IN THE HIGH COURT OF JUDICATURE AT MADRAS

Reserved On	02.09.2022
Pronounced On	29.12.2022

CORAM :

THE HONOURABLE MR.JUSTICE **S.VAIDYANATHAN**

AND

THE HONOURABLE MR.JUSTICE **C.SARAVANAN**

T.C.A.No.1025 of 2009

M/s.Ashok Leyland Finance Limited,
(A Division of M/s.Indus Ind Bank Ltd),
86, Chamiers Road, Chennai – 600 018.
Now at : 115 & 116, G.N.Chetty Road,
T.Nagar, Chennai – 600 017. ... Appellant

vs.

The Deputy Commissioner of Income Tax,
Company Circle 1(1),
Chennai – 600 034. ... Respondent

Appeal under Section 260A of the Income Tax Act, 1961, against the order of the Income Tax Appellate Tribunal, "A" Bench, Chennai dated 20th March 2009 in ITA.No.1864/Mds/2006.

For Appellant : Mr.R.Vijayaraghavan

For Respondent : Mr.T.Ravikumar
Standing Counsel

J U D G M E N T

S.VAIDYANATHAN, J.
AND
C.SARAVANAN, J.

The appellant, a leasing company is engaged in the business of hire, purchase, finance, leasing of motor vehicles and bill discounting etc. The appellant had filed its return of income under Section 139 of the Income Tax Act, 1961 on 31.10.2002 for the Assessment Year 2002-2003. In the return, the appellant had declared a "taxable income" of Rs.52,51,21,000/-.

2. The said return was processed under Section 143(1) of the Income Tax Act, 1961. Thereafter, the return was scrutinized. A notice under Section 143(2) of the Income Tax Act, 1961 was issued to the appellant on 11.08.2003. The Assessment was thereafter completed under Section 143(3) of the Income Tax Act, 1961 on 31.05.2005. The income of the appellant was re-determined as Rs.57,36,86,630/-.

3. The Commissioner of Income Tax later invoked Section 263 of the Income Tax Act, 1961 and issued a Show Cause Notice dated 04.04.2006 to the appellant to revise the assessment on the ground that an amount of Rs.338.92 Lakhs was wrongly debited under the head "Provisions and Write Off" as a diminution in value of repossessed stock was not an allowable expenditure.

4. The appellant replied to the above Show Cause Notice dated 04.04.2006. The Commissioner of Income Tax rejected the contention of the appellant and passed an order dated 26.05.2006 under Section 263 of the Income Tax Act, 1961.

5. By the aforesaid order dated 26.05.2006, the Commissioner of Income Tax directed the Assessing Officer to revise the assessment by adding back the amount debited by the appellant towards diminution in the value of repossessed assets.

6. Aggrieved by the order of the Commissioner of Income Tax, the appellant has preferred I.T.A.No.1864(Mds)/2006 before the Income Tax

Appellate Tribunal ('Tribunal' in short). I.T.A.No.1864(Mds)/2006 was dismissed by the Tribunal vide impugned order dated 20.03.2008. Aggrieved by the order of the Tribunal, appellant has preferred the present appeal before this Court under Section 260A of the Income Tax Act, 1961 ('Act' in short). The Tribunal relied on its order dated 11.04.2008 in I.T.A.No.78(Mds)/2007 in the appellant's own case for Assessment Year 2003-2004.

7. Following Substantial Questions of Laws were framed for being answered:-

i. Whether on the facts and in the circumstance of the case, the Tribunal was right in upholding the jurisdiction of the Commissioner of Income Tax u/s.263 in revising the assessment order?
ii. Whether on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the loss computed by the Appellant on account of diminution in value of repossessed vehicles is only a notional and unascertained loss and hence cannot be allowed as a deduction?

8. We have considered the arguments advanced by the learned counsel for the appellant and the respondent.

9. Wherever defaults were committed by lessees, the appellant re-possessed the vehicles. The appellant treated the amount due from the defaulting lessees as “receivable” in its books of account.

10. A further sum was reduced from the aforesaid amount as diminution in the value based on the prevailing market value of the seized vehicle. The appellant appears to have compared the book value of the repossessed vehicle with the prevailing market value. If the estimated market value was less than the book value at the time of the repossession of the leased asset (vehicle), the appellant reduced the value and transferred it to its profit and loss account.

11. If the vehicles were sold before the closes of the financial year, entries made towards diminution in the value were reversed on the actual loss arrived from the sale and suitable adjustments were made in the book. This method adopted by the appellant allowed it to reduce the value of the asset and thereby the income tax payable.

12. The appellant thus claimed a deduction under Section 36 of the

Act based on the estimated market value it determined at the time of repossession. This deduction was sought to be denied. Income tax is payable on the "income" as defined in Section 2(24) of the Act.

13. Section 36(1)(vii) of the Act allows deduction of amount towards any "bad debt" or part thereof which is written off as irrecoverable in the books of accounts of the assessee for the previous year. Deduction is subject to Section 36(2) of the Act. Sub-Section (1)(vii) and (2) to Section 36 of the Act which are relevant for the purpose of this case are reproduced below:-

Section 36 (1)(vii)	***Section 36(2)***
(1) The deduction provided for in the following clauses shall be allowed in respect of the 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: **Provided** that in the case of an	2. In making any deduction for a bad debt or part thereof, the following provisions shall apply- i. no such deduction shall be allowed unless such debt or part thereof has been taken into account in computing the income of the assessee of the previous year in which the amount of such debt or part thereof is written off or of an earlier previous year, or represents money lent in the ordinary course of the business of

assessee to which clause (viia) applies, the amount of the deduction relating to any such debt or part thereof shall be limited to the amount by which such debt or part thereof exceeds the credit balance in the provision for bad and doubtful debts account made under that clause; **Explanation**.—For the purposes of this clause, any bad debt or part thereof written off as irrecoverable in the accounts of the assessee shall not include any provision for bad and doubtful debts made in the accounts of the assessee.	banking or money- lending which is carried on by the assessee; ii. if the amount ultimately recovered on any such debt or part of debt is less than the difference between the debt or part and the amount so deducted, the deficiency shall be deductible in the previous year in which the ultimate recovery is made; iii. any such debt or part of debt may be deducted if it has already been written off as irrecoverable in the accounts of an earlier previous year (being a previous year relevant to the assessment year commencing on the 1st day of April, 1988, or any earlier assessment year), but theAssessing Officer had not allowed it to be deducted on the ground that it had not been established to have become a bad debt in that year; 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; v. where such debt or part of debt relates to advances made by an assessee to which clause (viia) of sub- section (1) applies, no such deduction shall be allowed unless the assessee has debited the amount of such debt or part of debt in that previous year to the provisions for bad and doubtful debts account made under that clause.

14. By Circular No.12/2016, dated 30.05.2016, the Income Tax Department clarified that claim for any debt or part thereof in any previous year, shall be admissible under Section 36(1)(vii) of the Act, if it is written off as "irrecoverable" in the Books of Accounts of the assessee for that previous year and it fulfils the conditions stipulated in Sub-Section (2) to Section 36 of the Act.

15. The above clarification was issued in the light of the decision of the Honourable Supreme Court in case of **T.R.F. Ltd.** Vs. **Commissioner of Income Tax, Ranchi**, (2010) 13 SCC 532, wherein, it was clarified that "After 1.4.1989, for allowing deduction for the amount of any bad

debt or part thereof under section 36(1)(vii) of the Act, it is not necessary for the assessee to establish that the debt, in fact has become irrecoverable; it is enough if bad debt is written off as irrecoverable in the Books of Accounts of the assessee".

16. In the present case, the appellant has not written off the receivables as bad debt. On the other hand, the appellant has reduced the amount from the receivable as diminution in the value of the re-possessed assets which were repossessed from the defaulting lessees based on its projected market value at the time of re-possession.

17. In RBI Circular dated 01.01.2002 bearing reference Ref.DNBS(PD). CC.No.18/02.01/2001-02, a reference was made to previous clarification of RBI dated 27.06.2001 bearing reference Ref DNBS (PD).CC.No.16/2001-01. A new procedure for accounting of repossessed assets for NBFC's and a revised guideline for accounting of the repossessed assets was given by RBI *vide* RBI Circular dated 01.01.2002 bearing reference Ref.DNBS(PD).CC.No.18/02.01/2001-02. Relevant portion of the RBI Circular dated 01.01.2002 bearing reference

Ref.DNBS(PD). CC.No.18/02.01/2001-02 reads as follows:-

Existing Guidelines	***Revised Guidelines***
In case the asset is taken as part of fixed asset for own use i. The repossession of the least or hire purchase asset should be treated as foreclosure of the contract of lease or hire purchase finance; ii. The accounting adjustment should be done in these cases by taking the assets at its book value; iii. In Case of Hire Purchase Assets, in arriving at the book value, the asset value should be depreciated by 20% per annum of the cost on the straight-line method; iv. The releasable value has to be arrived at after deducting the expenditure likely to be incurred on the sale of the assets; The provision in regard to deficit between book value and the realisable value should be made in the current year itself. In case the asset is still treated as part of Lease /hire purchase portfolio The asset should continue to be treated as non-performing and provision should be made according to the provisioning norms on the line of those applicable to the scheduled contracts.	A) The repossessed assets should be shown as distinct from "assets on lease" or "stock on hire" under the "Fixed Assets" of "Current Asset" as the case may be. B) Valuation of assets may be done as per accounting standards of ICA!.

18. The above clarification does not clearly spell out the relevant

Accounting Standard which is to be followed by a NBFC. The valuation has to be in accordance with the Accounting Standard (AS) 19 "Accounting for Leases" for all lease agreements (Financial Leases) executed on or after April 1, 2001.

19. Paragraphs 26 to 38 of the Accounting Standard (AS) 19 deals with leases in the Financial Statement of lessors. The appellant has not explained the same.

20. In **Vijaya Bank** Vs. **Commissioner of Income Tax**, (2010) 323 ITR 166, it was clarified that after the amendment to Section 36 of Act with effect from 01.04.1989, a distinct dichotomy has been brought. Consequently, a mere provision for bad debt is not sufficient to claim deduction unless there is a write-off in full or part. Explaining the concept, the Court gave an illustration. If an assessee debits an amount of doubtful debt to the Profit and Loss Account and credits the asset like sundry debtors account, it would constitute write-off of an actual debt. However, if an assessee debits "provision for doubtful debt" to the Profit and Loss Account and makes a corresponding credit to the "current

liabilities and provisions" on the liability side of the balance sheet, then it would constitute a provision for doubtful debt. In the latter case, it would not be entitled to deduction after 01.04.1989.

21. The loss from the repossessed vehicles can be ascertained only after they are resold. Till such time, loss cannot be determined. Estimated loss based on the difference between the receivable and the projected market value would not entitle the appellant to reduce the value of the asset to reduce the market value unless provided in the relevant Accounting Standard. We have also not been informed about any Accounting Standard as per which the diminution in the value is allowed.

22. There are also no materials before us to interfere with the finding of the Tribunal in the impugned order. Further, the balance amount, if any, will be recovered from the defaulter. Merely because there is erosion in the value based on the estimates would not *ipso facto* entitle diminution to claim deduction. Therefore, we answer the Substantial Question of Law No.2 against the appellant.

23. As far as the Substantial Question of Law No.1 is concerned,

the issue as to whether the Commissioner of Income Tax was entitled to invoke Section 263 of the Income Tax Act, 1961 or not, we are of the view that it has to be also answered against the appellant in view of our answer to Substantial Question of Law No.2.

24. The appellant had wrongly debited a sum of Rs.338.92 lakhs under the headings 'provision and write-off' as the diminution in the value of the repossessed stock. It was not allowable expenditure. Thus, it is evident that the order passed by the Assessing Officer was not only erroneous but also prejudicial to the interest of the revenue. Therefore, Substantial Questions of Law raised in this appeal are answered against the appellant.

25. Thus, the assessment made on 31.05.2005 under Section 143(3) of the Income Tax Act, 1961 was not only erroneous but had also passed in a manner which was prejudicial to the interest of the revenue. Therefore, the Commissioner of Income Tax Act, 1961 correctly invoked the power under Section 263 of the Income Tax Act, 1961.

26. Therefore, this Tax Case Appeal is liable to be dismissed and is accordingly dismissed. No cost.

[S.V.N., J.] [C.S.N., J.]
29.12.2022

(1/2)

Internet : Yes
Index : Yes / No
Jen/rgm

To

1. Income Tax Appellate Tribunal, "A" Bench,
   Chennai.

2. The Deputy Commissioner of Income Tax,
   Company Circle I(1),
   Chennai – 600 034.

S.VAIDYANATHAN, J.
and
C.SARAVANAN, J.

Jen/rgm

Pre-Delivery Judgment
in
T.C.A.No.1025 of 2009

29.12.2022

(1/2)