

IN THE HIGH COURT OF BOMBAY

Income Tax Appeal No. 43 OF 1997

HARSHAD J CHOKSI

Vs

THE COMMISSIONER OF INCOME TAX, BOMBAY CITY-IV

S J Vazifdar And M S Sanklecha, JJ

Dated : August 14, 2012

JUDGEMENT

Per : M S Sanklecha, J :

1. By this reference under Section 256(1) of the Income Tax Act, 1961 ('the Act'), the Income Tax Appellate Tribunal ('the Tribunal') has referred the following question of law for the opinion of this court.

"Whether on the facts and in the circumstances of the case, the 'vatav kasar' of Rs.44,98,210/- which was held to be not deductible as a bad debt in view of the provisions of Section 36(2) could be considered as an allowable business loss?"

2. This reference has been made at the instance of the assessee and arises out of the order of the Tribunal dated 19.12.1994 in Income Tax Appeal No.1495/Bom/94 relating to the assessment year 1991-1992.

3. Briefly the facts leading to this reference are as under:

a) The assessee is a stock and share broker. During the assessment year 1991-1992, the assessee sought to write off an amount of Rs.47.58 lacs as bad debts, due to breach committed by 3 members of the Bombay Stock Exchange. The Assessing Officer on examination of the assessee's claim held that the assessee was not entitled to claim the benefit of bad debts in respect of Rs.47.58 lacs, as the assessee has not satisfied the condition precedent as provided under Section 36(2) of the Act, which requires that the amount must be offered to tax in an earlier previous year.

4. On Appeal, the Commissioner of Income Tax (Appeals) upheld the finding of the Assessing Officer to the extent of Rs.44.98 lacs after having allowed an amount of Rs.2.60 lacs as a business loss. He also held that the amount of Rs.11.81 lacs was a speculation loss and could not be allowed as a trading loss. So far as, the balance amount of Rs.33.17 lacs was concerned the Commissioner of Income Tax (Appeals) held that the same could not be considered as a trading loss.

5. On appeal before the Tribunal the assessee contended that even if the deduction is not allowable as bad debts under Section 36(1)(vii) of the Act, the aforesaid amount of Rs.44.98 lacs should be allowed as a business loss in computing the profits and gains earned in carrying on a business. The Tribunal held that once an assessee has made a claim

for loss on account of bad debts then unless the assessee fulfills the requirements of Section 36(2) of the Act, the benefits of the same cannot be extended to the assessee. Further, it held that when there is a specific provision in the Act regarding allowability of bad debts as a deduction and relief is sought thereunder, the assessee is not entitled to claim relief as an allowable expenditure/deduction under any other provisions including the benefit of deduction as a business loss.

6. Mr. Sanjeev Shah, Learned Counsel appearing for the applicant submits as under:

a) The issue arising in the present reference stands concluded by the order of this court in the matter of *Commissioner of Income Tax v. Shreyas S. Morakhia* dated 28th February, 2012 in *Income Tax Appeal No. 89 of 2011 = (2012-TIOL-172-HC-MUM-IT)*. It has been held therein that even if a part of the bad debts has been taken into account while computing the income of the assessee, and offered for tax in a earlier year, the same would be sufficient satisfaction of Section 36(2) of the Act.

b) In any view of the matter, even if the amount of Rs.44.98 lacs is not allowable as a bad debt, the same should be considered as a allowable business loss in computing the profits and gains of business and profession under Section 28 of the Act.

c) The Act does not provide that the deduction available from the total receipts to compute profit & gain of business are only those deductions which are listed in Section 30 to 43 of the Act. This is because according to him the list is not exhaustive. It is his contentions that any loss which occurs in carrying on the business and is related to the business operation is entitled to be deducted to arrive at the profits and gains of a business under Section 28 of the Act. In support thereof, he relies upon the decision of this court in the matter of *Commissioner of Income Tax v. R.B. Rungta & co.* reported in 50 ITR page 233.

7. As against the above, Mr. Suresh Kumar appearing for the Revenue submits that:

a) The decision of this court in the matter of *Shreyas S. Morakhia (Supra)* will not apply to the present facts, as in this case the loss arose on account of a fellow member of the stock exchange not honoring its commitment;

b) The amount claimed as bad debts is specifically provided for under section 36 of the Act and in such cases it is not permissible to apply any other section of the Act to determine the allowability of the same as a deduction;

c) In any view of the matter, the Commissioner of Income Tax (Appeals) has come to a conclusion that there was no trading loss to the extent of Rs. 33.17 lacs, as there was no trading done in respect thereof and the deduction was therefore not allowable. So far as, deduction to the extent of Rs.11.81 lacs is concerned, the same is on account of speculation loss and hence, cannot be allowed as deduction from the general profits and gains earned by the assessee in respect of the other income. In support of the aforesaid submission, he invited our attention to explanation (2) to Section 28 of the Act.

8. We have considered the submission. So far as, the submission of Mr. Shah for the assessee that the decision of this court in the matter of *Shreyas S. Morakhia (Supra)* covers the issue is concerned, we are not expressing any opinion with regard to it as the same does not arise from the question referred to us. The Tribunal has considered that the amount of Rs.44.98 lacs is not deductible as bad debts in view of Section 36(2) of the Act

and sought our opinion only on the question whether in such a case the assessee could claim a deduction as a business loss to arrive at his profits and gains from business.

So far as, the submission of Mr. Suresh Kumar for the Revenue that the issue with regard to the loss being a loss on account of speculation is concerned, we are not expressing any opinion on the same. This for the reason that the issue framed for our opinion is whether, when the loss is not allowed as a bad debts can it be considered for the purposes of allowing the same as a business loss. In this case, we are not called upon to decide whether or not the loss claimed satisfied the test of the business loss but our opinion is on the more restricted issue namely whether such a loss could be considered as a allowable business loss. Therefore, we are not dealing with both the above issues.

9. Our opinion is sought on the issue, whether if an amount is held to be not deductible as a bad debt, in view of non compliance of the condition precedent as provided under Section 36(2) of the Act, could the same be considered as a allowable business loss. The Tribunal in its order dated 19.12.1994 has not considered the issue, whether or not a loss claimed by the assessee is allowable as a business loss on the basis of the evidence produced by the assessee. The Tribunal proceeded on a premise that once a claim is made for deduction as bad debts, then the deduction can be granted only if the provision of Section 36 of the Act are satisfied and it is not open to an assessee to claim a deduction in the alternative under any other provision of the Act. In view of the above, we are not making any observation with regard to whether the claim of the assessee on merits is allowable as a business loss. We are only examining the issue posed for us viz. that when the claim made for bad debts is not satisfied, could it be considered as a allowable business loss.

10. Section 28 of the Act imposes a charge on the profits or gains of business or profession. The expression "Profits and gains of business or profession" is to be understood in its ordinary commercial meaning and the same does not mean total receipts. What has to brought to tax is the net amount earned by carrying on a profession or a business which necessarily requires deducting expenses and losses incurred in carrying on business or profession. The Supreme Court in the matter of *Badridas Daga v. Commissioner of Income Tax*, reported in 34 ITR page 10, has held that in assessing the amount of profits and gains liable to tax, one must necessarily have regard to the accepted commercial practice that deduction of such expenses and losses is to be allowed, if it arises in carrying on business and is incidental to it.

11. On the basis of the aforesaid decisions, it can be concluded that even if the deduction is not allowable as bad debts, the Tribunal ought to have considered the assessee's claim for deduction as business loss. This is particularly so as there is no bar in claiming a loss as a business loss, if the same is incidental to carrying on of a business. The fact that condition of bad debts were not satisfied by the assessee would not prevent him from claiming deduction as a business loss incurred in the course of carrying on business as share broker.

12. In fact this court in the matter of *Commissioner of Income Tax v. R.B. Rungta & Co.* (*Supra*) upheld the finding of the Tribunal that the loss could be allowed on general principles governing computation of profits under Section 10 of the Indian Income Tax Act, 1922 which is similar/identical to Section 28 of the Act. The revenue in that case urged that the assessee having claimed deduction as a bad debt the benefit of the general principle of law that all expenditure incurred in carrying on the business must be deducted to arrive at a profit cannot be extended. This submission was negated by this court and it was held that even where the debt is not held to be allowable as bad debts yet the same would be

allowable as a deduction as a revenue loss in computing profits of the business under Section 10(1) of the Indian Income Tax Act, 1922.

13. In view of the above, the question as referred to us is answered in the affirmative i.e. in favour of the assessee and against the respondent. No order as to costs.