IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO.1743 OF 2016
WITH
INCOME TAX APPEAL NO.1744 OF 2016
WITH
INCOME TAX APPEAL NO.1834 OF 2016
IN
INCOME TAX APPEAL NO.15 OF 2017

The Pr. Commissioner of Income Tax, Central-2 .. Appellant.
v/s.
M/s. Welspun Steel Ltd., .. Respondent.

Mr. Ashok Kotangle with Mr. Prabhakar Ranshur , for the Appellant in all the Appeals.
Mr. F. V. Irani i/b. Mr. A. K. Jasani, for the Respondent in all the Appeals.

CORAM: AKIL KURESHI &
M.S.SANKLECHA, JJ.
DATE : 26th FEBRUARY, 2019.

P.C:-

Since these appeals involve similar questions and arise out of a common judgment of the Income Tax Appellate Tribunal (in short "the Tribunal") they have been heard together and would be disposed of finally by the common judgment. Facts may be noted from Income Tax Appeal No.1743 of 2016.

2 The Revenue is in Appeal against the Judgment of the Tribunal, raising following questions for our consideration:-

"(a) Whether on the facts and in the circumstances of the case and in law, the Tribunal was justified in directing the Assessing Officer to treat the incentives received in the form of Sales Tax and Central Excise benefit as capital receipt, ignoring the fact that the object of the subsidy scheme is to enable the assessee company to run the business more profitably by reducing the cost incurred through reimbursement in running the business, and therefore, such receipts are liable to be taxed as revenue receipts?

(b) Whether on the facts and in the circumstances of the case and in law, the Tribunal was justified in holding that subsidy cannot be considered as payment directly or indirectly to meet any portion of the actual cost ignoring the fact that if the assessee claims the same as capital receipt, the same shall be reduced from the cost of asset and depreciation claim should be on the net value/cost of the asset after reducing the amount of incentives in terms of Explanation 10 to Section 43(1) of the Act?

(c) Whether on the facts and in the circumstances of the case and in law, the Tribunal was justified in directing to follow the decision of this Court in case of HDFC Bank Ltd., reported in 366 ITR 505 holding that no disallowances u/s. 14A is warranted if the assessee has own surplus funds without appreciating that the department has not accepted the above cited decision of this Court and Department's SLP is pending?"

3 Respondent-Assessee is a Registered Company. The issues arise in return for the Assessment Year 2009-10. The first question raised by the Revenue arises out of the dispute between the Assessee and the Revenue with respect to the treatment that, the subsidy amounts received by the Respondent should be given. For setting up a new industry in Kutch District of the State of Gujarat, the Assessee was granted certain subsidies under the State Government as well as Central Government Schemes. As is well known, the State of Gujarat was hit by devastating earth-quake which took place on 26th January, 2001, the Kutch District being the worst hit. Post such calamity, to put development of Kutch District back on track, the State Government had introduced a Sales Tax

exemption/ deferment Scheme under which, at the option of the assesssee, for specified period, on new investment, there would either be exemption or deferment of sales tax. The preamble of the Schemes as noted by the Tribunal in the impugned judgment, read as under:-

> *" The economic activities in the district of Kutch came to a standstill on account of the devastating earthquake in the State on 26th January, 2001. New employment, opportunities could be created if new investment takes place. The Government is committed to attracting industries in the district to make the industrial and economic environment live. Government of India have announced excise duty exemption for new industries to promote large scale investment in the district, along with which the State Government has also decided to announce the scheme of sales tax incentives. Since the scheme is aimed at making the economic environment of Kutch district live, it has been decided to confine the same only to Kutch district."*

4 Somewhat similar incentives were offered by the Central Government under a Central Excise Exemption Scheme, under which, if a new industrial unit was set up in Kutch District, the excise duty would be waived for a specified period.

5 The Revenue argues that such incentives were in the nature of assessee's revenue receipts. The Assessee contends that, the receipts were capital in nature and so rightly held by the Tribunal.

6 Having heard the learned Counsel for the parties on this question, we notice that, the Government of Gujarat Sales Tax Incentive Scheme was envisaged to promote large scale investments in the Kutch District since on account of devastating earth-quake, development of the district had suffered. The Scheme envisaged that, the same was confined only with the Kutch District. Similar, being the purpose and philosophy of

the Government of India, while granting excise duty exemption, we may not separately take note of the back-ground thereof. In view of these facts, the question arises is - whether the Tribunal was justified in holding that Sales Tax and Excise duty exemption enjoyed by the assessee under the said subsidy scheme, was not taxable as revenue receipt. Such and similar issue has came up before different High Courts and Supreme Court on the numerous occasions. Reference to all those judgments would be un-necessary. However, the principle that has evolved is that, not the nomenclature of the subsidy or the fact that, the computation of the subsidy benefit is in terms of tax payable, would not be conclusive. What is to be examined in each case is the purpose for granting such subsidy. We may refer to the decision of the Supreme Court in case of ***CIT v/s. Chaphalkar Brothers*** reported in ***400 ITR 279***. It was a case arising out of judgment of this Court in which, the dispute between assessee and the Revenue was with respect to subsidy granted to the multiplex cinema operators in the form of entertainment tax waiver. The subsidy was granted in view of the fact that, industry was highly capital intensive. The Revenue argued that, the subsidy was revenue in nature. This Court after referring to several decisions of the Supreme Court including the case of ***Ponni Sugars and Chemicals Ltd.,*** reported in ***306 ITR 392*** and ***Sahney Steel and Press Works Ltd.,*** reported in ***228 ITR 253*** held that, subsidy had not been granted for construction but only after setting up of a new industry which was in the nature of assistance given for the purpose of carrying on business.

7 On further appeal by the Revenue, Supreme Court confirmed the decision of this Court. It was noted that, Maharashtra Government's subsidy was not in form of an exemption from payment of entertainment

duty to multiplex theater complex. The scheme was introduced to start new cinema houses in the State. The Supreme Court observed that, in such circumstance, the purpose tests for grant of subsidy should be applied. It was concluded as under:-

> *" Applying the aforesaid test contained in both Sahney Steel as well as Ponni Sugars, we are of the view that the object, as stated in the statement of objects and reasons, of the amendment ordinance was that since the average occupancy in cinema theatres has fallen considerably and hardly any new theatres have been started in the recent past, the concept of a complete family entertainment centre, more popularly known as multiplex theatre complex, has emerged. Those complexes offer various entertainment facilitate for the entire family as a whole. It was noticed that these complexes are highly capital intensive and their gestation period is quite long and therefore, they need Government support in the form of incentives qua entertainment duty. It was also added that Government with a view to commemorate the birth centenary of late Shri V. Shantaram decided to grant concession in entertainment duty to multiplex theatre complexes to promote construction of new cinema houses in the State. The aforesaid object is clear and unequivocal. The object of the grant of the subsidy was in order that persons come forward to construct multiplex theatre complexes, the idea being that exemption from entertainment duty for a period of three years and partial remission for a period of two years should go towards helping the industry to set up such highly capital intensive entertainment centres. This being the case, it is difficult to accept Mr. Narasimha's argument that it is only the immediate object and not the larger object which must be kept in mind in that the subsidy scheme kicks in only post construction, that is when cinema tickets are actually sold. We hasten to add that the object of the scheme is only one – there is no larger or immediate object. That the object is carried out in a particular manner is irrelevant, as has been held in both Ponni Sugars and Sahney Steel."*

8 In the present appeal also, as noted, the subsidy was granted

under schemes framed by the State and the Central Government, to be given to the assesses who set up new industry in Kutch District. The scheme was envisaged to encourage investment which would in turn, provide fresh employment opportunity in the district which had suffered due to devastating earthquake. The computation of subsidy may be on the basis of sales tax or excise duty. Nevertheless, the purpose test would ensure that, the subsidy was capital in nature.

9 The second question raised by the Revenue is consequent of the first question, in which, the Revenue argues that, if the subsidy is treated as a capital in nature, the same must bring down assessee's costs of acquisition of plant and machinery. The assessee's claim of depreciation to that extent must shrink. Assessee argues that, the Tribunal correctly held that, the subsidy had not been given in relation to acquisition of plant or machinery and that, therefore, same cannot be adjusted towards cost of acquisition.

10 It is undoubted that, the subsidy had no relation to the assessee's acquisition of plant or machinery. It was to be granted to an industry which had set up the new industrial unit in the District of Kutch. In such back-ground, question – arises whether such subsidy would be adjustable towards assessee's costs of acquisition of capital assets. We may notice that, a similar question was considered by Division Bench of Gujarat High Court in case of ***CIT v/s. Grace Paper Industries Pvt. Ltd.,*** reported in ***183 ITR 591***. The Court noted that, the subsidy was granted by the Government for development of industries in back-ward areas. It was not part of the actual cost of plant or machinery. The Court, therefore, held that it could not have been deducted towards costs of acquisition. The Court held as under:-

" We have carefully considered the provisions relating to the grant of cash subsidy under the schemes framed by the Central Government and the State Government. The Central Government as well as the State Government noticed that areas specified as backward areas and tribal areas were undeveloped or under-developed. Entrepreneurs were not willing to set up industries in such undeveloped or under-developed areas. The industries were concentrating only in urban areas. In other words, rapid urbanization was taking place. So far as the State of Gujarat is concerned, there was rapid industrial growth in cities like Baroda, Ahmedabad and Surat resulting in strain on municipal services. Urbanization created several problems such as pollution, growth of slums etc . It was also necessary to have balanced growth of industry in different regions. However, as pointed out above, entrepreneurs were reluctant to set up industries in backward areas. These areas were identified as backward because there was un-development or under-development of industries in these areas. It was, therefore, that the Government decided to give financial incentives to encourage and induce entrepreneurs to move to backward areas and establish industries there so that the region may develop and promote the welfare of the people living in that region. One of the incentives which the Government decided to grant was cash subsidy so that entrepreneurs could utilize such cash subsidy for any purpose connected with the establishment of industries in the backward areas. Once the decision to give cash subsidy was taken, the Government had to work out some method to determine the quantum of such subsidy. In other words, the question as to how the amount of cash subsidy should be determined had to be considered by the Government. The Government, in order to determine the amount of cash subsidy, decided to follow one of the recognized methods of working it out on the basis of the amount invested by an entrepreneurs in acquiring capital assets as cash subsidy. The scheme does not say as to in what manner the subsidy was granted is to be utilized. In other words, the entrepreneur to whom the subsidy was granted was free to utilize it in any manner he liked. It would, therefore, appear that quantification of subsidy on the basis of investment was a measure adopted by the Government for convenience to work out the subsidy. If subsidy could be utilized by the entrepreneur in any manner he liked, could it be said that it was

granted for meeting the cost of the capital assets? In our opinion, taking an overall view of the various provisions of the scheme, it is difficult to hold that cash subsidy was granted to entrepreneur to meet the cost of the fixed assets or part thereof. The cost of the fixed assets was merely adopted as a measure for working out subsidy. In fact, a careful examination of the scheme reveals that it is the value of the fixed assets and not its cost which is adopted as the basis for computing the amount of the subsidy. Emphasis on value and not the cost is evident from the fact that land and building already owned by an industrial unit, cost of tools, jigs, dies and moulds, transport charges, insurance premium, erection cost, value of second-hand machinery purchased by an industrial unit etc. were to be taken into account while computing the value of fixed assets for the purposes of subsidy. In other words, it was the value of the fixed assets which formed the basis for computation of subsidy to be granted under the scheme. Subsidy, in our opinion, did not meet the cost of the fixed assets directly or indirectly. Under the scheme of the Central Government or the scheme of the State Government, cash subsidy was quantified by determining the same at a specified percentage of the value/ cost of the fixed assets. Therefore, as observed above, the basis adopted for determining the cash subsidy with reference to the cost or value of fixed assets was only a measure for quantifying the subsidy and it could not be said that the subsidy was given for the specific purpose of meeting any portion of the cost of the fixed assets. The subsidy was granted to compensate the entrepreneur for the hardship and inconvenience which he might encounter while setting up industries in backward areas."

11 Similar issue came up for consideration again before the Gujarat High Court in ***CIT v/s. Swastik Sanitary Works Ltd.,*** reported in ***286 ITR 544.*** It was a case in which, the Government subsidy was intended as an incentive to encourage entrepreneurs to move to backward areas and establish industries. In such a case, specified percentage of the fixed capital cost, which was the basis for determining the subsidy, would be granted. The Court held that, such basis for determining the subsidy

was only a measure adopted under the scheme to quantify the financial aid and it was not a payment, directly or indirectly to meet any portion of the actual cost of acquisition of capital asset. It was held and observed as under:-

> *" In so far as question No.2 is concerned, this court finds that the same is squarely covered by the decision of the Supreme Court in CIT v. P. J. Chemicals Ltd., [1994] 210 ITR 830. In the said case, after review of the law on the point, the Supreme Court has held as under (headnote):*
>
> *" Where Government subsidy is intended as an incentive to encourage entrepreneurs to move to backward areas and establish industries, the specified percentage of the fixed capital cost, which is the basis for determining the subsidy, being only a measure adopted under the scheme to quantify the financial aid, is not a payment, directly or indirectly, to meet any portion of the 'actual cost'. The expression 'actual cost' in section 43(1) of the Income Tax Act,1961, needs to be interpreted liberally. Such a subsidy does not partake of the incidents which attract the conditions for its deductibility from 'actual cost'. The amount of subsidy is not to be deducted from the 'actual cost' under section 43(1) for the purpose of calculation of depreciation etc."*

No question of law, therefore, arises in this respect.

12 Question No.3 – itself records that the issue at hand is covered by the decision of this Court in case of ***HDFC v/s. DCIT*** reported in ***366 ITR 505*** but that, the department has not accepted the decision of the High Court. In that view, this question also is not required to be entertained.

13 In the result, all the **Appeals** are **dismissed.**

(M.S.SANKLECHA,J.) **(AKIL KURESHI,J.)**

S.R.JOSHI