

THE GAUHATI HIGH COURT

(The High Court of Assam, Nagaland, Mizoram & Arunachal Pradesh)

Income Tax Appeal No. 6 of 2014

M/s. Shiv Shakti Flour Mills (P) Ltd.,
Makum Road, Tinsukia—786125.

.....Appellant.

-Versus-

Commissioner of Income Tax,
Dibrugarh, C.R. Building,
Dibrugarh-786003, Assam.

.....Respondent.

For the Petitioner : Mr. R.P. Agarwalla (Sr. Adv.),
Mr. R. Goenka,
Mr. U.K. Borthakur,
Mr. A. Goenka.Advocates

For the Respondent : Mr. S. Sarma, SC, Income Tax.Advocate.

BEFORE
THE HON'BLE MR. JUSTICE HRISHIKESH ROY
THE HON'BLE MR. JUSTICE NELSON SAILO

Date of Hearing and Judgment : **29th November, 2016**

JUDGMENT AND ORDER (ORAL)

[Hrishikesh Roy, J.]

Heard Mr. R.P. Agarwalla, the learned senior counsel along with learned advocate Mr. R. Goenka for the appellant (assessee). Also heard Mr. S. Sarma, the learned standing counsel, Income Tax Department on behalf of the respondent.

2. This appeal is filed under *Section 260A* of the *Income Tax Act, 1961* (here-in-after referred to as '*the I.T. Act*'), against the common order dated 13.12.2013 (Annexure-G), of the Income Tax Appellate Tribunal, Guwahati. The departmental Appeal i.e. *ITA No.20/Gau/2005* came to be partially allowed, whereby the *transport subsidy* was ordered to be treated as revenue receipt,

taxable in the hands of the assessee, on account of the majority opinion of the 3 Member Tribunal.

3. This appeal is admitted on the following substantial question of law:-

“Whether on the facts and circumstances of the case, the Tribunal was justified in holding that the transport subsidy received by the assessee during the assessment year 2001-02 was in the nature of revenue receipt and not capital receipt and thus taxable in the hands of the assessee?”

4. The appellant is a company and is assessed to income tax within the jurisdiction of the Commissioner of Income Tax (CIT), Dibrugarh. On 22.10.2001 they submitted their return of income disclosing total income at Rs.1,82,940/- for the Assessment Year 2001-02. A non-scrutiny assessment was then made under *sub-section (1) of Section 143* of the *I.T. Act* and the intimation under that provision was issued to the assessee on 12.03.2002, by accepting their return and granting refund.

5. However the appellant's case was taken up for scrutiny under *sub-section (2) of Section 143* of the *I.T. Act* and an assessment order was passed on 30.03.2004 (Annexure-A), whereby the Rs.17,45,750/-, received as *transport subsidy*, was construed to be a supplementary trade receipt and not capital inflow and thus the concerned amount was added to the income of the assessee and accordingly assessment to tax was made by the Asstt. Commissioner of Income Tax, Circle Tinsukia on 30.03.2004 (Annexure-A).

6. The aggrieved assessee then preferred Appeal before the Commissioner of Income Tax (Appeals), where they disputed the inclusion of the *transport subsidy* sum towards income of the assessee. After due consideration of their contention, the 1st Appellate Authority noted that the *transport subsidy* received by the assessee was under the *Transport Subsidy Scheme, 1971* of the Govt. of India and the purpose of the subsidy was for promotion and growth of industries in the North Eastern Region, which is considered to be a backward and difficult area for development. Thus the nature of the receipt towards *transport subsidy* was declared to be capital in nature and hence not taxable, through the order dated 27.10.2014 (Annexure-B).

7. Aggrieved by the decision of the 1st Appellate Authority, the Revenue challenged the order before the Income Tax Appellate Tribunal, where the Judicial Member and the Accountant Member differed in their views. According to the Judicial Member, the main object of the scheme/industrial policy is to boost industrial development in the backward areas of the North Eastern States, which is lagging behind other parts of the country. He then opined that although the *transport subsidy* is disbursed after commencement of production, since the object of the scheme is to boost industrial development and the *transport subsidy* is an incentive to set up industry. Therefore it was construed to be capital receipt for the purpose of assessment to tax. However the learned Accountant Member differed with this view and in his separate opinion declared that since the *transport subsidy* is provided for assisting the assessee in carrying out his business operation after commencement of production, such receipt is revenue receipt and not capital in nature and therefore the amount in the hand of the assessee is to be construed as income, for the purpose of assessment.

8. On account of the differences between the two learned Members of the Appellate Tribunal, the matter was referred to a 3rd Member for his opinion. While the issue was under consideration by the 3rd Member, the first decision of 16.09.2010 of the jurisdictional High Court in *CIT vs. Meghalaya Steels Ltd. (Gauhati)*, reported in 332 ITR 91, was rendered whereby, the *transport subsidy* was declared to be a revenue receipt. Following this decision of the jurisdictional High Court for *Meghalaya Steels Ltd.*(supra), the 3rd Member opined that the *transport subsidy* should be treated as revenue receipt and therefore is taxable in the hands of the assessee, by his order dated 03.07.2012 (Annexure-F).

9. When the majority members accepted the contention of the Revenue, the Tribunal by its impugned order dated 13.12.2013 (Annexure-G), declared that *transport subsidy* is required to be treated as revenue receipt and thus the assessment to tax for the amount received, was upheld for the Assessment Year 2001-02.

10. At this stage, it may be relevant to point out that the above decision in *Meghalaya Steels Ltd.*(supra) was reviewed subsequently and the earlier judgment of September 16, 2010 was recalled. The later decision is

reported in *358 ITR 551*, whereby adjudication of the substantial question of law after due formulation was ordered by the High Court in the Review proceeding. Exercise of the review power by the High Court was challenged by the Revenue in *CIT vs. Meghalaya Steel*, reported in *377 ITR 112*, but the appeal was dismissed with the observation that the High Court has the inherent jurisdiction to correct its erroneous decision, while considering Appeals under *Section 260A* of the *I.T. Act*.

11.1 Mr. R.P. Agarwalla, the learned Sr. counsel refers to the office memorandum dated 24.12.1997, whereby incentive packages were provided for stimulating growth and development of industries in the North-Eastern States and submits that the *transport subsidy* sanctioned under the scheme, was intended for generating industrial activity in the backward region in order to offset the deterrent cost for the new entrepreneurs and also for those who wish to expand the production capacity, for the already established industries. He also refers to the *Transport Subsidy Scheme, 1971* (hereinafter referred to as the "Scheme") notified on 23.07.1971 to project that scheme was intended to promote growth and expansion of industries in the Northeast region and accordingly the appellant contends that reimbursement of the transportation cost for the permitted extent, is nothing but incentives provided for generation of industrial activity and the same cannot be construed as revenue receipt to augment the profit of the concerned entrepreneur.

11.2 The appellant relies on *Sahney Steel & Press Works Ltd. Vs. CIT* reported in *228 ITR 253 (SC)* and also *CIT Vs. Ponni Sugars & Chemicals Ltd.* reported in *306 ITR 392 (SC)* to contend that in order to determine the nature of the receipt of *transport subsidy*, whether it is revenue or capital receipt, the *purposive test* has to be applied and if this testing criterion is applied, it is clear enough that the sum received by the assessee cannot be characterized as revenue receipt, subject to taxation under the *I.T. Act*.

11.3 The Sr. counsel for the appellant cites *Jai Bhagwan Oil and Flour Mills Vs. Union of India* reported in *(2009)14 SCC 63* to argue that the character of *transport subsidy* under the scheme applicable for North-East region, was examined by the Apex Court and it was declared that the object of the *Transport Subsidy Scheme* is not augmentation of revenue but to improve trade and

commerce between the remote parts of the country and also to make it attractive for industrial entrepreneurs, to start and operate industries in remote region, by providing them a level playing field, so that they could compete with their counterparts in the non-remote areas of the country. Thus the receipt of the *transport subsidy* is submitted to be capital inflow.

12.1 On the other hand, Mr. S. Sarma, the learned standing counsel for the Income Tax Department submits that the assessee had credited the sum received as *transport subsidy* in their *reserve and surplus account*, but such accounting procedure is inconsistent with the method of accounting, specified under *Section 145* and *145A* of the *I.T. Act*. He submits that subsidy amount reimbursed to the assessee must be deemed as income for the year in which it is received and therefore he argues that it is taxable as revenue receipt, in the hand of the assessee.

12.2 The learned lawyer relies on *CIT Vs. Rajaram Maize Products* reported in *(2001) 251 ITR 427 (SC)* for the respondent to contend that the Apex Court had held that power subsidy received by the assessee was a revenue receipt and the same is subject to taxation under the *I.T. Act* and he submits that *transport subsidy* should be similarly construed in the hands of the assessee.

13. The submission made by the learned counsel for the parties have received our attentive consideration.

14. In order to answer the substantial question of law framed in this appeal, it is necessary to refer to the history of this litigation. The original assessing authority after noting the accounting procedure followed by the assessee, who credited the *transport subsidy* amount to the *reserve and surplus head* in their balance sheet for the assessment year 2001-02, referred to the decision in *Deputy Commissioner of Income Tax Vs. Assam Asbestos Ltd.* report in *(2003) 263 ITR 357* but noted that while incurring transportation cost for importing raw material from outside the State, the spent sum was debited as revenue expenses and if the same analogy is applied when the government subsidizes a part of the transportation expenses on a later date, that should be considered as supplementary trade receipt of revenue nature. With this understanding, the *transport subsidy* amount was added to the total income of

the assessee for the assessment year 2001-02 and the payable tax was computed on that basis.

15. However, the Commissioner of Income Tax (Appeals) while deciding the appeal filed by the aggrieved assessee referred to the *purpose* of the *Transport Subsidy Scheme, 1971* of the Govt. of India and noted that it was intended for promotion and growth of industries in the North-Eastern States which are considered to be backward and difficult areas, for development. Proceeding on this basis, the amount received towards *transport subsidy* was considered to be a capital receipt and declaration was thus made that the same is not taxable under the *I.T. Act*.

16. The issue was then taken by the revenue before the Income Tax Appellate Tribunal, where different opinion was expressed by the Judicial Member (in favour of the assessee) and the Accountant Member (in favour of the Revenue) and thus the finality was sought through the opinion of the 3rd Member. The learned Member considered the ratio in *Sahney Steel & Press Works Ltd.* (supra) and in *Ponni Sugars & Chemicals Ltd.* (supra) and also the decision of the Jammu and Kashmir High Court in *Shree Balaji Alloys Vs. CIT* reported in (2011) 333 ITR 335 (Jammu & Kashmir), where the *purposive* tests were applied. But by that time, the judgment of the jurisdictional High Court in *CIT Vs. Meghalaya Steels Ltd.* reported in (2011) 332 ITR 91 (Gauhati) was pronounced and in this case the Court declared that the *transport subsidy* in the hand of the assessee is a revenue receipt. This finding was given by the High Court only on account of the agreement of both parties since none had questioned that such receipt could be capital receipt. Therefore, influenced primarily by the 16.09.2010 judgment of the jurisdictional High Court, the 3rd Member on 03.07.2012 answered the issue in favour of the revenue and against the assessee. On account of the majority view, the final pronouncement of the Tribunal was rendered on 13.12.2013, whereby it was declared that *transport subsidy* should be treated as revenue receipt and is taxable, in the hands of the assessee.

17. However, as earlier noted when the assessee applied for review of the judgment in *Meghalaya Steels Ltd.* (supra) rendered on 16.09.2010, the Division Bench recalled the earlier order by observing that the substantial

question of law was not framed in the earlier proceeding and thus through the judgment dated 08.04.2013 in the Review case filed by the assessee in *Meghalaya Steels Ltd. Vs. CIT* reported in (2013) 358 ITR 551 (Gauhati), a fresh determination with formulation of the substantial question of law, was ordered by the Court. The resultant challenge of the revenue in the Supreme Court, we may note here, was dismissed on 05.08.2015 and this decision of the Supreme Court is reported in (2015) 377 ITR 112 (SC).

18. In respect of the same assessee i.e. *Meghalaya Steels Ltd.*, the nature of the receipt towards *transport subsidy* was reconsidered by the High Court in *CIT Vs. Meghalaya Steels Ltd.* reported in (2013) 356 ITR 235 (Gauhati). But in this case, the parties were in agreement that the subsidies are revenue receipt to help an industrial undertaking to earn profit and make gains and accordingly the Court declared that such undertaking is entitled to seek deduction of the sum received under subsidy head, under *Section 80-IB* or *80-IC* of the *I.T. Act*.

19. Similar industrial policy and concessions intended for accelerating the growth and development of industries as applicable in the N.E. States region (notified by the Central Government on 24.12.1997) was also formulated and made applicable in the State of Jammu & Kashmir. For an assessee who received refund of excise duty and interest subsidy in the Jammu & Kashmir State, the issue cropped up whether, such receipt would be treated as capital or revenue receipt, in the hand of the assessee. In order to decide on the character of the receipt, the Jammu & Kashmir High Court applied the *purpose test* formulated in *Sahney Steel & Press Works Ltd.* (supra) and *Ponni Sugars & Chemicals Ltd.* (supra) and noted that the object of the assistance under the subsidy scheme was to enable the assessee, to set up a new unit or to expand the production of an existing unit. It was observed that the scheme was intended for growth of industries and employment, creation of new assets and industrial environment in the State and thus the High Court declared that such sum received under subsidy head, cannot be construed as operational incentives for the benefit of the assessee alone. The object of the scheme was to create avenues of employment and to accelerate the industrial development in the State. Thus the concerned receipt was found to be non-taxable, in the hand of the assessee, as revenue

receipt. The challenge of the revenue against the verdict of the Jammu and Kashmir High Court was dismissed by the Supreme Court on 19.04.1996 in Civil Appeal No.10061/2011 by declaring that the issue is covered against the revenue, by the decision in *Ponni Sugars & Chemicals Ltd.* (supra) and in *CIT Vs. Meghalaya Steels Ltd.* reported in (2016) 383 ITR 217 (SC), where the *purpose test* was applied to clinch the issue.

20. What follows from the above discussion is the relevance and applicability of the *purpose test* to determine the nature of the receipt towards *transport subsidy* in the hand of the assessee. But before we proceed further with the matter, the Court has to deal with the contention of the revenue lawyer that the assessee cannot apply certain accounting method, in order to treat the received sum as capital receipt by including the amount in the reserve and surplus head, in the balance sheet. On this point we may benefit by referring to the ratio in *Tuticorin Alkali Chemicals & Fertilizers Ltd. Vs. CIT* reported in (1997) 227 ITR 172 (SC). Here the Supreme Court considered the accountancy practice and observed that when the question is whether a receipt of money is taxable or not or whether certain deduction from that receipt are permissible in law or not, the question has to be decided according to the principles of law and not in accordance with the accountancy practice. It was thus declared by the Supreme Court that accounting practice cannot overwrite the provision of the Income Tax law as the taxation law does not keep step in the footprints of the accountancy profession. If we apply the ratio of this verdict to the matter in hand, we can be assured that the question formulated for consideration need not be answered on the basis of the accounting procedure followed by the assessee but question has to be decided on the basis of the applicable principles of law.

21. To determine as to whether the *transport subsidy* received by the assessee from the Government is taxable as revenue receipt or not, the *purpose* of the incentive scheme will have to be considered. The Supreme Court in *Sahney Steel & Press Works Ltd.* (supra) after analyzing the relevant case laws declared that the character of the receipt in the hands of the assessee has to be determined with respect to the *purpose* for which the subsidy is given or in other words, one has to apply the *purpose test*. It was further declared by the Court that the point of time at which, the subsidy is paid is not relevant, the source

also is immaterial and the form of subsidy has no relevance for determination of the issue. The Court declared that if the object of the subsidy scheme was to enable the assessee to have a more profitable business, then the receipt is on revenue account. But on the other hand, if the object of the assistance under the subsidy scheme was to enable the assessee to set up a new industrial unit or to expand the existing facilities, then the receipt of the subsidy was on capital account. It was thus held that the object for which the subsidy is given will determine the nature of the incentive and the form of mechanism through which the subsidy is received by the assessee, is wholly irrelevant for deciding the issue.

22. Endorsing the *purpose test* enunciated in *Sahney Steel & Press Works Ltd.* (supra), the Apex Court in *Ponni Sugars & Chemicals Ltd.* (supra) reiterated that it is the object for which subsidy is given, that will determine the nature of the incentive subsidy and bearing in mind the objective behind the payment of incentive subsidy, the payment received by the assessee under the concerned head was declared to be categorized as capital receipt rather than revenue receipt and thus not taxable, in the hands of the assessee.

23. The *transport subsidy* received by a mustered oil unit located in Assam was the subject matter of consideration of the Apex Court in *Jai Bhagwan Oil and Flour Mills* (supra). In this case, the Supreme Court declared that the object of the *Transport Subsidy Scheme* is not augmentation of revenue but to improve trade and commerce between the remote parts of the country with other parts to bring about economic development of the remote and backward regions. The ratio of this case makes it clear that the amount received towards transportation cost in the hand of the assessee is capital receipt and the same cannot be subject to taxation in the hand of assessee, under the *I.T. Act*.

24. Before we part with the records, we must take into account implication of *Rajaram Maize Products* (supra) cited by the departmental lawyer. In this case, the Supreme Court declared that the *power subsidy* received by the assessee was a revenue receipt and therefore the same is subject to the levy of tax, in the hands of the assessee. In this context, reading the judgment in *Mepco Industries Ltd. Vs. CIT* reported in (2009) 319 ITR 208 (SC) will guide us. Here the Supreme Court opined that in order to determine the nature of the subsidy,

each case will have to be assessed on its own merit and as the nature of subsidies are different and distinct, in the cases under consideration of the Court. There can be no straightjacket formula of distinguishing a capital receipt from a revenue receipt and the answer will depend on the circumstances of each case. Therefore, only because *power subsidy* received by the assessee was declared to be a revenue receipt in *Rajaram Maize Products* (supra), we need not be influenced by this decision in answering the substantial question in the present case relating to determination of the receipt towards *transport subsidy*.

25. Following the above discussion and analysis and also the ratio of the decisions in *Sahney Steel & Press Works Ltd.* (supra), *Ponni Sugars & Chemicals Ltd.* (supra), *Jai Bhagwan Oil and Flour Mills* (supra) and applying the *purpose test*, we are of the considered opinion that the *transport subsidy* received by the assessee during the assessment year 2001-02 is intended to stimulate industrial activity in the backward region, to generate employment opportunities and bring about developments in the N.E. States and it is not meant to provide higher profit for the entrepreneur. It is intended to encourage investment in difficult and far flung states and the sum received under subsidy head cannot be treated as revenue receipt. Instead such incentives should be treated as capital receipt and thus not taxable, in the hands of the assessee. Accordingly the substantial question of law in this appeal is answered against the revenue and in favour of the assessee.

26. With the above declaration, the appeal stands disposed of by leaving the parties to bear their own cost.

Roy

JUDGE

JUDGE