

(1980) 03 GUJ CK 0006

Gujarat High Court

Case No: Income-tax Reference No"s. 145 and 146 of 1975

Commissioner of
Income Tax, Gujarat-II

APPELLANT

Vs

Gujarat Mineral
Development
Corporation

RESPONDENT

Date of Decision: March 31, 1980

Acts Referred:

- Income Tax Act, 1961 - Section 28, 37, 80HH, 80J, 84

Citation: (1981) 20 CTR 73 : (1981) 132 ITR 377

Hon'ble Judges: P.D. Desai, J; B.J. Diwan, J

Bench: Division Bench

Advocate: G.N. Desai, for the Appellant; J.P. Shah, for the Respondent

Judgement

Divan, C.J.

In these two reference which arise out of the same order of the Tribunal two questions have been referred to us at the instance of the Commissioner of Income Tax and three questions have been referred to as at the instance of the assessee. After the Tribunal delivered its order in appeal, two separate application of reference under s. 256(1) were filed one by the revenue and the other by the assessee and the relevant questions of law have been referred for our opinion by the Tribunal. Since all these questions arise out of the same order of the Tribunal these two reference are being disposed of by this common judgment. The questions referred to us at the instance of the revenue are :

"1. Whether, on the facts and in the circumstances of the case, the fixed deposits in the bank could be included in the capital computation for the purpose of section 84/80J of the Income Tax Act, 1961, in respect of the assessment years 1967-68, 1968-69 and 1969-70 ?

2. Whether on the facts and in the circumstance of the case, half of the profits of the year (i.e., the average profit of the year) should be included in the capital computation under rule 19(5) of the Income Tax Rules 1962, for the purpose of section 84 of the Income Tax Act, 1961, for the assessment year 1967-68 ?"

2. The three questions which are referred to us at the instance of the assessee are as follows :

(1) Whether the Tribunal was justified in holding that the above expenditure (i.e., the expenditure of Rs. 20.46 lakhs) did not relate to the business of the assessee for the year under appeal ?

(2) whether the Tribunal was justified in holding that the amount of Rs. 20.46 lakhs paid to the Gujarat Electricity Board was of a capital Nature ?

(3) Whether the Tribunal was justified in not allowing the above expenditure as revenue expenditure deductible u/s 28(1) or u/s 37 of the Income Tax Act, 1961 ?"

3. The facts leading to these reference are as follows : The relevant years under consideration are assessment years 1967-68, 1968-69 and 1969-70, the previous year for each assessment year under consideration being the financial year ending on March 31, 1967, March 31, 1968, and March 31, 1969, respectively. The assessee is a corporation wholly owned by the State of Gujarat. The assessee-company is carrying on business of mineral development and development of mines and extraction of ores, etc., in the State of Gujarat. At the relevant time, the assessee was carrying on business of extraction of Fluorspar at various places including Kadipani in Baroda District and it was also carrying on operation in Surendranagar District. We are concerned, so far as the present cases are concerned, with the operation which were being carried on at Kadipani in connection with the Fluorspar Project of the assessee-company.

4. While examining the claim of the assessee under the provisos of s. 84 for the assessment year 1967-68 and under s. 80J for the assessment years 1968-69 and 1969-70, the ITO found that the assessee had included in the capital computation a sum of Rs. 20.75 lakhs for assessment year 1967-68, a sum of Rs. 21 Lakhs for the assessment year 1968-69 and Rs. 27 lakhs for the assessment year 1969-70, being the average of the opening and the closings balances of fixed deposits and under r. 19A for the assessment years 1968-69 and 1969-70. This was done for the purpose of determining the capital for computing the relief under s. 84 or deduction under s. 80J. It was claimed before the ITO that either the closing balance in the fixed deposit account or the average of the opening and closing balances of the said deposit account should be included in the computation of capital under r. 19 or r. 19A, as the case might be. The ITO negated this contention on the ground that the investment made by the assessee in fixed deposits did not represent "an asset" which was used in the business of the assessee and, therefore, the question of including the same in the capital computation did not arise. He however, took the

view that for the assessment year 1967-68, a sum of Rs. 50,000 could at best be taken as available for utilization in business, having regard to the excess of the closing balance over the opening balance. For the assessment years 1968-69 and 1969-70 the ITO completely excluded the fixed deposits in computing the capital employed. He thus computed the capital employed in the business for the purpose of s. 84 read with r. 19(1)(c) for the assessment year 1967-68 and s. 80J read with r. 19A for the assessment year 1968-69 and 1969-70 after partially excluding the value of the same for the assessment years 1968-69 and 1969-70.

5. Against this part of the decision of the ITO when the matter was carried in appeal before the AAC by the assessee, the AAC agreed with the view of the ITO.

6. Again, when the matter was taken in further appeal before the income- tax Appellate Tribunal, the following figures were pointed out to the Tribunal namely that the opening balance in the fixed deposit account was Rs. 20.50 lakhs so far as the assessment year 1967-68 was concerned and the closing balance was Rs. 21 lakhs for the assessment year 1968-69 the opening balance was Rs. 21 lakhs and the closing balance was Rs. 27 lakhs and for the assessment year 1969-70, the opening balance was Rs. 27 lakhs and the closing balance was Rs. 21.50 lakhs. The assessee pointed out that the assessee had received the sum of Rs. 44 lakhs from the Govt. of Gujarat on December 18, 1967. Since a portion of this amount was not immediately required for the business of the assessee, the assessee, as a prudent businessman invested the surplus funds on short-term deposits with various banks. The majority of the fixed deposits were placed on short-term fixed deposit for periods ranging from 46 to 91 days for the assessment year 1967-68, for periods ranging from 46 to 180 days for the assessment year 1968-69 and for the period of 46 days for the assessment year 1969-70. The amounts in question all the same, formed part of the assets of the assessee for the purpose of its business and, therefore, the exclusion thereof in computing capital for giving relief under s. 84 or deduction under s. 80J by the authorities was not in order.

7. The Tribunal held that the assessee had kept its surplus funds which were not immediately required for business in short-term deposits in the manner indicated earlier. The Tribunal followed an earlier decision of the Bombay Bench of the Tribunal and held that the amounts in question were clearly not investments as suggested by the I.T. authorities. They remained and formed a part of the capital employed by the company in its industrial undertaking and, therefore, they could not be excluded from the capital employed by reference to which the company was entitled to exemption under s. 84. The Tribunal held that it was difficult to hold that the company's business. If the amounts lying idle in cash could form part of the assets utilised for the purpose of business, it was difficult to see how assume the character of investment as held by the authorities below. The Tribunal directed the ITO to recalculate the capital employed in the business after including the aforesaid amounts of fixed deposits in the capital computation. The first question which has

been referred to us for our opinion at the instance of the revenue relates to this aspect of the fixed deposits of short-term.

8. So far as question No. 2 is concerned the question is of computation of profits under r. 19(5) of the I.T. Rules and it was the assessee's contention before the authorities below that half of the profits of the previous year amounting to Rs. 1,64,019 should be included under r. 19(5) of the I.T. Rules in computing the capital base. This contention was negatived by the ITO and the AAC in appeal. The Tribunal following the decision of this High Court in [Commissioner of Income Tax, Gujarat II Vs. Elecon Engineering Co. Ltd.](#), held that one-half of the average profits should be included in computing the capital base under r. 19(5) of the I.T. Rules, 1962, and question No. 2 which has been referred to us at the instance of the revenue relates to this part of the Income Tax Appellate Tribunal order.

9. As regards the three questions referred to us at the instance of the assessee, the facts are that the assessee-company incurred an expenditure of Rs. 20.46 lakhs which amount was paid to the Gujarat Electricity Board for the purpose of laying elected transmission lines, cable lines, etc. This expenditure was claimed for the assessment year 1969-70. The ITO held that the impugned expenditure was of capital nature. This view of the ITO was upheld by the AAC. The ITO held that the impugned amount represented an advance to the Gujarat Electricity Board and did not represent any expenditure incurred by the assessee during the year under reference. On this ground the assessee went in further appeal to the Income Tax Appellate Tribunal and the assessee claimed that the impugned expenditure did not bring into existence any capital asset nor did the company get any enduring benefit out of this expenditure. The Tribunal held that the impugned expenditure could not be related to the business of the assessee for the year under reference and it was further held in the miscellaneous application that the expenditure was of a capital nature. Thereafter at the instance of the assessee, the three questions set out hereinafter have been referred to us for our opinion.

10. As regards the amounts kept in fixed deposits on short-term deposit by the assessee, the relevant provisions of the section have to be looked at. During the assessment year 1967-68, the provisions of s. 84 were on the statute book and s. 84, as it then stood, provided for relief in respect of the income of newly established undertakings or hotels and it provided.

"Save as otherwise hereinafter provided, Income Tax shall not be payable by assessee on so much of the profits or gains derived from any industrial undertaking or business of a hotel or from any ship, to which this section applies, as does not exceed six per cent. per annum on the capital employed in such undertaking or business or ship, computed in the prescribed manner."

11. Rule 19 of the I.T. Rules provided for the computation of capital employed in an industrial undertaking or a hotel and r. 19(1) provides : "For the purpose of section

84, the capital employed in an undertaking or a hotel to which the said section applies shall be taken to be..." and then the heads of computation of capital employed in the business or undertaking have been set out. Rule 19(1)(c) provides that in the case of assets being debts due to the person carrying on the business the nominal amounts of those debts have to be included as part of the capital, but under r. 19(4), any investment the income from which is not to be taken into account in computing the profits of the business and any moneys not required for the purpose of the business, shall be left out of account in computing the capital employed in the business. Under r. 19(5) :

"For the purpose of ascertaining the average amount of capital employed in a business during any competition period or losses made in that period shall, except so far as the contrary is shown be deemed -

(a) to have accrued at an even rate throughout the said period; and

(b) to have resulted, as they accrued, in corresponding increase or decrease, as the case may be, in the capital employed in the business."

12. It may be point out that so far as assessment years 1968-69 and 1969- 70 are concerned s. 84 was not in force but in those years s. 80J of the I.T. Act applied to deductions to be made in accordance with the provisions of the sections and the rules prescribed in that behalf. Section 80J provided :

"Where the gross total income of an assessee includes any profits and gains derived from an industrial undertaking or a ship or the business of hotel to which this section applies, 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 profits and gains (reduced by the deduction if any admissible to the assessee u/s 80HH) of so much of the amount thereof as decided ones not exceed the amount calculated at the rate of six per cent. per annum on the capital employed in the industrial undertaking or ship or business of the hotel as the case may be computed in the prescribed manner in respect of the previous year relevant to the assessment year (the amount calculated as aforesaid being hereafter in this section, referred to as the relevant amount of capital employed during the previous year)."

13. Rule 19A of the I.T. Rules provides fair computation of capital employed in an industrial undertaking or a ship or the business of a hotel for the purpose of s. 80J. There is no provision similar to r. 19(4) so far as r. 19A is concerned and r. 19A by sub-r. (2)(iv) provides :

"in the case of assets being debts due to the person carrying on the business the nominal amount of those debts." and clause (v) provides :

"in the case of assets being cash in hand or bank, the amount thereof."

14. The argument of Mr. Desai for the revenue is that since these amounts were invested in short-term deposits by the assessee-company during the assessment year 1967-68, by virtue of r. 19(4) they were not moneys required for the purpose of the assessee's business and they were required to be left out of account while computing the capital employed in the industrial undertaking.

15. Now, in our opinion, the main question that has to be considered is whether this amount which was deposited in short-term deposits represented any money not required for the purpose of the business and secondly, whether this amount could be said to be capital employed in the business. Both for the purpose of relief under s. 84 and/or deduction under s. 80J what has to be considered is capital employed in the business and r. 19(4) is part of the rules of the computation of the capital employed in the industrial undertaking. If the amounts were lying idle or in the coffers of the assessee-company they would undoubtedly be considered to be part of the assets of the company, being cash in hand. Similarly, if the amounts were allowed to lie in the current account of the assessee with any bank, that would have represented asses both under r. 19(1)(c) or (1)(d) so far as assessment year 1967-68 is concerned and under r. 19A(2)(v) so far as assessment years 1968-69 and 1969-70, are concerned.

16. The fact that instead of allowing these amounts to lie idle in its coffers or in the current account for such period as the use of the money was not immediately anticipated, the amount was invested in short-term deposits, did not mean that there was any investment of these moneys or that they ceased to be assets employed in the business of the company. The moneys were not immediately required for the purpose of the business of the company, but they were all the same required for the business of the company because only such moneys as were not immediately required were deposited by the assessee-company as a prudent businessman on short-term deposits. As the Tribunal has rightly pointed out, there was no intention of investing these moneys. It was merely with a view to earn some amount of interest these fixed deposits of moneys, not as part of its investment activity but doing something which a prudent business-man would do that the deposits were made. Under these circumstances, so far as this question, of amounts invested in short-term deposits is concerned, in our opinion, the Tribunal was right in holding that this amount did represent capital employed in the business in each of these three years under consideration and for the purpose of relief under s. 84 and deduction under s. 80J for the relevant years, these amounts were rightly directed to be included by the Tribunal in the capital employed in the business of the assessee-company.

17. As regards the question regarding profits is concerned, the decision of this High Court in [Commissioner of Income Tax, Gujarat II Vs. Elecon Engineering Co. Ltd.](#), is very clear and it was held in that case that the figure arrived at by computation under r. 19(5) has to be added to the figure arrived at by computation under r. 19(1)

for determining the average capital employed in the assessee's undertaking. The Tribunal has followed the principle laid down by this High Court in [Commissioner of Income Tax, Gujarat II Vs. Elecon Engineering Co. Ltd.](#), and, therefore, question No. 2 referred to us at the instance of the revenue must be decided in favour of the assessee and against the revenue and the decision of the Tribunal was right so far as that aspect of the case is concerned.

18. As regards the expenditure of Rs. 20.46 lakhs, which represents the amount paid by the assessee-company to the Gujarat Electricity Boards, the facts are that this sum represented fifty per cent. of the total amount spent by the Gujarat Electricity Board for the purpose of laying electric cables and other electric supply transmission lines to the mines and mining facilities of the assessee-company. The assessee-company has intended to install what is called a Beneficiation plant for the purpose of its mining operations at Kadipani in Baroda District and electric supply lines were laid at the instance of the assessee-company by the Gujarat Electricity Board. Under an agreement with that Board the assessee-company paid an amount of Rs. 20.46 lakhs to the Board. The ITO in his order referred to two aspects of the case. The first was whether it was incurred in the year under consideration, namely, in the assessment year 1969-70, for which this amount was claimed as revenue expenditure, and, secondly, whether it was a capital nature and that it has been incurred during the year 1969-70, but the amount was spent as an advance and no power has been supplied to the assessee in the assessment year under consideration. The same view had been taken by the AAC, and also by the Income Tax Appellate Tribunal.

19. Now, so far as the question of year is concerned, it is true that the Beneficiation Plant itself started functioning rather later but the company was, prior to the years under reference, carrying on mining operation of extracting fluorspar, a mineral, from its mining operations at the mines situated in Baroda District. What is meant by "Beneficiation Plant" can be gathered from McGraw-Hill Encyclopedia of Science and Technology, Vol. 9, at p. 449. It seems that beneficiation is a party of what is known as "Ore dressing"..... treatment for the purpose of improving the qualify of ore sold to customers by a company carrying on mining operation. It is "treatment of ores to concentrate their valuable constituents (minerals) into products (concentrate) of smaller bulk and simultaneously to collect the worthless material (gangue) into discardable waste (tailing). The fundamental operation of ore-dressing process are the breaking apart of the associated constituted of the ore by mechanical means (severance) and the separation of the severed components (beneficiation) into concentrate and tailing, using mechanical or physical methods which do not effect substantial chemical changes". It has been pointed out that the "step of beneficiation consists of two fundamental operation the determination that an individual particle is either a mineral or a gangue particle (selection) into the concentrate and tailing products. When middling particles occur, they will either be selected according to their mineral content and then caused to report as

concentrate or tailing, or be separate as a third product (middling)". Thus waste material is separate from useful mineral and it is this process of concentrating mineral into distinct and separate materials that is called beneficiation. Thus, this is the process of separating waste material that is to be found in all ores and which is required to be separated from the mineral which is to be purchased by a purchase from a mining company or mining operator. It is this type of beneficiation plant which the assessee-company wanted to install to enable it to sell its products better and to carry on its mining operation more efficiently. If the beneficiation plant were not to be installed, it would mean selling minerals mixed up with waste materials to the customers and thus entail all sorts of extra cost. It is, therefore, to enable the assessee-company to carry on its business more efficiently and more profitably that the assessee-company wanted to install the beneficiation plant. It must be emphasized once again that it was to enable the assessee-company to carry on its mining business more efficiently and more profitably that the beneficiation plant was installed and in order to run that beneficiation plant that the assessee-company wanted an electric supply of 3,000 KVA from the Gujarat Electricity Board.

20. Even on behalf of the revenue, it is not contended that this amount of Rs. 20.46 lakhs was spent by the assessee-company for the acquisition of a capital assets, Lines, cables and all other transmission lines were to be the property of the Gujarat Electricity Board and therefore, it is obvious that the assessee-company was not acquiring a benefit of an enduring nature whereby this connection placed on the well-known passage of Viscount Cave L. C. in *Atherton (H. M. Inspector of Taxes) v. British Insulated and Helsby Cables Ltd.* (1925) 10 TC 155, where the learned Lord Chancellor stated :

"But 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, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as property attributable not to revenue but to capital."

21. This passage from the speech of Lord Cave has been explained by the Supreme Court in [Empire Jute Co. Ltd. Vs. Commissioner of Income Tax](#), of the report, Bhagwati J., speaking for the Supreme Court, has pointed out :

"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.* (1965) 58 ITR 241 , 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 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 filed that the expenditure would be disallowable on an application of this test. If the advantage consists merely in facilitating the assessee's trading operation or enabling the management and conduct of the assessee's business to be carried on more efficiently more profitably while leaving the fixed capital introduced, expenditure would be on revenue account, even though the advantage may endure for an indefinite future."

22. Applying the test laid down by the Supreme Court in [Empire Jute Co. Ltd. Vs. Commissioner of Income Tax](#), to the facts before us, it is clear that even if securing electric supply for a period of seven years and longer if the agreement to supply is not terminated by the Electricity Board, is a benefit of an enduring nature, if the advantage consisted in facilitating the assessee's trading operation and enabled the assessee to conduct its business more efficiently and more profitably, then the expenditure would still be on revenue account and not on capital account. The peculiar feature in this case is that the amount was spent for securing electric supply for the Beneficiation Plant which was intended to enable the assessee-company to carry on its business more efficiently and more profitably. It was a business which was being previously carried on by the assessee-company, namely, of extracting fluorspar ore and selling it but in order to enable it to carry on that business more efficiently and more profitably, but the capital, in the sense of the block capital was remaining untouched by the expenditure of this amount of Rs. 20.46 lakhs. Hence, in the commercial sense, it was not an advantage in the capital filed. Since it left the fixed capital of the assessee employed for the main business of mining untouched and the advantage was not in the capital filed it could not be said to be an expenditure of a capital nature. As we have pointed out, while arriving at this conclusion, we are prepared to proceed on the footing that the advantage which the assessee-company got was an advantage of an enduring nature, but applying the test culled out by the Supreme Court in [Empire Jute Co. Ltd. Vs. Commissioner of Income Tax](#), it is obvious that, in spite of the presumption, it can be held on the facts and circumstances of this case that the expenditure was not of a capital nature but was of a revenue nature.

23. As regards the year of account, it must be pointed out that the assessee claims this expenditure in respect of assessment year 1969-70, the previous year being financial year 1968-69. It was pointed out to us that the electric supply started flowing in December, 1968, and by that time all connection were completed and the full amount of Rs. 20.46 lakhs was paid by the assessee-company to the Gujarat Electricity Board. It seems that in the earlier previous year, that is in the year of account 1967-68, the assessee has shown in its books pH the expenditure of the sum of Rs. 19,00,000 as having been paid by way of advance for the installation of these electric lines and in the relevant year of account, namely, the income year 1968-69, the assessee-company showed the entire amount of Rs. 20.46 lakhs as having been spent for laying of these electric transmission lines, etc. The fact

remains that the entire amount of Rs. 20.46 lakhs went out of the funds of the company during the previous year relevant to the assessment year 1969-70. That being the case, the fact that in an earlier year the amount of Rs. 19,00,000 was shown as advance payment to the Gujarat Electricity Board is totally immaterial. The further fact that in the subsequent years", one-seventh of the total amount was shown as revenue expenditure written off by way of expenditure for that purpose is again immaterial. As has been pointed out by the Supreme Court in [Commissioner of Income Tax, West Bengal I Vs. India Discount Co. Ltd.](#), the receipt being one which in law could not be regarded as income, it could not become income merely because the respondent erroneously credited it to the profit and loss account. Similarly, and expenditure which in law cannot be regarded as capital expenditure cannot become so merely because the assessee erroneously, made entire in its books of account in a particular manner. The same [The Kedarnath Jute Mfg. Co. Ltd. Vs. The Commissioner of Income Tax, \(Central\), Calcutta](#), :

"Whether the assessee is entitled to a particular deduction or not will depend on the provision of law relating thereto and not on the view which the assessee might take of his rights nor can the existence or absence of entire in the books of account be decisive or conclusive in the matter."

24. Therefore, the question whether the amount was spent in a particular year or not and if it was by way of revenue expenditure has to be decided in the light of the legal position and the facts of the case. The fact that certain entire were made or not made in a particular year of account is totally immaterial and, in any event, such entries are not decisive or conclusive of the matter. The fact remains that the electric installation was complete and the supply started in December, 1968, that is during the previous year relevant to the assessment year 1969-70. Under these circumstances, the company rightly claimed that this amount should be allowed by way of deduction in assessment year 1969-70.

25. In the light of the above discussion, we answer the question referred to us as follows :

Question referred at the instance of the revenue

Question No. 1-In the affirmative that is, in favour of the assessee and against the revenue.

Question No. 2-In the affirmative, that is, in favour of the assessee and against the revenue.

Question referred at the instance of the assessee

Question No. 1-In the negative that is, in favour of the assessee and against the revenue.

Question No. 2-In the negative, that is, favour of the assessee and against the revenue.

Question No. 3-In the negative, because once it is held that the expenditure was of a revenue nature and was incurred in the previous year relevant to the assessment year 1969-70, the assessee was entitled to deduction as revenue expenditure at least under s. 28(1) if not under s. 37 of the I.T. Act.

26. Under these circumstances, all the questions referred to us are decided in favour of the assessee and against the revenue. The Commissioner will pay the costs of these two references to the assessee.