

(2008) 04 RAJ CK 0058
In the Rajasthan High Court

Commissioner of Income Tax

APPELLANT

Vs

Kansara Modler Ltd.

RESPONDENT

Date of Decision : 25-04-2008

Acts Referred:

Income Tax Act, 1961 — Section 14, 43, 56

Citation : (2008) 218 CTR 21

Hon'ble Judges : N.P. Gupta, J;Kishan Swaroop Chaudhari, J

Bench : Division Bench

Final Decision : Dismissed

Judgement

N.P. Gupta, J.—This appeal has been filed by the Revenue, against the judgment of the Tribunal dt. 17th March, 2004, allowing the appeal of the assessee, relying upon the judgment of the Hon'ble Supreme Court, in Commissioner of Income Tax Vs. Karnal Co-operative Sugar Mills Ltd., and holding, that the receipts in question, by way of interest, are incidental to the main business of the assessee, and the receipts are taken to be as capital receipt, and not income of the assessee from any independent source.

2. The appeal was admitted by this Court, vide order dt. 23rd Aug., 2005, by framing the following substantial questions of law:

I. Whether on the facts and in the circumstances of the case, the learned Tribunal was legally justified in holding that the receipts in question by way of interest were incidental to the main business of the assessee and the receipts are to be taken as capital receipts and not income of the assessee from any independent source despite assessee's failure to adduce any evidence in this regard?

II. Whether on the facts and in the circumstances of the case, the learned Tribunal was legally justified in not applying the decision of the Hon'ble Supreme Court given in the case of Tuticorin Alkali Chemicals and Fertilizers Ltd., Madras Vs. Commissioner of Income Tax, Madras, despite the same being fully applicable

to the facts of the present case?

3. A perusal of the two questions show, that the substantive question is question No. 2, inasmuch as the question is as to whether the matter was required to be decided on the basis of judgment of the Hon''ble Supreme Court, in the case of Tuticorin Alkali Chemicals and Fertilizers Ltd., Madras Vs. Commissioner of Income Tax, Madras, , or was rightly decided on the basis of the judgment of the Hon''ble Supreme Court, in the case of Karnal Co-operative Sugar Mills Ltd. (supra).

4. The facts are not in dispute, that the assessee had got open LC (letter of credit) worth Rs. 10 crores from the bank, for the purchase of plant and machinery from foreign suppliers, and for that purpose the assessee deposited a sum of Rs. 1.5 crores with the bank, as margin money in the form of FDRs, on which the assessee earned interest to the tune of Rs. 6,22,877. On these facts, the precise question is, as to whether this receipt, is a revenue receipt liable to be taxed u/s 56, or is liable to be treated as capital receipt, so as to reduce the cost of the plant and machinery, within the meaning of Section 43(1) of the IT Act.

5. The learned Counsel for the Revenue relied upon the judgment of the Hon''ble Supreme Court in Tuticorin's case (supra), and then also cited the judgments of the Supreme Court in CIT v. Autokast Ltd. (2001) 165 CTR (SC) 162 : (2001) 248 ITR 110 , CIT v. Coromandal Cements Ltd. (1999) 153 CTR (SC) 209 : (1998) 234 ITR 412 , and two judgments of the Allahabad High Court, being in Chandpur Sugar Co. Ltd. Vs. Commissioner of Income Tax, and Commissioner of Income Tax Vs. Kisan Sahkari Chini Mills Ltd., On the other hand, the learned Counsel for the assessee relied upon the judgments of the Supreme Court, in Commissioner of Income Tax Bihar-II Patna Vs. Bokaro Steel Limited, Bokaro, , and Karnal Co-operative Sugar Mills Ltd. case (supra), and then also relied upon the judgment of the Hon''ble Supreme Court, in M.B. Abdulla v. CIT (1990) 82 CTR (SC) 362 : AIR 1999 SC 1451, and in CIT v. Max India Ltd. (2007) 213 CTR (SC) 266 : (2007) 295 ITR 282 . Learned Counsel also relied upon the later judgments of the Hon''ble Supreme Court, in CIT v. Kamataka Power Corporation (2000) 162 CTR (SC) 249 : (2001) 247 ITR 268 , and Bongaigaon Refinery and Petrochemicals Ltd. Vs. Commissioner of Income Tax,

6. We have heard learned Counsel for either side and have gone through various judgments cited on either side. It may be observed at the outset, that the judgment of the Hon''ble Supreme Court, in Tuticorin's case (supra) is decided by a Bench headed by three Hon''ble Judges. Likewise, the judgment in Autokast's case (supra) is also decided by a Bench headed by three Hon''ble Judges, and then the judgments in Kamataka Power Corporation, and Bongaigaon Refinery's case (supra), are also the judgments rendered by a Bench headed by three Hon''ble Judges. Other judgments of the Hon''ble Supreme Court are the judgments rendered by the Bench of two Hon''ble Judges.

7. Out of the cases cited on the either side, first case is Tuticorin's case (supra). In Tuticorin's case (supra), the facts were, that the assessee company was incorporated for the purpose of manufacturing heavy chemicals, like Ammonia Chloride and Soda Ash. The company was incorporated in the year 1971, and its trial production commenced in 1982. For the purpose of setting up of factories, the company had taken term loans from various banks and financial institutions. The part of the borrowed fund, which was not immediately required, was kept invested in short-term deposits with the banks. Such investments were permitted in the memorandum and articles of association. On these short-term deposits, the assessee earned income to the tune of Rs. 2,92,440. The company disclosed business losses to the extent of Rs. 3,21,802, and claimed the benefit of carry forward of a net loss of Rs. 29,360. However, then the company filed a revised return, showing business loss of Rs. 3,21,802, and claimed, that the interest and finance charges along with other pre-production expenses are required to be capitalized, and therefore, the interest income of Rs. 2,92,440 should reduce the pre-production expenses, which would ultimately be capitalized, and pointed out, that in the previous year the company had incurred a sum of Rs. 1,13,06,068 by way of interest and finance charges, which had to be capitalized along with other pre-production expenses, and thus it was claimed, that the interest earned amounting to Rs. 2,92,440 was not exigible to tax. It is on these facts, that Hon'ble Supreme Court noticed the difference of opinions of various High Courts. Hon'ble Supreme Court also considered its previous judgment, in Challapalli Sugar Ltd. Vs. The Commissioner of Income Tax, A.P., Hyderabad, and held, that the amount would be chargeable to tax, and such income has to be computed in accordance with the provisions of the IT Act, Section 14 whereof lays down, that for the purpose of computation, income of an assessee has to be classified under the six heads, and then it was found, that such income falls under head "F" being "Income from other sources". The argument about accountancy methods, not only of the company, but of the association of chartered accountants, was also considered. Challapally Sugars Ltd's case (supra) was explained, and was found to be different. It has been observed, that the phrase "actual cost" has not been defined in the Act, therefore, it has to be explained in the common parlance, and to find that out, the normal rules of accountancy, prevalent in the commercial and industrial circles were noted, but then the Hon'ble Supreme Court found, in Tuticorin's case (supra), that it [Challapally Sugars Ltd's case (supra)] is clearly a different case, inasmuch as the question required to be decided is, as to whether a particular receipt is of the nature of the income, which is a question of law, required to be decided by the Court, on the basis of the provisions of the Act, and the interpretation of the term "income", given in large number of decisions of the High Courts, and the Privy Council, and also of the Supreme Court. Then it was held, that it is well settled, that the income attracts tax as soon as it accrues, and the application, or destination of the income, has nothing to do with its accrual or taxability. It is also well settled, that interest income is always of a revenue nature, unless it is received by damages or compensation. Thus, a reference made to the Hon'ble Supreme Court, by

High Court, was decided.

8. Subsequent judgments cited by the learned Counsel for the Revenue, are in light of this judgment, therefore, we need not repeat the subsequent judgments cited by the learned Counsel for the Revenue, including Autokast's case (supra), Commanded Cements Ltd's case (supra), Chandpw Sugar Co. Ltd's case (supra) and even the Kisan Sahkari Chini Mills' case (supra).

9. Then in Bokaro Steel's case (supra), the facts regarding the relevant assessment order, involving the questions of law, viz. whether on the facts and circumstances of the case the Tribunal was justified in holding that the interest received by the assessee company on the amount of Rs. 7,50,502, advanced to the contractors, was not taxable? Likewise, in next asst. yr. 1971-72 the question involved was as to whether the learned Tribunal was justified in holding that the interest received by the assessee company on the amount of Rs. 14,98,993, advanced to the contractor was liable to tax? The facts were, that the assessee was a corporation, wholly owned by the Government of India, and was assessed in the status of a company. It was incorporated in January 1964, with the object to construct and own integrated iron and steel works. During the assessment years under consideration, the work of the construction of the company's factory and installation of plant was in the process of completion, and the company had not started any business during the assessment years in question. During this period, the assessee entered in the supplementary agreement with its contractors, under which assessee had made certain advances to the contractors, to enable them to execute large scale construction work smoothly, which advances were on payment of interest, with the result, that the contractors did not have to raise funds from outside agencies. Other items we need not go into. Then in para 5, Hon''ble Supreme Court in this case has held as under:

...We have to consider whether the amounts received by the assessee under these five heads can be treated as income of the assessee for the relevant assessment years. The Tribunal has held that all these amounts (under item Nos. 1 to 4) received by the assessee have gone to reduce the cost of construction. These are in the nature of capital receipts which can be set off against the capital expenditure incurred by the assessee during the relevant assessment years.

Thus, with this finding, the Hon''ble Supreme Court concluded, with respect to the amounts, which had been borrowed by the assessee for construction work, which were not immediately required, were put in short-term deposits, and earned interest, which was held to be taxable, and that the question is concluded by the decision in Tuticorin's case (supra). However, while proceeding further, the Hon''ble Supreme Court at p. 323, after recapitulating again the conclusions in Tuticorin's case (supra), held as under:

However, while interest earned by investing borrowed capital in short-term deposits is an independent source of income not connected with the construction activities or business activities of the assessee, the same cannot be said in the

present case where the utilisation of various assets of the company and the payments received for such utilisation are directly linked with the activity of setting up the steel plant of the assessee. These receipts are inextricably linked with the setting up of the capital structure of the assessee company. They must, therefore, be viewed as capital receipts going to reduce the cost of construction.

For this purpose reference was made to Challapalli Sugar Mill's case (*supra*), and it was held, that the receipts of interest being inextricably linked with its plant and machinery, such receipts would go to reduce the cost of its assets. The receipts, therefore, were held to be of capital nature, and not liable to be taxed. Then in CIT v. Karnal Co-operative Sugar Mill's case (*supra*), again the judgments in Tuticorin and Bokaro Steel were considered, and in that case the interest earned in such circumstances, as in the present case, were held to be capital receipt, and not liable to tax. The judgment runs in one para only, and therefore we think it more appropriate to quote it in extenso. That is as under:

In the present case, the assessee had deposited money to open a letter of credit for purchase of the machinery required for setting up its plant in terms of the assessee's agreement with the supplier. It was on the money so deposited that some interest has been earned. This is, therefore, not a case where any surplus share capital money which is lying idle has been deposited in the bank for the purpose of earning interest. The deposit of money in the present case is directly linked with the purchase of plant and machinery. Hence, any income earned on such deposit is incidental to the acquisition of assets for the setting up of the plant and machinery. In this view of the matter the ratio laid down by this Court in Tuticorin Alkali Chemicals and Fertilizers Ltd., Madras Vs. Commissioner of Income Tax, Madras, will not be attracted. The more appropriate decision in the factual situation in the present case is in Commissioner of Income Tax Bihar-II Patna Vs. Bokaro Steel Limited, Bokaro, The appeal is dismissed. There will be no order as to costs.

10. Thus, on the one hand the judgments are on the facts, where the income is received, and it falls within one of the categories, or which are classified in Section 14, then attracts tax as soon as it accrues, and the application or destination of the income, has nothing to do with its accrual or taxability, and that interest income is always of revenue nature, unless it is received by way of damages or compensation, which principle has been propounded, in the backdrop of the facts, that the funds lying with the company having been borrowed by way of loans, were not immediately required by the company, and were kept in short-term deposits with the banks. On the other hand are the judgment of the Hon''ble Supreme Court in Bokaro Steel's case (*supra*), where the amount was advanced to the contractor to facilitate working, and rendering for him not necessary to arrange funds from outside agency, and on that amount interest was earned, which, after considering Tuticorin's case (*supra*) has been held to be "inextricably of the capital structure of the company", and therefore must be considered as a capital receipt, going to reduce the cost of construction,

and this very principle has been laid down in Karnal Co-operative Sugar's case (supra), where again, in terms with the agreement with the supplier, for purchase of machinery, required for setting up of the plant, letter of credit was got opened by depositing margin money, and interest was earned on such money, which has been held to be incidental to the acquisition of assets, for setting up of plant and machinery, and therefore distinguishing Tuticorin's case (supra), and following Bokaro Steel's case (supra), the receipt of interest was held to be not taxable, being capital receipt.

11. The question is of course an intricate legal question, inasmuch as Tuticorin's case (supra) proceeds on one line of thought, being the receipt as income, and it is to be found whether it falls under the provisions of Section 14 or not, while the other two judgments proceed on the basis, that the income has the effect of reducing the cost of the capital asset, therefore, should be taken to be capital receipt. Of course, in Tuticorin's case (supra), it has been held, that application or destination of the amount received, is not relevant, but then, in the other two judgments, considering process and reasonings applied in Challapali's case (supra), it has been found, that it would reduce the cost of the capital asset.

12. In such circumstances the question is, as to which of the two views is required to be followed by this Court. That is precisely the substantial question of law framed by this Court while admitting this appeal. Tuticorin's case (supra) was decided by a Bench headed by three Hon'ble Judges, and Karnal Co-operative and Bokaro Steel's case (supra) are the cases decided by a Bench headed by two Hon'ble Judges, but since they adopted different line of reasoning, which clearly appears to be in line with the language of Section 43(1).

13. In that view of the matter, what we are required to consider is, as to whether the Tribunal was legally justified in not applying the judgment rendered in Tuticorin's case (supra), or that, the Tribunal was justified in applying the judgments given in Bokaro Steel, and Karnal Co-operative Sugar Mill's case. If this question were to come originally before us, perhaps we might have taken a task of undertaking the exercise, as to which of the views is required to be followed, and may be, that we might have come to any conclusion, either ways. In such circumstances, when the learned Tribunal, after examining all the three judgments, in Tuticorin's case (supra), Karnal Co-operative Sugar Mill's case (supra), and Bokaro Steel's case (supra), has examined the question, and found Karnal Cooperative's case (supra) to be the nearest, and latest case, on facts, in our view, it cannot be said, that the Tribunal was wholly wrong in adopting this course. It would have been equally the same situation, if the learned Tribunal would have adopted the other line of reasoning, following the judgment in Tuticorin's case (supra).

14. Therefore, when there are two sets of judgments of Hon'ble Supreme Court, proceeding on different lines, of reasonings, and both stand on their own logical footing, and in that event, if the learned Tribunal has accepted one line of reasoning, supported by one set of judgments, it cannot be said, that the learned

Tribunal was legally not justified in following the decision, as followed by it, simply because it might have been possible, or might be more appropriate to follow the other set of judgments, by following the other line of reasoning.

15. We may make it clear here, that we should not be understood to be deciding the question of law, as to whether, in such circumstances, the receipt would be revenue receipt or capital asset.

16. In that view of the matter, the questions, as framed, are also decided in favour of the assessee, and against Revenue, and the appeal is dismissed.