

IN THE HIGH COURT OF KARNATAKA AT BENGALURU

DATED THIS THE 29TH DAY OF MARCH, 2016

PRESENT

THE HON'BLE MR. JUSTICE JAYANT PATEL

AND

THE HON'BLE MRS. JUSTICE B.V.NAGARATHNA

I.T.A. NO.169/2015

BETWEEN:

COMMISSIONER OF INCOME TAX-III,
REVENUE BUILDINGS,
QUEENS ROAD,
BANGALORE - 560 001.

... APPELLANT

(BY SRI: K.V. ARAVIND, SENIOR STANDING COUNSEL)

AND:

M/S. SUBHASH KABINI POWER
CORPORATION LIMITED,
8/2, ULSOOR ROAD,
BANGALORE - 560 042.
PAN: AACCS0881J.

... RESPONDENT

(BY SRI: R.V. EASWAR, SENIOR ADVOCATE FOR
SMT. CHYTHANYA K.K., ADVOCATE)

THIS ITA IS FILED UNDER SEC.260-A OF INCOME TAX
ACT 1961, ARISING OUT OF ORDER DATED:28/11/2014
PASSED IN ITA NO.258/BANG/2014, FOR THE ASSESSMENT
YEAR 2009-2010.

THIS ITA COMING ON FOR ADMISSION THIS DAY,
JAYANT PATEL J., DELIVERED THE FOLLOWING:-

J U D G M E N T

The appellant/Revenue has preferred the present appeal by raising the following substantial questions of law:

1. *Whether on the facts and in the circumstances of the case, the Tribunal was justified in law in quashing the order under Section 263 of the Income Tax Act without appreciating the judgment of Supreme Court in the case of **M/s.Liberty India v. CIT [317 ITR 218]** and **M/s. Sterling Foods v. CIT [237 ITR 579]** that any ancillary profits should be excluded from the meaning of profits derived from the eligible business for the purpose of deduction under Section 80IA and the consideration received from the sale of carbon credits is not derived from the eligible business undertakings?*
2. *Whether on the facts and in the circumstances of the case, the Tribunal was justified in law in treating the sale proceeds of carbon credits as capital in nature without appreciating that the Carbon Emission Reduction Certificates issued by*

the UNFCC have intrinsic value and has a ready market for its redemption/trading, that the assessee pursues to obtain the said certificate and hence the sale proceeds arising out of sale of the carbon credits by the assessee is revenue in nature?

3. *Whether on the facts and circumstances of the case, the Tribunal was justified in relying upon the judgment passed by the jurisdictional High Court in the case of **CIT v. D.G. Gopala Gowda [354 ITR 501(2013)]** and thereby holding that the order passed under Section 263 as revenue neutral case and is not prejudicial to the interest of the Revenue?*

2. We have heard Mr. K.V.Aravind, learned Senior Standing Counsel for the appellant/Revenue and Mr. R.V.Easwar, learned Senior Counsel for Mr. Chythanya K.K., learned counsel appearing for respondent/assessee.

3. We may record the relevant discussion of the Tribunal from paragraph Nos.7 to 11 as under:

"7. We have duly considered the rival contentions and gone through the record carefully. Before embarking upon an inquiry about the facts available on record and how to construe them, we deem it pertinent to take note of the fundamental principles for judging the action of the CIT taken u/s 263. The ITAT in the case of M/s Khatiza S. Oomerbhoy Vs. ITO, Mumbai reported in 101 TTJ 1095, analyzed in details various authoritative pronouncements including the decision of the Hon'ble Supreme Court in the case of Malabar Industries Co. vs. CIT 243 ITR 83 and propounded the following broader tests:

- (i) The CIT must record satisfaction that the order of the AO is erroneous and prejudicial to the interest of the Revenue. Both the conditions must be fulfilled.
- (ii) Sec. 263 cannot be invoked to correct each and every type of mistake or error committed by the AO and it was only when an order is erroneous that the section will be attracted.

- (iii) *An incorrect assumption of facts or an incorrect application of law will suffice the requirement of order being erroneous.*
- (iv) *If the order is passed without application of mind, such order will fall under the category of erroneous order.*
- (v) *Every loss of revenue cannot be treated as prejudicial to the interests of the Revenue and if the AO has adopted one of the courses permissible under law or where two views are possible and the AO has taken one view with which the CIT does not agree. It cannot be treated as an erroneous order, unless the view taken by the AO is unsustainable under law*
- (vi) *If while making the assessment, the AO examines the accounts, makes enquiries, applies his mind to the facts and circumstances of the case and determine the*

income, the CIT, while exercising his power under s 263 is not permitted to substitute his estimate of income in place of the income estimated by the AO.

(vii) The AO exercises quasi-judicial power vested in his and if he exercises such power in accordance with law and arrive at a conclusion, such conclusion cannot be termed to be erroneous simply because the CIT does not see stratified with the conclusion.

(viii) The CIT, before exercising his jurisdiction under s. 263 must have material on record to arrive at a satisfaction.

(ix) If the AO has made enquiries during the course of assessment proceedings on the relevant issues and the assessee has given detailed explanation by a letter in writing and the AO allows the claim on being satisfied with the explanation of the assessee, the

decision of the AO cannot be held to be erroneous simply because in his order he does not make an elaborate discussion in that regard.

8. Before adverting to the facts of the present case, we would like to make a reference to the decision of the Hon'ble jurisdictional High Court in the case of CIT vs. D.G. Gopala Gowda, 354 ITR 501 (2013). In this case, the facts noticed by the Hon'ble High court read as under:

"2. The assessee had purchased a site at Rupena Agrahara in the financial year 1995-96 for a consideration of Rs.3,46,520/-. He started construction of the building in April 1999. He agreed to sell the said property under the agreement dated 9-9-2000 in unfinished condition. Under the terms of agreement, the assessee should complete the construction of the building before execution of sale deed with the help of the funds provided by the purchaser. On 22-11-2000 the assessee executed a sale deed in

favour of the purchaser for a consideration of Rs.1,38,00,000/- The assessee received a sum of Rs.40,00,000/- at the time of agreement. The total cost of construction was Rs.1,04,30,425/-. Thereafter, the assessee purchased another property at Koramangala. The Assessing Officer computed the income from the long term capital gains at Rs.22,17,940/- for the sale of the property. However, the assessee was exempted from paying tax since the fund was utilized fully towards purchase of another property at Koramangala. The Commissioner of Income Tax issued notice under Section 263 of the Act stating that the Assessing Officer was not justified in treating the sale as long term capital gain and according to him, it should have been treated as short term capital gain. The assessee filed his reply to the show cause notice. Thereafter, the Commissioner proceeded to pass the order setting aside the order of assessment on the

ground that it is prejudicial to the interest of the revenue. Aggrieved by the said order, the assessee preferred an appeal to the Tribunal. The Tribunal went into the factual aspects and took note of the legal position as settled in various judgments of the courts and in fact, calculated both the short term and long term capital gain and then found that the assessee is not liable to pay any tax. Therefore, it recorded the finding that even if the order of the Assessing Authority is erroneous, it is not prejudicial to the interest of the revenue. Therefore, set aside the order of the revisional authority and granted relief to the assessee".

9. The Hon'ble High Court while upholding the order of the ITAT has observed as under:

"Even if it is erroneous, unless the said erroneous order is prejudicial to the interest of the Revenue, the Commissioner could not have exercised the said power. From the

admitted material on record, the amount that is ordered to be refunded to the assessee is not the amount, which is lawfully due to the Revenue at all, it was an amount which is Revenue legitimately should have refunded if only the claim had been in the return enclosing the certificates under Section 203. The said amount should have been refunded to the assessee. Because he was handicapped by such certificates not being forwarded to him, consequently not able to make the claim, such a claim was not made. The moment he got possession of those certificates on 12.02.2001, within two years from the date of the end of the assessment year he has put forth the claim. The said amount was not a lawful amount to the Government. It was an amount which should have been refunded to the assessee.

Therefore, the condition precedent for exercising the revisional power under Section 263 of the Act is that the order under revision should not only

be erroneous, but such erroneous order should result in prejudice to the interest of the revenue. Mere error would not confer jurisdiction to exercise revisional power under Section 263 of the Act.

We have gone through the order passed by the revisional authority. It is a very cryptic order. It neither points out an error nor prejudice which has caused to the revenue. After declaring that the order is prejudicial, it refers to the notice being issued to the assessee and the assessee filing reply to the said notice and then review authority feels that it is a matter to be readjudicated by the Assessing Authority and therefore, the matter was remanded for fresh consideration. This is not the way, the revisional authority should exercise their power under Section 263 of the Act. The order of revisional authority should indicate the error committed by the Assessing Authority and consequential prejudice caused to the revenue because of the

erroneous order. Unless these two conditions exist, the revisional authority does not get jurisdiction to pass any order under Section 263 of the Act. Once these two conditions are set out in the order, then it is open to the revisional authority to consider the case on merits and pass final order or in its view, requires some adjudication or enquiry, the matter can be remanded to Assessing Authority. But such remand should be only after setting out the facts which show erroneous nature of the order and the consequential prejudice to the revenue which confer jurisdiction on the revisional authority.

Seen from that angle, in the impugned order though we could make out what is the error committed by the revisional authority, certainly there is no iota of evidence to show how it is prejudicial to the interest of the revenue. On the contrary, in the reply to the notice, the assessee had filed a statement. Even if the

assessment is to be made separately for the land on long term basis and to the building on short term basis, the assessee is not liable to pay any tax for the building. The assessee has demonstrated that in no event the order passed by the Assessing Officer is prejudicial to the interest of the revenue. That aspect has not been considered and there is no reference to that aspect in the entire order passed by the revisional authority and by a cryptic order, the matter is remanded to the Assessing Authority. Though the Tribunal was not expected to go into the merits of the case, in order to demonstrate that the order passed by the Assessing Authority even if it is erroneous, is not prejudicial to the interest of the revenue, they have set out computation of capital gains and demonstrated that the order was not prejudicial. Therefore, the order passed by the revisional authority is illegal and rightly it has been set aside.

In the light of what we have stated above, the substantial question of law is answered in favour of the assessee and against the revenue”.

10. The Hon’ble High Court has held that fulfillment of twin condition is must i.e. assessment order should be erroneous and it should cause a prejudice to the Revenue. If any one condition is lacking, then action u/s 263 would not be justified. In the above case, the assessment order was erroneous because the learned Assessing Officer failed to compute the long term capital gain and short term capital gain separately. But the Tribunal ultimately arrived at a conclusion that even if this exercise is being done, then there will not be any tax liability and therefore, there is no need to set aside the assessment order. The Hon’ble High Court has upheld this finding of the Tribunal. In the light of the above, let us examine the facts of the present case. There is no dispute that the assessee is in the business of Hydro Power Project. It has earned carbon credit which has been rated by the agency and it has

sold those carbon credit to a Japanese Company. The details indicating service from carbon management service, allotment of letter of carbon credit, sale bill for sale of carbon credits are available on page Nos. 102 to 110 of the paper book. The ITAT Hyderabad has decided this issue for the first time and the discussion made by the ITAT Hyderabad Bench worth to note, it read as under:

"24. We have heard both the parties and perused the material on record. Carbon credit is in the nature of "an entitlement" received to improve world atmosphere and environment reducing carbon, heat and gas emissions. The entitlement earned for carbon credits can, at best, be regarded as a capital receipt and cannot be taxed as a revenue receipt. It is not generated or created due to carrying on business but it is accrued due to "world concern". It has been made available assuming character of transferable right or entitlement only due to world concern. The source of carbon credit is world concern and

environment. Due to that the assessee gets a privilege in the nature of transfer of carbon credits. Thus, the amount received for carbon credits has no element of profit or gain and it cannot be subjected to tax in any manner under any head of income. It is not liable for tax for the assessment year under consideration in terms of sections 2(24), 28, 45 and 56 of the Income-tax Act, 1961. Carbon credits are made available to the assessee on account of saving of energy consumption and not because of its business. Further, in our opinion, carbon credits cannot be considered as a bi-product. It is a credit given to the assessee under the Kyoto Protocol and because of international understanding. Thus, the assessees who have surplus carbon credits can sell them to other assesses to have capped emission commitment under the Kyoto Protocol. Transferable carbon credit is not a result or incidence of one's business and it is a credit for reducing

emissions. The persons having carbon credits get benefit by selling the same to a person who needs carbon credits to overcome one's negative point carbon credit. The amount received is not received for producing and/or selling any product, bi-product or for rendering any service for carrying on the business. In our opinion, carbon credit is entitlement or accretion of capital and hence income earned on sale of these credits is capital receipt. For this proposition, we place reliance on the judgment of the Supreme Court in the case of CIT vs. Maheshwari Devi Jute Mills Ltd. (57 ITR 36) wherein held that transfer of surplus loom hours to other mill out of those allotted to the assessee under an agreement for control of production was capital receipt and not income. Being so, the consideration received by the assessee is similar to consideration received by transferring of loom hours. The Supreme Court considered this fact and observed that

taxability of payment received for sale of loom hours by the assessee is on account of exploitation of capital asset and it is capital receipt and not an income. Similarly, in the present case the assessee transferred the carbon credits like loom hours to some other concerns for certain consideration. Therefore, the receipt of such consideration cannot be considered as business income and it is a capital receipt. Accordingly, we are of the opinion that the consideration received on account of carbon credits cannot be considered as income as taxable in the assessment year under consideration. Carbon credit is not an offshoot of business but an offshoot of environmental concerns. No asset is generated in the course of business but it is generated due to environmental concerns. Credit for reducing carbon emission or greenhouse effect can be transferred to another party in need of reduction of carbon emission. It does not increase profit in any manner and

does not need any expenses. It is a nature of entitlement to reduce carbon emission, however, there is no cost of acquisition or cost of production to get this entitlement. Carbon credit is not in the nature of profit or in the nature of income.

25. Further, as per guidance note on accounting for Self-generated Certified Emission Reductions (CERs) issued by the Institute of Chartered Accountants of India (ICAI) in June, 2009 states that CERs should be recognised in books when those are created by UNFCCC and/or unconditionally available to the generating entity. CERs are inventories of the generating entities as they are generated and held for the purpose of sale in ordinary course. Even though CERs are intangible assets those should be accounted as per AS-2 (Valuation of inventories) at a cost or market price, whichever is lower. Since CERs are recognised as inventories, the generating assessee should apply AS-

9 to recognise revenue in respect of sale of CERs.

26. Thus, sale of carbon credits is to be considered as capital receipt. This ground is allowed.

27. As we have decided the main issue, the alternate ground of the assessee becomes infructuous and the same is dismissed.

28. In the result, assessee's appeal is allowed.

Order pronounced in the open court on 2nd November, 2012".

11. The decision has been upheld by the Hon'ble Andhra Pradesh High Court. This decision has been subsequently followed by the ITAT Chennai and Jaipur Benches. There is no decision either from the Hon'ble Supreme Court or from the Hon'ble jurisdictional High Court. These decisions indicate that sale of carbon credit would result capital receipt which is not taxable. When we confronted the learned DR with regard to this position, it was contended

that the position as on the day when the assessment order was passed, is to be seen and on that day these orders were not available. Therefore, the assessee cannot claim the benefit of these orders. However, we do not concur with this proposition of the learned CIT, because the Full Bench of the Hon'ble Punjab & Haryana High Court in the case of Aruna Luthra reported in 254 ITR 76 has held that a Court decide a dispute between the parties. The case can involve decision on facts. It can also involve a decision on point of law. Both may have bearing on the ultimate result of the case. When a Court interprets a provision, it decides as to what is the meaning and effect of the words used by the Legislature, it is the declaration regarding the statute. In other words the judgment declares as to what the legislature had said at the time of promulgation of the law, the declaration is....., this was the law, this is the law, this is how the provision shall be construed. Therefore, he cannot plead that the view taken by the Tribunal and upheld by the Hon'ble Andhra Pradesh High Court

could be considered as if applicable from the date of the decision. In the decision only the position of the law as to how receipts from sale of carbon credits are to be treated, has been explained. One of the argument raised by the DR was that at this stage, the additional ground ought not to be permitted to be raised. It is pertinent to mention here that basically, it is not a separate ground, it is a limb of arguments, which is affecting the ultimate tax liability of the assessee. The Hon'ble Supreme Court in the case of NTPC Ltd (Supra) has held that the Tribunal had jurisdiction to examine a question of law which arose from the fact as found by the Income Tax authorities and having a bearing on the tax liability of the assessee. As far as the nature of the receipt from sale of carbon credit is concerned, it is available from the assessment stage. It is not disputed even by the learned Commissioner, the dispute is, whether it has been derived from the eligible industrial undertaking for qualifying the grant of deduction u/s 80IA. The learned Commissioner felt that this receipt has not been derived from the industrial

undertaking which will be eligible for grant of deduction u/s 80IA and the Assessing Officer committed an error in including the receipt in the eligible profit. Those facts are already on the record. It is to be seen, whether the receipt is of capital nature or of a revenue nature. Even in case the order of the CIT is upheld, then, in law, it will affect the computation of income, ultimately because the receipt will not be taxable, it will not come under the ambit of computation of income. Simultaneously it will be excluded from the deduction u/s 80IA as well as of the total income. The result will remain as it is. It is a revenue neutral case. Therefore, in view of the ratio laid down by the Hon'ble jurisdictional High Court in the case of Gopala Gowda (Supra), the second condition for taking action u/s 263 does not exist. The assessment order is not prejudicial to the interests of the Revenue. In view of the above discussion, we allow the appeal of the assessee and quash the impugned order of the learned CIT passed u/s 263 of the Income Tax Act."

The aforesaid shows that, so far as the question as to whether, the income by sale of carbon credit could be termed as capital receipt or profit, is concerned, the Tribunal has considered the decision of the Hyderabad Bench and it has further taken note of the fact that decision of the Tribunal of Hyderabad Bench was carried before the Andhra Pradesh High Court and the said decision was not interfered with. The Tribunal, in its decision has also referred to the decision of the Apex Court with regard to power under Section 263 of the Income Tax Act, 1961 (hereinafter referred to as "the Act") of the revisional authority.

4. In our view, the principal question, which may arise is, as to whether by sale of carbon credit capital receipt is generated or a profit out of the business activity of the assessee. More or less, in a similar case, the Apex Court had an occasion to consider such an issue in the case of **Commissioner of Income Tax v. Maheshwari Devi Jute Mills Ltd. [(1965) 57 ITR 36(SC)]**, wherein the question

came up for consideration before the Apex Court as to whether by sale of loom-hours, the amount received could be termed as capital receipt or the income out of business. In the said decision, the Apex Court held that the amount received out of sale of loom-hours can be termed as capital receipt and not income out of business.

5. Subsequently, in a later decision of the Apex Court, a question came up for consideration in the case of ***M/s. Empire Jute Co. Ltd. v. Commissioner of Income Tax [(1980) 4 SCC 25]*** the question which arose before the Apex Court was, if loom-hours are purchased by the manufacturing mills, whether it can be termed as capital expenditure or revenue expenditure. In the said decision, the earlier decision of the Apex Court in the case of *Maheswari Devi Jute Mills* (supra) was also relied upon by the Revenue and after considering the same, the Apex Court at paragraph Nos.4 and 5 observed thus:

"4. Now an expenditure incurred by an assessee can qualify for deduction under Section 10(2) (xv) only if it is incurred wholly and exclusively for the purpose of his business, but even if it fulfils this requirement, it is not enough; it must further be of revenue as distinguished from capital nature. Here in the present case it was not contended on behalf of the Revenue that the sum of Rs. 2,03,255 was not laid out wholly and exclusively for the purpose of the assessee's business but the only argument was and this argument found favour with the High Court, that it represented capital expenditure and was hence not deductible under Section 10(2) (xv). The sole question which therefore arises for determination in the appeal is whether the sum of Rs. 2,03,255 paid by the assessee represented capital expenditure or revenue expenditure. We shall have to examine this question on principle but before we do so, we must refer to the decision of this Court in *Maheshwari Devi Jute Mills case*² since that is the decision which weighed heavily with the High Court, in fact, compelled it to

negative the claim of the assessee and hold the expenditure to be on capital account. That was a converse case where the question was whether an amount received by the assessee for sale of loom hours was in the nature of capital receipt or revenue receipt. The view taken by this Court was that it was in the nature of capital receipt and hence not taxable. It was contended on behalf of the Revenue, relying on this decision, that just as the amount realised for sale of loom hours was held to be capital receipt, so also the amount paid for purchase of loom hours must be held to be of capital nature. But this argument suffers from a double fallacy.

5. *In the first place it is not a universally true proposition that what may be capital receipt in the hands of the payee must necessarily be capital expenditure in relation to the payer. The fact that a certain payment constitutes income or capital receipt in the hands of the recipient is not material in determining whether the payment is revenue or capital disbursement qua the payer. It was felicitously pointed out by Macnaghten, J.*

in Racecourse Betting Control Board v. Wild³ that a "payment may be a revenue payment from the point of view of the payer and a capital payment from the point of view of the receiver and vice versa". Therefore, the decision in Maheshwari Devi Jute Mills case² cannot be regarded as an authority for the proposition that payment made by an assessee for purchase of loom hours would be capital expenditure. Whether it is capital expenditure or revenue expenditure would have to be determined having regard to the nature of the transaction and other relevant factors."

Thereafter, the Apex Court while considering the test to find out as to whether a particular expenditure can be termed as capital or revenue expenditure observed at paragraph Nos.8 and 9 as under:

"8. The decided cases have, from time to time, evolved various tests for distinguishing between capital and revenue expenditure but no test is paramount or conclusive. There is no all embracing formula which can provide a ready solution to the problem; no touchstone has been

devised. Every case has to be decided on its own facts keeping in mind the broad picture of the whole operation in respect of which the expenditure has been incurred. But a few tests formulated by the courts may be referred to as they might help to arrive at a correct decision of the controversy between the parties. One celebrated test is that laid down by Lord Cave, L. C., in Atherion v. British Insulated and Halsby Cables Ltd.⁴ where the learned law Lord stated:

When an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital.

This test, as the parenthetical clause shows, must yield where there are special circumstances leading to a contrary

conclusion and, as pointed out by Lord Radcliffe in Commissioner of Taxes v. Nchanga Consolidated Copper Mines Ltd.⁵, it would be misleading to suppose that in all cases, securing a benefit for the business would be prima facie capital expenditure "so long as the benefit is not so transitory as to have no endurance at all". There may be cases where expenditure, even if incurred for obtaining advantage of enduring benefit, may, nonetheless, be on revenue account and the test of enduring benefit may break down. It is not every advantage of enduring nature, acquired by an assessee that brings the case within the principle laid down in this test. What is material to consider is the nature of the advantage in a commercial sense and it is only where the advantage is in the capital field that the expenditure would be disallowable on an application of this test. If the advantage consists merely in facilitating the assessee's trading operations or enabling the management and conduct of the assessee's business to be carried on more efficiently or more profitably while leaving

the fixed capital untouched, the expenditure would be on revenue account, even though the advantage may endure for an indefinite future. The test of enduring benefit is therefore not a certain or conclusive test and it cannot be applied blindly and mechanically without regard to the particular facts and circumstances of a given case. But even if this test were applied in the present case, it does not yield a conclusion in favour of the Revenue. Here, by purchase of loom hours no new asset has been created. There is no addition to or expansion of the profit-making apparatus of the assessee. The income-earning machine remains what it was prior to the purchase of loom hours. The assessee is merely enabled to operate the profit-making structure for a longer number of hours. And this advantage is clearly not of an enduring nature. It is limited in its duration to six months and, moreover, the additional working hours per week transferred to the assessee have to be utilised during the week and cannot be carried forward to the next week. It is, therefore, not possible to say that any

advantage of enduring benefit in the capital field was acquired by the assessee in purchasing loom hours and the test of enduring benefit cannot help the Revenue.

9. Another test which is often applied is the one based on distinction between fixed and circulating capital. This test was applied by Lord Haldane in the leading case of *John Smith & Son v. Moore*⁶ where the learned law Lord drew the distinction between fixed capital and circulating capital in words which have almost acquired the status of a definition. He said:

Fixed capital (is) what the owner turns to profit by keeping it in his own possession; circulating capital (is) what he makes profit of by parting with it and letting it change masters.

Now so long as the expenditure in question can be clearly referred to the acquisition of an asset which falls within one or the other of these two categories, such a test would be a critical one. But this test also sometimes break down because there are

many forms of expenditure which do not fall easily within these two categories and not infrequently, as pointed out by Lord Radcliffe in *Commissioner of Taxes v. Nchanga Consolidated Copper Mines Ltd.*⁵, the line of demarcation is difficult to draw and leads to subtle distinctions between profit that is made "out of" assets and profit that is made "upon" assets or "with" assets. Moreover, there may be cases where expenditure, though referable to or in connection with fixed capital, is nevertheless allowable as revenue expenditure. An illustrative example would be of expenditure incurred in preserving or maintaining capital assets. This test is therefore clearly not one of universal application. But even if we were to apply this test, it would not be possible to characterise the amount paid for purchase of loom hours as capital expenditure, because acquisition of additional loom hours does not add at all to the fixed capital of the assessee. The permanent structure of which the income is to be the produce or fruit remains the same; it is not enlarged. We are not sure whether loom

hours can be regarded as part of circulating capital like labour, raw material, power etc., but it is clear beyond doubt that they are not part of fixed capital and hence even the application of this test does not compel the conclusion that the payment for purchase of loom hours was in the nature of capital expenditure."

After making the aforesaid observation, at paragraph No.10, the Apex Court, on the basis of the facts of the said case concluded as under:

"Similarly, if payment has to be made for securing additional power every week, such payment would also be part of the cost of operating the profit-making structure and hence in the nature of revenue expenditure, even though the effect of acquiring additional power would be to augment the productivity of the profit-making structure. On the same analogy payment made for purchase of loom hours which would enable the assessee to operate the profit-making structure for a longer number of hours than those permitted under the working time agreement would also be part of the cost of

performing the income-earning operations and hence revenue in character."

Accordingly, the payment made for purchase of loom-hours by Jute Mill Company was held to be Revenue expenditure.

6. At this stage, we may also refer to the decision of the Andhra Pradesh High Court, which has been relied upon by the Tribunal in the impugned order. More or less, identical question was raised and the Andhra Pradesh High Court in the case of ***Commissioner of Income Tax-IV v. My Home Power Ltd. [(2014) 46 Taxmann.com 314 (Andhra Pradesh)***, at paragraph No.3 observed thus:

"3. We have considered the aforesaid submission and we are unable to accept the same, as the learned Tribunal has factually found that "Carbon Credit is not an offshoot of business but an offshoot of environmental concerns. No asset is generated in the course of business but it is generated due to environmental concerns.

"We agree with this factual analysis as the assessee is carrying on the business of power generation. The Carbon Credit is not even directly linked with power generation. On the sale of excess Carbon Credits the income was received and hence as correctly held by the Tribunal it is capital receipt and it cannot be business receipt or income. In the circumstances, we do not find any element of law in this appeal."

The aforesaid shows that the Andhra Pradesh High Court has confirmed the view of the Tribunal that Carbon Credit is not an offshoot of business, but an offshoot of environmental concerns. No asset is generated in the course of business, but it is generated due to environmental concerns. It was also found that the carbon credit is not even directly linked with the power generation and the income is received by sale of the excess carbon credits. It was found that the Tribunal has rightly held that it is capital receipt and not business income.

7. As such, in our view, when the issue is already covered by the decision of the Andhra Pradesh High Court, wherein the view taken by the Tribunal of Hyderabad Bench has been followed in the present case, one may say that no substantial question of law would arise for consideration.

8. However, Mr.K.V. Aravind, learned counsel appearing for the appellant/Revenue, relied upon the provisions of Section 28 of the Act and contended that if any benefit or perquisite or credit is generated from the business, the same would be a profit from business and is taxable. Therefore, the same cannot be termed as capital receipt, but business income. In his submission, it was stated that on account of running the business of power generation, carbon credit is earned, which is marketable and therefore, it is an income out of business.

9. We cannot accept the said submission for the simple reason that earning of carbon credit is not the business of the assessee nor the same is

generated as a by product on account of business activity of power generation, but it is earned on account of concern for environment carbon credit is generated on account of employment of good and viable practices by the assessee.

10. Mr. Aravind, learned counsel for the Revenue also relied upon the decision of the Apex Court in the case of ***Oberoil Hotel (P) Ltd. v. Commissioner of Income Tax [(1999) 103 Taxman 236 (SC)]*** and another decision in the case of ***Kettlewell Bullen & Co. Ltd. v. Commissioner of Income Tax [(1964) 53 ITR 261]*** and contended that unless there is any adverse effect to the trading structure of the business, the income received cannot be termed as capital receipt.

11. In our view, the aforesaid decisions are of no help to the Revenue for the reason that to find out whether the particular amount received is a capital receipt or income out of business, there cannot be any standard yardstick or a straight-jacket formula as

observed by the Apex Court in the case of *M/s. Empire Jute Co. Ltd.* (Supra). The facts of the aforesaid two decisions of the Apex Court in the case of *Kettlewell Bullen* as well as *Oberoji Hotel* were concerning the issue of contract and the effect on the trading activity, which was undertaken pursuant to the contract. Therefore, such observations made by the Apex Court can not be applied to the fact situation in the present case. Hence, the said decisions are of no help to the appellant/Revenue.

12. Considering the above, we find that when the carbon credit is generated out of environmental concerns, and it is not having the character of trading activity, the Tribunal has rightly held that it is capital receipt and it is not income out of business and hence, not liable to pay income tax.

13. Once it is found that the amount realized by sale of carbon credit is not taxable as profit, naturally it will have no adverse effect on the Revenue. It is settled legal position that one of the

requirements for exercise of power under Section 263 of the Act, is that the order passed by the lower authority should not only be erroneous, but should also be prejudicial to the interest of the Revenue, which is lacking in the present case and rightly found so by the Tribunal.

14. In view of the above, we do not find any substantial question of law would arise as sought to be canvassed. Hence, the appeal is meritless and therefore, dismissed.

**Sd/-
JUDGE**

**Sd/-
JUDGE**

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