

IN THE HIGH COURT OF KARNATAKA AT BENGALURU

DATED THIS THE 16TH DAY OF JUNE 2016

PRESENT

THE HON'BLE MR.JUSTICE JAYANT PATEL

AND

THE HON'BLE MR.JUSTICE B.SREENIVASE GOWDA

ITA NO.50/2016

BETWEEN

1. PR. COMMISSIONER OF INCOME TAX-III
C.R. BUILDING,
QUEENS ROAD,
BANGALORE

2. DEPUTY COMMISSIONER OF INCOME TAX
CIRCLE 12(3),
BANGALORE

... APPELLANTS

(BY SRI.E.I.SANMATHI, ADVOCATE)

AND

M/S. SAMI LABS LTD.,
19/1 & 19/2, 2ND PHASE,
PEENYA INDUSTRIAL AREA,
BANGALORE-58

... RESPONDENT

THIS ITA IS FILED UNDER SEC.260-A OF INCOME TAX ACT 1961, ARISING OUT OF ORDER DATED:10/07/2015 PASSED IN ITA NO.1227/BANG/2014, FOR THE ASSESSMENT YEAR 2006-2007 PRAYING TO DECIDE THE FOREGOING QUESTION OF LAW AND / OR SUCH OTHER QUESTIONS OF LAW AS MAY BE FORMULATED BY THE HON'BLE COURT AS DEEMED FIT, SET ASIDE THE APPELLATE ORDER DATED:10/07/2015 PASSED BY THE ITAT, 'B' BENCH, BENGALURU AS SOUGHT FOR, IN THE RESPONDENT-ASSESSEE'S CASE, IN APPEAL PROCEEDINGS NO. ITA NO.1227/BANG/2014 AND GRANT SUCH OTHER RELIEF AS DEEMED FIT, INTEREST OF JUSTICE.

THIS APPEAL COMING ON FOR ADMISSION THIS DAY, **JAYANT PATEL J.**, DELIVERED THE FOLLOWING:

JUDGMENT

The appellants-Revenue has preferred the present appeal by raising the following substantial questions of law:

1. "Whether on the facts and circumstances of the case, the tribunal is justified in allowing cultivation expenses to be set-off against other business incomes on the ground that the same

were incurred due to commercial expediency, without appreciating that the assessee has undertaken cultivation as a separate activity by way of entering into agreements with the farmers which is in the nature of contract farming?"

2. Whether on the facts and circumstances of the case, the Tribunal is right in allowing setting of losses claimed by assessee by following the decision of this Hon'ble Court in case of CIT v/s. Yokogowa when same has not reached finality"?

2. We have heard Mr.E.I.Sanmathi, learned Counsel appearing for the appellants-Revenue.

3. The perusal of the order passed by the Tribunal which is impugned in the present appeal shows that the Tribunal has relied upon the decision of this Court in case of ITA No.207/2011 dated 21.02.2012 in respect of the very assessee for the assessment year 2004-05.

4. We may record that in the above referred decision of this Court in ITA No.207/2011, it was observed thus:

“The Revenue has preferred this appeal challenging the order passed by the Tribunal, which has held the cultivating expenses incurred by the Assessee is in the nature of expenditure in the course of business, as such assessee is entitled to claim deduction of said expenditure.

2. The Assessee is involved in the manufacture and export of standardized herbal extracts as well as in the manufacture of fine chemicals. The assessee filed return of Income for the year 2004-2005. Assessee claimed deduction under Section 10-B of the Income Tax Act, 1961 (for short hereinafter referred to as ‘the Act’). The Assessing Authority disallowed the cultivation expenses amounting to ₹.90.64 Lakhs. The Appeal preferred by the Assessee to the Commissioner of the Income Tax (Appeals) came to be dismissed. In the further appeal

against the said order to the Tribunal, the Tribunal held the assessee had not generated any agricultural income out of its venture; the Assessee has not engaged in any agricultural activities but for cultivation of coleus plants to facilitate its business and due to commercial expediency, it had incurred cultivation expenses to the tune of ₹.90.64 Lakhs. These expenses incurred by the Assessee were for a commercial expediency and wholly and exclusively for the purpose of its business. Therefore, the Tribunal held that authorities below were not justified in disallowing the cultivation expenses of ₹.90.64 Lakhs claimed by the Assessee. Aggrieved by the said order, Revenue is in appeal.

3. The learned Senior Counsel appearing for Revenue, assailing the impugned order, contended that the Tribunal has recorded a finding that Assessee was involved in agricultural activity. In fact, it has advanced money to the farmers for growing coleus crop. The expenses incurred in connection with the cultivation of said crop could be set-off against

the income which was exempted from payment of Income Tax. But, it cannot be construed as an expenditure incurred in carrying on the business. Such activity is a separate activity of the Assessee which is not in connection with the business and therefore, Assessee was not entitled to claim deduction under the heading "revenue expenditure".

4. The material on record disclose that coleus is a rare herbal plant which commands appreciation value in medicinal fraternity for research. The Assessee has been in the business of manufacture and export of herbal extracts including cultivation of coleus. To maximize the production and sale of herbal extract, the assessee incurred expenditure on cultivation activities for the development of coleus. The said plant was grown in wild. Vast research was required to make a commercial cultivation of the plant. To cultivate this plant, the Assessee had to undertake farm trials to optimize in different fields such as:-

- i) Optimization of the right season for cultivation.
- ii) Standardization of the right fertilizer application.
- iii) Optimization of the right solid conditions.
- iv) Use of various organic fertilizers.
- v) Use of bio-controls and other control measures for disease control.

These exercises done by the assessee during the relevant period for maximizing the yield, did not result in a desired effect. In order to promote the cultivation of coleus, the farmers were roped-in to cultivate this rare herbal plant and encouraged them to opt for this crop. For this purpose, the assessee had to incur expenditure for -

- i) Supply of planting materials to the farmers free of cost.
- ii) Supply of farm inputs free of cost &

iii) Arranging payments to them.

To propagate its intention to supply seedlings from its nursery to other farmers, it had entered into agreements and supplied coleus seedlings to the farmers with a condition to recover the cost of coleus seedling at 10 paise per seedling at the time of harvest. However, the Assessee was not able to achieve the desire of generating sufficient quantities of coleus. Instead, it had rather gone to purchase spree of coleus seedlings in a large scale from other farmers. Therefore, the assessee did not generate any agricultural income of the said income. In fact they did not involve themselves in any agricultural activities but they encouraged cultivation of coleus plants to facilitate business. In this context, they have incurred cultivation expenses to the tune of ₹.90.64 Lakhs. The fact that Assessee had incurred a sum of ₹.90.64 Lakhs expenses, in this regard, is not in dispute.

5. The question for consideration is, whether it is to be considered as capital expenditure or

revenue expenditure. The Tribunal relied on Circular No.6/2007 issued by the Board, wherein it has been clarified as under:-

“2..... These expenses are incurred by the sugar mills for ensuring an adequate and sustained supply of freshly cut sugarcane that is an essential input for the continuous running of such mills. These expenses are, therefore, incurred for a commercial expediency and are prima facie wholly and exclusively for the purpose of business. Such expenses are, therefore, allowable.....”

6. In fact, the Apex Court had an occasion to consider this question in the case of *Commissioner of Income Tax, Mysore Vs. Mysore Sugar Co. Ltd.*, reported in 1962 ITR Vol.XLVI page 649. The question which was posed for consideration was, for what was the money laid out? Was it to acquire an asset of an enduring nature for the benefit of the business or was it an outgoing in the doing of the business?. If money be lost in the first circumstance, it is a loss of capital, but if lost in the second circumstance, it is a revenue loss. In the first, it bears the character of an investment, but in the second, to use a commonly understood

phrase, it bears the character of current expenditure.

7. After referring to three English judgments, it was held to be a use of money in the course of the company's business and not an investment of capital at all. The cases referred to therein illustrate the distinction between an expenditure by way of investment and an expenditure in the course of business, which has been described as current expenditure. The first may truly be regarded as on the capital side but not the second. The amount was an advance against price of one crop. The oppigedars were to get the assistance not as an investment by the assessee company in its agriculture, but only as an advance payment of price. The amount, so far as the assessee company was concerned, represented the current expenditure towards the purchase of sugarcane and it makes no difference that the sugarcane thus purchased was grown by the oppigedars with the seedlings, fertilizers and money taken on account from the Assessee Company. In so far as the Assessee

Company was concerned, it was doing no more than making a forward arrangement for the next year's crop and paying an amount in advance out of the price, so that the growing of the crop may not suffer due to want of funds in the hands of the growers. There was hardly any element of investment which contemplates more than payment of advance price. The resulting loss to the assessee company was just as much a loss on the revenue side as would have been, if it had paid for the ready crop which was not delivered.

8. Therefore, the law on the point is clearly settled. If the money spent by the Assessee is by way of investment, then the Assessee is not entitled to deduct the same as expenditure. It would be in the nature of capital expenditure, which is not deductible. However, if the money spent is not for acquiring asset of enduring nature for the benefit of the business but which is only an outgoing in the doing of the business, then it would be an expenditure in the course of this business.

9. If the Assessee has spent money by way of financial accommodation to the farmers or expenses incurred in supplying seedling, fertilizers and for other cultivation expenses, then it would be in the nature of revenue expenditure. It is incurred by the Assessee for a commercial expediency. It was incurred wholly and exclusively for the purpose of business and the Assessee would be entitled for allowance of the said cultivation expenses as revenue expenditure.

10. In the instant case, material on record disclose, the Assessee is in the business of manufacture and export of standardized herbal extracts as well as in the manufacture of fine chemicals. In order to carry on their business, they were in need of herbal coleus plants. they thought of roping the farmers for growing said herbal plant. They provided seedlings, fertiliser and financial assistance to the farmers with an agreement to deduct the expenses out of the cost of the plant sold by the farmers. But, even the

farmers could not grow the said herbal plant. Consequently, they sustained loss and in turn the assessee sustained loss. The said cultivation expenses was ₹.90.64 Lakhs. Therefore, the assessee claimed the said amount as revenue expenditure as the said expenditure was incurred to facilitate its business and due commercial expediency. As such the loss are primarily attributable to the business which the Assessee is carrying on and the said expenses are wholly and exclusively for the purpose of business. The said cultivation expenses incurred by the Assessee is in the nature of revenue expenditure in the course of business and the Assessee is entitled to deduction of the same as business expenditure. Therefore, the Tribunal is justified in upholding such claim and granting relief to the assessee.

11. In that view of the matter, there is no merits in this appeal and accordingly the appeal is dismissed.”

5. In view of the above, as the questions are already covered by the decision of this Court, no substantial questions of law would arise for consideration as formulated in question No.1. So far as question No.2 is concerned, the matter is already covered by the decision of this Court in case of ***Commissioner of Income Tax And Another Vs. Yokogawa India Ltd.***, reported at **(2012) 341 ITR page 385**. Hence it cannot be said that any substantial question of law would arise for consideration.

Hence the appeal is dismissed.

**Sd/-
JUDGE**

**Sd/-
JUDGE**

JT/-