Commissioner of Income Tax Vs Asiatic Oxygen and Acetylene Co. Ltd.

Court: Calcutta High Court

Date of Decision: July 21, 1980

Acts Referred: Income Tax Act, 1922 â€" Section 10(2)

Citation: (1981) 132 ITR 506

Hon'ble Judges: Sudhindra Mohan Guha, J; Sabyasachi Mukharji, J

Bench: Division Bench

Advocate: B.K. Bagchi and B.K. Naha, for the Appellant; None, for the Respondent

Judgement

Sudhindra Mohan Guha, J.
The question as referred to this court in the present reference is as follows :

Whether, on the facts and in the circumstances of the case, fees of Rs. 21,137 paid for revaluation of the assets by the assessee-company was

rightly allowed by the Tribunal as a deduction u/s 10(2)(xv) of the Indian Income Tax Act, 1922?

2. The assessment relates to the year 1961-62 for which the relevant previous year ended on March 31, 1961.

3. The assessee-company was a manufacturer of oxygen and acetylene gas. It claimed an expenditure of Rs. 21,137 representing the fees paid by

it to M/s. Talbot & Co., Calcutta, in respect of their professional services of making a valuation report of the fixed assets of the company. The ITO

disallowed the claim holding the claim to be of capital nature. In appeal before the AAC, it was argued on behalf of the assessee that as a result of

revaluation of the assets of the assessee-company for which the payment was made, no asset or advantage of an enduring benefit had come into

existence and the only purpose of the revaluation was to improve the credit-worthiness of the company so that it could obtain loans for the purpose

of its business without difficulty or inconvenience. The AAC did not accept the argument of the assessee. But at the same time he made a reference

to the report of the directors dated May 1, 1961, to the shareholders of the assessee-company. Therein, it was stated :

The value of the fixed assets of the company as appearing in the balance-sheet was disproportionate to their present day valuation and the

directors, therefore, considered it fair that these assets may be revalued by expert valuers to bring them in line with the present day valuation in the

balance-sheet. The result of this has been an increase in the fixed assets valuation to the extent of Rs. 26,96,000, which has been debited to the

fixed assets and a capital reserve to this extent has been credited in the balance-sheet.

4. But the AAC opined that these affected the capital structure of the company and, therefore, the expenditure incurred for the same had been

secured by the assessee on the hypothecation of its stocks and the valuation of its fixed assets had nothing to do with the obtaining of the loan from

the banks. The order passed by the ITO was, accordingly, confirmed.

5. The assessee came in further appeal to the Tribunal. The arguments made before the AAC were reiterated before the Tribunal on behalf of the

assessee. On behalf of the department, however, it was contended that the expenditure was clearly not incurred for the day to day operational

activities of the assessee and related to the capital structure of the company and was, therefore, capital in nature.

6. The Tribunal, however, on a consideration of the arguments advanced by both the parties, came to the conclusion that the expenditure was

clearly revenue in nature. According to it, the assessee had not acquired any new capital asset through the process of revaluation. No advantage of

any enduring nature was also obtained by this process. The assets and liabilities of the assessee continued to remain the same except that their

valuation was shown at higher figures in the books of account. So, such an expenditure, in the opinion of the Tribunal, could not be categorised as

capital expenditure, and deleted the addition.

7. On behalf of the revenue, the decision of the Division Bench of this court in the case of Assam Bengal Cement Co. Ltd., Calcutta Vs.

Commissioner of Income Tax, West Bengal, Calcutta, was referred. In this case, tests have been laid down for ascertaining the distinction between

the capital and revenue expenditure. Capital expenditure was a fee that was going to be spent once for all, whereas an income expenditure was a

thing that was going to recur every year. While disposing of the case, their Lordships referred to certain English cases which were discussed at p.

49 of the report. It would be of some use, if we quote the lines whereby such distinction had been drawn by the English courts :

" When", he said, "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,...there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such

an expenditure as properly attributable not to revenue but to capital". To a certain extent this proposition was founded on what Scrutton L.J. had

said in the same case in the Court of Appeal and it had been anticipated by Rowlatt J. in Ounsworth v. Victors Ltd. [1915] 3 KB 267; 6 TC 671

(KB). But it was the first full statement of the whole principle and it has since served as the basic text of the rule, subsidiary propositions being

added from time to time by way of explanation or commentary. Thus, with reference to "enduring benefit", Rowlatt J., said in the case of Anglo-

Persian Oil Co. v. Dale [1932] 1 KB 124; 16 TC 253 (CA) that the benefit must endure in the way that fixed capital endures and not in the sense

that for a good number of years it relieves the business of a revenue payment. This interpretation of ''enduring benefit'' has been universally

accepted and approving of it in the same case in the Court of Appeal, Romer L.J. said that the benefit secured to the business must be a capital

benefit. ''Enduring'', however, it was explained by the Parcq L.J., in the case of HENRIKSEN (INSPECTOR OF TAXES) Vs. GRAFTON

HOTEL LTD., does not mean '' everlasting'', but only means that the benefit must be of sufficient durability to justify its being treated as a capital

asset. The asset need not be anything tangible (per Lawrence J., in Collins v. Joseph Adamson and Co. [1938] 1 KB 477 ; 21 TC 400 (KB) nor

capable of being shown at a value in the balance-sheet [per Lord Greene M.R., in Associated Portland Cement Manufacturers Ltd. v. Kerr

[1945] 27 TC 103 (CA)], but may even be of a negative character (per Romer L.J., in Anglo-Persian Oil Co. v. Dale). Again, it is not necessary

that some asset or advantage should actually be brought into existence. Expenditure is to be attributed to capital, if it is made with a view to

acquiring some asset or advantage of enduring benefit: it is not further necessary that it should have that result (per Romer L.J., ibid).

8. Again a reference was made in this very decision to an Australian case of Sun Newspapers Ltd. and Associated Newspapers Ltd. v. Federal

Commissioner of Taxation [1938] 61 CLR 337. It was held that though no material asset was acquired and the payment was made while carrying

on business to safeguard the profits by securing monopoly and preventing competition, the outlay was capital expenditure because apart from other

reasons it concerned the reinforcement of profit-yielding subject, the instrument for earning profits and was not concerned with the use or

employment of that instrument for the profit-earning purpose. It is argued by Mr. B.K. Bagchi, relying on this decision, that in this very case no

material asset was acquired. So the deduction was rightly refused by the AAC. It is true that no material asset was acquired, but the expenditure

was made with a definite purpose. This case could be very well distinguished from the facts and circumstances of the case in hand.

9. The Supreme Court considered the distinction between capital expender ture and revenue expenditure in an appeal from the decision of the

Calcutta High Court in the case of Assam Bengal Cement Co. Ltd. Vs. The Commissioner of Income Tax, West Bengal, of the report, their

Lordships observed as follows :

In cases where the expenditure is made for the initial outlay or for extension of a business or a substantial replacement of the equipment, there is

no doubt that it is a capital expenditure. A capital asset of the business is either acquired or extended or substantially replaced and that outlay

whatever be its source whether it is drawn from the capital or the income of the concern is certainly in the nature of capital expenditure. The

question, however, arises for consideration where the expenditure is incurred while the business is going on and is not incurred either for extension

of the business or for the substantial replacement of its equipment. Such expenditure can be looked at either from the point of view of what is

acquired or from the point of view of what is the source from which the expenditure is incurred. If the expenditure is made for acquiring or bringing

into existence an asset or advantage for the enduring benefit of the business it is properly attributable to capital and is of the nature of capital

expenditure. If, on the other hand, it is made not for the purpose of bringing into existence any such asset or advantage but for running the business

or working it with a view to produce the profits it is a revenue expenditure.

10. Next reference is made to another decision of the Supreme Court in the case of Commissioner of Income Tax, West Bengal II, Calcutta Vs.

Coal Shipment (P) Ltd., , it is stated therein :

The character of the payment can be determined, it was added, by looking at what is the true nature of the asset which has been acquired and not

by the fact whether it is a payment in a lump sum or by instalments. It is also an accepted proposition that the words ''permanent'' and ''enduring''

are only relative terms and not synonymous with perpetual or everlasting.

11. In the case of Lakshmiji Sugar Mills Co. P. Ltd. Vs. Commissioner of Income Tax, New Delhi, , wherein also to find out the distinction

between the capital expenditure and revenue expenditure, their Lordships quoted the passage of the judgment of Assam Bengal Cement Co. Ltd.

Vs. The Commissioner of Income Tax, West Bengal, which runs as follows :

If the expenditure is made for acquiring or bringing into existence an asset or advantage for the enduring benefit of the business it is properly

attributable to capital and is of the nature of capital expenditure.

If, on the other hand, it is made not for the purpose of bringing into existence any such asset or advantage but for running the business or working it

with a view to produce the profits it is a revenue expenditure.

12. Next reference is made to the decision of the Madras High Court in the case of Commissioner of Income Tax Vs. T.V. Sundaram Iyengar and

Sons (P.) Ltd., . In this case, the assessee-company purchased land in the name of the District Collector, Madurai, for the purpose of constructing

houses for the company''s workers by the Government under the subsidised industrial housing scheme and sponsored by the State Government

and claimed certain sums being the purchase price as a deduction u/s 10(2)(xv) of the Indian I.T. Act, 1922, as being in the nature of welfare

expenses. The departmental authorities rejected this claim, but the Tribunal upheld the claim on the ground that the expenditure was incurred

wholly and exclusively for the purpose of the business of the assessee and the assessee had not acquired any capital asset of an enduring nature nor

had any enduring benefit accrued to the assessee by the purchase. Further, as similar expenditure had to be incurred year after year, it could not be

said that the expenditure had been incurred once and for all. On a reference to the Supreme Court, it was held : (i) that the expenditure was

incurred wholly and exclusively for the purpose of the business of the assessee-company; (ii) that the assessee-company had not acquired for itself

any capital asset. Thus, the amount in question was a permissible deduction as a revenue expenditure.

13. The Himachal Pradesh High Court again in the case of Mohan Meakin Breweries Ltd. v. CIT (No. 2) [1919] 117 ITR 505 , while

distinguishing capital and revenue expenditure, reiterated the principles discussed above.

14. This court again in the case of Hindustan Gas and Industries Ltd. Vs. Commissioner of Income Tax, , held that in such a case the onus was

always on the assessee to prove the nature and character of the expenditure and in the facts and circumstances of that case it was held that the

expenditure incurred for payment of legal charges to solicitors on the issue of a prospectus for offering redeemable preference shares to the public

and payment of underwriting commission and brokerage for the issue of the same was capital expenditure and not revenue expenditure.

15. The Bombay High Court had also occasion to consider the question of onus in the case of Commissioner of Income Tax Vs. Ballarpur

Industries Ltd., . In this case also as the assessee could not discharge the onus that lay on him to prove that the item of expenditure in question was

not of a capital nature, the amount could not be allowed as a deduction.

16. In the case of COMMISSIONER OF Income Tax MADRAS Vs. MAHARAJAH OF PITHAPURAM., , Lawrence J. had considered the

distinction between capital and revenue expenditure. In this case, the legal expenses incurred by the assessee-company for defending its title to its

assets were held as revenue expenditure, for, the legal expenses did not create any asset at all, but were expenses incurred in the ordinary course

of maintaining the assets of the company. As to the payment, his Lordship opined that for the payment to be properly attributable to capital or to

revenue, the principle was that where a sum of money was laid out for the acquisition or the improving of a fixed capital asset it was attributable to

capital. But if no alteration is made in the fixed capital asset by the payment, then it was properly attributable to revenue being in substance a matter

of maintenance, the maintenance of the capital structure or the capital asset of the company. The Supreme Court cited this case of

COMMISSIONER OF Income Tax MADRAS Vs. MAHARAJAH OF PITHAPURAM., in the case of COMMISSIONER OF Income Tax,

BOMBAY Vs. FINLAY MILLS LIMITED., , with approval and, applying the principle of it, held that the fees payable in respect of registration

of trade mark were revenue in nature.

17. Before the authorities below on behalf of the assessee reliance was placed on the decision of the Supreme Court in the case of India Cements

Ltd. Vs. Commissioner of Income Tax, Madras, . In this case, the assessee obtained a loan of Rs. 40 lakhs from the Industrial Finance

Corporation secured by a charge on its fixed assets. In connection therewith, it spent a sum of Rs. 84,633 towards stamp duty, registration fees,

lawyers" fees, etc., and claimed this amount as business expenditure. It was held that the amount spent was not in the nature of capital expenditure

and was laid out or expended wholly and exclusively for the purpose of the assessee''s business and was, therefore, allowable as a deduction u/s

10(2)(xv) of the Indian I.T. Act, 1922.

18. It is further held that where there is no express prohibition, an outgoing, by means of which the assessee, procured the use of a thing, by which

he makes profit, is deductible from the receipts of the business to ascertain the taxable income. The loan obtained cannot be treated as an asset or

an advantage for the enduring benefit of the business of the assessee. Reference is also made to the decision of the Supreme Court in the case of

BOMBAY STEAM NAVIGATION CO. (1953) PRIVATE LTD. Vs. COMMISSIONER OF Income Tax, BOMBAY., . In this case,

pursuant to a scheme of amalgamation between two shipping companies, the assessee-company was incorporated on August 10, 1953, to take

over certain passenger and ferry services carried on by one of the former. On August 12, 1953, the assessee-company took over the assets,

which were finally valued at Rs. 81,55,000 and agreed that the price was to be satisfied partly by the allotment of Rs. 29,990 fully paid up shares

of Rs. 100 each and the balance was to be treated as a loan and secured by a promissory note and hypothecation of all immovable properties of

the assessee-company. The balance remaining unpaid from time to time was to carry simple interest at 6 per cent. By a supplemental agreement,

the original agreement was modified to the effect that the balance would be paid by the assessee-company until it was paid in full. The assessee-

company was to pay simple interest at 6 per cent, per annum on so much of the balance as remained due. The balance was also to be secured by

the hypothecation of all the movable properties of the assessee-company. During the relevant accounting years, the assessee paid interest as

balance outstanding and the question was whether the interest paid was allowable as a deduction u/s 10(2)(iii) or (xv) of the Indian I.T. Act, 1922,

in computing its profits. Their Lordships observed that in considering whether the expenditure was revenue expenditure, the court had to consider

the nature of the ordinary course of business and the objects for which the expenditure is incurred. The question whether a particular expenditure is

a revenue expenditure, incurred for the purpose of the business, must be reviewed in the larger context of business necessity or expediency. If the

outgoing or an expenditure is so related to the carrying on or conduct of the business that it may be regarded as an integral part of the profit earning

process and not for the acquisition of an asset or a right of a permanent character, the possession of which is a condition to the carrying on of the

business, the expenditure may be regarded as revenue expenditure.

19. Last of all, a reference may be made to the decision of the Kerala High Court in the case of Commissioner of Income Tax Vs. Commonwealth

Trust Ltd., , the facts of which were almost similar to the facts and circumstances of the present case. In this case, an expenditure for valuation of a

building and machinery of the assessee was found to be an allowable deduction as the expenditure incurred by the assessee towards valuation of its

properties was one wholly and exclusively for the purpose of its business. While agreeing with the findings of the Tribunal, their Lordships

observed that it was in accordance with sound commercial practice to see that the building and machinery of the assessee were kept and

maintained in a good state of efficiency for their work and functioning and valuation of these by the assessee, in the circumstances, must be

regarded as an expenditure incurred wholly and exclusively for the purpose of the business. There, the Tribunal''s order allowing that head of claim

for deduction was upheld.

20. On a consideration of the decisions discussed above, it appears that in order to find out the distinction between capital and revenue

expenditure, it is to be seen whether the expenditure would bring into existence an asset or advantage for the enduring benefit of a business. In the

present case, the assessee did not appear to have acquired any new capital asset at all. But, only the existing assets were valued afresh and in the

books of account the valuation was shown at higher figures for the purpose mainly to display the financial position of the assessee in a better way

so that it may facilitate the carrying on of the business more efficiently and smoothly.

21. In the above premises, we hold that the Tribunal was perfectly justified in holding the expenditure in question as revenue in nature and as such

deductible u/s 10(2)(xv) of the Indian I.T. Act, 1922, and, accordingly, we answer the question in the affirmative and in favour of the assessee.

22. There will, however, be no order as to costs.

Sabyasachi Mukharji, J.

23. I agree.