

Commissioner of Income Tax Vs Kissan Products Ltd.

Court: Karnataka High Court

Date of Decision: Jan. 14, 1991

Acts Referred: Income Tax Act, 1961 " Section 256 (2)

Citation: (1991) 95 CTR 44 : (1991) 190 ITR 649 : (1991) 1 KarLJ 408

Hon'ble Judges: R. Ramakrishna, J; K. Shivashankar Bhat, J

Bench: Division Bench

Advocate: Chandrakumar, for the Appellant; G. Sarangan, for the Respondent

Judgement

K. Shivashankar Bhat, J.

The following questions have been referred u/s 256(2) of the Income Tax Act, 1961 :

(i) Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in upholding the Commissioner of Income Tax

(Appeals") order who directed the Income Tax Officer to recompute the surtax liability after converting the foreign loan at the rate of exchange

available on the relevant date ?

(ii) Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in upholding the Commissioner of Income

Tax (Appeals") order who directed the Income Tax Officer to make adjustment for relief allowed in the Income Tax assessment ?

2. It is admitted by both sides that the answer to the second question depends upon the answer to the first question and if the answer to the first

question is against the Revenue, the second question will also have to be answered against the Revenue.

3. The assessee obtained a long-term loan from the Industrial Credit and Investment Corporation of India and claimed the benefit for the

assessment years 1975-76 and 1976-77. The borrowing was for the purchase of machinery by importing the same from abroad. The loan was

taken in foreign exchange and it was a long-term borrowing. The question arises under the Surtax Act. The borrowing to the extent it is outstanding

is treated as a part of the capital of the company and a particular percentage thereof is allowed as depreciation. The relevant date to compute the

capital is the first day of the accounting year and in this case it is 1st January. There is no dispute about the actual amount borrowed and

outstanding in foreign exchange terms. The assessee, while claiming the benefit, converted the foreign exchange liability into ""rupee liability"" by

applying the exchange rate prevalent as on the ""relevant date"" (1st day of the accounting year). However, the Revenue contended that the

exchange rate that prevailed on the date of the actual borrowing should be applied and any subsequent variation will have to be ignored. The

Income Tax Officer did not grant the benefit of the prevalent exchange rate to the assessee. However, the Commissioner of Income Tax (Appeals-

l) allowed the assessee's appeals and, thereafter, directed the Income Tax Officer to recompute the capital. Hence, the Revenue appealed to the

Appellate Tribunal contending that (i) the computation of the company's profits under the Surtax Act, made by the Commissioner of Appeals was

erroneous and the order of the assessing authority should be restored, and (ii) the Commissioner (Appeals) had no authority to direct

recomputation of the capital. The Tribunal affirmed the order of the Commissioner of Appeals. Hence, these references at the instance of the

Revenue.

4. Mr. Chandrakumar, learned counsel for the Revenue, reference to the Second Schedule to the Act wherein the rules for computing the capital

of a company for the purpose of surtax are found. Clause (v) of rule 1 reads thus :

(1) Subject to the other provisions contained in this Schedule, the capital of a company shall be the aggregate of the amounts, as on the first day of

the previous year relevant to the assessment year, of....

(i) to (iv) omitted as unnecessary.

(v) any moneys borrowed by it from Government or the Industrial Finance Corporation of India or the Industrial Credit and Investment

Corporation of India or any other financial institution which the Central Government may notify in this behalf in the Official Gazette or any banking

institution (not being a financial institution notified as aforesaid) or any person in a country outside India :

(rest omitted as unnecessary)

5. According to learned counsel for the Revenue, what is to be paid is the money borrowed by the assessee. For the purpose of computation, the

capital of the company and the borrowings of the company (in the process of aggregation) shall be included as on the first day of the previous year

relevant to the assessment year. Therefore, when the borrowing is complete and is stated in terms of the Indian rupee and is crystallised, the said

quantum cannot be varied.

6. The contention advanced by Mr. Chandrakumar does not flow from the rule referred to by him. The rule simply states that the borrowings as on

the first day of the accounting year will be aggregated to arrive at the capital. What is relevant is that there should be borrowing which necessarily

shows that there should be an outstanding payable to the creditor. The borrowing herein is in foreign exchange (foreign currency). It is that sum

which has to be paid to the foreign creditor that forms the capital of the company under rule 1 referred to above. With the fluctuation in the foreign

exchange rates, its liability in terms of the Indian rupee would fluctuate. The liability in terms of foreign currency is not varied. In reality, therefore,

the liability of the company, when computed in Indian currency, will have to be arrived at by applying the existing foreign exchange rate as on the

relevant date. Any other interpretation will lead to an absurd result. For example, if the borrowing is held to be crystallised in Indian currency, the

repayment made by the company in the course of 4 or 5 years may wipe out the said outstanding in Indian rupee, though, in reality, the company

still owes the foreign creditor.

7. The view we have expressed above also finds support from a decision of the Bombay High Court in Commissioner of Income Tax Vs. National

Rayon Corporation Ltd., . In the said case, the Bombay High Court accepted the claim of the assessee that the assessee was entitled to add on the

liability in Indian rupees by virtue of the liability incurred by the assessee on account of rupee devaluation.

8. Consequently, our answers to the questions are in the affirmative and against the Revenue.