(2004) 02 BOM CK 0070

Bombay High Court (Goa Bench)

Case No: Income-tax Appeal No. 14 of 2003

Nectar Beverages P. Ltd.		APPELLANT
	Vs	
Deputy Commissioner of Income Tax (Assessment)		RESPONDENT

Date of Decision: Feb. 10, 2004

Acts Referred:

- Income Tax Act, 1961 - Section 32, 32(1), 41, 41(1), 50

Citation: (2004) 190 CTR 319 : (2004) 267 ITR 385

Hon'ble Judges: P.V. Hardas, J; A.M. Khanwilkar, J

Bench: Division Bench

Advocate: A.A. Kulkarni and Sudesh Usgaonkar, for the Appellant; S.R. Rivonkar and Amina Fadte, for the Respondent

Final Decision: Dismissed

Judgement

A.M. KHANWILKAR J.

1. This appeal by the assessee u/s 260A of the Income Tax Act, 1961, (hereinafter referred to as "the said Act" for the sake of brevity), questions the judgment and order passed by the Income Tax Appellate Tribunal, Panaji Bench, Goa, in Income Tax Appeal No. 268(PN) of 1997 dated October 17, 2002, pertaining to the assessment year 1991-92.

2. The principal question, which is a substantial question of law that arises for our consideration in this appeal is : Whether the sale proceeds received by the assessee on selling the scrapped bottles and crates (trays) could be taxed as income by virtue of Section 41(1) of the Income Tax Act, 1961 ?

3. Briefly stated, the assessee is a private limited company, which derives income from the manufacture and sale of soft drinks. The assessee was claiming depreciation in respect of the bottles and crates (trays) purchased by the assessee,

being the full value of such purchase under the proviso to Section 32(1)(ii) of the said Act. That was allowed to the assessee from time to time. During the financial year, relevant to the assessment year 1991-92, the assessee sold scrap of bottles and trays (crates) for Rs. 50,850. However, in the computation of income, the assessee reduced the sale consideration from the income on the ground that the amount received is a capital receipt and since it does not form part of the block of assets, even the provision of Section 50 of the said Act, relating to short-term capital gain on the sale of depreciable asset was not attracted. The Assessing Officer negatived the plea taken by the assessee and, instead, held that what was allowed to the assessee being depreciation, the proviso to Section 50 of the said Act was applicable. Against this decision, the assessee carried the matter in appeal before the Commissioner of Income Tax (Appeals). The said appellate authority, on the other hand, held that a deduction has been made in an earlier assessment year in respect of the expenditure incurred and, subsequently, the assessee having obtained the amount in respect of such expenditure, the same was chargeable to tax u/s 41(1) of the Act. The assessee carried the matter in appeal before the Income Tax Appellate Tribunal, Panaji Bench. The appellate authority rejected the appeal preferred by the assessee and has affirmed the conclusion reached by the first appellate authority, but on different reasoning. The second appellate authority has held that on reading Section 32(1)(ii) and the proviso thereto, it is clear that what was allowed to the assessee is a deduction in respect of depreciation. Further, the depreciation is one of the items of expenditure, though may be of the nature of non-cash, but still it is an expenditure" allowed while computing the income under the head of "Profits and gains of business". It then proceeded to hold that Section 41(1) of the Act will apply where any deduction was allowed in respect of expenditure incurred by the assessee, and subsequently, the assessee has obtained any cash or in any other manner any amount in respect of such expenditure. It found that the expression "expenditure" occurring in Section 41(1) does not speak of any expenditure being only revenue in nature. It rejected the argument canvassed on behalf of the assessee that such amount could be taxed only u/s 41(2) of the Act ; and after omission of the said provision, the amount could not be charged to tax u/s 41(1) of the Act. To buttress this view, it noted that Section 41(2) was omitted from the statute book after the introduction of allowance of depreciation on block of assets, whereas, prior to that, an individual item of asset was eligible for depreciation at the rate prescribed, but subsequently, depreciation is allowable on the block as a whole and not on an individual item of asset. Understood, thus, according to the appellate authority, with the introduction of the concept of block of assets, Section 41(2) of the Act became redundant, for which reason it was omitted. It conclusively held that Section 41(1), as applicable at the relevant time, and on the plain language thereof, the same clearly applied to the case on hand and the omission of Section 41(2) from the statute book at the relevant time would make no difference. Accordingly, it held that the conclusion reached by the first appellate authority required no interference.

4. The above decision is the subject matter of challenge in this appeal at the instance of the assessee.

5. In the appeal memo, following two substantial questions of law have been formulated, which, according to the appellant, may arise for consideration of this court, namely :

"(a) Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the sum of Rs. 50,850 was liable to tax under the provisions of Section 41(1) of the Act ?

(b) Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the provisions of Section 41(1) of the Act are attracted so as to bring to tax the excess realised by an assessee over and above the written down value of an asset ?"

6. We have already formulated the principal question, which is a substantial question of law in paragraph 2 above, that would arise for our consideration.

7. According to counsel for the assessee, since the deduction given was not in respect of loss, expenditure or trading liability, the provisions of Section 41(1) of the Act were not applicable at all. On the other hand, the said item was chargeable to tax only by virtue of Section 41(2) of the Act, as it existed prior to 1988. However, after deletion of Section 41(2) of the Act, with effect from April 1, 1988, there is no provision in the said Act to bring the amount as taxable income. Reliance was placed on the decisions of this court reported in Commissioner of Income Tax, Bombay City Vs. Gagalbhai Jute Mills Ltd., and Commissioner of Income Tax, Bombay City-I Vs. Mafatlal Fine Spg. and Mfg. Co. Ltd., , to contend that while construing Section 10(2)(vii) and Section 10(2A) of the Act, which are pari materia with the provisions of Section 41(2) and Section 41(1) of the Act, the court negatived the claim of the Revenue that the item could be included as one u/s 10(2A), although it was specifically referable to Section 10(2)(vii), and especially when specific provision in that behalf existed. Learned counsel contends that applying that analogy, the claim of the Revenue in the present case that the item could be brought to tax by virtue of Section 41(1) cannot be countenanced. Reliance is also placed on the decision of the apex court reported in Indian Molasses Co. (Private) Ltd. Vs. Commissioner of Income Tax, West Bengal, , to contend that the expression "expenditure" has been considered in the said decision to mean what is paid out or away and is something which is gone irretrievably. According to the appellant, therefore, depreciation allowance cannot be labelled as an expenditure. Reliance is also placed on the decision of the apex court reported in Commissioner of Income Tax, Madras Vs. Ajax Products Ltd. through its Liquidator, , to contend that in a taxing Act, one has to look merely at what is clearly said and there is no room for intendment or equity about a tax nor presumption as to a tax. Learned counsel contends that besides, nothing is to be read in, nothing is to be implied and one can only look fairly at the language

used. Relying on this dictum, contends learned counsel, that the subject is not to be taxed unless the charging provision clearly imposes the obligation, and which is lacking in the present case. Reliance is also placed on another decision of the apex court in Nalnikant Ambalal Mody Vs. Commissioner of Income Tax, Bombay, , which has observed that there is no warranty for the assumption that whatever is included in total income u/s 4 must be liable to tax as Section 3 does not provide that the entire total income shall be chargeable to tax. Learned counsel has also placed extensive reliance on the Notes on Clauses of the Finance Minister''s Budget Speech for 1986-87 and the objects of the Finance Bill of 1995 to buttress his argument that reintroduction of Section 41(2) is a pointer that the subject cannot be said to be covered by Section 41(1) of the Act, for there would have been no reason for the Legislature to reintroduce Section 41(2) of the Act from 1998-99 onwards.

8. On the other hand, learned counsel for the Revenue has defended the decision passed by the appellate authority contending that the assessee made expenditure in paying for bottles and crates for its business, on which deduction in the form of depreciation u/s 32(1)(ii) of the Act was allowed to the assessee. Subsequently, the assessee having obtained/received amount of sale of the said bottles and crates as scrap, such amounts would be deemed profits and gains of business and, accordingly, chargeable to Income Tax u/s 41(1) of the Act, as income accrued to the assessee. According to him, the expression "expenditure" is wide enough not only to cover revenue expenditure, but also capital expenditure. To support this submission, reliance is placed on the decision of the apex court in Indian Molasses Co. (Private) Ltd. Vs. Commissioner of Income Tax, West Bengal, and another decision of the Gujarat High Court in Patel Filters Ltd. Vs. Commissioner of Income Tax, . It is then contended that the expression "expenditure" used in Section 41(1) relates to allowable deduction in computing the income from profits and gains of business u/s 29, which includes, inter alia, deduction u/s 32. It is then contended that allowance of depreciation u/s 32 is in the nature of deduction. Learned counsel, therefore, submits that the income earned by the assessee on the sale of bottles and creates is chargeable as profits and gains u/s 41(1) of the Act. The emphasis is laid on the deeming fiction in Section 41(1), whereby, contends learned counsel, any income obtained/derived on such expenditure is deemed to be profits and gains chargeable to tax as the income of the assessee. If it is so, the assessee cannot avoid the liability to pay the tax on such income and no other argument can come to the aid of the assessee. Learned counsel contends that while considering the liability of the assessee to pay tax, the provisions existing will have to be taken into account as they are, without reference to the legislative changes effected therein either anterior or posterior in point of time. He submits that on a plain language of Section 41(1), if it can be demonstrated that the same is attracted, then no other argument would be of any assistance to the assessee. Learned counsel has placed reliance on the decision of the apex court in The State of Bombay Vs. Pandurang Vinayak Chaphalkar and Others, , to contend that the deeming fiction appearing in Section

41(1) will have to be taken to its logical conclusion giving full effect to the intent thereof. Learned counsel contends that the decisions pressed into service on behalf of the appellant, referred to above, are not applicable to the fact situation of the present case and for considering the question which arises for our consideration. He has also relied on the decision of the apex court in Polyflex (India) Pvt. Ltd. Vs. Commissioner of Income Tax, Karnataka, , to contend that the expressions "remission and cessation thereof" occurring in Section 41(1) are referable to the expression "trading liability" and not to the expression "loss and expenditure". On the above arguments, learned counsel submits that no interference is warranted in this appeal.

9. Before we proceed to examine the rival submissions, we would think it apposite to advert to Section 41(1) of the Act, as it obtained during the assessment year 1991-92. The same reads thus :

"41. Profits chargeable to tax.--(1) Where an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee, and subsequently during any previous year the assessee has obtained, whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cession thereof, the amount obtained by him or the value of benefit accruing to him, shall be deemed to be profits and gains of business or profession and accordingly chargeable to Income Tax as the income of that previous year, whether the business or profession in respect of which the allowance or deduction has been made is in existence in that year or not".

10. In our view, it is rightly submitted on behalf of the Revenue that the court will have to adjudicate the question relating to the liability of the assessee in the context of the provisions, as existing at the relevant time. If that is so, it necessarily follows that we would be called upon only to examine the application of the above provision to the fact situation of the present case. No more and no less. However, before we analyse this aspect, reference can be made to the provision as existing prior to April 1, 1988 (assessment year 1988-89). Besides the above extracted provision, Section 41(2) was on the statute book, which reads thus :

"41. (2) Where any building, machinery, plant or furniture which is owned by the assessee and which was or has been used for the purposes of business or profession is sold, discarded, demolished or destroyed and the moneys payable in respect of such building, machinery, plant or furniture, as the case may be, together with the amount of scrap value, if any, exceed the written down value, so much of the excess as does not exceed the difference between the actual cost and the written down value shall be chargeable to Income Tax as income of the business or profession of the previous year in which the moneys payable for the building, machinery, plant or furniture became due."

11. Section 41(2) was, however, deleted with effect from April 1, 1988, by the Taxation Laws (Amendment and Miscellaneous Provisions) Act, 1986. Indeed, if Section 41(2) was on the statute book during the period, assessment year 1991-92, the assessee would have been liable to include the sale proceeds of scrap of bottles and crates as income chargeable to tax. However, it is on account of the deletion of the said provision and non-existence of that provision for the assessment year 1991-92, it is contended that the assessee was not liable to include the amount obtained by way of sale of scrap of bottles and crates in the income chargeable to tax. But, as mentioned earlier, the liability of the assessee will have to be adjudicated on the basis of the provision as obtaining during the assessment year 1991-92. The moot question is : Whether Section 41(1), as reproduced above, would envelop the transaction effected by the assessee so as to be treated as profits and gains of business and, accordingly, chargeable to income tax as income ? It is, therefore, necessary to revert back to Section 41(1) of the Act. If on the plain language of Section 41(1) of the Act, it is seen that the transaction was covered by that provision, then no other argument would be of any assistance to the assessee. In our view, Section 41(1), as it existed during the assessment year 1991-92, cannot be interpreted on the basis of the provisions which obtained prior to 1988 or as existing at present after 1998. We shall now turn to Section 41(1) as it existed during the assessment year 1991-92. In our opinion, Section 41(1) will be attracted if--(i) any loss, expenditure or trading liability has been incurred by the assessee in the assessment for any year ; (ii) allowance or deduction therefore has been made in the assessment for any year ; (iii) subsequently, during any previous year, the assessee obtains whether in cash or in any manner whatsoever any amounts in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof ; and (iv) the amount was obtained by the assessee or the value of or benefit accruing to him is irrespective of whether the business or profession is in existence in that year or not. On fulfilling the above requirements, by virtue of the deeming fiction in the latter part of the provision, the amount so obtained by the assessee or the value of benefit shall be deemed to be profits and gains of business and accordingly chargeable to Income Tax in that previous year. It is in that backdrop, the argument canvassed before this court on behalf of the assessee is that allowance of depreciation amount in respect of bottles and crates to the assessee cannot be said to be either loss or expenditure or trading liability. Whereas, according to the Revenue, allowance of depreciation was in the nature of expenditure. This is the moot question we have to first resolve and, if it were to be answered in favour of the Revenue, then, in our view, no other argument canvassed on behalf of the assessee would be of any consequence. Indeed, it was contended on behalf of the assessee that Section 41(1) of the Act was inapplicable to the facts on hand, as there was neither cessation nor remission on sale, which was a necessary condition for its application. This contention can be straightaway answered by referring to the recent decision of the Supreme Court in the case of Polyflex (India) Pvt. Ltd. Vs. Commissioner of Income Tax, Karnataka, , as rightly

relied upon on behalf of the Revenue. In this decision, while construing Section 41(1) of the Act, it has been held that the words employed therein would suggest that the test of cessation or remission of liability has to be applied vis-a-vis "trading liability" and it cannot be projected into the previous clause, i.e., loss or expenditure. In other words, the expression "remission or cessation thereof" is referable only to the expression "trading liability". Understood thus, the only argument that needs to be seriously considered is, whether the Revenue is right in contending that allowance of depreciation as deduction is in the nature of expenditure. And if it is so, the rigours of Section 41(1) would clearly apply to the case on hand. According to the assessee, the expression "expenditure" cannot be widely construed and, in any case, depreciation is not an expenditure. Reliance was placed on the decision of Indian Molasses Co. (Private) Ltd. Vs. Commissioner of Income Tax, West Bengal, , to support the argument that depreciation cannot be considered as expenditure. Relying on the dictum of the apex court, it was argued that "expenditure" is what is paid out or away or something which has gone irretrievably. In our opinion, the said decision will be of no assistance to the assessee. In that case, the court was considering the meaning of the expression in the context of the argument of actual liability in present and a liability de futuro, which, for the time being, is only contingent. The court went on to observe that the former is deductible but not the latter. In our opinion, this is not an authority for the proposition that depreciation is not in the nature of expenditure. On the other hand, we find force in the submission canvassed on behalf of the Revenue that the expression "expenditure" occurring in Section 41(1) of the Act is wide enough not only to include revenue, but also capital expenditure, The Act does not provide for the definition of the term "depreciation" nor, for that matter, the expression of "expenditure". It will be useful to advert to Black''s Law Dictionary, which provides for the meaning of "expenditure". It observes :
"Expenditure. Spending or payment of money ; the act of expending, disbursing, or laying out of money ; payment."

12. It also mentions that the meaning of the expression "expense" should also be referred to. The expression "expense" is defined as under :

"Expense. That which is expended, laid out or consumed. An outlay ; charge ; cost ; price. The expenditure of money, time, labour, resources, and thought. That which is expended in order to secure benefit or bring about a result."

13. It will be useful to also advert to the meaning of "tax deduction" given under the definition of "expense" by Black''s Law Dictionary, It mentions, "tax deduction", as :

"Tax deduction. Certain expenses such as those directly related to production of income are deductions from gross income for tax purposes."

14. It will be now useful to advert to the meaning of the expression "depreciation" given in Black''s Law Dictionary, which reads thus :

"Depreciation. In accounting, spreading out the cost of a capital asset over its estimated useful life. Depreciation expense reduces the taxable income of an entity but does not reduce the cash. A decline in value of property caused by wear or obsolescence and is usually measured by a set formula which reflects these elements over a given period of useful life of property. State Highway Commission v. Tubbs 147 Mont. 296 ; 411 P. 2d 739. Consistent, gradual process of estimating and allocating cost of capital investments over estimated useful life of asset in order to match cost against earnings. Coca-cola Bottling Co. of Baltimore v. US 203 Ct. Cl. 18 ; F. 2d 528. The depreciation expense recorded on the entity''s tax return may differ from that recorded on the entity''s financial statements. An entity usually uses an accelerated method on its tax return and the straight-line method on its financial statements due to the larger write-offs in the early years , . ."

15. On a conjoint reading of the aforesaid, in our opinion, the argument canvassed on behalf of the assessee that depreciation is not in the nature of expenditure cannot be countenanced. On the other hand, we have no hesitation in taking the view that the allowance for depreciation or deduction provided under the Act is in the nature of expenditure, as it reduces the liability of the assessee to pay Income Tax on such amount, being tax deduction availed of.

16. There can be no dispute that the amount spent towards purchase of bottles and crates (trays) will be covered by the expansive definition of "plant and machinery" (see Commissioner of Income Tax, Andhra Pradesh Vs. Taj Mahal Hotel, Secunderabad, and Scientific Engineering House (P) Ltd. Vs. Commissioner of Income Tax, Andhra Pradesh,). The amount spent for that purpose is obviously capital expenditure, but in view of 100 per cent. depreciation as was provided on account of Section 32 of the Act, as the cost thereof did not exceed five thousand rupees, the actual cost was allowed as deduction in respect of the previous year in which such items were first put to use by the assessee for the purpose of its business or profession. As 100 per cent. depreciation was claimed in respect of the said purchases, that was in the nature of expenditure and deductible from tax liability. If it is so, the assessee having made provision for allowance or deduction in the earlier assessment year in respect of such expenditure and subsequently during the previous year (i.e., the assessment year 1991-92) the assessee having sold the items and obtained cash being sale proceeds thereof, in respect of the said expenditure, the amount so obtained is deemed to be profits and gains from business or profession and, accordingly, chargeable to Income Tax, as the income of that previous year of the assessee. We, therefore, find no fault with the approach of the appellate authorities below in taking the view that Section 41(1) was attracted in the fact situation of the present case, so as to bring the said amount as chargeable to Income Tax, as the income of that previous year.

17. On the above reasoning, no other argument canvassed on behalf of the assessee would be of any avail, as has already been observed by us. The decisions of

the Bombay High Court in Commissioner of Income Tax, Bombay City Vs. Gagalbhai Jute Mills Ltd., and Commissioner of Income Tax, Bombay City-I Vs. Mafatlal Fine Spg. and Mfg. Co. Ltd., will be of no assistance to the assessee. Those decisions are with reference to the provisions of Section 10(2A) and Section 10(2)(vii) of the Act, which may be pari materia with Section 41(1) and 41(2) of the Act. However, as mentioned earlier, we have to adjudicate the matter on the basis of the provisions as obtaining during the relevant period. In the present case, during the relevant year, the provision applicable or prevailing was only in the shape of Section 41(1). Therefore, the question will have to be decided on the application of that provision. If Section 41(2) was also to prevail at the relevant time, in that situation alone, the decisions, referred to above, as relied on on behalf of the assessee, would have been of some significance. In that view of the matter, those decisions will be of no assistance to answer the question that arises in the present case.

18. In our view, even the other decisions relied on on behalf of the assessee reported in Commissioner of Income Tax, Madras Vs. Ajax Products Ltd. through its Liquidator, and in Nalnikant Ambalal Mody Vs. Commissioner of Income Tax, Bombay, are of no assistance to the assessee, The proposition enunciated in those decisions cannot be disputed at all. However, for the view that we have taken, it is obvious that there is express provision that the income derived by the assessee is liable to tax and we have not drawn any assumption or presumption, but only looked at the plain language of Section 41(1) of the Act, as applicable at the relevant time. Even the reasons behind the legislative changes will be of no relevance in examining the question that arises for our consideration. Indeed, Section 41(2) has been reintroduced, but on comparing the provision as existing prior to 1988, and the new provision after 1998, it appears that there is difference, as it is now restricted only in respect of that amount for which depreciation is claimed under Clause (i) of Sub-section (1) of Section 32 of the Act. This is obviously on account of the legislative changes effected by the Act of 1986 with effect from April 1, 1988, to provide for depreciation on blocks of assets instead of individual assets. It is relevant to note that the proviso to Section 32(1)(ii) of the Act was deleted with effect from April 1, 1996, by the Finance Act, 1995, which provided for 100 per cent. depreciation in respect of plant or machinery if its value did not exceed five thousand rupees. However, it is not necessary for us to dwell upon that aspect. As observed earlier, we have to adjudicate the question on the basis of provision as obtaining during the relevant assessment year i.e., 1991-92.

19. For the aforesaid reasons, in our opinion, the appeal is devoid of merit and the same is dismissed with no order as to costs.