IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO. 511 OF 2004
WITH
INCOME TAX APPEAL NO. 510 OF 2004

Industrial Development Bank of India, Mumbai … Appellant
(in which The United Western Bank Ltd. is amalgamated)

Versus

Deputy Commissioner of Income Tax, Spl. Range-I, Kolhapur …Respondent

Mr. Mihir Naniwadekar a/w. Mr. Ruturaj H. Gurjar for the appellant.
Mr. Subir Kumar a/w. Mr. Abhinav Palsikar for the respondent.

CORAM: G. S. KULKARNI &
SOMASEKHAR SUNDARESAN, JJ.
RESERVED ON : 18 September, 2024
PRONOUNCED ON: 19 September, 2024

Judgment (Per G.S. Kulkarni, J.)

1. These are two appeals filed by the assessee - The United Western Bank Ltd., which was merged with the 'Industrial Development Bank of India'. Both these appeals raise common questions of fact and law. The relevant assessment years are 1993-94 and 1994-95. We refer to the questions of law framed by the Court while admitting Income Tax Appeal No. 511 of 2024, which reads thus:

> "(i) Whether on the facts and in the circumstances of the case, the Appellate Tribunal was justified in rejecting the claim of the

appellant u/s. 36(1)(vii) and 36(1)(viia) aggregating to Rs.3,89,96,838/-?

(ii) Whether the Appellate Tribunal is right in law in holding in respect of amount written off by the rural branches, the difference between amount written off and doubtful debt account would be allowed without referring to the claim and calculation made by the appellant?

(iii) Whether on the fact and in the circumstances of the case, the Tribunal was justified in holding that post issue expenses of Rs.6,00,000/- on stamp duty on share certificates was capital expenditure particularly when the rights issue was in compliance with RBI's requirements?

2. At the outset, Mr. Naniwadekar, learned counsel for the appellant has submitted that the appeals are being confined to question nos. 1 and 2. These questions are interconnected.

3. The facts in the lead appeal (Income Tax Appeal No. 511 of 2004) can be noted hereunder:-

4. The appellant is stated to be a Scheduled Commercial Bank, which has rural branches as defined in clause (ia) of Explanation to Section 36(1)(viia) of the Income-tax Act (for short **"the Act"**). The assessee follows the practice of writing off in its books of accounts, bad debts during the course of the year as well as making provisions on the last day of the accounting year. The provision that may be made under Section 36(1)(viia) is a percentage of the total income and another percentage of the advances made during the

year, which necessarily means that it can only be computed at the end of the year. For the assessment year in question (AY 1993-94), the accounting year ended on 31 March, 1993. It is stated that there was opening balance as on 1 April, 1992 in the provision account made as per Section 36(1)(viia) of the Act, which permits the assessee to make a 'provision' for bad debts. It is the assessee's case that during the previous year, the assessee actually wrote off total bad debts of Rs.4,56,71,000/- which related to the debts arising in the prior years. The assessee contended that at the end of the year, i.e., on 31 March, 1993, the assessee made fresh provision and claimed deduction under section 36(1)(viia) of Rs. 1,11,79,936/-. Mr. Naniwadekar has prepared a table to indicate total bad debts written off; opening credit balance of bad debts provision; amount of bad debts claimed as deduction u/s. 36(1)(vii); provisions for bad debts made u/s. 36(1)(viia); and total deduction claimed for the assessment years 1993-94 and 1994-95. Such table is extracted hereunder:-

Sr. no.	A.Y.	Total Bad Debts written off	Op. Credit Balance of Bad Debts provision	Amount of Bad Debts claimed as deduction u/s. 36(1)(vii)	Provision for Bad Debts made u/s. 36(1)(viia)	Total Deduction claimed
1.	1993-94	4,56,71,000	1,78,54,098	2,78,16,902	1,11,79,936	3,89,96,838
2.	1994-95	13,00,55,738	1,11,79,936	11,88,75,802	2,15,65,529	14,04,41,331

5. In assessing the income of the assessee, in the context of the deductions on this count as claimed by the assessee, the Assessing Officer was of the view that not only the opening balance in the 'provision account' at the beginning of the year should be taken into account, but also the provision made at the end of the year be reduced, along with bad debts being an amount of Rs.1,11,79,936/- and allowed only the balance amount of bad debts.

6. The assessee carried the matter to CIT(A) who concurred with the views of the Assessing Officer to hold that the assessee was required to debit the provisions even in respect of the amounts of bad and doubtful debts to be written off under section 36(1)(vii) along with provision for bad debts as made under section 36(1)(viia). The assessee hence carried an appeal to the Tribunal contending that the provisions of Section 36(1)(vii) and 36(1)(viia) were independent and contemplated avoidance of double deduction in respect of the same amount. It was contended that these being two separate deductions, one cannot be curtailed by the other. The tribunal, however, making meager observations, rejected the assessee's appeal:-

> "2. Ground No. 1 is directed against the CIT(A) upholding the deduction allowed by the AO in respect of bad debts to the extent of Rs.16,62,36,932 as against Rs.2,78,16,936/- claimed by the assessee thereby confirming the addition of Rs.1,11,79,936/-. It has been submitted before us by ld. Authorized representative appearing on behalf

> of the assessee that ld. CIT(A) failed to appreciate the contention of the assessee that since the bad and doubtful debts are written off during the course of the year in working out the amount allowable as per proviso to Section 36(2)(vii), the excess to be considered was not with reference to the provision as at the end of the year. The deduction in respect of bad debt as claimed by the assessee was required to be allowed. The revenue, on the other hand, relied on the orders of the authorities below.
>
> 3. We have considered the rival submissions and we find that the decision of the Hon'ble Kerala High Court in the case of South Indian Bank Ltd. vs. CIT (262 ITR 579) is applicable in the instant case and in respect of amount written off by the Rural Branches, the difference between the amount off and doubtful debts account would be allowed. This is the action which the AO has taken and, therefore, we do not find any reason to interfere with the orders of the authorities below. In confirming their orders, therefore, we dismiss this ground taken by the assessee."

7. Mr. Naniwadekar has reiterated the assessee's case as urged before the authorities below. He contends that the provisions of Section 36(1)(vii) and Section 36(1)(viia) are independent of each other, which permits the assessee to have a separate deduction of the amount of bad debts under clause (vii) as also to have a provision for bad debts under clause (viia) of Section 36(1), in terms of the formula stipulated therein. According to Mr. Naniwadekar, the assessee was making such provision under both the said clauses for the assessment years in question, as also for the subsequent years, wherein the amount of bad debts of which a deduction was claimed under section 36(1)(vii) was arrived at, after reducing from it/utilizing the amounts in respect of which provision for bad debts was made in the previous assessment year, and

thereafter giving effect and/or utilizing such provision as permissible under section 36(1)(viia), a total deduction under both the clauses was claimed as clearly seen from the chart (supra). It is his submission that the account clearly depicted that the provision of Rs.1,11,79,936/- under the said provision (Section 36(1)(viia)) made for assessment year 1993-94 was actually reduced/utilized from the debts written off for the subsequent AY 1994-95 in arriving at the deduction of the bad debts, as claimed by the assessee under section 36(1)(vii). It is contended that added to such amount was the fresh provision made for the assessment year as per the provisions of clause (viia) so as to claim a total deduction of the bad debts under clause (vii) and clause (viia) of Section 36(1). He submits that as the assessee had strictly adhered to the provisions of Section 36(1)(vii) and (viia) read with sub-section (2)(v), hence, it was not proper for the authorities below to not allow the deduction as made by the assessee and/or to reject the same, referring to the decision of the Kerala High Court in **South Indian Bank Ltd. vs. Commissioner of Income Tax**[1]**.** Mr. Naniwadekar would submit that the Tribunal has in fact failed to given cogent reasons, on the case as made out by the assessee in its appeal in assailing the findings as recorded by the Assessing officer, as also confirmed by the CIT(A). In support of his submission, Mr.

[1] 262 ITR 579

Nandiwadekar has placed reliance on the decision of this Court in **The Director of Income Tax (International Taxation) v/s. M/s. Citi Bank NA**[2] as also on the decision of Gujarat High Court in **Commissioner of Income-tax-I vs. UTI Bank Ltd.**[3].

8. On the other hand on behalf of the Revenue, Mr. Subir Kumar, learned counsel has supported the orders passed by the tribunal confirming the view taken by the Assessing Officer on the interpretation of the provisions of Section 36(1)(vii) and (viia). In support of his contention, Mr. Subir Kumar has placed reliance on the decision of the Kerala High Court in **South Indian Bank Ltd.**(supra)

9. It is on such backdrop, we have heard learned counsel for the parties to adjudicate the questions of law which has arisen for consideration. As the controversy revolves around the interplay between the provisions of Section 36(1)(vii) and Section 36(1)(viia), it will be appropriate to note the provisions, which read thus:

> "**36. Other deductions.—**
>
> (1) The deductions 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—

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2 Income Tax Appeal No. 5758 of 2010 decided on 22 December, 2011

3 (2013) 29 taxmann.com 79 (Gujarat)

(i) ….
(ii) …..
…….
(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 assessee to which clause (vii-a) 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;
… … .

(vii-a) in respect of any provision for bad and doubtful debts made by—

(a) a scheduled bank (not being a bank approved by the Central Government for the purposes of clause (viiia) or a bank incorporated by or under the laws of a country outside India) or a non-scheduled bank, an amount not exceeding five percent of the total income (computed before making any deduction under this clause and Chapter VI-A) and an amount not exceeding two per cent of the aggregate average advances made by the rural branches of such bank computed in the prescribed manner:

(b) a bank, being a bank incorporated by or under the laws of a country outside India, an amount not exceeding five per cent of the total income (computed before making any deduction under this clause and Chapter VI-A);

… … …

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

… ….

(v) where such debt or part of debt relates to advances made by a bank to which clause (viia) of sub-section (1) applies, no such deduction shall be allowed unless the bank has debited the amount of such debt or part of debt in that previous year to the provision for bad and doubtful debts account made under that clause."

10. On a plain reading of the provision of Section 36(1)(vii) of the Act, it is clear that a deduction is allowed to the assessee, in computing the income

referred to in Section 28 of the Act, in respect of any bad debt or part thereof which is written off as irrecoverable in the accounts of the assessee for the previous year. The proviso below clause (vii) contemplates that in the case of a bank 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. Clause (viia) permits a deduction qua "a provision" being made for bad and doubtful debts, being eligible for deduction made by Scheduled Bank, of the description as contained in sub-clause (a) thereof. It provides that an amount not exceeding 5% of the total income (computed before making any deduction under this clause and Chapter VIA) and an amount not exceeding 2% of the aggregate average advances made by the Rural branches of such bank computed in the prescribed manner. However, such percentage is not in issue.

11. Thus, clause (viia) of Section 36(1) is a provision distinct and in addition to clause (vii) of Section 36(1) providing for deduction in respect of "a provision" for bad and doubtful debts to be made interalia by a Scheduled Bank.

12. There is another aspect which also needs to be noted, is the provision of sub-section (2)(v) of Section 36(1) which provides that in making any deduction for bad debt or part thereof in relation to debt or part of debt qua advances made by the bank to which clause (viia) of sub-section (1) applies, no such deduction shall be allowed unless the bank has debited the amount of such debt or part of debt in that previous year to the provision for bad and doubtful debts account, made under that clause.

13. Now applying the provisions of Section 36(1)(vii) and (viia) to the facts of the present case, it would be required to be seen as to whether the Tribunal was correct in confirming the findings of the authorities below. To examine the case of the assessee, it would be first required to be noted as to how the assessee has dealt with the actual bad debts [clause(vii)] and in regard to the provision for bad debts in its accounts [clause(viia)]. It appears to be quite clear from the chart which we have extracted hereinabove, that the assessee has accounted for the actual bad debts suffered by the assessee for the assessment year which is an amount of Rs.4,56,71,000/-. However, the deduction of bad debts claimed under section 36(1)(vii) is of an amount arrived at after deduction/subtracting the opening credit balance of the "bad debt provision", made in the previous assessment year from such amount of

bad debts written off, which was of the amount of Rs.1,78,54,098/-, from the total bad debts written off, resulting in an amount of Rs.2,78,16,902/- as bad debts claimed as deduction u/s. 36(1)(vii). In doing so, "the provision" for bad debts as made in the previous assessment year, namely, the opening balance in the "bad and doubtful debts account", has been utilized by the assessee to reduce the total bad debts written off in claiming the deduction. Added to this was a provision for bad debts made under section 36(1)(viia) which was an independent amount of Rs.1,11,79,936/- as per the prescribed limits. Thus, the total deduction being claimed by the assessee under Section 36(1)(vii) and (viia) was Rs.2,78,16,902 + Rs.1,11,79,936/- = Rs. 3,89,96,838/-. The same pattern was followed for the subsequent assessment year 1994-95 which is the subject matter of companion appeal, the figures however being different.

14. In our opinion, applying the provision of Section 36(1)(vii) and (viia) as it stands, there does not appear to be any infirmity in the assessee claiming deduction under both the provisions in the manner as done by the assessee. This more particularly for the reason, that it is not the case that a provision being made under clause (viia) in the previous assessment year, (i.e. closing balance as on 31 March, 1993) is not being reduced from the bad

debts written off in the next assessment year to reduce the total bad debts as written off for the purpose of claiming deduction. In other words, it is not the case that the assessee had sought for a deduction in the assessment year in question under Section 36(1)(viia) and again was seeking a double deduction in relation to the said amount, in the subsequent assessment year. This is clear from the fact that the provision made by the assessee in the subsequent assessment year was of a distinct amount calculated as per the estimates of bad debts and as permissible, which was totally unconnected with the deduction as sought either under Section 36(1)(vii) or with the provision for bad debts under Section 36(1)(viia), made in the previous year. For such reason, we are not persuaded to accept the following reasons as set out by the Assessing officer and as confirmed by the CIT(A) in rejecting the assessee's claim for deduction.

> "3. The assessee has debited a sum of Rs.13,12,61,902/- under the head, 'provisions & Contingencies'. This includes bad debts written off amounting to Rs.4,56,71,000/-. The assessee in its computation of income has claimed 2,78,16,902 as bad debts written off. **This amount was arrived at after deducting an amount of Rs.1,78,54,098 which was credited balance in the provision for bad & doubtful debts. As per the provisions of sec.36(1)(vii) of the I.T. Act, 1961 bad debts written off as bad debts will be to the extent it exceeds the credit balance in the provisions made for bad & doubtful debts by the assessee. While writing off bad debts the assessee has not taken into consideration the provion for bad & doubtful debts as on 31.3.1993. The amount allowable as provision for bad & doubtful debt as per the provisons of sec. 36(1)(viia) of the I.T. Act, 1961 for the year is 1,11,79,936/-. The assessee has not taken this credit balance into consideration while claiming bad debts. After deducting the provision for**

> **bad & doubtful debts allowable during the year under consideration the total bad debts written off allowable come to (2,78,16,902 – 1,11,79,936) Rs.1,66,36,962/-.**
>
> (emphasis supplied)

15. The highlighted portion of the Assessing officer's finding in fact is in the teeth of the provisions of Section 36(1)(viia) looked from any angle. It is inconceivable that the amount of bad debts claimed as deduction under Section 36(1)(vii) could have any bearing so as to require any deduction/ subtraction from the provision for bad debts, made by the assessee under Section 36(1)(viia). If such requirement as observed by the Assessing officer is considered to be the correct position, it would in fact amount to reading something in the provisions of Section 36(1)(vii) or for that matter Section 36(1)(viia), which the legislature itself had not provided for. Such reading of the provision also cannot be gathered from the reading of sub-section (2)(v) of Section 36. In fact such working of these provisions as sought to be canvassed on behalf of the revenue leads to an absurdity.

16. Considering the aforesaid position the provisions bring about, Mr. Naniwadekar would be correct in placing reliance on the decision in UTI Bank Ltd. (supra) wherein Division Bench of the Gujarat High Court in the context of the deduction as claimed under the provisions in question and applying the decision of the Supreme Court in **Catholic Syrian Bank Ltd. vs.**

CIT[4] as also considering the Circular No. 17/2008 dated 26 November, 2008 issued by the CBDT in that behalf, made the following observations :-

> "14. From the above statutory provisions, it can be seen that in addition to the deduction available to an assessee under s. 36(1)(vii) for bad debts, in case of special class of banks mentioned in cl. (viia), deductions subject to fulfillment of certain conditions is available in respect of any provision for bad and doubtful debts. One of the restrictions is of limiting such deduction to a maximum of a specified percentage of total income of the assessee computed before making any deduction under this clause and not exceeding prescribed percentage of aggregate average advance made by the rural branches of such bank. From the decision of the apex Court in the case of *Catholic Syrian Bank Ltd.* (supra), it can be gathered that under cl. (vii) of sub-s. (1) of s. 36, deduction is made available in computation of taxable profits of all scheduled commercial banks in respect of provisions made by them for bad and doubtful debts relating to advances made by them in the rural branches. Such deduction is limited to a specified percentage of the aggregate average advances made by the rural branches. The apex Court held that the deduction on account of provision for bad and doubtful debts is distinct and independent of the provisions of s. 36(1)(vii) relating to allowance of the bad debts. Contention of the Revenue that the banks covered by cl. (viia) were not entitled to deduction under s. 36(1)(vii) was rejected. The Court held that proviso to s. 36(1)(vii) would ensure that there would be no double benefit of deduction in such cases.
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> 15. In the present case, however, the question of method of operation of proviso to s. 36(1 (vii) arises. Such proviso as noted, provides that in case of an assessee to which cl. (viia) applies, the amount of 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. The Revenue's contention is that by virtue of such proviso, the claim of the assessee for deduction for debts written off, should be reduced by the closing balance of the assessee in his account for the provision of bad and doubtful debts. On the other hand, the assessee contends that such diminution should be limited to the opening balance of such account.
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> 16. We notice that in this respect the provision is silent. **We may therefore record that the interpretation adopted by the Tribunal in the impugned judgment would ordinarily give rise to a question of law**

[4] (2012) 343 ITR 270

particularly when it is pointed out that there is no previous decision of any High Court on the subject. However, the issue has been made sufficiently clear by the CBDT Circular No. 17 of 2008 dt. 26th Nov., 2008 [(2008) 220 CTR (St) 41 : (2008) 16 DTR (St) 5]. In the said circular, this very issue has been examined and clarified in the following manner:

> "2. In a recent review of assessment of banks carried out by C & AG, it has been observed that while computing the income of banks under the head 'Profit and gains of business & profession', deductions of large amounts under different sections are being allowed by the AOs without proper verification, leading to substantial loss of revenue. It is, therefore, necessary that assessments in the cases of banks are completed with due care and after proper verification. In particular, deductions under the provisions referred to below should be allowed only after a thorough examination of the claim on facts and on law as per the provisions of the IT Act, 1961.
>
> (i) Under s. 36(1)(vii) of the Act, deduction on account of bad debts which are written off as irrecoverable in the accounts of the assessee is admissible. However, this should be allowed only if the assessee had debited the amount of such debts to the provision for bad and doubtful debt account under s. 36(1)(viia) of the Act, as required by s. 36(2)(v) of the Act.
>
> (ii) While considering the claim for bad debts under s. 36(1)(vii), the AO should allow only such amount of bad debts written off as exceeds the credit balance available in the provision for bad and doubtful debt account created under s. 36(1)(viia) of the Act. The credit balance for this purpose will be the opening credit balance i.e., the balance brought forward as on 1st April of the relevant accounting year."
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> (emphasis supplied)

17. Similarly, in **M/s. Citi Bank NA** (supra), a Division Bench of this Court in interpreting provisions of Section 36(1)(vii) and (viia) has made the following observations which supports the case of the assessee:-

> 12. The first question to be considered herein is, whether the expression 'credit balance' in the proviso to Section 36(1)(vii) is relatable to the opening credit balance in the provision for bad and doubtful debts

account as on 1st April of the relevant accounting year or the closing credit balance as on 31st March of the relevant accounting year. In view of the Boards' Instruction No.17/2008 dated 26th November 2008, it is clear that the expression 'credit balance' in the proviso to Section 36(1)(vii) is relatable to the opening credit balance in the provision for bad and doubtful debts account i.e. the balance brought forward as on 1st day of April of the relevant accounting year.

13. The question then to be considered is, whether the deduction allowed in the present case under Section 36(1)(vii) and under Section 36(1) (viia) exceed the limits prescribed under the respective sections? Under Section 36(1)(vii) of the Act any bad debt written off as irrecoverable in the accounts of the assessee is allowable deduction. Proviso to Section 36(1) (vii) provides that in the case of an assessee to which clause (viia) of Section 36(1) applies, the deduction under Section 36(1)(vii) shall be limited to the bad debt that exceeds the credit balance in the provision of bad and doubtful debts account maintained under Section 36(1)(viia) of the Act. It is not in dispute that the assessee is a bank incorporated by or under the laws of a country outside India. Therefore, under clause (b) of Section 36(1)(viia), the assessee is entitled to a deduction in respect of any provision made for bad and doubtful debts, to the extent, not exceeding five per cent of the total income computed before making any deduction under clause (viia) of Section 36(1) and Chapter VIA of the Act.

14. Admittedly, the opening credit balance in the provision for bad and doubtful debts account was Rs.2crores which according to the assessee was allowable in the assessment year 1999-2000. The lower authorities have not disputed this contention of the assessee. If the above amount of Rs.2 crores is held allowable in the assessment year 1999-2000, then, the opening credit balance in the provision for bad and doubtful debt as on the first day of the accounting year being 'nil', the entire amount of Rs.52.36 crores written off would have been allowable under Section 36(1)(vii) of the Act."

18. Mr. Subir Kumar has placed reliance on the decision of **South Indian Bank** (supra) to justify the view taken by the authorities below, however, we are not inclined to accept such contention as, in our opinion, in such case the High Court applying the proviso to clause (vii), which ordained a limit to the amount by which such bad debt or part thereof exceeds the credit balance in

the provision for bad and doubtful debts account made under that clause, observed that such mandate of the provision was not given effect to and/or applied by the Tribunal. The facts in the present case demonstrate a different position as clearly seen from the assessment order as also the impugned order passed by the Tribunal, which we have extracted hereinabove, so as to form the basis of the assessee not been granted a deduction as claimed for. In fact, **South Indian Bank (supra)** too highlights the fact that the deductions under the aforesaid two provisions are distinct and separate.

19. We are thus of the clear opinion that the assessee's case appropriately fall within the parameters of the deduction as per the requirements of clause (vii) as also clause (viia) of Section 36(1). There was nothing erroneous or illegal for the assessee to make an independent provision for bad and doubtful debts under clause (viia), to be adjusted in the subsequent assessment year, so as to claim the benefit under clause (vii) as observed by us. Such approach of the assessee certainly would not fall foul of the stipulation of the proviso below clause (vii) of Section 36(1). It is not the revenue's case that the assessee had exceeded the deduction beyond the limits as prescribed by the proviso, namely, the amount by which the bad

debts or part thereof exceeds the credit balance in the provision, for bad and doubtful debts account, made under clause (viia).

20. For the aforesaid reasons, we hold that the assessee was entitled for the deductions under clauses (vii) and (viia) of Section 36(1) of the Act for the assessment years in question. We, accordingly, allow the appeals by answering the questions of law in favour of the assessee and against the revenue. No costs.

(SOMASEKHAR SUNDARESAN, J.) (G. S. KULKARNI , J.)