IN THE INCOME TAX APPELLATE TRIBUNAL
[DELHI BENCH "**D**" DELHI]

BEFORE SHRI K. D. RANJAN, AM & SHRI GEORGE MATHAN, JM

I. T. Appeal No. 1404 (Del) of 2007.

Assessment year : 2002–03.

M/s. L G Electronics India Pvt. Ltd.		Addl. Commissioner of Income-tax,
Plot No. 51, Udyog Vihar,	Vs.	R a n g e : 4,
Surajpur - Kasna Road,		N E W D E L H I.
Greater Noida [U. P.]		

P A N / G I R No. AAA CL 1745 Q.

(Appellant) (Respondent)

Assessee by : Shri S. Ganesh, Sr. Adv.;
Shri Sumit Chadha, C. A.; &
Shri Veenu Aggarwal, C. A.;

Department by : Ms. Kavita Bhatnagar [CIT] - D. R.;

O R D E R.

PER K. D. RANJAN, AM :

This appeal by the assessee for assessment year 2002-03 arises out of the order of the ld. Commissioner of Income Tax (Appeals)-VII, New Delhi.

2. The first issue for consideration relates to non-acceptance of the amount of Rs.28,28,53,871/- in nature of capital subsidy received towards Sales-tax exemption availed by the assessee in accordance with the U.P. Industrial Policy, 1998. The facts of the case stated in brief are that the assessee during the relevant previous year was engaged in the business of manufacturing, marketing and sales of electronic and electrical appliances of

consumer goods such as Colour TV, Refrigerators, Air-conditioners, Washing machines, Micro-wave ovens etc. During the financial year 2001-02 relevant to assessment year 2002-03 the total sales made by the assessee in Uttar Pradesh eligible for Sales-tax exemption was at Rs.2,42,43,75,336/- which included sales tax component of Rs.28,28,53,871/-. The assessee in the original return of income included the sales tax component in the total income, but subsequently based upon the judgement of ITAT, Mumbai Special Bench in ITA. No. 4045 (Bom.) of 1991 for assessment year 1986-87 claimed the sales tax component as capital receipt by filing revised return of income. The assessing officer treated the sales tax component as revenue receipt in the hands of the assessee relying on the decision of Bombay High Court in the case of Sudichha Chitra v CIT 189 ITR 774 (Bom.) wherein on similar facts subsidy was held to be revenue in nature. In this case Hon'ble Bombay High Court held that the subsidies were not granted for production of or bringing into existence any new asset. The subsidies were granted year after year only after setting up of the new industry and commencement of the production. Such a subsidy could only be treated as assistance given for the purpose of carrying on of the business of the assessee. The assessing officer also placed reliance on the decision of Hon'ble Calcutta High Court in the case of Kesho Ram Industries & Cotton Mills 191 ITR 518 (Cal.) and the decision of Hon'ble Supreme Court in the case of Sahni Steel & Press Works Ltd. & Others Vs. CIT 228 ITR 253 (SC). He was of the opinion that the sales tax subsidy was received by the assessee for carrying out business operations and not for setting up of the industry. The sales tax was incidental to the sales and, therefore, it was part of the trading receipts and could not be treated as capital receipt. The assessing officer distinguished the facts of the case from the case of ITAT, Mumbai Special Bench by observing that the facts of the case of the assessee were not similar with that of the case of Reliance Industries in view of the facts that the assessee had admitted that the company had uniform pricing policy called *'dealer price'* in the state of U.P. and other States, which was inclusive of Sales-tax. The assessee with an intention to get back investment as allowed by the U.P. Govt. sold the products in the State of U.P. on same dealer price as was for other States. Thus by selling the goods at same dealer price in the State of U.P. and other States, the assessee had received excess price in the State of U.P. as pay-back of investment as allowed by the U.P. Govt. in the form of Sales-tax, which was not required to pay back to the U.P. Govt. as compared to net price [dealers' price minus Sales tax paid to Govt.] received in other States. The assessee had collected Sales tax along with the price of

the goods and since liability to pay the sales tax so collected to the State Govt. seized to exist, such amount automatically assumed the character of income in the hands of the assessee. The assessing officer accordingly came to the conclusion that : (i) the sales tax exemption was given after the assessee had already set up its business and commenced production; (ii) the subsidy was given not to set up business, but to carry out existing and on-going business; (iii) the issue has been dealt with the Sahney Steel & Press Works' case (supra); (iv) the reliance placed by the assessee in the case of Special Bench in the case of Reliance Industries (supra) was not applicable in the case of the assessee as it had already collected sales tax, which was not supposed to have been collected. Once the amount had been collected and the liability to pay the same to the State Govt. did not exist, such receipts could only be treated as income in the hands of the assessee. The assessing officer accordingly treated the sales tax component of Rs.28,28,53,871/- as revenue receipts.

3. Before the ld. CIT (Appeals) it was submitted that Uttar Pradesh Govt., under Uttar Pradesh State Industrial Policy, 1989 had granted subsidy to new industries to encourage the setting up of new industrial units during a particular period in certain specified areas of U.P. which needed huge capital investment, in the form of sales tax exemption. Since the State Govt. could not give subsidy in cash, the assessee had been granted right to retain the sales tax payable to the State Govt. It was also submitted that the company had set up its manufacturing unit in Greater Noida, U.P. to avail the project set up subsidy / facility under the U.P. State Industrial Policy, 1998. The manufacturing unit was set up with initial investment of Rs.62,05,18,132/- upto 31st March, 1998 and further additional investment of Rs.60,13,83,450/- were made during financial years 1998-99 to 2000-01. It was also submitted that Additional Director of Industries, Greater Noida, in accordance with the provisions of industrial policy and section 4-A of U.P. Sales Tax Act, 1948 read with Notification No.640/641 dated 21/02/1997 issued certificate No.4027 dated 7/03/2003 enabling the Greater Noida unit of the company eligible to get back the investment made for setting up new unit by way of subsidy in the form of sales tax exemption. The total amount of exemption granted by the said certificate is Rs.2,03,73,53,192/- which is to be utilized within the period of 15 years commencing from 27/03/1998 to 26th March, 2013.

4. The company had uniformed pricing policy called *'dealer price'* which included sales tax. The assessee with an intention to get back investment as allowed by the U.P. Govt. sold the products in the State of U.P. on the same dealer price as applicable to other States. Thus the selling of goods at the same dealer price in the State of U.P. and other States, the company had received excess price in the State of U.P., as pay back of investment as allowed by the U.P. Govt. in the form of sales tax, which was not required to be paid back to the U.P. Govt. as compared to net price received in other States. It was also submitted that the sales tax incentive was the subsidy given to the company not for assisting it in carrying out the business operations, but the object of subsidy was to encourage of setting up of industries in the backward areas. The assessee placed reliance on several decisions for the proposition that assessee became eligible for sales tax refund only when it invested in its factory in the backward area and not otherwise and, therefore, it was inextricably linked with the setting up of the industry in the backward area. However the ld. CIT (Appeals) was of the view that subsidy was a capital receipt if the same was given for setting up of factory and was directly linked with the capital cost of the project. Contrary to that if subsidy had been given to assisting the carrying on the trade or business, the same was to be treated as revenue receipt. In the case of the assessee, the industrial policy formulated by the U.P. Govt. in 1998 came much after the setting up of its industry as it had commenced production of goods on 9/03/1998 and also sales were affected on 27/03/1998. Therefore, it could not be said that the investment in setting up of industry by the assessee before 9/03/1998 was only in view of the various incentives given by the U.P. Industrial Policy. He also observed that the industrial policy formulated by the U.P. Govt. included various incentives such as private participation, promotion of exports; wooing NRI investments, strengthening of traditional industries, review of tax structure, preservation of environment and cultural incentive and many others. Therefore, it could not be said that the industrial policy was formulated only in a view to encourage the capital investment in Noida area. He further noted that sales tax could have been collected only after commencement of business and the sales carried out by the assessee company. Therefore, the assistance given by the U.P. Govt. in the form of sales tax subsidy was subsequent to commencement of business and under these circumstances it had to be considered assistance for carrying out the business. As regards the investment of Rs.50 crores by the assessee, the ld. CIT (Appeals) noted that the same was one of the conditions for granting sales tax subsidy, which had nothing to do with the setting up of the industry.

Had the assessee made the investment of Rs.50 crores or more without effecting the production and sales of its goods, it would have not been entitled for sales tax subsidy. He, therefore, concluded that the subsidy was inextricably linked with the production and sales effected by the industry i.e. after commencement of the business. Therefore, as per the ratio laid down by various courts including Hon'ble Supreme Court of India in the case of Sahney Steel & Press Works Ltd. & Others Vs. CIT (supra) the sales tax subsidy was to be treated as revenue receipt. He accordingly rejected the ground raised by the assessee.

5. Before us it has been submitted that the liability to pay sales tax arises on making of a sale and the amount of sales tax is paid by dealer / manufacturer out of total amount recovered by the dealer / manufacturer from its customers. The effect of the grant of exemption from sales tax is that the amount which is otherwise payable out of total amount recovered by the dealer / manufacturer from its customer can instead be retained by him. This amount is known and is in fact precisely quantified. This amount is based on total amount of capital investment made by the assessee. The State Govt. has permitted the manufacturer / dealer to retain and which, but for exemption, would have to be parted with by the dealer / manufacturer. Further the object of exemption is very clear i.e. promotion of industrial development in the State of Utter Pradesh. This object is specifically set out in the U.P. State Industrial Policy, which specifically seeks to encourage the setting up of new industrial unit / expanded unit / modernise unit. The exemption is granted to such units which are established during a particular period in certain specified areas of U.P. Since the State of U.P. was not in a position to grant cash subsidy to the industries, it has instead adopted a system for method of permitting the manufacturer / dealer to retain entire amount collected from its customer without having to part with a portion thereof as and by way of sales tax, which would otherwise, but for exemption, have to be paid over to the State Govt. The benefit of exemption from sales tax is granted only to knew, substantially expanded / modernize units and not to other units nor generally to all units. This factor, apart from the provisions of the U.P. State Industrial Policy, also makes it abundantly clear that the object of grant of exemption was to promote capital investment in industries and thereby achieving industrial goal and development. Relying on the decision of Hon'ble Supreme Court in the case of Ponny Sugars, it has been submitted that the subsidy which is granted with object of

promoting capital investment and industrial growth is a capital receipt in the hands of recipient. Therefore, the decision of Hon'ble Supreme Court is squarely applicable to the facts of the assessee's case. Hence, the portion of sales proceeds which is permitted to be retained by reason of grant of sales tax exemption to the assessee is nothing, but capital receipt in its hands on the ground that this amount was permitted to be retained only for the purpose of promoting industrial growth and development. It has further been submitted that whether the amount of sales tax collected is a capital receipt or revenue receipt, the colour and character of the receipt has to be seen in the hands of the recipient. The assessee had received and retained the amount of sales tax collected only in respect of capital investment for promoting the industrial growth. Therefore, the same is in the nature of capital receipt. It has further been submitted that the assessee has a pricing policy under which it charges a uniform dealer price in the State of U.P. and in other States, which is inclusive of sales tax. In other States the benefit of sales tax exemption is not available, the assessee has to pay sales tax to the State Govt. and hence, it is only the balance amount which is revenue receipt in its hands. However, in the State of U.P. the amount of sales tax has been allowed to be retained by the dealer / manufacturer by grant of sales tax exemption in order to promote the industrial growth and capital investment. Therefore, the amount of sales tax collected as a part of dealers' price is capital receipt in the hands of the assessee.

6. The ld. AR of the assessee further submitted that if instead of granting sales tax exemption to the assessee, the sales tax authorities have instantly recovered sales tax from the assessee then have returned very same amount back to the assessee as sales tax subsidy, then under that situation there would have been no doubt whatsoever that the said subsidy was clearly a capital receipt in the hands of the assessee. The grant of exemption has the very same effect and consequence, financially and otherwise, at the end of the day, because the amount representing sales tax that would otherwise have been payable but for grant of exemption is permitted to be retained by the assessee. Therefore, the amount of sales tax collected as a part of dealers price is un-questionable a capital receipt in the hands of the assessee. The correct approach to be adopted is to consider this substance of the matter as a whole and not to go by the narrow technical legalistic consideration. Therefore, a broad approach of businessman has to be adopted in order to understand the real colour and

character of the receipt in the hands of the assessee. He placed reliance on the decision of Special Bench in the case of DCIT Vs. Reliance Industries Ltd. (2004) 88 I.T.D. 273 (SB). It has been submitted that in that case also exemption from sales tax was granted by State of Maharashtra to new / expanded / modernized industrial units established in specified backward areas. In that case also Reliance Industries Ltd. did not recover any amount of sales tax from its customers and its invoices were only for the sale price of its products. Indeed, as Reliance Industries Ltd. was exempted from paying sales tax it could lawfully recover any sales tax from its customers. Reliance Industries Ltd. computed amount of sales tax exemption and deducted it from its sales proceeds and claimed the same as a notional or deemed sales tax subsidy, which was capital receipt. The claim of Reliance Industries Ltd. was upheld by Special Bench of the ITAT. It has, therefore, been submitted that the decision of Special Bench is directly and squarely covers the present case and has to be followed by the assessee and applied in the present case as well. He further submitted that apart from the decision of Special Bench in the case of Reliance Industries Ltd. the decision of Delhi Bench of the Tribunal in the case of Bhushan Steels & Strips Ltd. 91 TTJ 108 (Del.) and the decision of Bombay Bench in the case of Zenith Power Ltd. (2009) TIOL 468 ITAT, Mumbai is also applicable.

7. He also submitted that the decision of Hon'ble Punjab & Haryana High Court in the case of Abhishek Industries Ltd. (2006) 286 ITR 1 (P & H) fully supports the case of the assessee. In that case sales tax exemption was treated by the High Court to be a case of sales tax subsidy. The only reason why the assessee's claim was rejected was that the assessee in that case had not placed any material on record to show that the object of grant of sales tax subsidy was for the promotion of industrial growth and development. However, in the case of the assessee there is ample material on record which fully establish that the object of grant of sales tax exemption/deemed sales tax subsidy was for the promotion of industrial growth and development and capital investment in the State of U.P. Therefore, the assessee's case is also supported by the decision of Hon'ble Punjab & Haryana High Court in the case of Abhishek Industries Ltd. (supra).

8. On the other hand, the ld. CIT-DR submitted that Uttar Pradesh Govt. under the U.P. State Industrial Policy, 1998 in order to encourage the setting up of new industrial units during a particular period in certain specified areas of Uttar Pradesh has granted sales tax exemption. The company had already set up a manufacturing unit in Greater Noida in earlier years. It had made now additional investment during the financial year 1998-99 to financial year 2000-01. The company had a uniform price called *"dealers price"* which it follows all over India. Even for Uttar Pradesh, the company continued to follow its *"dealers price"* . Thus by selling the goods on the same *"dealers price"* in U.P. and other States, the company has received excess price in the State of U.P. as pay back of investment as allowed by the U.P. Govt. in the form of sales tax, which it is not required to pay back to the U.P. Govt. as compared to net price [dealers' price minus sales tax paid to the Govt.] received in other States. Therefore, it has been pleaded that excess price collected on account of sales tax is a trading receipt in the hands of the assessee, which is chargeable to tax as such. As regards the assessee's contention that an identical issue was decided by the ITAT, Special Bench in the case of Reliance Industries Ltd. (supra), the ld. CIT - DR submitted that the decision in the case of Reliance Industries Ltd. is not applicable to the facts of the assessee's case. In that case the state Industrial Investment Corporation of Maharashtra (SICOM) which is the implementing agency for Maharashtra Sales Tax Act had permitted the assessee to adjust its price so as to include therein the sales tax element, which otherwise could be fastened on the assessee and recovered in the absence of exemption from payment of tax. Whereas in U.P. Sales Tax no such condition or specific treatment has been given for permitting the assessee to adjust its price. She further submitted that in U.P. Sales Tax the word used is "Sales Tax" and not "Notional Sales Tax". Therefore, these two conditions made the assessee's case distinguishable from Reliance Industries case decided by the Special Bench. She also submitted that the assessee had followed its own *"dealer's price"* policy, which was uniform all over India. It did not have separate policy for U.P. The assessee was already manufacturing in Greater Noida. It only expanded its manufacturing unit to avail subsidy. She placed reliance on the decision of Hon'ble Supreme Court in the case of Sahney Steel & Press Works (supra) for the proposition that if the payments in the nature of subsidy from public fund are made to assist the assessee in carrying on his trade or business, then they are trading receipts. The character of subsidy in the hands of recipient whether revenue or capital will have to be determined having regard to the purpose for which subsidy is given. She also

placed reliance on the decision of Hon'ble SC in the case of Ponny Sugar & Chemicals Ltd. (supra). She further placed reliance on the decision of Hon'ble Punjab & Haryana High Court in the case of Abhishek Industries Ltd. (supra) wherein it has been held that where subsidy was given for business after industry had been set up and commenced commercial production, the subsidy was in nature of the trading receipt. On the basis of above arguments it has been submitted that in this case also the assessee had collected sales tax as part of *"dealers price"* and, therefore, the same is chargeable to tax as revenue receipt.

9. We have heard both the parties and gone through the material available on record. In this case the assessee had collected sales tax as a part of dealers' price. At the year end the sales tax portion, which formed the part of dealers' price had been bifurcated and has been claimed as capital subsidy. We have also gone through the Notification No. 1179 dated 31.03.1995 issued by the State Government of Uttar Pradesh. The State Govt. has provided sales tax exemption with an objective to promote the development of certain industries which have been set up or undertaken modernisation, diversification, backward integration by way of fixed capital investment of Rs.50 crores or more. The exemption of from sales tax or benefit of reduced rate of tax is available to those units which have started production or have carried out expansion or modernisation or backward integration etc. between 1.12.1994 and 31.03.2000. Para 2 of the notification specifies that the exemption or reduction in the rate of sales tax including the additional tax would not be more than 5 per cent of sale of goods. In case where tax rate was more than 5 per cent including additional tax, the balance was to be paid by the unit. Para7 (2) of the notification provides for the exemption of sales tax to the extent of exemption or reduction in tax. Item (2) of the Schedule includes Greater Noida Industrial Development Area wherein exemption from sales tax to the extent of 200 per cent of capital investment has been provided. None of the clauses of the Notification authorises the assessee to collect the sales tax and retain the same with it. The exemption of sales tax was available from the date of first sale or the date within the period of six months from the date of production, whichever is earlier. The said notification also provided that the eligibility certificate to the assessee will be issued by the joint/additional director of concerned Development Authority and the same will be produced before the concerned assessing officer. The Addl. Director Industries, Greater Noida Industrial Development

Authority, vide letter No. 1344 dated 23/06/1999 issued eligibility certificate to the assessee. As per this certificate fixed capital investment is of Rs.51,57,95,446/-. The date of commencement of production is 9/03/1998 and the first sale was affected on 27th March, 1998. The assessee applied for exemption from trade tax [sales tax] vide application dated 10/09/1998. The exemption from trade tax [sales tax] was provided from 27th March, 1998 to 26th March, 2013 for a period of 15 years or till the time the exemption of sales tax was availed of to the extent of 200 per cent of fixed capital investment i.e. Rs.1,02,75,90,892/- whichever was earlier. This certificate also provided the items i.e. Colour TV, Washing machine and Air-conditioners on which exemption from sales tax was provided. Another certificate was issued on 27th September, 2000 vide letter No. 1519 in respect of printed circuit voice for CTV number 8,12,000 and Micro-wave Oven 1,00,000. In this certificate, the sales tax exemption in first three years has been provided to the extent of 100 per cent, next three years 75 per cent, next two years 50 per cent and next two years 25 per cent. In all exemption from sales tax was provided for 10 years.

10. Neither the certificates issued by Greater Noida Industrial Development Authority nor the Notification issued by the State Govt. authorises the assessee to collect sales tax from its customers. The assessee has been exempted from collecting the sales tax from customers on the sales made with effect from 27th March, 1998. In fact, the ld. counsel for the assessee made a statement at the bar, during the course of hearing, that neither the Notification has authorized the assessee to collect sales tax nor the assessee had collected the sales tax as such. The assessee had included the element of sales tax in the dealers' price as a sale price of the product. In the States other than Uttar Pradesh, the sales tax so collected as a part of dealers' price has been paid to respective State Governments, whereas in the case of the assessee, since the assessee was not liable to pay sales tax, as exemption has been provided to the extent of 200 per cent of fixed capital investment, the sales tax element which is embedded in the sale price have been retained by the assessee as excess sales consideration. At the year-end the assessee has allocated the sales tax element from dealer’s price and has claimed the same as capital subsidy. Therefore, the collection of dealers' price has been made in the ordinary course of trading activities. When the assessee is not permitted to collect the

sales tax under the notification issued by the State Govt. the collection of sales tax as a part of dealers' price is nothing but constitutes a trading receipt.

11. Our view that the sales tax collected by the assessee as a part of dealer's price would constitute trading receipt is supported by the decision of Hon'ble Supreme court in the case of Sinclair Murray and Co. P. Ltd. Vs. CIT (1974) 97 ITR 615 (SC). In this case during the accounting period relevant to the assessment year 1953-54, the assessee company, with its head office in Calcutta, sold jute in Orissa to certain mills for being used in Andhra Pradesh and charged sales tax under a separate head in the bill as "Sales tax : Buyer's account..... to be paid to the Orissa Government". The sales tax was not paid to the Orissa Government on the ground that the sales were inter-State sales. The Appellate Tribunal held that where a dealer collected sales tax under section 9-B(3) of the Orissa Sales Tax Act, 1947, as it then stood, the amount of the tax did not form part of the sale price and the dealer did not acquire any beneficial interest therein and that the sum of Rs.7,14,398/- collected by the appellant did not form part of its total income. On a reference, the High Court held that the sales tax collected was part of the trading receipt and was to be included in the appellant's total income since the money realised from the purchaser was employed by the appellant for the purpose of making profit and the appellant did not earmark the amount realised as sales tax and did not put it in a different account or deposit it with the Government in terms of section 9-B(3). On further appeal the Hon'ble Supreme Court held as under :-

Held, affirming the decision of the High Court,

(i) that, assuming that section 9-B(3) of the Orissa Sales Tax Act, 1947, was valid, the fact that the dealer was compelled to deposit the amount of sales tax in the State exchequer did not prevent the applicability of the principle laid down by the Supreme Court in Chowringhee Sales Bureau P. Ltd. Vs. CIT (1973) 87 ITR 542;

(ii) that the amount collected by the appellant as sales tax constituted its trading receipt and had to be included in its total income;

(iii) that if and when the appellant paid the amount collected to the State Government or refunded any part thereof to the purchaser, the appellant would be entitled to claim deduction of the sum so paid or refunded."

From the Notification issued by State Government, as discussed above, it is clear that exemption from Sales tax / trade tax or reduction in sales tax / trade tax has been provided to the industrial units, which have been set up or carried out expansion, modernisation or backward integration. The sales tax exemption is available from the date of first sale of eligible units. In the case of the assessee the production of expended unit started from 9th March, 1998 and the first sale was effected on 27th March, 1998. The assessee had made application for the purpose of exemption on 19/09/1998. It is a undisputed fact that none of the clause of the Notification issued under section 4-A of Trade Tax Act, 1948 had authorised the assessee to collect sales tax / trade tax. It is also a fact that the collection of sales tax / trade tax has been made after the eligible industrial unit started production. Nowhere in the Notification has it been stated that exemption from sales tax / trade tax was provided for the setting up of the eligible unit. Therefore, the exemption from sales tax was granted in the course of carrying out of the business of the assessee. Hence, the grant of exemption from sales tax cannot be treated for the purpose of setting up of the industry. In other words, the industry was to be first set up and after it went into production and made the first sale, the assessee became eligible for exemption of sales tax / trade tax. The eligibility certificate was to be produced before the sales tax authorities in order to enable the assessee to claim exemption from sales tax. Since the assessee has collected the sales tax as part of dealer's price, the sales tax element will be trading receipt in the hands of the assessee. Our view is supported by the decision of Hon'ble Allahabad High Court in the case of CIT Vs. K. M. Sugar Mills Ltd. 164 Taxman 562 (All.) as discussed below.

12.1 In the case of CIT Vs. K. M. Sugar Mills Ltd. (supra) the assessee had paid purchase tax of Rs.20,12,046/- against which it had received a subsidy of Rs.20,11,000/-. The claim of the assessee was that the amount received on account of subsidy was a capital receipt and not liable to tax. This was negative by the assessing officer. In appeal, the ld. CIT (Appeals) observed that the nature of subsidy received by the assessee was different from the subsidy

which was held to be a capital receipt by the Madhya Pradesh High Court in the case of CIT Vs. Dusadh Industries (1986) 162 ITR 784 because it was neither for encouragement of industries in the backward areas nor for setting up of industries. After referring to the relevant Notification and the fact that the purchase tax, when paid, was claimed as deduction, the ld. CIT (A) held that the refund of the same purchase tax received by the assessee as subsidy was taxable as a trading receipt. On further appeal the Tribunal upheld the findings of the ld. CIT (A) that the subsidy received by the assessee against the payment of purchase tax was a trading receipt in its hands and, therefore, liable to tax.

12.2 At the instance of the assessee the following question was referred to Their Lordships of Hon'ble Allahabad High Court for consideration:

> *" Whether on a true and correct interpretation of the scheme under which the subsidy was granted by the Govt. of Uttar Pradesh, read with the provisions of section 28 of the Income-tax Act, the Tribunal was legally correct in holding that the sum of Rs.20,11,000/- receivable from the State Govt. was taxable as revenue receipt? "*

Hon'ble Allahabad High Court held as under :-

> *" 15. So far as the question referred at the instance of the assessee is concerned, we find that under the Govt. order dated 24/08/1984 issued by the State Govt. providing aid was to be given to the extent of the purchase tax paid by the sugar mill on purchase of sugar cane in order to facilitate payment of cane price. It may be mentioned here that the cane price paid by the assessee is a revenue expenditure and, therefore, any amount provided as aid for making revenue expenditure, would partake the nature of revenue receipt."*

12.3 Similar view has been taken by Hon'ble Punjab & Haryana High Court in the case of CIT Vs. Abhishek Industries Ltd. (supra). The facts of this case were that the assessee

initially while filing the return of income treated the sales tax subsidy as a revenue receipt. Even though a revised return was filed by the assessee on 12/08/1994, still no claim was made for treating the sales tax subsidy as capital receipt as against the revenue receipt. However, it was only at the time of framing the assessment the assessee changed its stand where vide letter dated 29/2/1996, a plea was sought to be raised that the sales tax subsidy was inadvertently treated as revenue receipt. The claim of the assessee was that the sales tax subsidy was in the form of sales tax exemption granted by the State of Punjab under the 1991 Rules, as amended by Notification dated 29th September, 1992. The relevant Rule as was sought to be relied upon by the counsel for the assessee is extracted below:-

> *" 4. A (1) Notwithstanding anything contained in any provisions of these Ruyles and subject to provisions of sub rule (2),*
>
> *(i) Group of industries which are set up in A category area on or after the 1st day of October, 1992 and the goods produced by them shall be exempt from the payment of sales tax for a period of 10 years commencing from the date of production for the first time in the State of Punjab, subject to condition that total sales tax exemption shall not exceed 300 per cent of their fixed capital investment;*
>
> *(ii) Group of industries which are set up in B category area on or after the 1st day of October, 1992 shall be exempt from the payment of sales tax for a period of 7 years from the date of production for the first time in the State of Punjab, subject to the condition that the total sales tax exemption shall not exceed 150 per cent of their fixed capital investment. "*

12.4 Hon'ble Punjab & Haryana High Court after examining the contention of the assessee and also various decisions at page 25 observed as under :-

> *" ..... In the present case, all that is claimed and is put on record by the assessee is that the sales tax subsidy is being received by it from the State.*

It is not disputed that the same is being received on recurring basis after the unit came into production. There is no document or material placed on record by the assessee to substantiate its plea that subsidy of the kind under consideration was to enable it to acquire new plant and machinery or as an aid to set up the industry. Rather, it is quite evident that subsidy in the present case is in the form of an operational subsidy provided by the State after the industry had been set up and commenced commercial production. The subsidy is not in the form of a financial assistance granted to the assessee for setting up of the industry. The endeavour of the State was to provide the newly set up industries, a helping hand for specified period to enable them to be viable and competitive vis-a-vis the industries were already set up and were in production since long. The assessee has failed to establish on record that the kind of subsidy involved in the present case was in the form of a subsidy to enable it to carry out capital investment. In the absence thereof, it cannot possibly be presumed by the authorities that such a subsidy would be in the nature of capital subsidy. The onus to provide the same strongly lay on the assessee, which it had failed to discharge. "

12.5 Likewise in the case of Mudit Refrigeration P. Ltd. Vs. ACIT (2003) 84 I.T.D. 289 (All.) according to scheme notified by State Govt. the assessee company, a cinema owner was entitled to grants-in-aid or subsidy by way of adjustment of Entertainment Tax, which was treated as paid by way of adjustment and retained by the assessee. The assessee claimed it as a capital receipt, on plea that subsidy was paid to carry on trade and that its quantification on the basis of entertainment tax was only a measure to determine it and that it was not a fact that entertainment tax was not payable by the assessee to the Govt. The assessing officer treated it as revenue receipt. The question before the Bench was whether if grants in aid were given by way of assistance to the assessee in carrying on of his trade or business and for purpose of making cinema business more profitable in backward areas, and not to acquire any asset or against capital outlay it had to be treated as a trading receipt and the source of funds was quite immaterial. It was also held that grant in aid received by way of adjustment of Entertainment Tax, which was treated as paid by way of adjustment and

retained by the assessee could not be regarded anything, but a revenue receipt. If the facts of the case are examined in the light of decision of the ITAT, Allahabad Bench in Mudit Refrigeration P. Ltd. Vs. ACIT (supra) the collection of sales tax as part of dealer's price would be a trading receipt in the hands of the assessee even if it is assumed that the assessee was authorised to collect and retain with it the sales tax as part of dealer's price. Moreover, there is nothing on record to suggest that sales tax exemption was granted for acquiring of capital assets. Similar view has been taken in the case of U. P. State Handloom Corporation Vs. DCIT 42 I.T.D. 436 (All). In this case the assessee received subsidy amount from Govt. under a specified scheme called "Janta Cloth Scheme" in the capacity of trader and it was compensation for loss of profit or for loss on cost of production. It was held that subsidy received by trader under "Janta Cloth Scheme" to compensate trader for loss on cost of production was a revenue receipt.

13.1 In the case of Sahney Steel & Press Works Ltd. & Others (supra) a notification was issued by the Andhra Pradesh Government that certain facilities and incentives were to be given to all the new industrial undertakings, which commenced production on or after 1st January, 1969 with investment capital (excluding working capital) not exceeding Rs.5 crores. The incentives were to be allowed for a period of five years from the date of commencement of production. Concession was also available for subsequent expansion of 50 per cent and above of the existing capacity provided in each case, the expansion was located in a city or town or panchayat area other than that in which existing unit was located. The salient features of the scheme formulated by the Andhra Pradesh Govt. were that the incentives were not available unless and until the production had commenced; the availability of incentive would be limited to a period of five years from the date of commencement of production; the incentives were to be given by way of refund of sales tax and also by way of subsidy on power consumed for production to the extent stated in the notification; the exemptions were given from payment of water drawn from Govt. sources. The assessee-company, S, set up a factory at P which went into production in the year 1973. The assessee maintained its accounts according to the calendar year. It was, therefore, entitled to the benefits of the said Government order in the calendar year 1973, which meant the assessment year 1974-75. In the said accounting year, the assessee obtained refund totalling Rs.14,665.70 being refund of

sales tax on purchase of machines, purchase of raw materials and sale of finished goods. The Income-tax Officer, while making the assessment for the year 1974-75, included the said amount in the assessable income of the assessee which was confirmed on appeal by the Commissioner of Income-tax (Appeals). On further appeal, however, the Tribunal upheld the assessee's contention and held that the amount of Rs.14,665.70 refunded to the assessee in terms of the said Government order "did not represent refund of sales tax" but was a development subsidy in the nature of a capital receipt. The High Court held that the amount was assessable. On appeal to the Supreme Court by the assessee :

> *" Held, dismissing the appeal, that, under the notification in question the payments were made to assist the new industries at the commencement of business to carry on their business. The payments were nothing but supplementary trade receipts. It was true that the assessee could not use this money for distribution as dividend to its share-holders. But the assessee was free to use the money in its business entirely as it liked and was not obliged to spend the money for a particular purpose. The subsidies had not been granted for production of, or bringing into existence any new asset. The subsidies were granted year after year, only after the setting up of the new industry and commencement of production. Such a subsidy could only be treated as assistance given for the purpose of carrying on of the business of the assessee. The subsidies were of revenue nature and would have to be taxed accordingly."*

13.2 The principle laid down in the case of Sahney Steel and Press Works (supra) is that if the purpose of subsidy is to help the assessee to set up its business or complete a project, the moneys must be treated as having been received for capital purposes. But if moneys are given to the assessee for assessing him in carrying out the business operations and the moneys are given only after and conditional upon commencement of production, such subsidies must be treated as assistance for the purpose of the trade. The facts of the case before us are similar to the facts of Sahney Steel and Press Works (supra). The purpose of notification issued by Uttar Pradesh Government was to provide sales tax exemption to all new industrial undertakings or the industrial undertakings which have been expanded or

modernised or went in backward integration between 1/12/1994 to 31st March, 2000. The assessee had collected the amount of sales tax equal to exemption granted in the course of carrying out business. The assessee was not obliged to spend the sales tax collected for any particular purpose. The notification as stated above has neither authorised the assessee to collect the sales tax nor has the assessee collected sales tax as such. The sales tax element is embedded in dealer's price and has been collected as part of dealer's price. Even if it is assumed that the assessee was authorised to collect sales tax and retain with it, the same will be chargeable to tax as trading receipt in view of decision of Hon'ble Supreme Court in the case of Sahney Steel and Press Works (supra).

14. The contention of the assessee that the issue is covered in favour of the assessee by the decision of Special Bench of the Tribunal in the case of Reliance Industries (supra), in our view, is not correct in view of the decision of Hon'ble Punjab & Haryana High Court in the case of Abhishek Industries P. Ltd. (supra); the decision of jurisdictional High Court in the case of CIT Vs. K. M. Sugar Mills Ltd. (supra) and the decision of Sahney Steel and Press Works (supra). Moreover, the decision of Special Bench of the Tribunal was rendered before the decision in the case of Abhishek Industries P. Ltd. (supra). The assessee had not been able to produce any evidence that the assessee was authorised to collect sales tax as authorised by the State Government or collection of sales tax was required for investment in setting up of the industry or expansion of the industrial unit. Hence, in view of the decision of Punjab & Haryana High Court in the case of Abhishek Industries P. Ltd. (supra); and the decision of jurisdictional High Court K.M. Sugars as well as Hon'ble Supreme Court in the case of Sahney Steel and Press Works (supra) the sales collected by the assessee as dealers price and retained with it has to be taxed as revenue receipt.

15.1 The alternative contention of the assessee that if the State Govt. has permitted the assessee to collect sales tax and had refunded the same in the form of subsidy, the things would have been different and the refund of sales tax in the form of subsidy would have been capital receipt in the hands of the assessee, this, in our view, is not correct. We have already discussed that that even the refund of sales tax will be chargeable tax as the same was

collected in the course of carrying out the business by the assessee. Hence the alternate submission of assessee deserves to be rejected.

15.2 In view of the above discussion, in our considered opinion, the ld. CIT (Appeals) was justified in treating the sales tax collected by the assessee as trading receipt and hence no interference is called for.

16.1 The next issue for consideration relates to confirming the disallowance of Rs.24,82,307/- being the loss on account of exchange fluctuation on revenue items accounted for in the books of accounts on accrual basis. On a query raised by the assessing officer it was explained that loss on foreign exchange fluctuation occurred on account of settlement of bills for import of trading goods / raw material and also on account of conversion of liability of foreign outstanding bills at the exchange rate prevailing at the close of the year. The assessing officer, however, rejected the contention of the assessee on the ground that the additional liability cast upon the assessee on account of fluctuation in exchange rate was only a notional liability determined at the end of the financial year by the assessee. Under the accrual system of accounting the liability, which can be allowed are those which have either been paid during the year or which have been crystalised and became ascertain. There should exist a certainty that it will arise. The assessing officer also noted that the amounts were payable at some future date and there was no certainty as to when the liability would arise nor the time when the payment will be made. Therefore the liability was not quantifiable because the ultimate liability will depend when amount was actually paid and any provision due to exchange rate fluctuation at any intermediate date will be notional liability. The assessing officer after considering the matter in detail treated the liability on account of foreign exchange fluctuation as contingent in nature. On appeal the ld. CIT (Appeals) confirmed the stand taken by the assessing officer on the basis of a decision in preceding year.

16.2 Before us the ld. AR of the assessee submitted that foreign exchange fluctuation is on account of trading bills and hence loss on foreign exchange rate fluctuation is revenue in nature. He placed reliance on the decision of Hon'ble Delhi High Court in the case of CIT

Vs. Woodward Governor India Pvt. Ltd. 294 ITR 451. On the other hand, the ld. CIT-DR supported the order of the ld. CIT (Appeals).

17.1 We have heard both the parties. We find that this issue is squarely covered by the decision of Hon'ble Delhi High Court in the case of Woodward Governor (supra). We also find that an identical issue came up before the Tribunal in ITA. Nos. 198 and 199 (Del) of 2004 for assessment years 1998-99 and 2001-02, ITAT, Delhi Bench "E" wherein loss on foreign exchange fluctuation was allowed as revenue expenditure. Hon'ble Delhi High Court in the case of CIT Vs. Woodward Governor India Pvt. Ltd. has held that the liability arising out of contracts had already stood accrued the minute the contract was entered into and the mere postponement of the payment of such liability to a future date would not extinguish the same so as to render it notional or contingent. It was also held that any increase in such liability as a result of fluctuation in the value of foreign currency in relation to Indian currency thus was a fate-accompli and such increase in liability as per the exchange rate prevailing on the last date of the financial year was allowable as deduction being not notional or contingent. The decision of Hon'ble Delhi High Court has been upheld by Hon'ble Supreme Court in Civil Appeal No. 2206 of 2009 dated 8th April, 2009. Since the facts of the case are identical to the facts of the case for assessment years 1998-99 and 2001-02, respectfully following the precedent, we do not find any reason to interfere with the findings of the ld. CIT (Appeals) and this ground of appeal raised by the Revenue is dismissed.

17.2 The next issue for consideration relates to confirming the addition to total turnover of excise duty and sales tax for the purposes of computation of deduction under section 80-HHC of the Act. The facts of the case stated in brief are that the assessing officer for the purpose of computation of deduction under section 80-HHC of the Act included element of excise duty and sales tax in total turnover. This resulted in reduction in deduction under section 80-HHC of the Act. On appeal the ld. CIT (Appeals) upheld the stand taken by the assessing officer.

17.3 We have heard both the parties and gone through the material available on record. We find that this issue is now covered in favour of the assessee by the decision of Hon'ble Supreme Court in the case of CIT Vs. Lakshmi Machine Works 290 ITR 667 (SC) wherein Hon'ble Supreme Court has held as under :-

> *" Section 80-HHC of the Income-tax Act, 1961, is a beneficial section; it was intended to provide incentive to promote exports. The intention was to exempt profits relatable to exports. Just as commission received by the assessee is relatable to exports and yet it cannot form part of 'turnover' for the purposes of section 80-HHC of the Act, Excise Duty and Sales-tax also cannot form part of the turnover. Just as interest, commission etc., do not emanate from the 'turnover' so also excise duty and Sales-tax do not emanate from such turnover. Since the Excise Duty and Sales-tax did not involve any such turnover, such taxes had to be included. Commission, interest, rent, etc. do yield profits, but they do not partake of the character of turnover and, therefore, they are not includible in the 'total turnover'. If so, Excise Duty and Sales-tax also cannot form part of 'total turnover' under section 80-HHC (3)." Respectfully following the precedent, it is held that the interest, commission and bill discounting charges will not form part of the total turnover. Accordingly, we do not find any infirmity in the order passed by the ld. CIT (Appeals).*

17.4 Respectfully following the precedent, it is held that the excise duty and sales tax will not form part of total turnover for the purpose of deduction under section 880-HHC of the Act. We accordingly set aside the order of the ld. CIT (Appeals) and direct the assessing officer not to include excise duty and sales tax in total turnover.

18. In the result, the appeal filed by the assessee is partly allowed.

Order pronounced in the open court today on : **26th February, 2010.**

Sd/-	Sd/-
[GEORGE MATHAN]	**[K. D. RANJAN]**
JUDICIAL MEMBER	**ACCOUNTANT MEMBER**

Dated : 26th February, 2010.

MEHTA

" Copy of the order forwarded to : -

1. Appellant.
2. Respondent.
3. CIT,
4. CIT (Appeals),
5. DR, ITAT, NEW DELHI.

True Copy. By Order.

Assistant Registrar, ITAT. "