

**IN THE INCOME TAX APPELLATE TRIBUNAL  
"C" Bench, Mumbai**

**Before Shri D. Manmohan, Vice President  
and Shri B. Ramakotaiah, Accountant Member**

**ITA No. 530/Mum/2009**  
(Assessment Year: 2005-06)

Shri Pawan Kumar Parmeshwarlal  
4th Floor, Singhanla Wadi  
187, Dady Seth Agyari Lane  
Mumbai 400002  
PAN - AAAPC 5238 N

ACIT 4(2)  
Vs. Mumbai

**Appellant**

**Respondent**

Appellant by: Assessee in person  
Respondent by: Shri P.N. Devdasan

**ORDER**

**Per B. Ramakotaiah, A.M.**

This appeal by the assessee is against the order of the CIT(A)-IV, Mumbai dated 19.11.2008.

2. Assessee has raised the following two grounds: -

- I. *On the facts & circumstances of the case the learned CIT erred applying Rule 8D which is an exhaustive calculating system toward interest, while interest is not wholly/solely/completely and/or exhaustively associated/devoted to only one factor of dividend and as such the complete implication of interest factor towards the factional out-come factor i.e. entitlement of dividend through the application of rule 8D is improper and unjust and need to be deleted/set aside.*
- II. *Claim of Bad debts: - the learned CIT erred in disallowing the claim of bad debts of Rs.1316192/- without appreciating the facts on record and the law pertaining to allowance of Bad Debts."*

3. Assessee is an individual who is also a stock broker and member of the Bombay Stock Exchange. He is the proprietor of M/s. Pawankumar Parmeshwarlal dealing in shares and securities. Assessee has filed return of income declaring total income of ₹14,34,977/- for the impugned assessment year which included income from share transactions undertaken as a broker, business income, capital gains being long term capital gains and

income from other sources being interest received. While scrutinising the return the A.O. noticed that the assessee has earned a dividend of ₹3,19,797/-, interest on RBI bonds of ₹1,11,617/- and PPF interest of ₹6,696/- apart from bank interest of ₹97,252/-. The first three items were claimed as exempt. The A.O. asked the assessee why expenditure should not be disallowed on earning interest from incomes. It was the submission of the assessee that no expenditure was incurred by him as most of the shares were in his demat account for long years and dividend was automatically credited to the bank account as and when the companies declared dividend and interest on RBI bonds were also tax free interest and likewise PPF interest is also on the investments made for income tax purposes. It was his submission that none of these activities require any expenditure and as such no amount is disallowable under section 14A. The A.O. was of the view that assessee would have spent some amount for earning the tax free incomes and disallowed an amount of ₹20,000/- under section 14A. When it was contested before the CIT(A), the CIT(A) instead of examining the issue on factual basis analysed provisions of section 14A and Rule 8D and directed the A.O. to compute deduction as per Rule 8D. Assessee is contesting the same.

4. After hearing the assessee in person and arguments of the learned D.R. we are of the opinion that no disallowance is called for under section 14A. Obviously the assessee is maintaining separate books of account for the purpose of business and these investments are in his personal capacity. The A.O. also has not disallowed any expenditure of personal nature out of the income from business or profession in the computation of income in the assessment order. In view of this we are of the opinion that the expenditure claimed in the business of share dealings cannot be correlated to the incomes earned in personal capacity that too on dividend, PPF interest and tax free interest on RBI bonds. In view of this, we are of the opinion that estimation of expenditure of ₹20,000/- out of business expenditure claimed in business activity cannot be considered for being incurred for this earning of tax free income of above nature. In view of this disallowance so made under section 14A of ₹20,000/- is deleted. Not only that the CIT(A) directed

the A.O. to consider the allowance invoking Rule 8D. The Hon'ble Bombay High Court in the case of Godrej & Boyce Mfg. Co. Ltd. vs. DCIT 328 ITR 81 has considered Rule 8D to be applicable prospective and since the assessment year involved is before the introduction of sub-section (2) & (3) of section 14A, there is no question of disallowing the amounts invoking Rule 8D. Therefore, the CIT(A)'s direction on this is set aside and the additions so made by the A.O. in the computation of business income is deleted. Ground is considered allowed.

5. Ground No. 2 pertains to the claim of bad-debts of ₹13,16,192/-. Assessee claimed the following three amounts of bad debts in the business of vyaj badla:

i) Shri Samir Kedia	₹ 11,682
ii) Shri Sushil B. Gupta	₹ 2,04,510
iii) KNA Securities P. Ltd.	<u>₹11,00,000</u>
Total	₹13,16,192

It was assessee's submission that these amounts are advanced in the course of assessee's business as stock broker and supported the contention that badla activity is a financing activity as per Securities and Exchange Board of India notification dated 15<sup>th</sup> July 2004 and these amounts which are advanced in the course of business activity, which become irrecoverable should be allowed as bad debts, otherwise should be treated as business loss. The A.O. discussed the issue on three reasons: (i) whether the claim is allowable as bad debt, (ii) whether the claim is allowable as loss, and (iii) whether irrecoverable loss and advances can be written off as bad debts in the case of person who is not a money lender. He discussed the issue elaborately and held that the assessee's claim on account of bad debts is not allowable and disallowed the entire amount. Assessee contested the issue before the CIT(A) both on legal principles as well as on factual basis and made detailed submissions which was extracted by the CIT(A) in the order and rejected the contention holding that the debt has not become bad and the conditions under section 36(2) are not satisfied in the badla transactions as held by the ITAT in the case of Arshad J. Choksi vs. ACIT 51 ITD 511. Assessee explained that as part of consortium an amount of ₹93 lakhs was

advanced to M/s. KNA Securities P. Ltd. vide MOU dated 30.10.1998 and assessee has advanced total of ₹11 lakhs on 30.10.1998, 02.11.1998 and 05.11.1998 on a condition that money was to be returned on 31.03.1999. On 31.03.1999 the said person had not returned the money due to certain family problems and business operations and assessee furnished the correspondence with the President of the Bombay Stock Exchange and letter addressed to various people about the steps taken to recover the amount and ultimately, after exhausting the legal requirements wrote off the amount in the impugned assessment year. It was submitted that the assessee is in the business of vyaj badla and monies were extended towards purchase of shares in the stock exchange and the amounts are to be allowed as bad debts. It was his submission that the amount has become bad and the A.O. and CIT(A) were not correct in disallowing the amount which could not be recovered.

6. The learned D.R., however, supported the orders of the A.O. and the CIT(A) to state that the conditions under section 36(2) are not fulfilled.

7. We have considered the issue and considered rival contentions. In our opinion the A.O. and CIT(A) are not correct in disallowing the claim of bad debts. First of all there is no denial of the fact that assessee has advanced money as part of business activity, being stock broker. The amount advanced by the stock broker and claim of bad debt was considered by the Special Bench in the case of DCIT vs. Shreyas S. Morakhia (Mum) (SB) 5 ITR TRIB.1 wherein it was held as under: -

*The condition stipulated in the first limb of cl. (i) of sub-s. (2) of s. 36 is that no deduction on account of bad debt or part thereof 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. As per the second limb of cl. (i) of sub-s. (2) of s. 36, the said condition is not applicable where such debt represents money lent in the ordinary business of banking or moneylending which is carried on by the assessee. In the present case, the debt in question undisputedly does not represent money lent in the ordinary course of banking or moneylending business carried on by the assessee and therefore the second limb of cl. (i) of sub-s. (2) of s. 36 is not relevant. In the present case at least at this stage. However, the same has to be considered at appropriate stage while dealing with the arguments raised by the*

*Departmental Representative referring to the said limb. At this stage what is to be considered is whether the condition stipulated in the first limb of s. 36(2)(i) is satisfied in the case of the assessee in as much as whether the debt representing amount receivable by the assessee as share broker from his clients against purchase of shares on their behalf or part thereof can be said to have been taken into account in computing the income of the assessee.*

Hence the amounts advanced by the assessee in the course of business activity are to be treated as an allowable amount under section 36(2). Considering the facts of the case and the fact that assessee has written off the amount in the books of account, we are of the opinion that the amounts are allowable as bad debt. A.O. is free to bring it to tax in the year in which the assessee recovers the amount, if any. Therefore, ground No. 2 is also considered allowed. A.O. is directed to allow the amount as claimed.

8. In the result, appeal of the assessee is allowed.

Order pronounced in the open court on 11<sup>th</sup> January 2011.

Sd/-  
**(D. Manmohan)**  
**Vice President**

Sd/-  
**(B. Ramakotiah)**  
**Accountant Member**

Mumbai, Dated: 11<sup>th</sup> January 2011

Copy to:

1. *The Appellant*
2. *The Respondent*
3. *The CIT(A) – IV, Mumbai*
4. *The CIT– IV, Mumbai City*
5. *The DR, “C” Bench, ITAT, Mumbai*

*By Order*

//True Copy//

*Assistant Registrar*  
*ITAT, Mumbai Benches, Mumbai*

n.p.