by the assessee in the course of its business. This alternative claim definitely is reasonable and can be entertained as it is not necessary to make further investigation into the facts for entertaining it. We agree with the assessee''s representative, Dr. Pal, that some of the observations of the Supreme Court in the two decisions relied upon by him are of assistance to him. No doubt in the cases decided by the Supreme Court the question was about the allowability of the loss in respect of the managing agency income but here we have given a finding that the assessee was engaged in the business of financing its subsidiaries or that, at any rate, financing the subsidiaries was incidental to the assessee''s main business activities which were diverse in nature. Therefore, the loss incurred by the assessee has to be allowed as on business account.

As the Tribunal held that the assessee was engaged in the business as a holding company for financing its subsidiaries and on that basis and the other facts found by the Tribunal and the fact that the loan was in fact given, which is also a finding of fact, and in the usual course of business the assessee gave loans, the question now posed before us is really a question based on facts. But no question of challenging the finding of fact as perverse or based on no materials has been referred to this Court. In fact, that question has been refused and if the findings stand then the conclusion of the Tribunal on those findings become irresistible.

15. We are in agreement with the reasoning of the Bench of the Calcutta High Court which considered the identical issue and held in favour of the assessee.

16. In the present case on hand, both the first appellate authority as well as the Tribunal have considered the materials on record and came to the conclusion that the transactions involved are true and genuine. They have also held that the advances have been made during the course of the business and they have become irrecoverable as bad debts and, hence, the assessee is entitled to the benefit u/s 36(1)(vii) of the Income Tax Act, 1961. The said decision being based upon the findings of fact, the same cannot be agitated before this Court. The question as to whether a debt had became bad or not is a pure question of fact and, therefore, the same cannot be construed as a question of law.

17. In Travancore Tea Estates Co. Ltd. Vs. Commissioner of Income Tax, Cochin, , the hon''ble Supreme Court was pleased to hold that the question whether a debt had become bad or point of time when it became bad were pure questions of fact and no question of law. Similarly, in Amarchand Sobhachand Vs. Commissioner of Income Tax, Madras, , the hon''ble apex court was pleased to hold that even if the conclusion registered by the Tribunal was not supported by proper discussion of the material before it, if the findings were supported by evidence on record, the same cannot be interfered with.

18. Therefore, we are of the opinion that the appeal filed by the Revenue is liable to be dismissed both on the facts and law. Accordingly, the questions of law raised by the Revenue have been answered in the affirmative and against the Revenue and, hence, the appeal is dismissed.