(1990) 02 CAL CK 0002

Calcutta High Court

Case No: IT Reference No. 163 of 1983

Union Carbide India Ltd.		APPELLANT
	Vs	
Commissioner of Income Tax		RESPONDENT

Date of Decision: Feb. 22, 1990

Acts Referred:

- Constitution of India, 1950 - Article 31A(1)(e)
- Income Tax Act, 1961 - Section 10(2)(iii), 10(2)(xv), 147(b), 2(47), 220(2)

Citation: (1995) 80 TAXMAN 197

Hon'ble Judges: Suhas Chandra Sen, J; Bhagabati Prasad Banerjee, J

Bench: Division Bench

Advocate: Debi Pal and Smt. M. Sil, for the Appellant; B.K. Bagchi and A.N. Bhattacherji, for the Respondent

Judgement

@JUDGMENTTAG-ORDER

Suhas Chandra Sen, J.
The Tribunal has referred to this Court, the following questions of law, u/s 256(1) of the income tax Act, 1961 (''the Act''):

Questions at the instance of the revenue :

"1. Whether, on the facts and in the circumstances of the case, the Tribunal was justified in law in holding that the legal expenses incurred for challenging the jurisdiction assumed by the Assessing Officer u/s 147(b) of the income tax Act are not hit by section 80VV of the income tax Act, 1961 ?

2. Whether, on the facts and in the circumstances of the case and on a correct interpretation of provision of section 32A(1) of the income tax Act, 1961, the Tribunal was justified in holding that the internal telephone system was ''plant'' and not office appliances and in that view the assessee was entitled to investment allowance u/s 32A of the income tax Act on the installation of internal telephone system ?

3. Whether, on the facts and in the circumstances of the case, the Tribunal was justified in law in directing the ITO to allow one-fifth deduction of 100 per cent (instead of 80 per cent) of the initial contribution made by the assessee to superannuation fund ?"

Questions at the instance of the assessee:

"1. Whether, on the facts'' and in the circumstances of the case, the Tribunal ought to have allowed depreciation on the assets representing the capital expenditure on scientific research fully allowed as deduction in computing the total income for the earlier assessment years ?

2. Whether, on the facts and in the circumstances of the case and on a true construction of section 45 of the income tax Act, 1961, the Tribunal erred in holding that the amount received from the insurance company in respect of a trawler ''Jaya Rani'' which sank in deep waters is taxable as the same arises on a transfer and the excess over cost is, therefore, taxable under the head ''Capital gains'' ?

3. Whether, on the facts and in the circumstances of the case and on a true construction of section 45 of the income tax Act, the amount of insurance money received from the insurance company in respect of a trawler which sank in deep waters, is received on a transfer of assets within the meaning of that expression as contemplated u/s 45 of the Act ?

4. Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the interest paid u/s 220(2) of the Act amounting to Rs. 1,42,993 was not deductible in computing the business income of the assessee ?

5. Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the assessee''s claim for deduction of interest paid u/s 220(2) of the Act cannot be allowed even u/s 80V of the Act ?"

The assessment year involved is 1978-79 for which the accounting year ended on 25-12-1977.

2. The question No. 1 raised at the instance of revenue is concluded by a judgment of this Court in the case of CIT v. Sri Krishan Sugar Mills [IT Reference No. 102 of 1983, dated 17-7-1989]. Following the said judgment, question No. 1 at the instance of the revenue is answered in the affirmative and in favour of the assessee.

3. The second question raised by the revenue is about the internal telephone system installed by the assessee-company. The case of the revenue is that the internal telephone system installed in the assessee''s pesticides complex No. 1 at Bhopal cannot be treated as the office appliances and the assessee could not claim investment allowance u/s 32A of the Act, for installation of such internal telephone system.

Section 32A provides as follows :

"32A. Investment allowance. -(1) In respect of a ship or an aircraft or machinery or plant specified in sub-section (2), which is owned by the assessee and is wholly used for the purposes of the business carried on by him, there shall, in accordance with and subject to the provisions of this section, be allowed a deduction, in respect of the previous year in which the ship or aircraft was acquired or the machinery or plant was installed or, if the ship, aircraft, machinery or plant is first put to use in the immediately succeeding previous year, then, in respect of that previous year, of a sum by way of investment allowance equal to 25 per cent of the actual cost of the ship, aircraft, machinery or plant to the assessee :

Provided that no deduction shall be allowed under this section in respect of-

(a) any machinery or plant installed in any office premises or any residential accommodation, including any accommodation in the nature of a guest house;

(b) any office appliances or road transport vehicle;

(c) any ship, machinery or plant in respect of which the deduction by way of development rebate is allowable u/s 33; and

(d) any machinery or plant, the whole of the actual cost of which is allowed as a deduction (whether by way of depreciation or otherwise) in computing the income chargeable under the head ''Profits and gains of business or profession'' of any one previous year.

(2) The ship or aircraft or machinery or plant referred to in sub-section (1) shall be the following, namely :-

(a) a new ship or new aircraft acquired after the 31st day of March, 1976, by an assessee engaged in the business of operation of ships or aircraft;

(b) any new machinery or plant installed after the 31st day of March, 1976,-

(i) for the purposes of business of generation or distribution of electricity or any other form of power; or

(ii) for the purposes of business of construction, manufacture or production of any one or more of the articles or things specified in the list in the Ninth Schedule; or

(iii) in a small-scale industrial undertaking for the purposes of business of manufacture or production of any other articles or things."

It has been contended on behalf of the revenue that office appliances have been specifically excluded from the ambit of section 32A by the proviso. No investment allowance can be given in respect of any office appliance on the ground that it came within the expression ''plant''. However wide the amplitude of the word ''plant'' may be, when specific exclusion of office appliance has been made in the proviso, then no investment allowance can be given.

4. The finding of the Commissioner (Appeals) was that the internal telephone system was installed in the assessee''s pesticides complex at Bhopal. It was held by the Commissioner (Appeals) as follows :

"It was further urged that the ITO should have granted such investment allowance on the Internal Telephone System installed in the appellant''s pesticides complex at Bhopal. He relied on the decision of the Himachal Pradesh High Court in the case of Commissioner of Income Tax Vs. Mohan Meakin Breweries Ltd., It was decided thereunder that Internal Telephone System was a scientific apparatus used for the purpose of the business of the assessee and was, therefore, a plant. It was installed in the factories for the purpose of efficient organisation of the manufacturing process carried on by it. Hence, it could not be construed as ''office appliances''. Therefore, such plant and machinery were entitled to development rebate u/s 33 of the income tax Act.

It was urged by the learned representative that since such Internal Telephone System was construed as ''plant'', the same construction may be put in the case of the assessee''s installation at Bhopal, and, thus, this be entitled to investment allowance.

While appreciating the line or argument advanced by the learned representative, I cannot but observe that grant of investment allowance for installation of new machinery or plant was not automatic. As per provisions of section 32A(2)(b) such machinery shall be such which were used in any industrial undertaking for the purpose of business of production of any article or thing. As the Telephone-Installation was not such type of machinery or plant, it was not entitled to development rebate. Hence, I decline to interfere."

The Tribunal on further appeal held as follows :

"The next objection of the assessee is about the disallowance of investment allowance on Internal Telephone System installed in the pesticides complex at Bhopal. The assessee claimed investment allowance of Rs. 1,96,36,023 u/s 32A of the Act. It included Rs. 8,33,129 in respect of Deep Sea Fishing Divisions I and II. The above amount was disallowed by the ITO.

The assessee came in appeal before the Commissioner (Appeals) and contended that the internal telephone installation was plant and machinery on which the assessee is entitled for investment allowance. The Commissioner (Appeals) was not impressed with the argument of the assessee and consequently he declined to interfere with the order of the ITO on this issue.

Dr. Pal referred to the decision in Commissioner of Income Tax Vs. Mohan Meakin Breweries Ltd., at page 215 and contended that this issue had specifically been considered by the Hon''ble High Court and the High Court has come to the decision that the installation of internal telephone system is plant and machinery and it is not

office appliance. Accordingly, he urged that the investment allowance u/s 32A should be allowed. Shri Lahiri, the departmental representative, relied upon the order of the Commissioner (Appeals) on this issue.

The question whether the installation of internal telephone system is plant and machinery within the meaning of section 32A had been answered by the Hon''ble High Court in Mohan Meakin Breweries Ltd.''s case (supra). Consequently, following the aforesaid decision of the High Court, the ITO is directed to allow investment allowance on the installation of internal telephone system to the assessee."

5. In the case of Commissioner of Income Tax Vs. Mohan Meakin Breweries Ltd., it was held by the Himachal Pradesh High Court that development rebate had to be allowed on internal telephone system installed by the assessee in its factory premises. There, it was observed that the assessee had constructed a net work of telephones in its factory complex for the purpose of efficient organisation of the manufacturing process. This telephone system in the factory was an internal phone system in which 50 telephones were installed during the accounting period. In the back ground of these facts, It was held that installation of internal telephone system must be construed as a ''plant'' in view of the definition of the word ''plant'' given in section 43 of the Act. It is to be noted that the assessment year involved in the case before the Himachal Pradesh High Court was 1963-64 and the question was whether the assessee was entitled to get development rebate u/s 33 of the Act.

6. Section 43(3) has defined ''plant'' to include ship, vehicle, books, scientific apparatus, surgical equipments used for the purpose of business or profession. This wide definition may include office appliances. But by virtue of the proviso to section 32A office appliances have been specifically excluded from the benefit of section 32A.

7. The case of the assessee is that the telephone system was not an office appliance at all but was installed in the factory premises to facilitate and synchronise the working of different parts of the factory.

8. The assessee had contended that the facts of the instant case are identical to the facts in the aforesaid case of Mohan Meakin Breweries Ltd (supra) before the Commissioner (Appeals). Neither the Commissioner (Appeals) nor the Tribunal come to a specific finding as to the correctness of that argument. If the internal telephone system has been installed in the factory premises of the assessee-company substantially and essentially for efficient organisation of manufacturing process development rebate u/s 32A has to be allowed. But if the internal telephone system is primarily for office work of the assessee-company then such allowance may not be allowed. The case, therefore, is remanded back to the Tribunal to find out the relevant facts. If necessary, the Tribunal will take additional evidence and allow both parties opportunity to adduce evidence to substantiate their cases. The Tribunal may also, if it thinks fit, remand the case for further investigation on this aspect of

the matter.

9. Question No. 3 raised at the instance of the revenue is concluded by the judgment of this Court in the assessee''s own case in CIT v. Union Carbide Ltd [IT Reference No. 113 of 1985, dated 5-2-1990]. Following the said judgment, question No. 3 is answered in the affirmative and in favour of the assessee.

10. Coming to the questions raised by the assessee, it appears that the question No. 1 is concluded by the judgment of this Court in the case of Union Carbide India Ltd. Vs. Commissioner of Income Tax, Following the principles laid down in the said judgment, question No. 1 raised at the instance of the assessee is answered in the negative and in favour of the revenue.

11. Question Nos. 2 and 3 raise interesting points relating to capital gains.

The case of the department is that the compensation money received from the insurance company in respect of loss of the trawler ''Jaya Rani'' in deep sea is taxable as capital gains. The facts found by the Tribunal in this respect are as under:

"The assessee''s trawler ''Jaya Rani'' sank in deep waters and it was a total loss to the assessee. The assessee has received the compensation of Rs. 96,00,000 whereas the cost of the trawler was only Rs. 88,16,707. Once the assessee has received the compensation for the trawler, the assessee has subrogated its right for the trawler to the insurance company. Under the circumstances, the provisions of section 45 are clearly attracted. Moreover, the decision taken by the ITO is supported by the cases relied upon by Shri Lahiri, the departmental representative in Commissioner of Income Tax Vs. Vania Silk Mills (P.) Ltd., and Marybong and Kyel Tea Estates Ltd. (since amalgamated with Duncan Agro Industries Ltd.) Vs. Commissioner of Income Tax, Consequently, the action of the Commissioner (Appeals) on this issue is maintained."

12. In order to decide these questions, reference must be made to section 2 (47) which defines ''transfer'' and also section 45 which defines and imposes income tax on ''capital gains'':

"2(47). ''transfer'', in relation to a capital asset, includes the sale, exchange or relinquishment of the asset or the extinguishment of any rights therein or the compulsory acquisition thereof under any law;"

"45. Capital gains. - (1) Any profits or gains arising from the transfer of a capital asset effected in the previous year shall, save as otherwise provided in sections 53, 54, 54B and 54D, be chargeable to income tax under the head ''Capital gains'', and shall be deemed to be the income of the previous year in which the transfer took place.

(2) Notwithstanding anything contained in sub-section (1), the profits or gains arising from the transfer by way of conversion by the owner of a capital asset into,

or its treatment by him as, stock-in-trade of a business carried on by him shall be chargeable to income tax as his income of the previous year in which such stock-in-trade is sold or otherwise transferred by him and, for the purposes of section 48, the fair market value of the asset on the date of such conversion or treatment shall be deemed to be the full value of the consideration received or accruing as a result of the transfer of the capital asset."

13. It is well-settled that compensation paid by an insurance company may be of capital or revenue nature depending upon the nature of the property insured. If the compensation is paid for damage or destruction of trading assets, the amount in the hand of the recipients is to be treated as revenue receipt. But if the compensation is paid for loss or destruction of a capital asset or if any damage is caused to the capital asset, the money received under an insurance policy will be of capital nature. In the case of IR v. Williams 26 TC 23, 35 and in the case of Green v. Gliksten 14 TC 364, the principle was laid down that in the case of insurance of trading stock, the insurance moneys must be treated in exactly the same manner as receipt from a sale of the goods; would have been. The trader did not trade in fires but in goods; but for tax purposes there was no difference between the proceeds of goods sold and insurance moneys in respect of goods destroyed by fire. By this reasoning it must be held that when a capital asset is insured, the compensation money received from a insurance company for loss or destruction of the capital assets must be of capital nature. But every type of capital receipt is not chargeable to tax as capital gain. Therefore, it has to be seen whether the compensation amount paid by the insurance company for the loss of the trawler can be treated as capital gains under the provisions of the Act.

14. Mr. Bagchi has contended that in this case there has been a loss of a trawler and the compensation has been paid for such loss and the legal consequence is that the insurance company, under the insurance con tract has acquired the right of ownership over the sunken trawler. If and when the trawler is salvaged, it will belong to the insurance company.

15. We are unable to uphold this contention.

16. The insurance company compensates the insured for the loss suffered in respect of the goods insured. In the instant case, the trawler which was a capital asset of the assessee was insured. If there was any damage to the trawler and had the insurance money been paid for it, the amount of compensation would have been shown in the capital account of the recipient. In the instant case the trawler was lost entirely in deep sea. The insurance money has been paid for the total loss of a capital asset. Under the policy of insurance if the trawler is eventually salvaged, it will belong to the insurance company. The question is whether this will amount to ''transfer'' of a capital asset as defined in section 2(47).

17. This clearly is not a case of sale or exchange of the trawler. It is also not a case of compulsory acquisition of the trawler by anybody. There fore, the only question is : has there been any relinquishment of the trawler or extinguishment of any right therein. In common parlance loss of a trawler in deep sea cannot be described as relinquishment of the trawler. The Dictionary meaning of the ''Relinquishment'' is ''give up, abandon, cease from, resign, surrender (habit, plan, hope, belief, right, possession); loose hold of (object held) '' -. The Concise Oxford Dictionary, 4th edn.

18. The assessee has not given up or abandoned the trawler. On the contrary, it lost the trawler due to reasons over which it had no control. There is a fundamental difference between loss and relinquishment. If a man loses his money, it cannot be said that he has relinquished the money. Relinquishment of anything by a person would indicate that the person has done something out of his own volition. Involuntary loss of property cannot be described as relinquishment.

19. The next question is whether there has been extinguishment of any right of the assessee in the trawler. There is no question about it that the assessee has lost the trawler.

20. Section 2(47) which defines ''transfer'' opens with the phrase ''transfer in relation to a capital asset''. If the capital asset is totally lost or ceases to exist, there cannot be any transfer.

21. I am also unable to uphold the contention that as a result of the loss of the trawler, there has been an extinguishment of the right of the assessee in that trawler and, therefore, a transfer of a capital asset has taken place. The capital asset in this case is the trawler, ''Jaya Rani''. To adopt the phraseology of section 2(47), ''transfer'' in relation to Jaya Rani includes ''extinguishment of any rights therein''. The word ''therein'' cannot be treated as surplusage and some meaning has to be given to it. The definition of the word ''transfer'' in section 2(47) contemplates existence of a capital asset and extinguishment of any right in that capital asset. The total loss of the capital asset or extinguishment of the capital asset itself will not come within the phrase ''extinguishment of any rights therein Section 2(47) makes it clear that transfer in relation to a capital asset will include sale, exchange or relinquishment of that asset. It will also include compulsory acquisition of that asset under any law. All these are cases of out and out transfer of the capital asset itself. The fifth category of transfer mentioned in section 2(47) is the extinguishment of any right in the capital asset.

22. The Legislature has not adopted the same phraseology for all the five types of ''transfer'' mentioned in section 2(47). It speaks of ''the sale, exchange or relinquishment of the asset or ''the extinguishment of any rights therein or compulsory acquisition thereof [Emphasis supplied]. If an assessee sells, exchanges, or relinquishes any capital asset, a transfer will take place within the meaning of section 2(47). But if no sale, exchange or relinquishment of the asset takes place but

any right in the asset is extinguished, that will also amount to transfer. Compulsory acquisition of the asset will also amount to transfer. The Legislature has deliberately not used the expression "the extinguishment thereof or of any rights therein". Neither by clear words of the statute nor by necessary implication, total loss of a capital asset can be brought within the phrase "the extinguishment of any rights therein".

23. In this connection, it has to be borne in mind that section 45 is the charging section. It brings to tax the capital gains made by an assessee in the relevant year of account. The well-settled law is that a charging provision must be strictly construed. If a case does not come fairly and squarely within the clear meaning of the words of a charging provision, an assessee cannot be made liable to pay tax by giving an extended meaning to the words of the charging section. In the words of Lord Salmon, it is not possible by torturing the statutory language or by any other means to construe it so as to give it a meaning which the Parliament clearly did not intend it to bear - IRC v. Rossminster Ltd 53 TC 160. In the instant case, in order to uphold the contention of the revenue, the word ''extinguishment'' has to be given an artificial meaning and the word ''therein'' has to be treated as surplusage.

24. The word ''extinguishment'' has been used by the Parliament in a number of statutes and its import in legal parlance is well-known and understood. Article 31A(1)(e) of the Constitution speaks of ''the acquisition by the State of any estate or of any rights therein or the extinguishment or modification of any rights''. Section 27 of the Indian Limitation Act, provides that ''at the determination of the period hereby limited to any person for instituting a suit for possession of any property, his right to such property shall be extinguished''. In both the cases, extinguishment of right in the property takes place while the property continues to be in existence.

The word ''extinguishment'' has also been used to text books in the sense of disappearance or loss of any interest in a property while the property continues to be in existence. A mortgaged security may be extinguished in various ways. Total loss of property has never been regarded either in any statute or in the legal parlance as ''extinguishment of any rights therein''. There is another aspect of this case.

25. There is no specific finding by the Tribunal that because the compensation amount was paid by the insurance company to the assessee, the trawler, if salvaged, will belong to the insurance company. Even assuming that this is the position, I fail to see how the sinking of a trawler in deep sea can be treated as a case of transfer of capital asset. The insurance company has paid compensation to the assessee for the loss of the trawler, Jaya Rani. As a consequence of the payment of compensation for the total loss of the trawler, the insurance company may have acquired a right to get possession of the trawler in the unlikely event of the trawler being recovered from the bottom of the sea. But this right of the insurance company accrued as a consequence of the payment of compensation and not the reason why the

compensation was paid. The compensation was paid for the loss of trawler and not for the transfer of any asset.

26. There is no finding by the Tribunal that there is any likelihood of recovery of the trawler from the bottom of the sea. The assessee could not possibly transfer the trawler or any right, title or interest in the trawler after the trawler was lost. The provisions of section 45 are attracted only when profits and gains arise ''from the transfer of a capital asset effected in the previous year''. The assessee, in the instant case, has not effected any transfer of capital asset. The assessee cannot possibly transfer something which the assessee does not have.

27. We were referred to a large number of decisions, both on behalf of the revenue and the assessee on these points.

28. The first judgment is in the case of Commissioner of Income Tax Vs. Vania Silk Mills (P.) Ltd., The facts before the Gujarat High Court were that the assessee, a private limited company, was carrying on manufacture and sale of art-silk and had purchased machineries worth Rs. 2,81,741 which were given on hire to one Jasmine Mills Ltd., at an annual rent of Rs. 33,900. On 11-8-1966, a fire broke out in the premises of Jasmine Mills Ltd. causing extensive damages to the machinery hired from the assessee- company and other machinery belonging to Jasmine Mills Ltd. The assessee''s machinery was damaged to such an extent it could not any longer be put to use and Jasmine Mills (P.) Ltd. received an insurance claim of Rs. 6,32,533 on account of the destruction of the machinery. The Gujarat High Court held that the difference between the compensation received by the assessee-company and the costs of the assets was chargeable to tax as the said amounts are the capital gains. In that case, it was observed as follows :

"On the plain language of section 45 itself and even by reading the said provision along with section 48, therefore, it is manifest that the profit or gain must have been received by or accrued to the assessee as a result of the extinguishment of any rights in a capital asset and not on account of extinction of some other distinct rights." (p. 313)

It appears that the Court overlooked the import of the word ''effected'' used in section 45 - transfers must be effected. It cannot be said that the destruction of an asset will mean transfer of that asset has been effected. In the judgment the significance of the words ''extinguishment of any rights therein'' has been overlooked. In order to bring a case within ''capital gains'' it has to be established that there has been extinguishment of any right in capital asset. Therefore, there must be a capital asset in which the right of the assessee has been extinguished. If an assessee surrenders, lease in a building, then it can be said that there has been extinguishment of the right of the assessee in that building. If leasehold property has been compulsorily acquired by the Government, then the assessee''s right as a lessor has been completely extinguished involuntarily. But where an asset is

destroyed totally it cannot be a case of extinguishment of rights in the capital asset. The ownership of possession may confer a bundle of rights on the assessee. If those or some of those rights are surrendered, then it may amount to extinguishment of any right or all of the rights in the capital asset. But loss of the capital asset altogether cannot amount to extinguishment of any right therein. In fact, this phrase ''extinguishment of rights therein'' has to be contrasted with the precedent phrase ''relinquishment of the assets''. It has also to be juxtaposed with the phrase ''compulsory acquisition thereof. If that is done, it will be seen that total relinquishment of right in the asset presupposes continued existence of the asset. The asset may be lost to the assessee by compulsory acquisition but when the section speaks of extinguishment of any right therein it means an asset is in existence but the assessee''s right in those assets have been given up or lost. To take a common example, if an owner of a house gives up possession of the house, it may be extinguishment of the possessory right of the owner but if the house is totally destroyed by fire, it cannot be described as extinguishment of the rights of the owner in the house. It is the loss of the house in its entirety. Moreover, section 45 speaks of transfer effected. Some meaning has to be given to the word ''effected''. If a transfer has been effected voluntarily or involuntarily, then section 45 will come into operation and capital gains can be levied. But total loss of the asset cannot be treated on transfer effected by the assessee. In the instant case, it cannot be said that either the assessee or the insurance company has effected any transfer or extinguishment of any right in the capital asset.

29. The next judgment to which our attention has been drawn is the case of Marybong and Kyel Tea Estates Ltd. (since amalgamated with Duncan Agro Industries Ltd.) Vs. Commissioner of Income Tax, In that case, a fire broke out in the assessee''s factory resulting in the damage and destruction of some assets. The assessee received an amount of Rs. 6 lakhs from the insurance company. The question was whether the difference between the original cost and the letting down value of the assets destroyed and the amount received by the assessee will be treated as capital gains. The Tribunal found that under the terms of the insurance policy the insurer had the right to take possession of the property of the insured at the time of loss and damage and had the right to remove the property or otherwise deal with the same. The left-over property was actually taken over by the insurance company. It was held that the sum of Rs. 4,95,044 was assessable as capital gains. This case proceeded on the footing that the insurance company took over the assets and paid compensation to the assessee.

In this case there was a case of transfer of capital assets in a changed shape or form and the gains arising therefrom to the extent of Rs. 4,95,044 were assessable as capital gains but in the instant case there is no finding that the insurance company has been able to get any assets. The ship has sunk in the deep sea. There is no finding that the ship was recovered in the relevant accounting period or in any subsequent accounting period.

30. It has been contended by Mr. Bagchi, that the ship may well be recovered and if such recovery is made, it will be the insurance company which will be entitled to get possession of the ship. But the question is whether in the relevant year of account any transfer of capital asset has taken place.

31. The compensation paid by the insurance company was for the loss of the trawler. If the trawler had not been lost, the insurance company would not have paid any compensation. The compensation money was not paid in order to effect transfer of the property. The loss of a property cannot be treated as transfer of property. It is not a case of sale of the trawler, exchange of the trawler or relinquishment of the trawler by the assessee, nor is it a case of compulsory acquisition of the trawler. The only question is : has there been any extinguishment of any right by the assessee in the trawler ? In our opinion, it is not extinguishment of right in the trawler but loss of the trawler itself altogether.

32. Moreover, section 45 speaks of ''any profits or gains arising from the transfer of a capital asset in the previous year''. The compensation that has been received by the assessee is not from any extinction of the rights in the trawler effected by the assessee. The assessee has lost the trawler in the deep sea and has claimed and obtained compensation for the loss. If the trawler is recovered in future, then the insurance company may claim the trawler as its own, if there is any clause in the insurance policy to that effect. But even if there is such a clause, it is a remote possibility of the trawler being salvaged, enabling the insurance company to get it.

33. Therefore, we are of the view that Dr. Pal is right in his contention that the compensation has been paid for total destruction and total loss of the trawler and this amount of compensation cannot be treated as a consideration for transfer of a capital asset. On the facts of this case no transfer can be said to have been effected by the assessee.

34. In the case of C. Leo Machodo Vs. Commissioner of Income Tax, , the Madras High Court had to deal with the facts which were very similar to the facts of the instant case. That was a case where a boat sank in the high seas and compensation was paid by the insurance company.

The facts in that case were that the assessee was carrying on business of plying boats and during the relevant accounting year the boat belonging to the assessee met with an accident on 17-8-1974 and the boat sank in the sea. The boat was insured with the United India Fire & General Insurance Co. and in accordance with the contract of insurance, the assessee received a sum of Rs. 1 lakh from the insurance company on 25-11-1974. In the assessment proceedings for the assessment year 1976-77, the ITO held that the assessee was liable to pay tax on capital gains on the amount of compensation received by the assessee and the compensation calculated by the ITO was Rs. 5,00,008. The Tribunal held that since the boat had sunk in the sea, the right of the assessee in the boat stood

extinguished and this extinction of the right in the capital asset cannot be treated as being transferred. In that case, M.N. Chandurkar, CJ. has observed as follows :

"Now, so far as the definition of ''transfer'' is concerned, it is undoubtedly a very wide definition and that definition includes extinguishment of any rights in the capital asset or the compulsory acquisition thereof under any law. That definition cannot be read in isolation, but it has to be read along with section 45 and the substantive provision in section 45 which positively requires that for the transfer of the asset as contemplated by section 2(47), the assessee who is the owner of the capital asset must either receive consideration for the transfer or the consideration must accrue to him as a result of the transfer of the capital asset. The capital gain contemplated by section 45 is to be worked out in the mode prescribed in section 48. Unless, therefore, it is established that consideration has either been received or has accrued to the assessee for the transfer as contemplated by section 2(47), the provisions relating to capital gains will not be attracted and there will not be any liability for capital gains tax. It is also important to bear in mind that section 45 refers to ''the transfer of a capital asset effected in the previous year''. The concept of capital gains, therefore, contemplates that unless the transfer is effected by somebody or by some agency, it will not be a transfer for the purpose of section 45 of the Act.

Having regard to the context in which the word ''effected'' is used in section 45, it is clear that it contemplates some agency by the act of which the transfer is brought about. The meaning of the word ''effected'', which is relevant for our purpose, given in the Concise Oxford Dictionary, sixth edn., is ''bring about; accomplish; cause to exist or occur''. It is, therefore, implicit in section 45 that a sale, exchange or relinquishment of the asset or the extinguishment of any rights in the capital asset or the compulsory acquisition of the capital asset must be the result of the act of some agency. There is no difficulty insofar as the sale, exchange or relinquishment of the asset is concerned, because it is the owner of the capital asset who can bring about the sale, exchange or relinquishment of the asset. Insofar as the compulsory acquisition of the asset is concerned, the definition itself says that it could be under any law which means that by giving an artificial meaning to the word ''transfer'', acquisition of a capital asset under a law providing for such compulsory acquisition is treated as transfer of the capital asset. The only other part of the definition of ''transfer'' is ''the extinguishment of any right therein''. Since the definition has already provided for relinquishment which would be a voluntary act of the owner of the capital asset, extinguishment of the rights in the capital asset must result from some act other than the act of relinquishment of the capital asset. We are not in this case concerned with relinquishment of rights in an incorporeal asset. We are concerned with extinguishment of rights in a corporeal property. Insofar as the capital asset which is in the nature of a corporeal property is concerned, such extinguishment of the rights in the capital asset must, in our view necessarily be brought about by action of some agency other than the transferor and for such

extinguishment, there must also be consideration. Such agency may not be an individual. This extinguishment of the right may result from a contract with the owner in which case it will be a voluntary act or the only other agency which can deprive the owner of his right in the capital asset will be the Legislature. Such a law may be different from a law providing not for acquisition but for extinguishment, of rights of the owner. Therefore, reading the word ''transfer'' in the light of the use of the word ''effected'' in section 45, it appears to us that in the case of corporeal property, unless the owner of the capital asset is divested of his right by the process of extinguishment resorted to by some agency and unless there is consideration for such extinguishment, by the mere fact that the asset stands destroyed either by fire or by sinking in the sea as in the instant case, there can be no transfer of the capital asset for the purpose of sections 45 and 48 of the Act. The mere fact that the definition of ''transfer'' is an inclusive definition does not mean that every extinguishment of the rights of the owner of the capital asset howsoever brought about will necessarily amount to a transfer. It is undoubtedly true that when a definition expressly includes things which are not covered within the ordinary meaning of the word, the intention of the Legislature is to give a wide meaning to the word itself and when we are dealing with an inclusive definition, it is inappropriate to put a restrictive interpretation upon terms of wider denomination. But it is also true that notwithstanding the inclusive definition, when that definition is to be substituted for the word defined and used in a statutory provision, the extended meaning will be controlled by the other words used in the section, and if necessary, by the other provisions relevant for working out the main provision. As pointed earlier, section 45 refers to the transfer of a capital asset being effected and, therefore, notwithstanding the inclusive definition of the word ''transfer'', we must read that definition in section 45 in the light of the use of the word ''effected''. Insofar as the present controversy is concerned, section 45 will have to be read as follows :

''Any profits or gains arising from the extinguishment of any rights in a capital asset affected in the previous year... shall be chargeable to income tax under the head ''Capital gains'' and shall be deemed to be the income of the previous year in which the transfer took place.''

It must, therefore, be established that the extinguishment of the rights of the assessee was effected by some agency." (p. 751)

35. After referring to the Gujarat High Court in the case of Vadilal Soda Ice Factory Vs. Commissioner of Income Tax, Gujarat II, it was further observed that:

"The other question which becomes material for the decision of the present reference is whether the compensation paid in pursuance of the contract of insurance can be considered as consideration: The money which is received by the assessee is not by way of consideration for extinguishment of any rights. Section 48 of the Act refers to ''the full value of the consideration received or accruing as a

result of the transfer of the capital asset.'' The normal concept of consideration contemplates a quid pro quo for something of which a person is divested, and in the light of the what have been said earlier, voluntarily or involuntarily, through some agency. In cases of compulsory acquisition, the capital asset vests in the acquiring body and, though what is paid by the acquiring body is called compensation, it can also be described as consideration for the acquisition. But where moneys are paid by an insurance company consequent upon total destruction of the property and no transfer results from such destruction or extinguishment of all rights in the capital asset, the amount paid by the insurance company cannot, in our view, be described as a consideration as a result of the transfer of the capital asset. When something is said to be paid or received as a result of the transfer, there has to be a direct nexus between the transfer and the receipt. As we have already pointed out, if there was no transfer of the capital asset, the question of nexus between the payment made by the insurance company and the transfer does not arise in the instant case. The payment received in pursuance of a contract of indemnity cannot be considered to be payment as a result of the transfer of property. It is well-established that a contract of insurance is a contract of indemnity. In Halsbury ''s Laws of England, fourth edition, Vol. 25, under the heading Insurance'' in paragraph 3, it is observed as follows:

''Most contracts of insurance belong to the general category of contracts of indemnity in the sense that the insurer''s liability is limited to the actual loss which is in fact proved. The happening of the event does not of itself entitle the assured to payment of the sum stipulated in the policy; the event must in fact result in a pecuniary loss to the assured, who then becomes entitled to be indemnified subject to the limitations of his contract. He cannot recover more than the sum insured, for that sum is all that he has stipulated for by his premiums and it fixed the maximum liability of the insurers. Even within that limit, however, he cannot recover more than what he establishes to be the actual amount of his loss. The contract being one of indemnity, and indemnity only, he can recover the actual amount of his loss and no more, whatever may have been his estimate of what his loss would be likely to be, and whatever the premiums he may have paid, calculated on the basis of that estimate.''

When a person who has insured his goods or property receives compensation from the insurance company, it is a compensation for the pecuniary loss which the person has suffered. To equate such amount received by way of compensation for the pecuniary loss with consideration for transfer of a capital asset, in our view, is not at all warranted, having regard to the peculiar nature of the principle of indemnity on which contracts of insurance are based. We are, therefore, of the considered view that the amount received by the assessee in pursuance of the contract of indemnity cannot be considered as consideration for the transfer of a capital asset as contemplated by section 45 read with section 4 of the Act." (p. 755)

It was held in that case that when the boat sank in the sea, compensation was paid by the insurance company for the loss suffered by the assessee. No ''transfer'' took place as contemplated by section 45, read with section 48.

We respectfully agree with the views expressed by the Madras High Court in the case of C. Leo Machodo (supra).

36. Accordingly, question No. 2 has to be answered in the negative and in favour of the assessee and the question No. 3 has to be answered in the affirmative and in favour of the assessee.

37. Question Nos. 4 and 5 raised at the instance of the assessee relate to charging of interest u/s 220(2). The contention of the assessee is that the sum of Rs. 1,42,993 was charged by way of interest and this amount is deductible as business expenditure u/s 37. It has been contended by Dr. Pal that the Supreme Court has held that levy of interest cannot be equated with imposition of penalty. The assessee has not paid the tax in time and the assessee has been obliged to pay interest and such payment is compensatory.

38. In the case of Balrampur Sugar Co. Ltd. Vs. Commissioner of Income Tax, Sabyasachi Mukharji, J. (as His Lordship then was) held that the liability to pay interest u/s 3(3) of the U.P. Sugarcane (Purchase Tax) Act, 1961 which arose for the delayed payment of cess was compensatory and not in the nature of penalty and was an allowable deduction in computing the business income of an assessee who carried on the business of manufacture and sale of sugar.

39. Reliance has been placed on the judgment of the Supreme Court in the case of Central Provinces Manganese Ore Co. Ltd. Vs. Commissioner of Income Tax, The Supreme Court held that the levy of interest was in the nature of compensation and not penalty and application for waiver for reduction of interest should be made first before the ITO. The revision application before the Commissioner was maintainable only if such claim was made in accordance with the provisions of the Act. But before the revisional jurisdiction of the Commissioner could be invoked, it was necessary for the assessee to demonstrate before the ITO that there was no case for revision or reducing levy of interest.

40. In the case of Ganesh Dass Sreeram Vs. Income Tax Officer, ''A'' Ward, Shillong and Others, it was held by the Supreme Court once again that interest was levied by way of compensation and not by way of penalty.

41. Dr. Pal next invited our attention to another judgment of the Supreme Court in the case of Mahalaxmi Sugar Mills Co. Vs. Commissioner of Income Tax , Delhi, where the Supreme Court held that interest paid by the assessee- company engaged in the business of manufacture and sale of sugar on arrears of cess payable was a permissible deduction u/s 10(2)(xv). The Supreme Court observed that interest payable on arrear of cess u/s 3(3) was, in reality, the liability to pay cess. If

the cess was not paid within the prescribed period, a larger sum became payable as cess.

But these observations of the Supreme Court cannot come to the aid of the assessee in the instant case. This is a case of interest paid for delayed payment of income tax. This may be compensatory but the amount of income tax paid by an assessee is not a deductible expenditure u/s 37. The payment of income tax is not treated as an expenditure incurred wholly and exclusively for the purpose of carrying on the business of the assessee. In the case of cess, if the company has to pay the statutory duties to carry on its business, it has to pay levies like cess. The amount of such levies paid by the assessee is deductible as a business expenditure of the assessee. The assessee has to incur these expenses in order to carry on its business. The Supreme Court has pointed out that the result of levy of interest under the Cess Act was the enlargement of the cess liability. That being so, the amount of cess paid being a deductible expenditure, any such liability also become a deductible expenditure automatically. But, in the instant case, the amount of income tax paid by the assessee was not a deductible expenditure. If that amount got enlarged by levy of interest, the enlarged amount could not be treated as a deductible expenditure.

42. In the case of Waldies Ltd. Vs. Commissioner of Income Tax, it was held by the Division Bench of this Court that the interest paid on the amount borrowed for payment of tax was not deductible as business expenditure. This was given in accordance with the law, as it stood in the assessment year 1971-72 and continued till the introduction of section 80B in the Act. The ratio of that judgment was that the payment of income tax was not a part of the business expenditure of the assessee. Therefore, the interest paid by the assessee on account of borrowed money for payment of tax was not a deductible income.

43. In the case of Balmer Lawrie and Co. Ltd. Vs. Commissioner of Income Tax, Calcutta, it was held by the Division Bench of this Court in a case decided under the 1922 Act that interest paid by the assessee u/s 18A(vi) was not interest in respect of any capital borrowed and was not allowable u/s 10(2)(iii). It was further held that the payment of interest for borrowed money to pay advance tax in time was in no sense incidental to the business and the interest was not allowable u/s 10(2)(xv).

44. In the case of National Engineering Industries Ltd. Vs. Commissioner of Income Tax (Central), it was held by the Division Bench of this Court that in view of the absence of any statutory provisions the sum of Rs. 2,50,790 was paid on account of interest u/s 220(2). It was held that even if the available amount was invested in the assessee''s business and the sum claimed as deductible, it could not be allowed as deduction on the ground of business expenditure.

45. In the case of Federal Bank Ltd. Vs. Commissioner of Income Tax, the Kerala High Court held that any amount paid on account of income tax was not a

permissible deduction. Therefore, interest for delayed payment of income tax stands on the same footing as a liability to pay income tax and, as such, was not a permissible deduction u/s 37(1).

46. Same view has been taken by the Gauhati High Court in the case of Assam Forest Products (P.) Ltd. Vs. Commissioner of Income Tax,

47. Therefore, in view of these decisions and the principles laid down in these cases it cannot be said that the interest paid u/s 220(2) by an assessee was a deductible expenditure u/s 37. If the amount paid as income tax is not a deductible expenditure, then the amount paid as interest for delayed payment of such tax cannot be allowed as deduction.

48. There is another aspect of this case. If interest that has been levied for delayed payment of income tax is allowed as a deductible expenditure u/s 37, then, in reality, the assessee will get the double benefit because the assessee will be rewarded for not paying the tax in time by getting the interest paid deducted as business expenditure. In effect, the assessee will not suffer in any way for payment of this interest. Such construction will lead to absurdity and will be avoided. If this construction is adopted, then the department will not be compensated in any way. The Supreme Court has held that interest that is levied for delayed payment of tax is compensatory. But if the amount what is paid as compensation for the delay is allowed to be. deducted as business expenditure, then, in effect, there is no compensation to the department for such delayed payment.

49. In view of the aforesaid question Nos. 4 and 5, raised at the instance of the assessee, are answered in the affirmative and in favour of the revenue.

50. In the result, question No. 1 raised at the instance of the revenue is answered in the affirmative and in favour of the assessee.

Second question raised on behalf of the revenue is remanded back to the Tribunal to find out the relevant facts. If necessary, the Tribunal will take additional evidence and allow both parties to adduce evidence to substantiate their cases. The Tribunal may also, if it thinks fit, remand the case for further investigation on this aspect of the matter.

Third question raised on behalf of the revenue is answered in the affirmative and in favour of the assessee.

51. Question No. 1 raised at the instance of the assessee is answered in the negative and in favour of the revenue.

Second question raised on behalf of the assessee is answered in the negative and in favour of the assessee.

Third question raised on behalf of the assessee is answered in the affirmative and in favour of the assessee.

Fourth and fifth questions raised at the instance of the assessee are answered in the affirmative and in favour of the revenue.

52. There will be no order as to costs.

Bhagabati Prasad Banerjee, J.

I agree.