(2002) 11 KL CK 0073

In the High Court Of Kerala

Case No : Income Tax A. No. 81 of 2002

Co-operative Sugars Ltd. APPELLANT

Vs

Commissioner of Income Tax and Another RESPONDENT

Date of Decision : 22-11-2002

Acts Referred:
Income Tax Act, 1961 — Section 260A

Citation : (2003) 262 ITR 252

Hon'ble Judges : K. Balakrishnan Nair, J;G. Sivarajan, J

Bench : Division Bench

Advocate : K. Anand and Latha Krishnan, for the Appellant; P.K.R. Menon, for the Respondent

Judgement

G. Sivarajan J.

1. This appeal is filed by an assessee to Income Tax u/s 260A of the Income Tax Act, 1961 (for short, "the Act") against the order of the Income Tax Appellate Tribunal, Cochin Bench, in I.T.A. No. 10 of 1997 in respect of the assessment year 1993-94. The question involved in this case is as to whether the expenditure incurred by the assessee in the matter of replacement of a manually operated crane by an electrically operated crane, is a capital expenditure or not. The Assessing Officer took the view that the expenditure is capital in nature. According to him, the assessee had introduced a new independent self-contained machinery. He took the view that the E.O.T. crane acquired is an addition to plant and machinery and further that the assessee had claimed depreciation on M.O.T. crane also which would show that the said crane was also used. The first appellate authority in appeal took the view that this is actually a replacement of the old machinery for overall improvement and efficiency of the company and allowed the claim as a revenue expenditure. In appeal by the department the Tribunal took the view that the E.O.T. crane is not a part of the other machinery and that it can work independently and the other existing machinery can also work without the machinery newly introduced. The Tribunal accordingly set aside

the order of the first appellate authority and restored the order of the Assessing Officer. The assessee is thus aggrieved by the order of the Tribunal. The assessee has formulated the following questions of law for decision.

"1. Whether, on the facts and in the circumstances of the case, the Tribunal is right in law in holding that the expenditure incurred by the assessee in the matter of replacement of the manually operated crane by an electrically operated crane is a capital expenditure ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal is right in law in holding that the E.O.T. crane was totally new and independent machinery without which the other machinery can work and therefore the expenditure incurred by the assessee is a capital expenditure ?

3. Whether, on the facts and in the circumstances of the case, the Tribunal is right in law in holding that this is a case where the assessee had introduced a new independent and self-contained machinery which is not a part of any other machinery and therefore the expenditure incurred is capital expenditure ?"

2. We have heard Sri K. Anand, learned counsel for the appellant, and Sri P.K.R. Menon, senior Central Government standing counsel appearing for the Revenue. We have also perused the orders of the three authorities. The assessing authority in paragraph 4 of the assessment order considered the question thus :

"The assessee has debited an amount of Rs. 6,42,000 being the cost of E.O.T. crane. In the audit report it has been rightly pointed out that the payment is capital in nature. The assessee has debited this amount in the profit and loss account on the contention that the E.O.T. crane is replacement in place of the old M.O.T. crane. The E.O.T. crane by itself is a machinery and it can be operated by electric power and the old one manually. In view of these facts I hold that the E.O.T. crane acquired is an addition to plant and machinery and not replacement as contended. It may be seen from the depreciation statement that the assessee has claimed depreciation on old M.O.T. crane also and this fact also shows that the old one is in use during the previous year. Hence, the assessee''s argument of replacement does not agree with the details furnished in the depreciation statement. Therefore, the E.O.T. crane is taken to be addition to plant, and machinery."

3. The first appellate authority referred to the decision of the Supreme Court in Commissioner of Income Tax, Madras Vs. Mahalakshmi Textile Mills Ltd., , and the decision of this court in Vanaja Textiles Ltd. v. CIT [1994] 208 ITR 161 and thereafter observed as follows :

"The case of the assessee is that the old M.O.T. crane was replaced by a better efficient crane, i.e., an electronically operated crane. This is actually a replacement of the old machinery for overall improvement and efficiency of the company."

4. The appellate authority on that basis held that the expenses have to be

treated as revenue expenditure. The Tribunal held that the decisions relied on by the first appellate authority are distinguishable and observed as follows :

"In both the cases, some parts of the existing machinery were changed though such change was effected on the basis of a comprehensive scheme of modernization and rehabilitation, whereas in the instant case of the assessee, the assessee had introduced a new independent and self-contained machinery. This machinery is not part of any other machinery. It can work independently. The other existing machineries can also work without the machinery newly introduced by the assessee."

5. The Tribunal accordingly set aside the order of the first appellate authority.

6. We notice that in the case of the assessee itself a question came up before this court on similar circumstances in Commissioner of Income Tax Vs. Co-operative Sugars Ltd., . The question was as to whether the expenses incurred for the replacement of items high velocity juice heater, sugar grader, centrifugal machinery, juice sulphiter, vacuum filter drum, pumps and meters are of capital nature. In that case the assessing authority has taken the view that the sugar plant of the assessee consisted of several independent components such as the items already mentioned, that each unit is a separate entity by itself which could perform the assigned task of each stage of operation and processing ; that none of such components is part of other machinery; that the assessee replaced the entire machinery, namely, the items mentioned above, that it is not a case of replacement of accessories of such components; that the asses-see received benefits of enduring nature from the replacement of each equipment independent in itself; that a new asset by purchasing each such machinery has come into existence and, therefore, the expenditure incurred by the assessee on the acquisition and installation of such assets cannot be said to be expenditure incurred on repairs or replacement of some of the accessories of such independent equipment. This view of the Assessing Officer was upheld by the first appellate authority. However, the Tribunal held that each machinery, though has distinct function, is an integral part of the sugar plant and sugar manufacturing process is a continuous process and unless the sugar-cane juice as such or in a different form passes through all the requisite components, the sugar, which is the end-product of the sugar mill, cannot be produced ; that none of the machinery purchased by the assessee during the relevant year to replace the old ones, can produce sugar by itself ; that sugar can be produced only when all the machinery, which are integral parts of the entire sugar plant, function in harmony and, therefore, the expenditure was incurred only on the maintenance of the sugar mill, a profit earning apparatus.

7. This court considered the question as to how to approach to solve the ticklish question as to what is the distinction between capital and revenue expenditure. Considering the principles laid down in the decision of the Privy Council in B.P. Australia Ltd. v. Commission of Taxation of the Commonwealth of Australia [1966] ACC 224 and the decision of the Supreme Court in Alembic Chemical

Works Co. Ltd. v. CIT : [1989]177ITR377(SC) this court observed as follows (page 349 of 235 ITR) :

"From the above reproduced observations, it is nothing but clear that the answer to the question whether a given expenditure is capital in nature or revenue in nature, will depend on the facts and circumstances of each case. Both the Assessing Officer and the Commissioner of Income Tax (Appeals) took the view, in the instant case, that each equipment, on which the expenditure was incurred by the assessee, was independent in nature. On the facts and in the circumstances of the case, the view so taken by them is not at all correct. It may be true that sugarcane juice processed through each equipment may undergo some change, but the end-product of the sugar mill would be available only after the entire processing is complete and that would be complete only after the completion of the processing through all the machinery on which the expenditure was incurred by the assessee. Simply because each equipment changes the form or shape of the sugarcane juice, that does not mean that sugar is produced by each equipment or machinery. This being so, there is a basic fallacy in the approach of the Assessing Officer and the appellate authority."

8. Regarding the further contention advanced by senior standing counsel for the Revenue that a considerable expenditure was incurred by the assessee on each machinery and some of the machinery was replaced after 17 years of service and, therefore, the expenditure so incurred was capital in nature inasmuch as the machinery acquired, constituted an asset of an enduring benefit, the court further observed (page 350) :

"The sugar mill is a gigantic plant. The Assessing Officer should not have been swayed by the extent of expenditure, incurred on major components purchased for replacing the old ones. The vital question is whether the sugar mill can work in the absence of machinery, expenditure incurred on which is claimed by the assessee. This question has to be answered in the negative. For the manufacture of sugar, all the machinery claimed are necessary. No doubt, the expenditure was incurred on the principal components of the sugar mill, still, however, it would be wrong to hold each machinery as an independent unit. All machinery put together complete the sugar plant. We, therefore, entirely agree with the view taken by the Appellate Tribunal."

9. Yet another contention taken by senior standing counsel for the Revenue that the expenditure incurred on substantial replacement is capital in nature the Division Bench further observed (page 350) :

"But, in the case in hand, it does not hold to be good. No doubt, expenditure was incurred on substantial replacement, but the fact remains that the sugar plant was there and the same plant existed even after replacement, and, therefore, it is wrong to say that any new asset of enduring nature has come into existence. Whether or not a new asset has come into existence--this question has to be considered vis-a-vis the integrated sugar plant and not vis-a-vis each integral part of it. When expenditure incurred on technical know-how on consideration of ''once for all payment'' was held to be the expenditure as revenue in nature in the case of Alembic Chemical Works Co. Ltd. : [1989]177ITR377(SC) , we see no reason why expenditure incurred on purchasing of new machinery to ensure sound functioning of the sugar mill to replace the old ones, should not be held as revenue expenditure."

10. We have also extracted the relevant findings of the three authorities. In view of the abovesaid decision of this court in the assessee''s own case; what is necessary to be found was whether the electrically operated crane which is acquired and installed is an integral part in the process of manufacture of the end-product, namely, sugar. The assessee had clearly stated that the existing manually operated crane was replaced by an electrically operated crane only to improve the efficiency of the plant and that it is only a part of the main manufacturing plant. None of the authorities approached this question with reference to the factual situation obtained, namely, whether the electrically operated crane was installed as part of the plant consisting of various machineries for bringing out the end-product, namely, sugar. Each of the authorities without ascertaining the factual position, if necessary, by conducting a spot inspection had straightaway gone into various circumstances including the decisions of courts and taken his or its own view on the facts. This approach really is unfortunate. In every case, the authorities must make sure of the factual position with regard to the issues involved and then apply the law. In this case what happened was that all the authorities including the Tribunal have assumed certain facts which had no foundation and decided the matter by applying the principles laid down by courts.

11. In these circumstances, we are of the view that this question must be considered by the assessing authority for the said purpose. We accordingly set aside the orders of the assessing authority, the first appellate authority and the Tribunal on this point and direct the assessing authority to consider this question in the light of the principles laid down by this court in the assessee''s case mentioned supra and in the light of the observations contained herein. It is open to the assessing authority to arrange for an inspection of the sugar factory of the assessee with notice to the assessee for the purpose of ascertaining the correct factual situation and a decision will be taken by the assessing authority as directed above thereafter.

The appeal is disposed of as above.