

IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

TAX APPEAL NO. 255 of 2007

FOR APPROVAL AND SIGNATURE:

HONOURABLE MS.JUSTICE HARSHA DEVANI

and

HONOURABLE MR.JUSTICE A.G.URAIZEE

1	Whether Reporters of Local Papers may be allowed to see the judgment ?	No
2	To be referred to the Reporter or not ?	No
3	Whether their Lordships wish to see the fair copy of the judgment ?	No
4	Whether this case involves a substantial question of law as to the interpretation of the Constitution of India or any order made thereunder ?	No

BANCO PRODUCTS (INDIA) LTD.....Appellant(s)

Versus

DEPUTY COMMISSIONER OF INCOME TAX....Opponent(s)

Appearance:

MR SN SOPARKAR, SENIOR ADVOCATE with MRS SWATI SOPARKAR,
ADVOCATE for the Appellant(s) No. 1

MR KM PARIKH, ADVOCATE for the Opponent(s) No. 1

CORAM: HONOURABLE MS.JUSTICE HARSHA DEVANI
and
HONOURABLE MR.JUSTICE A.G.URAIZEE

Date : 05/10/2015

ORAL JUDGMENT

(PER : HONOURABLE MS.JUSTICE HARSHA DEVANI)

1. The appellant assessee in this appeal under section 260A of the Income Tax Act, 1961 (hereinafter referred to as “the Act”) has challenged the order dated 31.7.2006 passed by the Income Tax Appellate Tribunal, Ahmedabad Bench “A”, Ahmedabad (hereinafter referred to as “the Tribunal”) in ITA No.2673/Ahd/2004.

2. By an order dated 19.11.2007, this court had admitted the appeal on the following substantial questions of law:

“(i) Whether in the facts and circumstances of the case the Income Tax Appellate Tribunal was right in law in holding that amount of subsidy received prior to insertion of Explanation 10 to section 43(1) of the Act can still be reduced from the cost of assets?

(ii) Whether in the facts and circumstances of the case, the Income Tax Appellate Tribunal was right in law in holding that for the purpose of calculating deduction u/s 80HHC of the Act, gross interest income without reducing therefrom the interest expenditure, is required to be excluded?”

3. The assessment year is 2000-2001 and the relevant accounting period is the previous year 1999-2000. The assessee is a public limited company engaged in the business of manufacturing of radiators, gaskets and compressed fiber

jointing sheets (CFJS). The assessee had got a subsidy of Rs.25,00,000/- (rupees twenty five lakhs) from the Commissioner of Industries, Gandhinagar for the investment made in building, plant and machinery and electrification in its industrial unit at Ankhi, District Baroda for production of compressed fiber jointing sheets. The subsidy was sanctioned on 17.8.1989 for investment in the capital assets but was received only in the year under consideration. The Assessing Officer was of the view that the subsidy having been given against investments in fixed capital assets, in view of the provisions of Explanation 10 to section 43(1) of the Act, the proportionate cost of the assets is required to be reduced to the extent of Rs.25,00,000/- because this cost has been met by the State Government in the form of subsidy. The assessee carried the matter in appeal before the Commissioner (Appeals) but did not succeed. The assessee carried the matter in further appeal on various grounds before the Tribunal, which dismissed this ground of appeal and confirmed the order passed by the Commissioner (Appeals) to that extent.

4. In relation to question No.1, Mr. S.N. Soparkar, Senior Advocate, learned counsel for the appellant submitted that the subsidy had been received in respect of the project which was set-up and commissioned in the year 1993-94. The plant and machinery and building and other investments which were made in the said plant were capitalised in 1993-94 as per the law prevailing on that day. The attention of the court was invited to the definition of "written down value" as contained in section 43(6)(c) of the Act, to submit that written down value in the case of block of assets means the opening written down value as increased or decreased by the two circumstances

enumerated thereunder, namely, increase in the block of assets on account of acquisition of new asset, provided such asset is put to be use in the year under consideration; and decrease in case where the asset is sold or otherwise disposed of in the previous year. It was submitted that section 43(6)(c) of the Act does not permit any other adjustment to be made from the written down value. Accordingly, adjustment cannot be made in the written down value of the block of assets by reducing the same by the amount of subsidy. It was further submitted that at the time when the assets came to be purchased, Explanation 10 to sub-section (1) of section 43 was not in existence and therefore, also the same would not be applicable to the facts of the present case. According to the learned counsel, the concept of actual cost has bearing only in year No.1, once the asset enters the block, it loses its identity and thereafter the question of calling upon the assessee to forego depreciation on the ground that the cost has been subsequently reduced, would not arise. It was pointed out that Explanation 10 to sub-section (1) of section 43 of the Act came to be inserted with effect from 1.4.1999 whereas the assets were purchased prior thereto.

4.1 In support of his submissions, the learned counsel placed reliance upon the decision of the Kerala High Court in the case of **Commissioner of Income Tax, Cochin v. Sun Fibre Optics Pvt, Ltd., (2012) 207 TAXMAN 8 (Kerala)**, wherein it has been held that Explanation 10 to sub-section (1) of section 43 introduced with effect from 1.4.1999 is prospective in nature and is applicable to depreciable assets after 1.4.1999. In the facts of the said case, since the subsidies had been received prior to 31.3.1998, the court held that Explanation 10

to sub-section (1) of section 43 was not applicable.

4.2 Reliance was also placed upon the decision of the Supreme Court in the case of **Commissioner of Income Tax v. Tata Iron and Steel Company Ltd., 1998 (231) ITR 285**, wherein it was held that what is the actual cost must depend on the amount paid by the assessee to acquire the asset. The amount may have been borrowed by the assessee. But even if the assessee does not repay the loan it will not alter the cost of the asset. Even if an asset is purchased from non-repayable subsidy received from the Government, the cost of the asset will be the price paid by the assessee for acquiring the asset. The court held that the price cannot change by any event subsequent to the acquisition of the asset. The learned counsel submitted that the subsidy received in the year under consideration cannot go to reduce the actual cost of the assets which were acquired in 1992-93 and which form block of assets with no independent identity of their own.

5. On the other hand, Mr. K. M. Parikh, learned senior standing counsel for the respondent supported the impugned order passed by the Tribunal by submitting that having regard to the provisions of Explanation 10 to sub-section (1) of section 43 of the Act, the amount received by way of subsidy is required to be reduced from the actual cost of the assets. It was submitted that Explanation 10 has been brought on the statute book with effect from 1.4.1999 and the subsidy has been received subsequent thereto, and hence, the actual cost of the asset was required to be reduced in terms of the Explanation. The Tribunal was, therefore, justified in holding that the actual cost of the assets is to be reduced by the

amount as per Explanation 10 to sub-section (1) of section 43 of the Act and the written down value of the assets has to be determined on the basis of the actual cost minus the depreciation allowed to the assessee from year to year and actual cost has to be the cost of the assets to the assessee minus the subsidy received by it.

5.1 In support of his submissions, the learned counsel placed reliance upon the decision of the Allahabad High Court in the case of **Commissioner of Income Tax v. Paliwal Glass Works**, 2010 (326) ITR 407 (All) wherein the court held that the subsidy received from the Government for the purpose of generator set was liable to be deducted to find out the actual cost of the asset. It was submitted that the impugned order passed by the Tribunal being in consonance with the provisions of Explanation 10 to sub-section (1) of section 43 of the Act, there is no warrant for interference by this court.

6. Before adverting to the merits of the rival submissions, it may be necessary to refer to certain statutory provisions. Sub-section (1) of section 43 of the Act, defines "actual cost" to mean the actual cost of the assets to the assessee, reduced by that portion of the cost thereof, if any, as has been met directly or indirectly by any other person or authority. Explanation 10 thereto, which has been inserted with effect from 1.4.1999, postulates that where a portion of the cost of an asset acquired by the assessee has been met directly or indirectly by the Central Government or a State Government or any authority established under any law or by any other person, in the form of a subsidy or grant of reimbursement (by whatever name called), then, so much of the cost as is relatable to such

subsidy or grant or reimbursement shall not be included in the actual cost of the asset to the assessee. The proviso to Explanation 10 says that where such subsidy or grant or reimbursement is of such nature that it cannot be directly relatable to the asset acquired, so much of the amount which bears to the total subsidy or reimbursement or grant the same proportion as such asset bears to all the assets in respect of or with reference to which the subsidy or grant or reimbursement is so received, shall not be included in the actual cost of the asset to the assessee.

7. Sub-section (6) of section 43 of the Act which defines “written down value”, and to the extent the same is relevant for the present purpose, reads thus:

“(6) “written-down value” means—

(a) in the case of assets acquired in the previous year, the actual cost to the assessee;

(b) in the case of assets acquired before the previous year, the actual cost to the assessee less all depreciation actually allowed to him under this Act, or under the Indian Income Tax Act, 1922 (11 of 1922), or any Act repealed by that Act, or under any executive orders issued when the Indian Income Tax Act 1886 (2 of 1886), was in force:

Provided that in determining the written-down value in respect of buildings, machinery or plant for the purposes of clause (ii) of sub-section (1) of Section 32, “depreciation actually allowed” shall not include depreciation allowed under sub-clauses (a), (b) and (c) of clause (vi) of sub-section (2) of Section 10 of the Indian Income Tax Act, 1922 (11 of 1922), where such depreciation was not deductible in determining the written-down value for the purposes of the said clause (vi);

(c) in the case of any block of assets,—

(i) in respect of any previous year relevant to the assessment year commencing on the 1st day of April, 1988, the aggregate of the written-down values of all the assets falling within that block of assets at the beginning of the previous year and adjusted,—

(A) by the increase by the actual cost of any asset falling within that block, acquired during the previous year; and

(B) by the reduction of the moneys payable in respect of any asset falling within that block, which is sold or discarded or demolished or destroyed during that previous year together with the amount of the scrap value, if any, so, however, that the amount of such reduction does not exceed the written-down value as so increased; and

(C) xxxxxx”

8. The facts of the case are required to be examined in the light of the above statutory provisions. At the relevant time when the assets came to be acquired in the year 1993-94, the subsidy, though sanctioned had not been disbursed. At the time when the assets came to be acquired, section 43(1) of the Act did not provide for non-inclusion of the subsidy received in the actual cost. Accordingly, the actual cost came to be computed in terms of the provisions in force at the relevant time. It may be noted that the assets in relation to which subsidy has been granted, form part of a block of assets and depreciation is granted on the written down value of the block of assets. In relation to block of assets, it is not possible to segregate items falling within the block for the purposes of granting depreciation or restricting the claim thereof. The

subsidy of Rs.25,00,000/- in relation to the assets in question came to be released in the year under consideration, by which time Explanation 10 to section 43(1) came to be inserted in the statute book, and accordingly, the Assessing Officer held that the cost of assets is required to be reduced out of the written down value of their respective blocks to the extent of Rs.25,00,000/-.

9. At this juncture, it may be noted that the expression “actual cost” envisages the actual cost of asset as reduced by any amount received directly or indirectly from any person or authority and Explanation 10 to section 43 (1) of the Act, clearly provides that where a portion of the cost of an asset acquired by the assessee had been met directly or indirectly by the Central Government or a State Government or any authority established under any law or by any person, in the form of a subsidy, then, so much of the cost as is relatable to such subsidy, shall not be included in the actual cost of the asset to the assessee. A plain reading of section 43 (1) of the Act, shows that, ordinarily, when any subsidy is received qua an asset, it would not be included in the actual cost of the asset to the assessee. In other words, the cost of the asset in the hands of the assessee would stand reduced to the extent of subsidy received by the assessee for the purchase of such asset. However, in the present case, the assessee created total facility by constructing building and installing various machineries in 1993-94. Thus, the actual cost of the assets in respect of which subsidy has been granted, came to be determined at the relevant time. Thereafter, the assets entered the block of assets and lost their independent identity and the cost of such assets merged with the other assets in the

block. At the time when the actual cost of the assets came to be computed under section 43(1) of the Act, Explanation 10 was not on the statute book and therefore, the assessee was not required to reduce the amount of subsidy from the actual cost. Moreover, at that point of time, though the subsidy had been sanctioned, the same was not disbursed. The subsidy came to be actually given in the year under consideration; a long time after the actual cost of assets came to be determined under section 43(1) of the Act. The question that arises for consideration is as to whether Explanation 10 to section 43(1) of the Act can be given effect to in the facts and circumstances of this case, by reducing the actual cost of the assets by the amount of subsidy received by the assessee. To put it differently, whether at this stage it would be possible to ascertain the actual cost of such assets in terms of Explanation 10 to section 43(1) of the Act, inasmuch as, once such assets enter the block, the depreciation is computed on the written down value of the block of assets as envisaged in section 43(6) (c) of the Act. In terms of section 43(6)(c) of the Act, the written down value can be computed only in the manner provided thereunder, namely, by adding the actual cost of any asset falling within that block acquired during the previous year or by deducting the moneys payable in respect of any asset within the block, which is sold, discarded or demolished or destroyed during the previous year together with the amount of the scrap value. The statute does not contemplate any other category for computing the written down value of a block of assets. Therefore, section 43(6)(c) of the Act does not permit reducing the written down value of the block of assets by the amount of subsidy received in relation to some of the assets forming part of the block of assets. Consequently, the

costs of assets cannot be reduced out of the written down value of their respective blocks to the extent of Rs.25,00,000/- as the statute does not envisage any manner of doing so. When the Assessing Officer reduces the cost of assets out of the written down value of the block of assets, he is reducing not only the cost of assets in relation to which the subsidy is granted, but the cost of all assets forming part of the block, irrespective of whether any subsidy was granted in respect of such assets. Under the circumstances, when the statute does not contemplate computation of actual cost of asset after it becomes part of a block of assets, Explanation 10 to sub-section (1) of section 43 of the Act cannot be made applicable to assets of which the actual cost has been determined much before the insertion thereof and which also form part of a block of assets. Therefore, when it is not possible to apply Explanation 10 of section 43(1) of the Act, in relation to an asset which has entered into the block much before the insertion thereof, it must be regarded as never having been intended by the legislature to apply to assets forming part of a block of assets which have entered the block much before the insertion of Explanation 10 to sub-section (1) of section 43 of the Act.

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10. Another aspect of the matter is that on the date when the assessee had invested in fixed capital assets, Explanation 10 to sub-section (1) of section 43 of the Act was not on the statute book and hence, the actual cost came to be computed in terms of the law as existing at the relevant time. Nothing happened in the year under consideration so as to justify the action of reduction from the written down value of the block of assets. Explanation 10 to sub-section (1) of section 43 of the

Act came into effect only from 1.4.1999 that too prospectively and, therefore, has no application, more so, when plant itself was set-up in assessment year 1993-94.

11. In the light of the above discussion, the first question is answered in the negative that is in favour of the appellant assessee and against the revenue. It is, accordingly, held that the Income Tax Appellate Tribunal was not right in law in holding that the amount of subsidy received prior to insertion of Explanation 10 to sub-section (1) of section 43 of the Act can still be reduced from the cost of assets.

12. As regards the second question, the Assessing Officer noticed that the assessee had income from interest of Rs.18,81,874/- and miscellaneous income of Rs.1,42,237/- which was not taken into consideration for deduction as per Explanation (baa) to sub-section (4B) of section 80HHC of the Act. It was the case of the assessee that such income was not other income and was to be treated as business income and, therefore, should not be reduced for the purpose of section 80HHC. It was submitted that the entire interest was out of application of the money made by the company from borrowed funds and, therefore, only the net interest should be taken into consideration and not the gross interest. The Assessing Officer found that the interest received was not incidental to the normal business activity of the assessee. Part of this interest was earned out of funds deposited with the bank and interest on bonds from Bank of Baroda. The assessee charged interest from its debtors for late payment of sale proceeds. Besides, Rs.11,85,291/- represented interest received on refunds from the Income Tax Department. The Assessing Officer was of the

view that the assessee had surplus funds which it had parked with the bank and had also made excess payment of income tax with the intention of earning interest. Placing reliance on various decisions of the Supreme Court as referred to in the assessment order, the Assessing Officer held that interest income cannot be considered as income from business and that no netting is possible as the interest paid is for the purpose of business whereas the interest earned by the assessee on deposits with banks, excess payment of income tax etc. from income from other sources. He, accordingly, held that 90% of such interest is required to be reduced from the profits of business as per Explanation (baa) to sub-section (4B) of section 80HHC of the Act.

13. In this regard, the learned senior counsel for the appellant has drawn the attention of the court to the decision of the Supreme Court in the case of **ACG Associated Capsules Pvt. Ltd. v. Commissioner of Income Tax**, 2012 (343) ITR 89 wherein it has been held thus :

“9. Explanation (baa) extracted above states that “profits of the business” means the profits of the business as computed under the head “Profits and Gains of Business or Profession” as reduced by the receipts of the nature mentioned in clauses (1) and (2) of the Explanation (baa). Thus, profits of the business of an assessee will have to be first computed under the head “Profits and Gains of Business or Profession” in accordance with provisions of Section 28 to 44D of the Act. In the computation of such profits of business, all receipts of income which are chargeable as profits and gains of business under Section 28 of the Act will have to be included. Similarly, in computation of such profits of business, different expenses which are allowable under Sections 30 to 44D have to be allowed as expenses. After including such receipts of income and after deducting

such expenses, the total of the net receipts are profits of the business of the assessee computed under the head "Profits and Gains of Business or Profession" from which deductions are to be made under clauses (1) and (2) of Explanation (baa).

10. *Under Clause (1) of Explanation (baa), ninety per cent of any receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in any such profits are to be deducted from the profits of the business as computed under the head "Profits and Gains of Business or Profession". The expression "included any such profits" in clause (1) of the Explanation (baa) would mean only such receipts by way of brokerage, commission, interest, rent, charges or any other receipt which are included in the profits of the business as computed under the head "Profits and Gains of Business or Profession". Therefore, if any quantum of the receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature is allowed as expenses under Sections 30 to 44D of the Act and is not included in the profits of business as computed under the head "Profits and Gains of Business or Profession", ninety per cent of such quantum of receipts cannot be reduced under Clause (1) of Explanation (baa) from the profits of the business. In other words, only ninety per cent of the net amount of any receipt of the nature mentioned in clause (1) which is actually included in the profits of the assessee is to be deducted from the profits of the assessee for determining "profits of the business" of the assessee under Explanation (baa) to Section 80HHC.*

11. *For this interpretation of Explanation (baa) to Section 80HHC of the Act, we rely on the judgment of the Constitution Bench of this Court in Distributors (Baroda) P. Ltd. v. Union of India and Others (supra). Section 80M of the Act provided for deduction in respect of certain intercorporate dividends and it provided in sub-section (1) of Section 80M that "where the gross total income of an assessee being a company includes any income by way of dividends received by it from a domestic company, there shall, in accordance with and subject to the provisions of this Section, be allowed, in computing the total income of the assessee, a deduction from such*

income by way of dividends an amount equal to" a certain percentage of the income mentioned in this Section. The Constitution Bench held that the Court must construe Section 80M on its own language and arrive at its true interpretation according to the plain natural meaning of the words used by the legislature and so construed the words "such income by way of dividends" in sub-section (1) of Section 80M must be referable not only to the category of income included in the gross total income but also to the quantum of the income so included. Similarly, Explanation (baa) has to be construed on its own language and as per the plain natural meaning of the words used in Explanation (baa), the words "receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in such profits" will not only refer to the nature of receipts but also the quantum of receipts included in the profits of the business as computed under the head "Profits and Gains of Business or Profession" referred to in the first part of the Explanation (baa). Accordingly, if any quantum of any receipt of the nature mentioned in clause (1) of Explanation (baa) has not been included in the profits of business of an assessee as computed under the head "Profits and Gains of Business or Profession", ninety per cent of such quantum of the receipt cannot be deducted under Explanation (baa) to Section 80HHC.

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12. If we now apply Explanation (baa) as interpreted by us in this judgment to the facts of the case before us, if the rent or interest is a receipt chargeable as profits and gains of business and chargeable to tax under Section 28 of the Act, and if any quantum of the rent or interest of the assessee is allowable as an expense in accordance with Sections 30 to 44D of the Act and is not to be included in the profits of the business of the assessee as computed under the head "Profits and Gains of Business or Profession", ninety per cent of such quantum of the receipt of rent or interest will not be deducted under clause (1) of Explanation (baa) to Section 80HHC. In other words, ninety per cent of not the gross rent or gross interest but only the net interest or net rent, which has been included in the profits of business of the assessee as computed under the head "Profits and Gains of Business or Profession", is to be deducted under clause (1) of Explanation (baa) to Section 80HHC for

determining the profits of the business.”

14. It was accordingly submitted that the controversy raised by the second question stands concluded in favour of the assessee by the said decision. The learned counsel further submitted that the matter is required to be restored to the file of the Assessing Officer for the purpose of computing deduction in terms of Explanation (baa) to section 80HHC of the Act, as interpreted by the Supreme Court in the above decision.

15. In the light of the above discussion, the appeal is allowed by setting aside the impugned order passed by the Tribunal. However, in respect of deduction under section 80HHC of the Act, the matter is restored to the file of the Assessing Officer to work out the deduction in the light of the decision of the Supreme Court in the case of **ACG Associated Capsules Pvt. Ltd. v. Commissioner of Income Tax** (supra).

THE HIGH COURT
OF GUJARAT

(HARSHA DEVANI, J.)

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(A.G.URAIZEE, J.)

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