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

\+ **ITA No.174 of 211**

Reserved on: 13th October, 2011

% Decision Delivered On: 18th November, 2011

CIT . . . APPELLANT

Through: Mr. Sanjeev Sabharwal, Sr. Standing Counsel.

VERSUS

SUMANGAL OVERSEAS LTD. . . .RESPONDENT

Through: Mr. Ved Jain, Advocate.

CORAM :-

HON'BLE THE ACTING CHIEF JUSTICE
HON'BLE MR. JUSTICE SIDDHARTH MRIDUL

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, Acting Chief Justice

1. Penalty of ₹73,85,322/- imposed upon the respondent assessee by the Assessing Officer (AO) under Section 271(1)(c) of the Income Tax Act (hereinafter referred to as 'the Act') was affirmed by the CIT (A). However, the Income Tax Appellate Tribunal ('the Tribunal' for brevity) has reversed the view taken by the AO and the CIT (A) and deleted the said penalty. It is under these circumstances,

present appeal is preferred by the Revenue questioning the wisdom of the Tribunal contained in its order dated 30.10.2009 and the appeal was admitted on the following substantial question of law:

> "Whether on the facts and in the circumstances of the case, the ITAT erred in law and on merits in deleting the penalty of Rs.73,85,322?- levied u/s 271(1)(c) of the Income Tax Act, 1961?"

2. The reason for initiating penalty proceedings was that the AO in the assessment order framed on 29.12.2006 in respect of assessment year 2004-05 held the view that the assessee had falsely claimed bad debts of ₹2,05,86,262.75/- The assessee had given various advances to its suppliers which amounts to ₹2,89,56,836.75/-. Out of these amount, the aforesaid amount of ₹2,05 Crores was written off as bad and doubtful advances. The AO took the view that the prerequisite conditions for writing off the amount as bad debts had not been satisfied, as it was included in the income of the previous year and therefore, there was no question of treating is as bad debts under provision of Section 36(1)(vii) and Section 36(2) of the Act. The assessee had not challenged the order of the AO.

3. In the penalty proceedings, the AO held that the aforesaid finding had become final and conclusive and it clearly reflected the falsity of claim preferred by the assessee.

4. The CIT(A) dismissed the appeal of the assessee by holding that undetection of the said claim, as 97% of the returns are not subjected to scrutiny, would have rendered such false claim to be untaxed. The claim on bad debts to be patently wrong and erroneous in law is manifest in the conduct of the assessee in admitting the falsity of the claim and not preferring any further appeal. The CIT (A) observed that the assessee was a corporate whose accounts were duly audited by qualified Chartered Accounts and thus, the claim of *bona fide* mistake, due to lack of professional held is untenable on its very face. The CIT (A) rejected the claim of non-leviability of penalty on the ground that the assessment was a loss of ₹76,61,830/- in view of the provisions of Explanation 4(a) to Section 271(1)(c) of the Act.

5. The Tribunal, however, while deleting the penalty has examined the matter from a different perspective altogether. It is observed that no doubt, the claim could not be written off as bad debt. At the same time, however, going by the

nature of the transaction, viz., these were the loans and advances given by the assessee to the suppliers and were written off as unrecoverable, the same could have been allowed to be written off as business advance under Section 29 read with Section 37(1) of the Act, simply because the assessee made claim of deduction under a wrong head, viz., treating it as bad debt would not mean that the claim was false and therefore, penalty could not be imposed. This discussion is contained in the following paragraph of the Tribunal's order:

> "8. We have heard the rival contentions and perused the material on record. It has not been disputed that assessee had filed its return of income accompanied with Schedule E of accounts making a claim of doubtful advances written off. AO himself had observed that loans and advances to suppliers have been shown in the books of account, therefore, the correct proposition was the allowability of claim of the assessee in respect of business advances written off will fall u/s 29 read with Section 37(1). AO, however, proposed the addition on the ground that the same was not allowable as "bad debt" since these advances were not included in income as income in earlier years. Assessee on the proposition of AO realized that they were not included as income in earlier years and were not allowable a bad debt, therefore, the same was offer to tax specifically on this ground. In our view, the decision of Hon'ble Delhi High Court in the case of Escort Finance (supra) is not applicable to assessee's case as the same is applicable in the cases of allowances or claims, which are ex facie i.e. on the fact itself inadmissible. In this case, ex facie the assessee's claim was of write off of advances and not of bad debt.

> AO proposed the disallowance and accepted by the assessee as non-allowable being bad debts. In our view, the learned counsel has made out a proper case that assessee's specific claim was write off of business losses/advances which has not been examined at all. The learned counsel has relied on various case laws. In our view, the assessee had made proper disclosure of facts. The amount has been disallowed not as business advance, which was the actual claim of assessee but the same has been disallowed as bad debt on an impression that it was not included in the income of all the earlier years whereas there is no said requirement for allowability of business advances. Penalty should not be levied merely because it is lawful to do so, has been held by Hon'ble Supreme Court in the case of Hindustan Steels Ltd., 83 ITR 26. Relying on these facts and authorities, we hold that the penalty u/s 271(1) (c) is not impossible in assessee's case, which is deleted."

6. After hearing the counsel for the parties that we are of the opinion that it is a correct view taken by the Tribunal. Facts are not in dispute. The amount relates to advances to suppliers which were duly shown and declared by the assessee in the Profit & Loss account. The AO did not dispute the genuineness of these advances given. The stand of the assessee that the advances to the extent of ₹2,05,86,262.75/- had become irrecoverable was also not disputed by the AO. However, the assessee had shown the same in Profit and Loss Account under the head "bad and doubtful advances written off" and did not use the words "bad debts written off". During the assessment proceedings,

the AO treated the same as bad debts written off and for that reason applied the provisions of Section 36(1)(vii) of the Act and claiming that the conditions stipulated therein were not satisfied, viz., when it was not shown as income in the previous year, how it could be shown as debt written off.

7. It is trite law that during the penalty proceedings, it is open to the Tribunal to look into the transaction to see as to whether the claim was *bona fide* or it was bogus and result of falsehood. From that angle, when the Tribunal examined the matter, it found that on the facts of this case when advances given to the suppliers were not written off as irrecoverable, the same was allowable under Section 28 of the Act. A trading loss has a wider connotation than a bad debt. A bad debt may also be a trading loss, but a trading loss need not necessarily be a bad debt. There may be a bad debt which may not fall within the purview of Section 36(1)(vii) of the Act, but may well be regarded as one eligible for deduction incurred in the course of carrying on business will come under that category and will naturally enter into computing the net total income as the real profit

chargeable to tax cannot be arrived at without setting off legitimate trading loss.

8. On these facts, it is apparent that the claim was neither *mala fide* nor false. It was a *bona fide* claim preferred by the assessee, who had also disclosed all the facts relating to and material to the computation of his income. In these circumstances, the assessee fulfilled both the conditions to be outside the purview of Explanation (1) to Section 271(1)(c) of the Act. The case of the assessee is covered by the judgment of the Supreme Court in the case of ***CIT Vs. Reliance Petroproducts (P) Ltd.***, 322 ITR 158 (SC), where it was held that the assessee must be found to have failed to prove that his explanation is not only *bona fide*, but all the facts relating to the same and material to the computation of his income were also not disclosed by him. It was further held that the explanation must be preceded by finding as to how and in what manner the assessee had furnished inaccurate particulars of his income.

9. In fact, had the assessee pressed his claim in a proper manner during the assessment proceedings, he might have even succeeded in getting the said deduction allowed. Be as

it may, in such a case, the assessee cannot be fastened with penalty also.

10. We, thus, answer the question in favour of the assessee and dismiss this appeal.

ACTING CHIEF JUSTICE

(SIDDHARTH MRIDUL)
JUDGE

November 18, 2011
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