

**IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI "E" BENCH, - SPECIAL BENCH**

**BEFORE HON'BLE SHRI. R.V. EASWAR (PRESIDENT)
AND
SHRI D.K. AGARWAL (J.M.) AND SHRI. T.R. SOOD (A.M.)**

**I.T.A. No.2944/MUM/2007
Assessment Year : 2003-2004**

Sulzer India Ltd. Sulzer House Baner Road, Aundh Pune – 411 007. PAN : AAACS 7876 U	Vs.	Jt.CIT – Range 8(3), R.No.204, 2 nd Flr., Aayakar Bhavan, M.K. Marg, Mumbai – 400 020.
(Appellant)		(Respondent)

**I.T.A. No.2871/MUM/2007
Assessment Year : 2003-2004**

ACIT – Range 8(3), R.No.204, 2 nd Flr., Aayakar Bhavan, M.K. Marg, Mumbai – 400 020.	Vs.	Sulzer India Ltd. Karmyog Bldg., Parsi Panchayat Rd., Andheri (E), Mumbai – 400 059. PAN : AAACS 7876 U
(Appellant)		(Respondent)

Assessee by: S/Shri. S.E. Dastur, Yogesh Thar and
Ronak G. Doshi
Department by : Shri. Hemant Lal (CIT DR)

INTERVENER

ITA No.	Name of Assessee	Name of the Counsel for Intervener
1317/PN/2007 Assessment Year : 2004-05	Akzo Nobel Chemicals (India) Limited 501,502, 5 th Floor San Mahu Complex 5, Bund Garden Road Opposite Poona Club Pune-411 001. PAN : AADCA 3941 N	Shri Yogesh Thar

ORDER**PER D.K. AGARWAL, J.M.**

The Hon'ble President, vide his order dated 23.11.2009 has constituted the Special Bench under section 255(3) of the Income tax Act, 1961(the Act) to hear and decide the following question in accordance with law:

"Whether in the facts and circumstances of the case, the remission of deferred sales tax liability is chargeable to tax as business income of the assessee u/s.41(1) being remission of trading liability or the same is exempt from tax as capital receipt being remission of loan liability."

2. At the time of hearing the Id Sr. Counsel for the assessee Shri S.E. Dastur, at the outset, submits that this Special Bench was constituted as there were diversion of views of the Co-ordinate Benches of the Tribunal on the above issue. In the case of Dy.CIT vs. Sterlite Optical Technologies Ltd. and vice-versa in ITA No.7136 & 7177/M/04 for Assessment Year 2001-02 order dated 08.01.2008 the Tribunal has treated the difference between the deferred Sales Tax and its present value as capital receipt, not chargeable to tax, whereas in the case of Schenectady Specialities Asia (P.) Ltd. vs. ACIT (2009) 29 SOT 1 (Mum) relied on by the Id DR wherein it has been held that the same is chargeable to tax u/s.41(1) of the Act. He further submits that on an appeal filed by SI Group India Ltd formerly known as Schenectady Specialities Asia (P.) Ltd., recently, the Hon'ble Jurisdictional High Court in SI Group India Ltd. vs. ACIT (2010) 192 Taxman 91(Bom); on the question of law "Whether on the facts and in the circumstances of the case and in law, the Tribunal was right in completely disregarding the contention of the Appellant that there was no remission or cessation of the sale-tax liability on account of payment of the present value thereof being made to SICOM since the sales tax authorities had not given credit of the said payment against the sales tax

liability”, has held that one of the requirements spelt out for the applicability of sec.41(1)(a) has not been fulfilled in the facts of the present case, therefore, Their Lordships answered the question of law in favour of the assessee. He further submits that since there is no dispute that the facts of the assessee's case and the facts of the SI Group India Ltd.(supra), and also Sterlite Optical Technologies Ltd. (supra), are the same and the Hon'ble Jurisdictional High Court while reversing order of the Tribunal in SI Group India Ltd. (supra) has decided the issue in favour of the assessee, therefore, there is no diversion of views of the Tribunal and, therefore, the basis for referring matter to the Special Bench on the issue need not now be considered and, hence, the reference of the same issue to the Special Bench is no longer necessary. He further submits that in case the said plea is not accepted then it is suggested that the question should be redrafted to read as follows:-

“Whether on the facts and in the circumstances of the case and in law the sum of Rs.4,14,87,985/- has rightly been charged to tax under section 41(1) of the Income tax Act, 1961.”

3. On the other hand, the Id. CIT (DR) Shri Hemant J. Lal while objecting to the plea of the Id Sr. Counsel for the assessee submits that the Hon'ble Jurisdictional High Court while deciding the issue on different ground in favour of the assessee has kept the issue open to be adjudicated upon at the appropriate stage in appropriate proceeding, therefore the issue referred to the Special Bench has not been resolved by the Hon'ble Jurisdictional High Court and therefore the question referred to Special Bench which is borne out from the records, may be decided without any change, accordingly.

4. We have carefully considered the submissions of the rival parties and perused the material available on record. After considering the judgment of the Hon'ble Jurisdictional High Court in SI Group India Ltd.

(supra), we find merit in the plea of the Id DR. Their Lordships in the case of SI Group India Ltd.(supra) have observed vide placitum-11 appearing at pg.122 of 326 ITR as under:

“In the view that we have taken it is not necessary for the court to address itself to the wider issue as to whether the assessee, in paying the net present value of the deferred sale tax liability should be regarded as having obtained any benefit within the meaning of clause(a) of the sub-section (1) of section 41. The aforesaid issue is kept open to be adjudicated upon at the appropriate stage in appropriate proceedings.”

Since the issue raised for the Special Bench has not been decided and kept open by Their Lordships to be adjudicated upon at the appropriate stage in appropriate proceedings, we do not find any merit in the plea of the Id Sr. Counsel for the assessee that there is no requirement to constitute the Special Bench on the question referred and accordingly we reject the said objection raised by the Id. Sr. Counsel for the assessee. However, at the same time we find force in the submissions of the Id. Sr. Counsel for the assessee that the question needs to be re-drafted because the present question before the Special Bench starts with the presumption that it is a case of remission. In fact the Id. Sr. Counsel stressed that most of his arguments will be on the facts of the case that no remission at all is involved and consequently is there no benefit as envisaged by sec.41(1)(a) of the Act.

5. After considering the facts and circumstances of the case, we are of the view that instead of original question, the following question should be considered by the Special Bench:

“Whether on the facts and in the circumstances of the case and in law, the sum of Rs.4,14,87,985/- being the difference between the payment of net present value of Rs.3,37,13,393/- against the future liability of Rs.7,52,,01,378/- has rightly been charged to tax under section 41(1) of the Income tax Act, 1961.”

6. Briefly stated facts of the case are that the assessee company is engaged in the business of Equipment manufacturing and total project supplier. The assessee company has an industrial unit at Kondhapuri, Tal. Shirur, Dist. Pune which at the relevant time was a notified backward area, classified under group 'D' comprising the least developed area of the state of Maharashtra, not covered under group 'A', group 'B' or group 'C' under the modified package scheme of incentives (hereinafter referred to as "the 1983 Scheme"). In order to achieve dispersal of industries outside the Bombay-Thane-Pune belt and to attract them to the under developed and developing areas of the State, the Government of Maharashtra issued a modified package scheme of incentive "the 1983 Scheme" by which a scheme for the deferral of sales-tax dues was announced. The assessee company had opted "sales-tax deferral schemes of 1983 and 1988" of Government of Maharashtra. According to 1983 Scheme the sales-tax was to be deferred and payable after 12 years in six equal instalments, vide Resolution No. IDL-1082/(4096)-IND-8, dated 04.05.1983, wherein it was interalia stated:

(B) DEFERRAL

"An eligible unit not covered under the provision of para 5.3 will be entitled to sales tax incentive by way of Deferral as follows:-

Subject to the provisions of the Bombay Sales Tax Act, 1959/Bombay Sales Tax Rules, 1959/Central Sales Tax Act, 1956/Central Sales Tax (Registration and Turnover) Rules, 1957/The Central Sales Tax (Bombay) Rules, 1957 and the conditions/stipulations in the Certificate of Entitlement issued by the Commissioner of Sales Tax, the payment of the sales tax liability as per returns to be furnished for any period

covered by the Eligibility Certificate or as finally assessed thereunder will be deferred. The sales tax liability as per the returns so deferred shall be paid by the unit after twelve years/ in one lumpsum or in instalments, subject to such conditions as may be prescribed pursuant to the provisions of the Bombay Sales tax Act, 1959, the Bombay Sales Tax Rules, 1959. The Central Sales Tax Act, 1956, the Central Sales Tax (Bombay) Rules 1957, and Central Sales Tax (Registration and Turnover) Rules, 1957, as amended from time to time."

Assessee opted for the said deferral scheme. Government of Maharashtra again brought a scheme vide Resolution No. IDL-1088/(6603)-IND-8, dated 30.09.1988. According to this scheme, the benefit was available even on expansion or diversification of the existing unit. Assessee accordingly again opted for deferral scheme in respect of its expansion. In 2002, Government of Maharashtra brought Trade Circular No.PSI-2002/91/Adm-13/B-1041/Circular No.39T of 2002, dated 12.12.2002. The subject of this Trade Circular reads as follows:

"Sub:Premature Repayment of the amount of deferred taxes by the Eligible Units at Net Present Value (NPV)"

Trade Circular has mentioned sub-section (4) of section 38 of B.S.T. Act, 1959 which was amended as follows:

"Provided also that, notwithstanding anything to the contrary contained in the Act or in the rules or in any of the Package Scheme of Incentives or in the Power Generation Promotion Policy, 1998, the Eligible Unit to whom an Entitlement Certificate has been granted for availing of the incentives by way of deferment of sales tax, purchase tax, additional tax, turnover tax or surcharge, as the case may be, may, in respect of any of the periods during which the said certificate is valid, at its option, prematurely pay in place of the amount of tax deferred by it an amount, equal to the net present value of the deferred tax as may be prescribed, and on making such payments, in the public interest, the deferred tax shall be deemed to have been paid."

It was further stated in the said Circular that:

"5. It is, however, clarified that the amount of taxes paid at NPV is subject to determination by the Assessing, Appellate or as the case may be the Revising Authority at the appropriate stages. It is further clarified that even if the issue of determination of the amount of deferred tax is in dispute and pending before the Appellate Authority, the deferral unit desirous of prepaying any part of the amount of deferred taxes at NPV will be free to avail this facility. Such payment at NPV will amount to discharge of the corresponding amount of the deferred taxes."

7. The assessee company collected sales-tax during the period 1.11.1989 to 31.10.1996, (7 years) under 1983 Scheme Rs. 3,29,93,863/- and under 1988 Scheme Rs. 4,22,07,515/- aggregating to Rs. 7,52,01,378/-. Under the 1983 Scheme the amount was payable after twelve years in six equal annual instalments commencing from 1.5.2003 and the aggregate liability of Rs. 7,52,01,378/- was treated as an unsecured loan in the books of account of the assessee. The State Industrial and Investment Corporation of Maharashtra Ltd. (SICOM) being the Implementing Agency under 1979/1983/1988 Scheme offered to the assessee an option for the settlement of the deferred sales-tax liability by an immediate one-time payment at Net Present Value (NPV). The assessee paid an amount of Rs. 3,37,13,393/- (Rs. 1,76,02,272/- of 1983 Scheme + Rs. 1,61,11,121/- of 1988 Scheme) to SICOM which according to the assessee represented the NPV as determined by SICOM. Payment was made by the assessee to SICOM on 30.12.2002. The difference between the deferred sales-tax and its present value amounting to Rs. 4,14,87,795/- was treated as capital receipt and was credited in the books of account of the assessee to the capital reserve account.

8. Before the Assessing Officer the assessee while relying on CBDT Circulars No.496 dated 25.09.1987 and 674 dated 29.12.1993, submitted that deferral sales-tax under the Deferral Scheme is required to be treated as actually paid so that statutory liability will be taken to have

been discharged for the purpose of sec.43B. It was further submitted that as per Board Circular conversion of sales-tax liability into loan shall be taken to be the discharge of liability for sales-tax. It was further submitted that though the sales tax collected from customers was a trading receipt, the same is taken to have been paid to the Government under the deferral scheme. After such deemed payment, the unpaid sales tax is by way of deferral loan and not a trading receipt and hence the remission of loan cannot be taxed as income of the assessee. However, the Assessing Officer observed that the Circular relied on by the assessee has been followed in the earlier years in the assessee's case by not making any disallowance u/s.43B of the Act in respect of the deferred sales-tax on the ground that under the scheme, the sales tax liability is deemed to have been paid. The Assessing Officer further observed that, at present the real question for consideration is whether the remission of deferred sales tax results into taxable income or otherwise. Therefore, the Board Circular referred by the assessee is confined to the treatment u/s.43B and hence, not at all relevant. He further observed that, the scheme provides for three categories of incentives. The First Category is sales tax exemption which is not applicable to the facts of the present case. The Second Category is where the sales tax liability is deferred and is allowed to be paid beyond the due dates specified under the sales tax laws. The Third Category is where the sales tax payable is treated as loan at the time of collection of sales tax on sales or, the deferred sales tax liability is permitted to be converted, mid-stream, into a loan liability. The Assessing Officer further observed that, the assessee has not furnished any document or order in terms of which sales tax liability treated as loan or is converted into a loan at any subsequent stage. On the contrary, evidence on record demonstrates that the assessee has opted for the Second Category of incentive viz., mere deferment of sales tax liability. Therefore, the assessee's contention that the amount remitted is a part of loan liability is not borne out from the evidence filed

by the assessee. According to the Assessing Officer the sales tax liability has been allowed as a deduction u/s.43B of the Act from the business income of the assessee in the earlier years, therefore, as per provision of sec.41(1) if a trading liability is deducted from the business income and the same is remitted wholly or partly, the remission of sales tax liability is to be added to the income of the assessee as business income and accordingly the Assessing Officer brought to tax the aforesaid difference of Rs. 4,14,87,985/- u/s.41(1) of the Act.

9. On appeal before the Id. CIT(A), it was inter-alia contended that the appellant has paid the present value of his future liability which both have equivalent value, therefore, there is neither any gain nor any loss to either of the party included in the transaction. Therefore, the question of treating the difference as income in the present case does not arise. The reliance was also placed on various decisions for the proposition that the notional income should not be subject to tax and provisions creating a deeming fiction are to be construed strictly. Relying on the ratio of the decisions as referred in the order of the Id. CIT(A) at pages 11 to 13 and CBDT Circular as referred above it was, therefore, submitted that nothing has been accrued to the assessee and therefore question of adding anything to its income does not arise and, hence, the provisions of sec.41(1) are not applicable.

10. The Id CIT(A) after considering the assessee's submission in the light of the 1983 and 1988 schemes and also the CBDT Circulars and the ratio of decisions relied on by the assessee observed that the combined reading of documents, proves beyond a shadow of doubt that appellant had collected sales tax which was not paid earlier, which remained as deferred sales tax liability, it was never converted into a loan and even if it is presumed that deferred sales tax liability was converted into loan, the amount was paid at Net Present Value of the deferred sales liability

resulting into remission within the ambit of revenue/ trading receipt/ expenditure and would attract provisions of sec.41(1) of the Act. He further observed that in the present case the NPV means that Rs. 3,37,13,393/- is same as Rs. 7.52 crores after 12 years so far as sales tax Department is concerned, then why the appellant has taken the amount of Rs.4,14,87,985/- to reserve. The Id CIT(A) while distinguishing the decisions relied on by the assessee, upheld the addition made by the Assessing Officer.

11. At the time of hearing the Id. Sr. Counsel for the assessee after referring to the facts of the case in the light of the salient features of 1983 Scheme and 1988 Scheme appearing at page 102 to 116 and 117 to 150, 153, 151 and 101 of the assessee's paper book further submits that as per the 1983 Scheme, the assessee's Shirur unit was entitled to defer the payment of sales-tax collected during the period 1.11.89 to 31.10.96 (7 years) upto the maximum of Rs.666.94 lacs being 85% of the Fixed Capital Investment of Rs.784.64 lacs. He further submits that the incentives under the 1988 scheme are similar to the 1983 scheme and hence not repeated for sake of brevity. The amount of tax actually deferred under the 1983-1988 scheme was Rs.4,22,07,515 -(Pg.101). The aggregate deferral under the 1983 and 1988 scheme was Rs.7,52,01,378. [Rs.3,29,93,863 + Rs. 4,22,07,515]. The aggregate prepayment was Rs.1,76,02,272 + Rs.1,61,11,121 = Rs.3,37,13,393.

12. He further submits that in the present case, section 41(1) has been invoked on the alleged ground that the assessee has obtained some benefit in respect of a trading liability by way of remission or cessation thereof. According to Id. Sr. Counsel for the assessee Section 41(1) does not apply in the present case because (1) the Appellant has not obtained any benefit (2) there has not been any remission of a liability (3) the benefit if any obtained by the Appellant is not in respect of a trading

liability (4) the benefit if any obtained by the Appellant is on capital account.

13. He further submits that in Board Circular No.496 dated 25th September, 1987, it was stated that if the State Governments make an amendment in the Sales-tax Act to the effect that the sales-tax deferred under the scheme shall be treated as actually paid, such a deeming provision will meet the requirement of s.43B. By the 1987 amendment, by the insertion of the 3rd proviso to section 38(4) of the Bombay Sales tax Act, 1959, the Maharashtra Government made such an amendment, SICOM an implementing agency was authorised to convert the deferred sales tax into a loan. In 1995, a fourth proviso was inserted entitling an assessee to prepay such loan. Thereafter, as per the 2002 amendment, 4th proviso to sec.38(4) (By which the earlier 4th proviso was substituted) provided that where the net present value of the deferred tax was paid, the deferred tax would be deemed, in the public interest, to have been paid. Detailed procedure for such prepayment was prescribed vide Circular dated 12th December, 2002 (Pg. 174-186). The assessee made the prepayment on 30th December, 2002 (Pg.188-189 and 207-208). He further submits that the fourth proviso to section 38(4) of the Bombay Sales-tax Act provides that the Eligible Unit to whom an Entitlement Certificate has been granted for availing the deferment incentives may prematurely pay in place of the amount of tax deferred by it an amount equal to the net present value of the deferred tax and on making such payment, the deferred tax shall be deemed to have been paid. Pursuant to the said fourth proviso, Trade Circular dated 12.12.2002 (Pg.174) laid down the procedure of prepayment of the amount of deferred sales-tax (para 3.1) as per the rates of discounting mentioned in the annexure (Page 178-179). Circular No.20T of 1995 clarifies that the prepayment provision is in the interest of the Revenue. The Appellant opted for the prepayment as per the fourth proviso. The summary of the prepayments

is at Pg.101 and the actual prepayment certificates are at Pg.188-189 and 207-208. Accordingly, the liability of Rs.7,52,01,378, which was payable after 12 years in six equal instalments, was fully discharged by payment of Rs.3,37,13,393 being the present value thereof. Sec.41(1) is attracted where a liability for payment of Rs.X which is presently payable is settled for Rs.X-Y. as per the table prescribed by the State Government itself the amount of liability presently due was Rs.3,37,13,393 and this sum was fully paid. The present is not a case where a liability presently payable is settled for a lesser amount. When a future liability is discharged in full by payment of its net present value, no benefit can be said to have been obtained. The difference of Rs.4,14,87,985 cannot be regarded as a benefit obtained by the Appellant. Reference was invited to the table prescribed by the Government to determine NPV (Pages 178-179) and the prepayment amounts computed by the sales-tax authority (pages 188-189 and 207-208) which shows that the net present value has been determined by the Sales-tax Department itself as per the rules prescribed by the Government. Moreover, the 4th proviso to section 38(4) provides that on payment of the net present value, the deferred tax shall be deemed to have been paid. Thus, it is specifically mentioned that the deferred tax is fully paid and not waived or remitted. Therefore, there is no question of any benefit arising to the Appellant. 'Benefit' is to be understood commercially and not by mathematical difference. The benefit if at all arose when the sales-tax deferment was availed of. The pre-payment is a mere consequence or working out. If a payment as per the terms of the deferral scheme does not result in a benefit the same payment earlier made cannot be treated as benefit obtained. Again whether there is a benefit has to be determined by applying a uniform principle and not depending on the facts of a case or a particular situation. Every debtor would have his own concept and point of view on whether to prepay depending on his present value for money, his view of the future, his use for money, etc. He further submits that when the full

present value of a liability is paid there is no remission. Since there is no benefit, the question whether the liability is a trading liability or a loan becomes irrelevant and hence the prepayment benefit if at all is in the capital field.

14. He further submits that in Dy. CIT vs. Reliance Industries Ltd.(2004) 88 ITD 273, the Special Bench of the Mumbai Tribunal took the view that an incentive received under the 1979 Package Scheme of Incentive is a capital receipt. The purpose and object and terms of the 1979 Scheme is so far as are relevant are the same as under the 1983/1988 Schemes. The form is not relevant but only that it is an incentive for dispersal of industries and setting up of industries in the less developed parts of the State. According to him similarities between the 1979 Scheme (with which Reliance was concerned) and 1983/1988 schemes (with which the present case is concerned.) are as under :-

	1979 Scheme	1983 Shceme	1988 Scheme
Object	Para 22, Pg.298 (19 th line from top) of the Reliance Report "Under the Maharashtra Scheme, the aim was to disperse the industries outside the Bombay-Thane-Pune belt"	Pg.102 of the PB(Preamable): "in order to achieve dispersal of industries outside the Bombay-Thane-Pune belt and to attract them to the underdeveloped and developing areas of the State,"	Page 119 of the PB(Preamable): "in order to achieve dispersal of industries outside the Bombay-Thane-Pune belt and to attract them to the underdeveloped and developing areas of the State,"
Calculation of incentive	Para 22, page 298 (9 th line from bottom): "Further, the incentives under the Maharashtra	Pg.108 of the PB Table: Group D 85% of the Fixed Capital Investment – 7 yrs or earlier if	Pg.135 of the PB Table: Group C 60% of the Fixed Capital Investment – 6 yrs or earlier if

	Scheme were subject to monetary ceilings directly related to the fixed capital investment."	the ceilings are reached. Pg.153-4: Eligibility certificate showing calculation of incentive at 85% of the Fixed Capital Investment	the ceilings are reached. Pg.153-4: Eligibility certificate showing calculation of incentive at 60% of the Fixed Capital Investment
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15. He further submits that the Hon'ble Supreme Court in CIT vs. Ponni Sugars and Chemicals Ltd. (2008) 174 Taxman 87 (SC) has held that the test of the character of the receipt of a subsidy in the hands of the assessee under a scheme has to be determined with respect to the purpose for which the subsidy is granted. It is to be noted that in Ponni Sugar's case the proceeds from the sale of sugar (the assessee's stock-in-trade) were held to be on capital account and so also collection of excise duty. It is for this reason that the Hon'ble Supreme Court stated that even a subsidy to acquire raw materials may be in the capital field depending on the object of the Scheme. He further submits that the purpose of the 1983 and 1988 scheme are the same as the object and purpose of the 1979 scheme with which Reliance Industries Ltd. Special Bench (supra), was concerned, viz., dispersal of industries outside the Bombay-Thane-Pune belt. In Reliance's case, the subsidy opted for was exemption from payment of sales-tax and the sales tax deemed to have been collected by assessee (which was not to be paid to the Government) was held to be on capital account or in the capital field. It was held that the sales tax ought to be regarded as paid to the Government and returned to Reliance in the form of a subsidy (in the present case a subsidized loan). So also the sales tax collected in the present case was on capital account and the subsequent payment to the Government whether in the period prescribed in the scheme or the prepayment would

be on capital account, i.e., one has to determine the character of the subsidy in the form of sales-tax collection. Therefore, the present receipt must also be regarded as being of the same nature as the receipt in the Reliance/Ponni Sugar's case, viz., a receipt on capital account. If a receipt is on capital account, then, the benefit if any obtained on its prepayment is also on capital account to which sec.41(1) does not apply. He further submits that the decision of the Special Bench in Reliance's case has been approved by the Hon'ble Bombay High Court in CIT vs. Reliance Industries Ltd. in Central Excise Appeal No.1299 Of 2008 dated 15.4.2009. The principle of Reliance (wherein the incentive was in the form of sales-tax exemption) has been applied to the case of sales-tax deferral. In that case, looking at the object of the scheme, the Tribunal has held that the receipt in question was a capital receipt.

16. He further submits that in ACIT vs. Associated Capsules Ltd. ITA No.4818/Mum/08, for Assessment Year 2004-05 order dated 20.10.2009, the Tribunal has followed the decision in Sterlite's case (supra), and decided the similar issue in favour of the assessee.

17. He further submits that in Everest Industries vs. ACIT in ITA No.814/Mum/2007, for Assessment Year 2003-04, order dated 4.12.2009, the Tribunal has compared the 1979 scheme with which Reliance was concerned and the 1993 scheme (which is a successor to the 1983 scheme and the 1988 scheme) with which Everest was concerned. The Tribunal has thereafter come to the conclusion that the two schemes are similar in all material respects when determining the question as to whether the incentive was capital or revenue in nature and hence decided the issue in favour of the assessee.

18. He further submits that the decision of the Tribunal in Cartini India Ltd. vs ITO ITA No.1051/Mum/2008 for Assessment Year 2004-05, order

dated 19.5.2009 is distinguishable. In that case, the issue involved was about "the taxability of Rs.5,48,517/- is being the remission under the 'prepayment of sales tax deferral scheme 2003'. Thus, the decision proceeded on the footing that there was a remission of the liability. In the case of the assessee there is no remission or cessation of a liability as the liability has been fully paid (Payment of the present value is as good as payment of the full liability on the due date.). In the Appellant's case, it has not been accepted that there is a remission. In Sterlite, Everest and Associated Capsule's cases the assessee did not urge that there was no benefit and that there was no remission of a liability. Moreover, in Cartini's case, the assessee was entitled to an incentive only to the extent of 15% of the fixed capital investment, which is a material difference between that case and the Appellant's case, whereas the Appellant is entitled to an incentive to the extent of 85% of the fixed capital investment. He further submits that an incentive of Rs.18,93,750 on a fixed capital investment of Rs.1,26,25,000 (15%) can hardly be regarded as an incentive for setting up the unit and incurring the cost of fixed capital investment, whereas in the appellant's case there can be no doubt that the incentive was for setting up the unit in a backward area. Also, in Cartini's case, the assessee did not at all argue that (1) the incentive was on capital account (in view of Reliance Special Bench and other decision referred to above) and (2) There was no benefit on payment of present value of the future liability. In Cartini's case (para 7 and 8), it has been held that the benefit is really the right to defer the sales-tax payment.

19. He further submits that even assuming whilst strongly denying that any benefit has been obtained by the Appellant, such 'benefit' is not in respect of the sales-tax deferral liability but in respect of loan. The 3rd Proviso to Section 38(4) of the Bombay Sales-tax Act provides that where a loan liability equal to the amount of deferral has been raised by SICOM, the sales tax shall be deemed to have been paid. Pursuant to the said

proviso, Government Resolution dt.21st July, 1988 was passed prescribing the procedure for conversion of the sale-tax deferral into interest free loan [Pg.232 onwards of the Paper book]. On 08.10.2002 the Appellant wrote to SICOM opting for conversion of the sales-tax deferral liability into a loan (Pg.251). On 10.10.2002 further letters were written by the Appellant to SICOM furnishing the details required by SICOM (Pg.258-259). On 21.10.2002 SICOM being fully satisfied that the conditions for effective such conversion were fulfilled wrote to the Sales-tax Department for carrying out the ministerial act of issuing a modified Entitlement Certificate on the basis of the modified Eligibility Certificate issued by SICOM and forwarded to the sales-tax authorities as per the administrative orders for conversion of the deferred sales-tax liability to a loan liability. This shows that SICOM was satisfied that all the conditions for converting the sales-tax deferral liability to a loan were fulfilled. (Pg.260-1). On 30.10.2002 Asstt. Sales-tax Commissioner wrote to the Appellant asking for certain details (Pg.262). On 11.11.2002: The Appellant replied to the Sales-tax Department (Pg.263). Thereafter, the Appellant did not receive any communication from the sales-tax department which means that the sales tax department was satisfied that the Entitlement Certificate had to be modified as directed by SICOM. In the circumstances, he submits that the Appellant had done all that was required from him to convert the deferred sales-tax liability into a loan. Therefore, according to him the liability has been converted into a loan and the condition prescribed in Board Circular No.674 dated 29.12.1993 read with Circular No.496 dated 25.09.1987 have been fulfilled. Assuming that there was some doubt in the matter it must be resolved in favour of the appellant. An authority must be regarded as having done that which ought to have been done, otherwise the assessee would be denied a benefit to which it was legitimately entitled for no fault of its own. Reliance was also placed on CIT vs. Mrs. Hilla J.B. Wadia (1995) 216 ITR 376 (Bom) wherein it was held that if the assessee had done all

he/she could to purchase the house but the purchase could not be finalized for no fault of his/her, the assessee could not be denied exemption u/s.54. In that case the investment of a small sum of Rs.8,000 out of the total sum of Rs.2,59,238/- in the house still had to be done, nevertheless the Hon'ble Bombay High Court held that substantially the entire cost of construction had been paid by the assessee within the stipulated period and therefore deduction u/s.54 was allowed. The present case stands on a much stronger footing where everything that the appellant could do was done and the process of conversion could not be completed because the sales-tax authorities did not issue the modified Entitlement Certificate.

20. He further submits that once the modified Eligibility Certificate is issued by the Implementing Agency, the sales-tax authority is bound by it and has no jurisdiction to question it. See: *Laxmi Industries vs. State of Rajasthan* 99 STC 584 (Raj); *Swastik Metal Works vs. The State of Maharashtra* (1998) 17 MTJ 332 (Mumbai Tribunal). In any event, from the correspondence exchanged between the appellant and SICOM/Sales-tax authority regarding conversion of sales-tax into a loan, it is apparent that a loan of an equivalent amount has for all practical purposes been raised by SICOM. Therefore, the crucial part in the entire process was obtaining the approval of the SICOM to the proposed conversion as SICOM was to convert the sales-tax deferral liability into loan. Sales-tax Department was getting its dues and therefore they should not have any objection to the said process of conversion. Once SICOM had agreed to the proposed conversion by issuing a modified Eligibility Certificate, sales-tax authorities were only required to perform the ministerial act of issuing a modified Certificate of Entitlement. This can be seen from the fact that on 30th October, 2002, i.e., within only 9 days of SICOM writing to the sales-tax department, the sales-tax authorities had called for the details of the status of assessments (received by the appellant on 07.11.2002),

to which the assessee had promptly provided vide letter dated 11.11.2002 (page-263). The sales-tax authorities did not require any further information nor required the appellant to do anything further. In the meantime, on 12.12.2002, the prepayment scheme under the fourth proviso was notified as noted earlier and accordingly, the appellant applied under the fourth proviso to section 38(4) for prepayment and made such prepayment on 30.12.2002. As SICOM had expressed its unequivocal satisfaction, the condition for conversion into a loan were satisfied and the amount prepaid was really the prepayment of a loan and this is a transaction in the capital field. The fourth proviso properly construed would apply both in the case of loan as well as deferred sales-tax by prepayment as otherwise the assessee who had converted the sales-tax liability into a loan would be worse-off.

21. He further submits that the third proviso to section 38(4) of the Sales tax Act speaks of conversion of sales-tax liability into loan by SICOM. Since in the present case, SICOM has given its consent for the conversion, the conversion by SICOM has been done and the requirement of third proviso to section 38(4) is also fulfilled. Therefore, the sales-tax liability on the facts of the present case is to be regarded as having been converted into a loan and the prepayment thereof ought to be regarded as prepayment of such converted loan liability. Therefore, the benefit, if any, on such prepayment is on capital account. Reliance was placed on the recent decision of Hon'ble Jurisdictional High Court in *S.I. Group India Ltd. vs. ACIT* (2010) 192 Taxman 91(Bom.), wherein on the similar facts and circumstances, it has been held that there was no remission or cessation of liability, one of the requirements spelt out for the applicability of section 41(1)(a) has not been fulfilled. Reliance was also placed on the decision of the Hon'ble Bombay High Court in *Mahindra and Mahindra Ltd. vs. CIT* 261 ITR 501 (Bom), wherein it has been held that section 41(1) does not apply to a benefit received on capital account. The said decision

of the Bombay High Court has been followed by Delhi High Court in CIT vs. Tosha International Ltd. 176 Taxman 187 (Del). The Department's SLP against the Delhi High Court's decision has been dismissed by the Supreme Court [see 319 ITR (Statutes) 7]. He, therefore, submits that the provision of section 41(1), does not apply to the facts of the present case and, therefore, the addition made by the Assessing Officer and sustained by the Id. CIT(A) be deleted.

22. On the other hand, the Id.DR while referring to the question referred to the Special Bench and the provision of section 41(1) of the Act further submits that the Hon'ble Supreme Court in the case of Polyflex (India) (P) Ltd. vs. CIT 257 ITR 343(SC), while holding the applicability of 41(1) has observed:

"In the assessment for the relevant year an allowance or deduction has been made in respect of any loss, expenditure or trading liability incurred by the assessee. This is the first step. Coming to the next step the assessee must have subsequently (i) obtained any amount in respect of such loss or expenditure or (ii) obtained any benefit in respect of such trading liability by way of remission or cessation thereof. In case either of these events happen, the deeming provision enacted in the closing part of sub-s.(1) comes into play. Accordingly, the amount obtained by the assessee or the value of benefit accruing to him is deemed to be profits and gains of business or profession and it becomes chargeable to income-tax as the income of that previous year."

Therefore , what is then required to be seen for invoking the provisions of sec. 41(1) is that the assessee should have

- i) incurred a trading liability,
- ii) a deduction should have been made in respect of such trading liability, and
- iii) the assessee must have subsequently obtained any benefit in respect of such trading liability by way of remission or cessation thereof.

23. He further submits that sales tax is charged on goods sold by an assessee during the course of its trading activity. Hence, sales tax accrued / collected on the sale of goods by the assessee becomes a trading receipt of the assessee. This is the settled position of law in view of the decision of Hon'ble Supreme Court in the cases of Chowringhee Sales Bureau P. Ltd. vs. CIT (1993) 87 ITR 542(SC) and Sinclair Murray And Co. P. Ltd. vs. CIT (1974) 97 ITR 615(SC). Reference may also be made to the decision of the Hon'ble High Court of Gujarat in the case of Wolkem (P) Ltd. vs. CIT reported in 259 ITR 430.(Guj.).

24. In the present case the assessee has itself been treating the sales tax collected as part of trading and not as capital receipts in its books of account and returns of income filed by it, even during the period when it was eligible for the benefits of sales tax deferral under the "Package of Incentive" Schemes. In support he placed on record the copy of audit report u/s. 44AB of the I.T. Act, 1961 for the Assessment Years 2000-01, 2001-02 & 2002-03. He further submits that in column 13(e) of the Tax Audit Report, in respect of "amounts not credited to the Profit & Loss A/c., being capital receipts, if any, the auditor has categorically stated "Nil". This clearly shows that it is accepted position that sales tax receipts have not been treated as capital receipts. The assessee, in the proceedings before the Assessing Officer and Ld. CIT(A) has admitted that the receipts on account of sales tax was a trading receipt, and the liability to the State Government on account of the sales tax was a trading liability. The returns of income for the Assessment Years, including the returns for the Assessment Years during the period the assessee was eligible for the benefits under the sales tax deferral scheme, were filed by the assessee voluntarily disclosing the above position. Even if the sales tax collected and the liability towards the sales tax incurred were not routed through the P&L account of the assessee, it would make no difference since the sales tax collected would get offset by the deduction claimed and allowed

on account of the sales tax paid. This is again settled position of law in view of decision of Hon'ble Supreme Court in the case Chowringhee Sales Bureau P.Ltd. (supra).

25. As per the "Package of Incentive" scheme, sales tax liability has been defined to mean the following:-

- (i) Sales tax / General sales tax / Purchase tax as the case may be, payable and paid or deferred under the local sales tax law during that period on purchase of raw materials reduced by the set off at appropriate rates, if any, admissible there under and also on sales of finished products of the eligible units.
- (ii) Central sales tax payable and paid or deferred under the Sales Tax Act, 1956 during that period on the sales of finished products of the eligible units made in the course of inter State Trade or Commerce.

Undisputably, any liability relating to a trading receipt would be a trading liability. As has been pointed out, sales tax liability has been incurred by the assessee and deduction has also been claimed and allowed in respect of such trading liability in the return of income filed by the assessee in accordance with Circular No. 496 dated 25.09.1987. This is an undisputed fact and admitted by the assessee before the lower authorities as well as by the Ld. Counsel for the assessee during the course of present hearing. The assessment for all the years, including the years during which the assessee was eligible for the benefits of deferral of the sales tax liability, for which the returns were filed voluntarily by the assessee have been completed, and have attained finality. Hence, for the assessee to now make a claim that the sales tax received during this period was not a trading receipt on revenue account, but was a capital receipt is not tenable and cannot be accepted. It may be noted that the prepayment of deferred sales tax liability, which is the subject matter of the appeal, of the sales tax collected and disclosed as trading receipt, relate to the

earlier Assessment Years, the assessments of which stand completed and have attained finality, and not related to the Assessment Year 2003-04 which is the subject matter of appeal.

26. He further submits that while deciding the case of S.I. Group India Ltd.(supra), the Hon'ble Bombay High Court, after considering the facts of the case, has categorically held that " the liability of the assessee to pay sales tax is indisputably a trading liability in respect of which an allowance or deduction has been made u/s. 43B". In this case also, the facts are identical and the assessee had availed benefits of sales tax deferral under the "Package of Incentive" Schemes of the Maharashtra Government. In view of the above, it is clear that the assessee has incurred a trading liability, which has been deferred under the Schemes. It is important to appreciate that the trading liability had been incurred and had accrued the moment sales were effected by the assessee.

27. Another argument which was taken by the Id. Counsel for the assessee was that the receipts on account of sales tax were capital receipts in view of the decision of the Hon'ble Special Bench in the case of Reliance Industries Ltd. reported in 88 ITD 273 (Mum.) (SB), wherein the Tribunal had taken the view that the incentive received by the assessee on account of complete exemption from payment of sales tax under the 1979 "Package of Incentive" Scheme was capital in nature. Accordingly, the incentive by way of deferral of sales tax under the 1983 and the 1988 "Package of Incentive" Schemes, under which the assessee has claimed benefits of deferral of sales tax in respect of its units, should also be treated as capital receipts. In this regard he submits that in the 1979 scheme, since, the unit was completely exempted from payment of the sales tax, no liability on account of sales tax collected by the unit ever accrued to it. Hence, no sales tax was payable to the Government.

Provisions of section 43B would, therefore, not apply in the case of Reliance Industries Ltd. However, in the case of the assessee, which was covered under the 1983 and the 1988 "Package of Incentive" Schemes, the liability towards the sales tax accrued the moment sales were effected by the unit. This liability was deferred to be paid at a future date. The Special Bench, in the case of Reliance Industries Ltd. (supra), held the receipts on account of sales tax as capital receipts on a finding of fact that the eligibility of the unit to receive the incentive, i.e., the subsidy in the form of complete exemption from the payment of sales tax, arose even before the unit was set up. It also gave a finding of fact that the subsidy was given for the purpose of setting up the unit. Reference was also made to page no. 305 of the decision of Special Bench in the case of Reliance Industries Ltd. (supra), the relevant portion reads as under:-

"On an analysis of the Scheme, the Tribunal has come to the conclusion that the thrust of the Scheme is that the assessee would become entitled for the sales tax incentive even before the commencement of the production, which implies that the object of the incentive is to fund a part of the cost of the setting up of the factory in the notified backward area".

This finding of fact of the Tribunal has been approved by the Special Bench and it is on this finding of fact that the Special Bench after applying the ratio of the decision of the Hon'ble Supreme Court in the case of Sahney Steel & Press Works Ltd. Vs. CIT reported in (1979) 142 CTR (SC) 261 has held the subsidy to be capital in nature. According to him on perusal of the 1983 and 1988 "Package of Incentive" Schemes nowhere show that the incentives with respect to the sales tax were given for the purpose of funding a part of cost of setting up of the factory or that the units became eligible / entitled for the sales tax incentive even before the commencement of the production. It could not be pointed out by the Id. Counsel for the assessee as to which clause in the Schemes even suggests that the subsidies were given for the purpose of funding a part of cost of setting up of the factory or that the units became eligible / entitled for the sales tax incentive even before the commencement of the

production. The only reason given by the Id. Counsel for the assessee in support of his claim is his reliance on decision of Hon'ble Special Bench in the case of Reliance Industries Ltd. (supra). According to the Id. DR the findings given in the context of the 1979 scheme cannot hold good for the 1983 and 1988 schemes when nothing could be pointed out by the Id. Counsel that under the 1983 and 1988 Schemes, the subsidies were given for the purpose of funding a part of cost of setting up of the unit or that the units became eligible / entitled for the sales tax incentive even before the commencement of the production. In the absence of such conditions, the binding ratio of the Hon'ble Supreme Court in the case of Sahney Steel & Press Works Ltd. (supra) has to be necessarily followed.

28. According to the Id. DR the ratio of the said decision is that if subsidies are given to the assessee for assisting him in carrying out the business operation and the money is given only after and conditional upon commencement of production, such subsidies must be treated as assistance for the purpose of the trade and revenue in nature. At para 4 of the decision the Hon'ble Supreme Court has observed:-

"The contention of Mr. Ganesh that the subsidies were capital in nature and were given for the purpose of stimulating setting up and expansion of industries in the state cannot be upheld because of the subsidy scheme itself. No financial assistance was granted to the assessee for setting up of the industry. It is only when the assessee had set up its industry and commenced production that various incentives were given for the limited period of five years. It appears that the endeavor of the State was to provide the newly set up industries a helping hand for five years to enable them to be viable and competitive. Sales tax refund and the relief on account of water rate, land revenue as well as electricity charges were all intended to enable the assessee to run the business more profitably."

According to the Id. DR the above observations also bring out one point very clearly which is that the subsidy scheme itself would not decide the

nature of the subsidy, whether revenue or capital. Rather, it is the purpose for which the specific subsidy is given which will decide the nature of the subsidy. Within a subsidy scheme, whether for dispersal of the industries outside a certain belt or for encouraging setting up of industries in a particular area of the State or the entire State, a number of subsidies / assistance / incentives are given. In fact, the Maharashtra Schemes which we are concerned with at present is itself called "Package of Incentive" Scheme. This itself shows that the Scheme contains a package of incentives/ subsidies / assistance like sales tax incentive, octroi incentive, special capital incentive, contribution towards the cost of feasibility studies of the project, etc. Within the same Scheme, while the units are eligible for the sales tax incentive only after the commencement of the production, the units are eligible to draw the special capital incentive at a certain percentage of the fixed capital investment after the completion of all effective steps during the process of setting up the unit and, even before the commencement of the production (page no. 112 of the paper book) and it is the specific purpose for which each incentive / subsidy is given which will decide as to whether the subsidy is in the nature of a capital subsidy or revenue subsidy. The Hon'ble Supreme Court has in para 8 of *Sahney Steel* (supra) has held as follows:-

"....The sales tax upon collection forms part of public funds of the State. If any subsidy is given, the character of the subsidy in the hands of the recipient - whether revenue or capital - will have to be determined by having regard to the purpose for which the subsidy is given....."

This has been demonstrated by the Hon'ble Supreme Court by way of an example which is reproduced below:

"If the scheme was that the assessee will be given refund of sales tax on purchase of machinery as well as on raw materials to enable the assessee to acquire new plants and machinery for further expansion of its manufacturing capacity in a backward area, the entire subsidy must be held to be a capital receipt in the hands of the assessee. It will not be

open to the Revenue to contend that the refund of sales tax paid on raw materials or finished products must be treated as revenue receipt in the hands of the assessee. In both the cases, the Government is paying out of public funds to the assessee for a definite purpose. If the purpose is to help the assessee to set up its business or complete a project as in Seaham Harbour Dock Co.'s case (*supra*), the monies must be treated as to have been received for capital purpose. But, if monies are given to the assessee for assisting him in carrying out the business operation and the money is given only after and conditional upon commencement of production, such subsidies must be treated as assistance for the purpose of the trade."

The above example given by the Hon'ble Supreme Court once again demonstrates the point that under the Scheme, it is the purpose for which the subsidy is given that decides the nature of the subsidy – revenue or capital. It is not the object of the Scheme of the Government (which in such circumstances will necessarily be capital intensive) which would decide the nature and character of the subsidy, but it is the purpose for which the subsidy under the Scheme is given which would decide the character and nature of the subsidy. In Seaham Harbour case, which has been extensively discussed and relied upon by the Hon'ble Supreme Court in *Sahney Steel*, the subsidy was realized at different times during the course of the expansion of the project itself. Although, subsidy in the form of refund of sales tax paid on raw materials or finished products is normally treated as revenue receipt, however, since in the above example, the purpose of the subsidy in the form of refund of sales tax paid on raw materials or finished products was to enable the assessee to acquire new plants and machinery for further expansion of its manufacturing capacity in a backward area, it has been held to be capital in nature. The contention of the Ld. Counsel for the assessee that the Supreme Court has stated that even a subsidy to acquire for raw materials may be in the capital field depending on the object of the Scheme is not correct. As per the decision of the Hon'ble Supreme Court in *Sahney Steel* (*supra*) it is not the object of the Scheme, but the

purpose for which the subsidy is given under the Scheme which will decide the nature of the subsidy. In *Ponni Sugars & Chemicals Ltd.* 219 CTR (SC) 105, it has been categorically held in para 14 that it is the object for which the subsidy / assistance is given which determines the nature of the incentive subsidy. Applying the above principles in the case of the assessee, there is no clause under the 1983 and 1988 Schemes, even suggests, that the sales tax subsidy was given for enabling the assessee to set up the industrial unit. Infact, the unit under these Schemes would become eligible for the sales tax incentives only after commencement of commercial production and after the unit was set up. Clause 2.1 of the 1983 "Package of Incentive" Scheme lays down that "the Eligibility Certificate under Part I of the 1983 Scheme will be issued by the Implementing Agency after commencement of commercial production as may be determined by it, based on the totality of the documentary evidence led by the eligible unit in this behalf, as also such other information, details, etc. required / called for in connection therewith such as the date of power connection, electricity consumption bills over a period, first sale bill, excise license, extract of Excise Register or of Production Register, etc." Same is the position in clause 2.1 of the 1988 "Package of Incentive" Scheme. There is nothing in the Schemes that lays down any condition that the deferred amount of sales tax subsidy / liability was to be utilized only for repayment of term loans taken for setting up the units or for the purchase of any capital asset. He further submits that in para no. 13 of its judgment, the Hon'ble Supreme Court in *Sahney Steel* (supra) has held as follows:-

"In the case before us, subsidies have not been 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 production. Such a subsidy could only be treated as assistance given for the purpose of carrying on of the business of the assessee. Applying the test of Viscount Simon in the case of *Ostime* (supra), it must be held

that these subsidies are of revenue character and will have to be taxed accordingly.”

Similar is the position in the case of the assessee. The sales tax subsidy was granted year after year only after the setting up of the industry and upon commencement of the production. It was not granted for production of or bringing into existence any new asset.

29. He further submits that the Id. Counsel’s contention that in Ponni Sugar case the proceeds from the sale of sugar (the assessee’s stock-in-trade) were held to be on capital account is not entirely correct. In the said case the subsidy on the sale of sugar was held to be in the nature of capital receipt only because, it was found by the Hon’ble Court that the incentive, i.e., the subsidy was mandatorily required to be utilized for repayment of loans taken by the assessee to set up new units or for substantial expansion of existing units. The ratio laid down by the Hon’ble Court in Sahney Steel has not been deviated from at all. In Sahney Steel (supra), the Hon’ble Court found that the assessee was free to use the money in its business entirely as it liked. Similar is the situation in the case of the assessee. In the case of Sahney Steel, the refund of sales tax on raw materials, machinery and finished goods was subject to a maximum of 10% of the equity capital paid up in the case of Public Limited companies and the actual capital in the case of others. Hence, the maximum limit of the subsidy was capped on the basis of a capital asset. In the case of the assessee the maximum limit of the subsidy was also capped on the basis of fixed capital investments, which were capital assets. While the objective of the Scheme under which Sahney Steel received the incentive was stimulating setting up and expansion of industries in the State, the objective of the Maharashtra Schemes under which the assessee received the incentives was dispersal of industries outside the Bombay-Thane-Pune Belt and stimulating setting up of the industries to the other underdeveloped and developing areas of the State.

The object of the both Schemes were the same in substance. In the Maharashtra Schemes of 1983 & 1988 also, there is a system of yearly review to ensure that the units remain in normal production and were eligible for the incentive / subsidy. In the case of the assessee, the sales tax subsidy under the 1983 & 1988 "Package of Incentive" Schemes were not given to enable the assessee to set up the unit. It was given to the assessee to help it in the initial years to remain competitive vis-a-vis established units in the developed parts of the State which had better infrastructure facilities, easy availability of manpower, raw materials, customers, etc., so that they could stand on their own feet. In para no. 31 on page 14 of the judgment of the Hon'ble Andhra Pradesh High Court reported in 152 ITR 39, it has been held that benefits like tax holiday etc. are given to the industrial units in the initial years with a view to strengthen them so that they could be run efficiently and these subsidies are revenue in nature. The decision of the Hon'ble High Court has been endorsed and upheld by the Hon'ble Supreme Court.

30. It was argued by the Id. Counsel for the assessee that the Scheme of 1979 was identical to the Schemes of 1983 and 1988. Since, the subsidy in the form of sales tax exemption in the case of Reliance Industries Ltd.(supra), which was covered under the 1979 Scheme was held to be capital in nature, the subsidy on account of deferred sales tax liability under the 1983 and 1988 Scheme should also be held to be capital. The contention of the assessee cannot be accepted for the detailed reasons already given in respect of nature of subsidy under the 1983 and 1988 Scheme and also in view of the binding decisions of the Hon'ble Supreme Court in the case of Sahney Steel and Ponni Sugar. If the 1979 Scheme is identical to the 1983 and 1988 Schemes, then the finding of facts recorded for arriving at the decision in the case of Reliance Industries Ltd.(supra) with utmost respect, is not correct. A decision based on incorrect findings of fact and without following the binding ratio

laid down by the Hon'ble Supreme Court cannot be said to have laid down correct law. There is nothing in the 1979 Scheme also to even suggest that the sales tax subsidy was given to the units to assist them directly or indirectly in the setting up of the unit and that the unit became eligible for the subsidy even before the commencement of the commercial production. There is nothing in the Scheme which even suggests remotely that the subsidy was required to be used for repayment of any loan taken for setting up the unit or for purchase of any capital asset. The assessee was free to use the money in its business as it liked. Infact, the Order of the Division Bench in the case of Reliance Industries Ltd.(supra), which has been approved by the Special Bench itself holds that ".....it is a fact of life of the setting up of industries in the modern era that the cost of machinery and plant, etc. are generally defrayed by way of repayment of borrowings from out of the internal accruals of the industry during the course of its business operations....." (para 31 of the order of Special Bench in the case of Reliance Industries Ltd (supra). The above itself is sufficient to show that even the Tribunal was of the view that the cost of setting up of the industry has been met through profits earned by the assessee and out of internal accruals during the course of its day to day business operations. There was no requirement that the subsidy was required to be employed for the purpose of repayment of borrowings taken for setting up the unit.

31. The Id. Counsel for the assessee has also argued that the decision of the Special Bench in the case of Reliance Industries Ltd. has been approved by the Hon'ble Bombay High Court in the case of Reliance Industries Ltd. (Appeal No. 1299 of 2008, dated 15.4.2009), wherein the Tribunal decision for a subsequent year following the decision of the Special Bench has been affirmed. According to the Id. DR the question as framed was not admitted by the Hon'ble High Court in view of the findings recorded by the Special Bench that "the object of the subsidy was to set

up a new unit in a backward area to generate employment". The Hon'ble High Court has applied the purpose test as laid down by the Hon'ble Supreme Court in the case of Ponni Sugars and Chemicals Ltd. 306 ITR 392 (SC) to the above findings recorded by the Special Bench and, has, accordingly held that the subsidy is clearly on capital account. There is nothing in the Schemes (and specially 1983 and 1988 Schemes with which we are concerned in the present appeal) which suggests that the subsidy by way of sales tax deferral was given directly or indirectly to the assessee for setting up the units or for the creation or purchase of capital assets. The units were eligible and entitled to the claim of the sales tax subsidy only after and conditional upon the commencement of commercial production. Hence, in view of the decisions of the Hon'ble Supreme Court in the cases of Sahney Steel and Ponni Sugars, these were operational subsidies and, therefore, revenue in nature.

32. The reliance was also placed by the Id. DR on the decision of the Hon'ble Punjab and Haryana High Court in the case of Abhishek Industries Ltd. 286 ITR 1 in support of his arguments. In the said case the number of years for which the units were eligible for sales tax incentive depended upon their location and the overall quantum of exemption was limited to a percentage of the fixed capital investment made by the units. It was held by the Hon'ble High Court that since the units became eligible for the subsidy (sales tax) only after the commencement of production, these were operational subsidies and, revenue in nature. No document or material has been placed on records by the assessee to substantiate its plea that the subsidy by way of sales tax deferral was to enable the unit / assessee to acquire new plant and machinery or that it was to be used directly or indirectly to set up the industry.

33. The decision of the Tribunal in the case of Sterlite Optical Technologies Ltd. and Everest Industries Ltd.(supra), would not help the assessee in view of the above reasons and further it has simply followed the decision of Hon'ble Special Bench in the case of Reliance Industries Ltd. (supra) without examining the nature of subsidies as per the ratio laid down by the Hon'ble Supreme Court in Sahney Steel and Ponni Sugars. Further, the assessee has himself admitted and disclosed that the sales tax receipts as trading receipts, revenue in nature. For the same reason, the reliance of the assessee on M/s. Associated Capsules Pvt. Ltd.(supra), which has simply followed Sterlite Optical Technologies Ltd., would be of no help to the assessee for the reason given above. In any case, the question as to whether sales tax receipt is revenue or capital is of no consequence to the issue before the Bench since the assessee has itself admitted and disclosed the same as revenue receipt and, the assessments have also been completed, and have attained finality.

34. Another contention of the Ld. Counsel that since the prepayment benefits emanate out of the "Package of Incentive" Schemes, they should be held as capital is not tenable because prepayment of deferred sales tax liability is not part of the said Scheme. Rather, it is a part of a separate Scheme floated by the State Government and, in nature, was merely a business arrangement between the State Government and the unit holders who opted to take benefit of the said business arrangement. The benefits of prepayment of the deferred sales tax liability do not flow out of the "Package of Incentive" Schemes and have no relation to the said Schemes.

35. It was an admitted position of the assessee both before the lower authorities as well as of the Ld. Counsel for the assessee before the Hon'ble Bench that deduction on account of the sales tax liability has been

made. Thus condition in section 41(1) is, therefore, satisfied. Now, it has been stated that "since the receipt is a capital receipt at inception, there was no question of including it in the sales. Therefore, there was no debit to the Profit & Loss account of the amount of sales tax or obtaining deduction in respect of the same u/s. 43B. Since deduction has not been obtained for the sales tax, sec. 41(1) of the I.T. Act, 1961 does not apply." The said stand taken by the Id. Counsel is contrary to the earlier stand taken by him wherein it was admitted by him that deduction u/s. 43B had been taken and allowed in terms of Circular No. 496 of the Board. In fact, he had himself also submitted a copy of the Circular to the Bench in support of his contention that the sales tax liability has been discharged since deduction u/s. 43B has been allowed by the Department. It has been stated by the Id. Counsel for the assessee that sec. 41(1) does not apply in the present case because "(1) the appellant has not obtained any benefit (2) there has not been any remission of a liability (3) the benefit if any obtained by the appellant is not in respect of a trading liability (4) the benefit if any obtained by the appellant is on capital account". There is no mention that sec. 41(1) does not apply because no deduction has been obtained. Infact, the Id. Counsel has admitted that deduction u/s.43B has been allowed. Before the Id.CIT(A) also, this fact has been admitted by the assessee. At page no. 9 of the CIT(A)'s order, assessee's submissions have been noted. In the third last line, the submission of the aassessee is as follows:

" The sales tax so collected would be treated as deemed payment by virtue of the amendment by Circular No. 496 dated September 25, 1987 and Circular No. 674 dated December 29, 1983 issued by the Central Board of Direct Taxes (CBDT) for the purpose of Sales Tax Act."

Again at page no. 12, the following submission of the assessee is noted:-

"Therefore, in the present case the sales tax liability though not paid, by virtue of amendment of Sales Tax Act, would be regarded as actually paid"

On page no. 13 of the CIT(A)'s order, the following submission of the assessee is noted in the first four lines:-

"From the above it is clear that although the sales tax collected from the customers was a trading receipt, due to the deferral scheme the same is deemed to have been paid to the Government, thereby discharging the liability."

All the above not only prove that the assessee was itself admitting that the sales tax receipts, even during the period when it was eligible for the deferral incentive, were trading receipts, and disclosed as such in its books of account as well as the returns of income filed by it, it had also claimed and was allowed deduction of the trading liability under section 43B in respect of the sales tax collected / accrued. The claim made now that the receipts on account of sales tax was in the nature of capital receipts, and that no deduction has been obtained for the sales tax is, therefore, neither correct nor tenable. This argument of the Ld. Counsel cannot be, therefore, accepted.

36. The Id. DR further submits that it has been contended by the Id. Counsel that even assuming that any benefit has been obtained by the appellant, it is in respect of a loan liability because, as per the 3rd proviso to sec. 38(4) of the Bombay Sales Tax Act, 1959 where a loan liability equal to the amount of any deferred tax payable by an eligible unit has been raised by the SICOM, then such tax shall be deemed, in the public interest, to have been paid. It has been contended that the appellant has gone in for changeover to the interest free loan scheme as provided for in Resolution No. IDL 1087/6245/Ind. 8 Mantralaya dated the 21st July, 1988 (page nos. 232 to 250 of the paper book). It has been submitted by him that although they had applied in the prescribed form 'A' for changeover, only modification in the "Eligibility Certificate" has been carried out by SICOM, the Implementing Agency. Although, SICOM had

forwarded the necessary Entitlement Certificate to the Sales tax authorities for carrying out the required modification therein, the necessary modification has not been carried out by the Sales tax authority. It was admitted by the Ld. Counsel that such approval for changeover has not been received by the appellant. It has, however, been argued that since they had applied for the conversion, it should be deemed that conversion has been approved. Decision of the Hon'ble Bombay High Court in the case of Hilla J.B. Wadia has been relied upon by the Ld. Counsel in support of this proposition. In this regard the Id. DR submits that :

- i) The procedure for changeover to the interest free loan scheme from the deferral scheme is provided exhaustively in clauses 6.9 to 6.18 of the Resolution dated 21.07.2002.
- ii) As per clause 6.13, the procedures set out in clauses 6.14 onwards leading to the changeover can be undertaken only by a unit whose Eligibility Certificate and Certificate of Entitlement have been modified. Admittedly, the Certificate of Entitlement of the appellant was not modified. Hence, question of it complying with the procedures in the succeeding clauses would not arise.
- iii) Assessee also has not been able to give any evidence that it has complied with any of the procedures required to be complied by it as per clause 6.13 onwards of the scheme.
- iv) Modification in the Eligibility Certificate only signifies that instead of the benefits under the deferral scheme, the unit holder is now eligible for benefits under the interest free loan Scheme. This does not in anyway mean that its deferred sales tax liability has changed into interest free loan.
- v) After all the formalities laid down in the procedure have been complied with and SICOM is satisfied that the application for provisional loan is in order, it will sanction sales tax loan equivalent to total amount of tax payable as shown in the returns and eligible for deferral (clause 6.16).

He further submits that evidences on record and the submissions of the Id. Counsel leave no doubt that there is no such sanction order from

SICOM / an Implementing Agency raising a loan liability equal to the total amount of tax payable but deferred. It is, therefore, clear that the deferred sales tax of the assessee has not been converted into interest free loan. Further, the assessee has applied for opting into the interest free loan scheme for the past period. Under the circumstances, it was required to comply with the procedures laid down in the clauses 6.21 and 6.22 of the Resolution. The assessee, admittedly has failed to do so. The question of the conversion of deferred sales tax liability into interest free loan would, therefore, not arise. There is no provision in the Resolution or the Scheme wherein it has been provided that once an application has been made, and no sanction order of conversion has been received, it would be deemed that conversion has been made. In absence of such provision, the conversion cannot be deemed to have been made. The reliance of the Ld. Counsel on the decision of the Hon'ble Bombay High Court in the case of Hilla J.B. Wadia is completely misplaced as no such proposition has been laid down in the said decision nor is it relevant to the facts of the case. In the said case, almost the entire payment towards the purchase of the flat was paid by the assessee within the period prescribed under the Act and, the Hon'ble High Court held that considering the facts of the case, the assessee had acquired substantial domain over the flat in question under the agreement with the society coupled with payment of almost entire cost of construction within a period of two years. Hence, the assessee was eligible for the claim u/s. 54 of I.T.Act, 1961. In the present case, the sanction of SICOM raising loan liability equal to the deferred sales tax was a mandatory requirement under the 3rd proviso to section 38 of the Sales Tax Act for the conversion of the deferred sales tax liability into interest free loan to take place. In absence of such sanction allowing conversion, no conversion into interest free loan can be said to have taken place.

37. The Id. DR further submits that it may be noted that conversion is to be allowed only during the period when the unit is eligible for the deferral benefits. In respect of the unit under the 1983 scheme, the period of eligibility was 01.11.1989 to 31.10.1996 (Eligibility Certificate dated 08.11.1989 at page 153 of the paper book filed by the assessee). The unit could have applied for the conversion only during 01.11.1989 to 31.10.1996. The assessee was not eligible for such conversion when it applied for the same on 08.10.2002 in Annexure 'A' (page no. 255 and 256 of the paper book filed by the assessee). The question of the deferred sales tax of this unit being converted into interest free loan would not, therefore, arise. In support the reference was made to clause 6.10 of the Resolution dated 21.07.1998 which states as follows:-

"An eligible unit will be entitled to exercise option covering the past period i.e., the period prior to the date of option in part or in full as well as the remaining portion of the period covered by the Eligibility Certificate. But the option once exercised shall be final and binding on eligible unit and that it will not be open for the unit to change the option once exercised."

Similarly, the option in respect of the conversion from the sales tax deferral into the interest free loan scheme is to be exercised for the past period of eligibility in part or in full as well as the remaining period. This means that while for the past period during the eligibility period, the option can be exercised for a part of the past period or the full period, the same option should cover the remaining part of the eligibility period also. For the expansion unit covered under the 1988 "Package of Incentive" Scheme, assessee claims to have applied for the entire past period prior to the date of option but has not applied for the conversion for the remaining part of the period during which the unit is eligible under the scheme for deferral unit. Hence, the application itself is not correct. For

the above reasons the Certificate of Entitlement was not modified by the Sales tax authorities.

38. He further submits that the Id. Counsel has raised an argument that once the modified Eligibility Certificate is issued by the Implementing Agency, the Sales tax Authority is bound by it and has no jurisdiction to question it and in support he placed reliance on two decisions, viz., (1) Laxmi Industries Vs. State of Rajasthan 99 STC 584 (Raj.) and (2) Swastik Metal Works Vs. The State of Maharashtra 17 MTJ 332 (Mumbai Tribunal). According to the Id. DR, the argument of the Id. Counsel is not tenable and cannot be accepted in the facts of the present case. The two decisions also do not come to the aid of the assessee. The issue before us is not the conflict of power and authority between SICOM and Sales tax authorities. As already submitted it has been categorically laid down in the Resolution of the State Government dated 21.07.1988 (page 234 of the paper book) that both the Eligibility Certificate and the Certificate of Entitlement are required to be modified for the actual process of conversion to loan to be started by following the procedures laid down in the Resolution itself. Even if it is presumed that once the Eligibility Certificate is modified, it should be accepted that the Entitlement Certificate also stands modified would not help the arguments of the Id. Counsel. Modification in the Eligibility Certificate is only for the purpose of certifying that the unit is now eligible for benefits of interest – free loan under the Scheme in place of deferral of sales tax. It does not mean for a moment that the conversion has taken place. It is only when SICOM, on being satisfied that the application for provisional loan is in order and sanctions sales tax loan equivalent to the total amount of tax payable shown in the return and eligible for “Deferral” and, on receipt of such sanction letter, the eligible unit execute necessary agreement in this regard, the conversion to loan can be said to have taken place (clause 6.16 of the Resolution dated 21.07.1988 – page 234 of the paper book).

Admittedly, no such sanction has been issued. The Ld. Counsel has also admitted that "the process of conversion could not be completed because the Sales tax authorities did not issue the modified Entitlement Certificate". If process of conversion itself had not been completed, the question of the deferred sales tax liability getting converted into interest free loan cannot arise.

39. The Id. DR further submits that during the course of his preliminary arguments the Id. Counsel for the assessee has contended that the fact that Department has allowed deduction u/s. 43B itself means that the deferred sales tax liability stands discharged and that it has been accepted that the said deferred tax liability has been converted into a loan. In this regard the Id. DR submits that allowing of deduction u/s. 43B under no circumstances even suggests that it has been accepted by the Department that the deferred tax liability has been converted into loan. The liability towards sales tax is to be allowed u/s. 43B of I.T. Act, 1961 only when it is actually paid. However, by virtue of Circular No. 496 dated 25.09.1987 of the Central Board of Direct Taxes (CBDT), since, amendment has been made in the Sales Tax Act itself to the effect that sales tax deferred under the Scheme shall be deemed as actually paid, the statutory liability is treated to have been discharged for the purposes of sec. 43B. The Circular was issued in view of representation received from various State Governments and others to the effect that the operation of the provisions of sec. 43B had the effect of diluting the incentives offered by the deferral schemes. He pointed out that it is not important whether deduction has been rightly allowed or not. The only condition in sec. 41(1) which is required to be seen in this context is whether deduction has been made on account of the trading liability or not. If the deduction has been made, one of the conditions laid down in sec. 41(1) is satisfied. Whether the deferred sales tax liability has been converted into interest free loan or not is a question of fact and, the facts

very categorically and unequivocally show that such conversion of deferred sales tax liability into interest free loan could not have been done and has not been done. In fact, the fact that the assessee applied and obtained the benefit of pre payment under the 4th proviso to sec.38 of the Sales Tax Act, which was only with respect to the deferred sales tax liability, itself proves that what it prepaid was only its deferred sales tax liability and nothing else. The allowing of deduction u/s. 43B also does not mean that the liability has actually been paid. It is merely treated as paid in line with the amendment in the Sales Tax Act and in compliance to the Board's Circular. Hence, the deeming fiction has been taken to its logical conclusion.

40. With regard to the application of the 4th proviso to sec. 38 of the Bombay Sales Tax Act to include prepayment facility to unit holders who have opted for interest free loan since, the said unit holders cannot be placed at a disadvantage with respect to unit holders under the deferral scheme under the same "Package of Incentive" Scheme, the Id. DR submits that it is settled law that nothing can be read into the provisions of the Act. It is very clear from the 4th proviso that it seeks to extend the benefit of prepayment only to the unit holders falling under the deferral scheme. If it had been the intention of the Government to also include the unit holders covered by the interest free loan scheme, they would have also been specifically included in the said proviso. It is also pertinent to mention that 4th proviso was added by the Maharashtra Tax Laws (Levy and Amendment) Act, 1995 dated 18.08.1995 with effect from 01.10.1995 and again the proviso was substituted by the Maharashtra Act No. 20 of 2002 dated 04.05.2002 w.e.f. 01.05.2002. It is under this substituted proviso that the benefits of prepayment have been made available to the eligible unit which have opted for deferral scheme. Prior to substitution similar benefits were made available to dealers to discharge their loan liability under the 4th proviso. What emerges is that

similar benefits were made specifically available in respect of loan liability also prior to 01.05.2002 and now the benefits of prepayment have been granted specifically to the eligible units for the discharge of their deferred sales tax liability. This shows that the benefits of the 4th proviso to sec. 38 of the Sales Tax Act is available only to the eligible units for discharging their deferred sales tax liability and not to dealers who have incurred loan liability, in view of the 4th proviso before its substitution by the current proviso w.e.f. 01.05.2002, which provided with the option of prepaying their loan liability separately under the same Act.

41. With regard to the Id. Counsel's plea that the assessee had been treating the sales tax deferred as a loan in its books of account which was evidenced by the Balance Sheet filed by it for the earlier years to show that the sales tax deferred was nothing but a loan liability the Id. DR submits that application for the conversion of deferred sales tax liability into loan itself was filed with the Competent Authority, i.e, SICOM only on 08.10.2002. This means that before this date, i.e., 08.10.2002, the liability was nothing but a deferred sales tax liability. Hence, the question of treating it as a loan before this date does not arise. In any case, it is settled law that entries in the books of accounts are not determinative of the nature of transactions (*Tuticorin Alkali Chemicals And Fertilizers Ltd. vs. CIT* (1997) 227 ITR 172 (SC)).

42. He further submits that even presuming for the sake of argument but not accepting that the sales tax liability was converted into a loan liability, it would not alter the character of the liability in the hands of the assessee. The conversion has taken place merely by way of journal entries. Only a new nomenclature has been given to the liability. This has been done merely for the effective monitoring and implementation of the benefits under the Scheme. Income Tax Act and State Government

Schemes operate in different fields. State Government Schemes have nothing do with the computation of taxable income. Nature of expenditure / liability cannot be conclusively determined by the manner in which accounts are made in terms of State Government Schemes. The Government Scheme would not override the provision of the I. T. Act, 1961. Reliance was also placed on the ratio of the decision in the case of Southern Technologies Ltd. vs. JCIT (2010) 320 ITR 577 (SC).

43. He further submits that the assessee has incurred a trading liability in respect of which deduction has also been made. It has been the contention of the Ld. Counsel for the assessee that no benefit has accrued to the assessee on account of prepayment of the deferred liability at NPV. Alternatively, it has been argued by the Ld. Counsel that if at all any benefit has accrued, it is on capital account. According to the Id. DR, the assessee has, infact, obtained benefit in respect of the deferred sales tax liability, which is a trading liability on account of its prepayment at NPV, the working of which was prescribed by the State Government, by way of remission and cessation of such liability. For finding out whether the assessee has obtained any benefit or not, one need not travel beyond the Balance Sheets and accounts filed by the assessee. In Schedule 'P' to the Notes to accounts (page no. 90 of the paper book) filed alongwith the return of income for the A.Y. 2003-04 (during the period when the prepayment has taken place), it has been stated as follows:-

"The company has, in response to a notification issued by the Government of Maharashtra, regarding 'Premature repayment of Deferral Sales Tax at Net Present Value', gone in for repayment of the total liability of Rs.75,201,378 on 30th December, 2002 at Net Present Value. The total amount of payment made is Rs.33,713,393. Based on the opinion obtained by the Company, it has taken the view that the balance of Rs.41,487,985 arising out of the remission of the

loan liability, being capital in nature, is credited to Capital Reserve”.

Perusal of the above leaves no doubt in mind that the assessee itself is of the view that there is a remission of the liability, albeit, a loan liability and that it has become richer by Rs.4,14,87,985 which it has itself credited to the Capital Reserve. The reflection of this amount in the Capital Reserve itself proves that there is a benefit to the assessee and that this benefit is real. Even if the amount had been credited under some other head, it would have made no difference because it is settled law that nomenclature given a particular transaction is not determinative of its true nature. He further submits that an analysis of the Balance Sheet reveals that the assessee had deferred tax liability of Rs.7,52,01,378 immediately prior to prepayment which, after prepayment, has been reduced to Nil. However, the assets to this extent have not diminished. The assets of the value of only Rs.3,37,13,393 have got reduced leaving assets of the value of Rs.4,14,87,985 with the assessee which is matched with the credit of the same amount in the Capital Reserve. This is because, out of the total liability on account of deferred sales tax of Rs.7,52,01,378, which the assessee was required to pay, an amount of Rs.3,37,13,393 only has been paid, which is deemed to be full discharge of the existing liability of the assessee, leaving a surplus of Rs.4,14,87,985 in the hands of the assessee which is not required to be paid any more. This is the benefit obtained by the assessee. The assessee has obtained a benefit is demonstrated by the following simple example:-

Before the prepayment, the entries relating to the liability would in the most simple terms look like this.

Balance Sheet as at

Liability (in Rs.)	Asset (in Rs.)
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Sales Tax Liability	7,52,01,378	Bank A/c. (Sales tax deposited)	7,52,01,378
	7,52,01,378		7,52,01,378

After the prepayment, the entries would in the most simple terms look like this :

Liability (in Rs.)		Asset (in Rs.)		
Capital Reserve	4,14,87,985	Bank A/c. (Sales tax deposited)	7,52,01,378	
Sales Tax Liability	Nil	Less: Sales tax liability paid	3,37,13,393	4,14,87,985
	4,14,87,985			4,14,87,985

Hence, from owing liability of Rs.7.52 crores, the assessee is now owner of assets of the value of Rs.4.15 crores which he is no longer required to pay to any one. It goes without saying that the assessee has benefited by Rs.4.15 crores. The condition of section 41(1) is, therefore, satisfied. Assessee collected Rs.7.52 crores from its customers on account of sales tax. This money was required to be paid to the State Government after the requisite number of years as per the terms of the 1983 and 1988 Schemes. The assessee also obtained deduction on account of Sales tax accrued u/s. 43B, thereby, reducing its income to that extent. Later on, instead of Rs.7.52 crores which the assessee was required to pay, it paid only Rs.3.37 crores and, the balance amount of Rs.4.15 crores became

his own due to the remission of this liability and the deeming provision of the 4th proviso to sec. 38 of the Sales Tax Act. The assessee immediately benefited by Rs.4.15 crores which it appropriated to itself, and rightly reflected this benefit by crediting it to the Capital Reserve. This was real benefit, a commercial benefit and not some notional benefit. Infact, the said 4th proviso itself recognizes the fact that full liability is different and higher than the payment actually made since it deems that the payment of Rs.3.37 crores made would be treated as full discharge of the deferred liability of Rs.7.52 crores.

44. With regard to the argument of the Id. Counsel that the NPV of its liability was only Rs.3,37,13,393 and, since, it had paid this amount as worked out by the Government itself, it had not obtained any benefit. In other words the present value of its liability is only Rs.3.37 crores and the liability of Rs.7.52 crores was only its future liability. According to the Id. DR this is not correct since the sales tax liability was fixed the day it accrued. It cannot diminish over a period of time. It can get reduced only if a part of the liability is paid or if the person to whom the liability is owed gives up / waives / remits part of the liability. The admitted liability as per the Balance Sheet itself was Rs.7,52,01,378. The assessee had not paid any part of the liability till its prepayment in view of the deferral incentive given to it that it could pay this entire liability after a certain period of time in future. Hence, the present liability was Rs.7.52 crores which was allowed to be discharged at a specified future date. It was not a future liability since the same was already fixed the day it had accrued. The Id. DR, while drawing our attention to the definition of the net present value (NPV) from the BusinessDictionary.com (<http://www.businessdictionary.com/definition/net-present-value-NPV.html>), (copy filed) submits that NPV is always from the perspective of the investor. It is the difference between the Present Value of the future cash flows from an

investment and the amount of investment. In calculating the NPV, the person who is liable to pay has no role to play. In calculating the NPV, the question asked by the investor (in this case, the State Government) always is, "How much is the cash which would flow in to me, after a certain time in future from now, worth today?". One thing is clear. What is being done by the State Government is finding out the worth of the Rs.7.52 crores, which it would get in future from the assessee today. The Government may require money to invest in its several welfare or infrastructure projects. It may find it more beneficial to get back its money available with the unit holders in the form of deferred sales tax liability prematurely, rather than to borrow money from other agencies at high interest rates. Hence, it works out the present worth of its money available with the unit holders and, consequently, the NPV and offers a prepayment Scheme to the unit holders. It is important to note that NPV does not mean the actual value of the asset (available in the form of deferred sales tax liability with the unit holders), but the present worth of the said asset considering that it would be able to use the asset only at a later date while the requirement for the money is today. It follows then that the liability that has been prepaid by the assessee is not the actual liability, but only the present worth of the liability in the eyes of the State Government as on the date of prepayment. If the Government had not come out with the Scheme of prepayment, could the assessee have prepaid its liability of Rs.7.52 crores by paying a mere Rs.3.37 crores? The answer is no.

45. The Government came up with the Scheme of prepayment of the deferred sales tax liability by enacting the 4th proviso to sec. 38 of the Sales Tax Act. As per this, the unit holders were given an option to prepay the sales tax deferred liability at a reduced amount worked out as per the Rules prescribed by the Government. It is because the option to prepay was beneficial to the assessee that it opted to benefit from the

Scheme and went for prepayment of its deferred sales tax liability. In effect, what the Government has done is that it has offered to the assessee that as against the liability of Rs.7.52 crores payable at a future date, if it paid only Rs.3.37 crores (which was the present worth of the future cash inflow of the Government), the Government would deem it to be full discharge of the total liability and the Government would not ask for the balance liability of Rs.4.15 crores. In effect, the Government has granted in public interest, a remission of sales tax liability of Rs.4.15 crores to the assessee. It has given up this amount on the date when prepayment is made, thereby taking the deeming provision in the 4th proviso to sec. 38 of the Sales Tax Act to its logical end. In the process, the assessee has benefited by Rs.4.15 crores. The liability of Rs.4.15 crores has, therefore, been remitted by the Government. In the books of the assessee, liability of the value of Rs.4.15 crores has ceased, i.e., it has come to an end. Consequently, there is a cessation of liability also to the extent of Rs.4.15 crores. This benefit as result of remission and cessation is reflected in the Balance Sheet by an increase in the asset and credit to the Capital Reserve account. In the case of Sterlite Optical Technologies (*supra*), relied upon by the Ld. Counsel the Tribunal has been accepted that there was a waiver as well as benefit which accrued to the assessee.

46. The contention of the Ld. Counsel that by prepayment, the assessee is deprived of cash in praesenti and, hence, there cannot be a benefit, is not tenable. The assessee has opted for prepayment only because it was beneficial to it. The only argument of the assessee can be that if it had not made the prepayment, it could have earned some income on the amount it paid to the Government in discharge of its deferred liability. Conversely, it could have even lost this money. These are all hypothetical situations and there is no need to travel into the realms of imagination.

47. To sum up according to the Id. DR, all the conditions for invoking the provisions of sec. 41(1) are satisfied. It has been held by the Hon'ble Rajasthan High Court in the case of Wolkem (P) Ltd. 259 ITR 430 that "sec. 41 enacts adjustment provisions whereby the Revenue takes back what it has already allowed, if certain conditions come to pass and the assessee recoups something for which an allowance had already been made and deducted from his business income." Similar view has been held by the Hon'ble Karnataka High Court in the case of Mysore Thermo Electric (P) Ltd. 221 ITR 504, in the case of Express Newspapers Pvt. Ltd. Vs. CIT 227 ITR 325 (Mad.) and in the case of Solid Containers Ltd. vs. DCIT and Another (2009) 308 ITR 417 (Bom.) and also in ACIT vs. Cosmo Films Ltd. 28 SOT 353 (Del.). The Income Tax Department has already allowed a deduction u/s. 43B to the assessee of sales tax liability of Rs.7.52 crores. Although, the deduction u/s. 43B is to be allowed only on "actually paid" basis, the same was allowed in view of the amendment made by the State Government in the 3rd proviso to sec. 38 of the Sales Tax Act and Board's Circular. However, the assessee has finally paid only Rs.3.37 crores as against the deduction of Rs.7.52 crores claimed and allowed to it. The balance liability of Rs.4.15 crores is not required to be paid by it, now or in future. The amount of Rs.4.15 crores has, therefore, been rightly taxed in the assessment year 2003-04 u/s. 41(1). The Id. DR while also relying on the order of the Assessing Officer and the Id. CIT(A) submits that in view of his submissions, the addition made by the Assessing Officer u/s. 41(1) be upheld.

48. In the rejoinder the Id. Sr. Counsel submits that the Id. DR has relied on the decision of the Supreme Court in Chowringhee Sales Bureau to contend that sales-tax is a trading receipt. This is undoubtedly so when the sales-tax is collected in normal circumstances and not where collection under a subsidy scheme as per 1979, 1983 or 1988 Schemes as

held in Reliance's case (Special Bench/ Bombay High Court). He further submits that sales-tax when collected and deferred as per the Package Scheme of Incentives cannot be regarded as a trading receipt but is a capital receipt. In this connection, reliance was again placed on the decision of the Special Bench of the Tribunal in Reliance's case wherein a sales-tax incentive received under the Package Scheme of Incentives was treated as a capital receipt. The decision of the Special Bench has been approved by the Bombay High Court.

49. He further submits that the Id. DR also stated that the appellant has always accepted that the deferred sales-tax is a trading receipt. It is to be noted that in the Annual Accounts for FY 2001-02, the item is mentioned as 'Deferred Sales tax Loan' (see Pg.80). Similar is the position for the earlier years. Even at page 90, reference is made to repayment of 'loan liability' though the word 'remission' is wrongly used bearing in mind the earlier part of the note. It is submitted that the Appellant has raised a contention before the lower authorities that in view of Reliance Special Bench decision, the amount should be regarded as a capital receipt. Therefore, the DR is not justified in contending that the receipt has always been treated by the Appellant as a trading receipt. In any event treatment in the books of account is not relevant. See Tuticorin Alkali's case 227 ITR 172 (SC).

50. The Id. Sr. Counsel further submits that the benefit must be determined by an application of universal test. It depends upon person to person. Therefore, in a given case there is no benefit. The Govt. did not give up the money. It is only an early payment. One rupee today is more valuable than one rupee after ten years. Therefore, there is no benefit at all. There is no remission as the assessee has paid the amount as per State Govt. Scheme. It is an economic concept, commercial concept or common sense concept.

51. He further submits that the Id. DR also referred to pg.7, para 8 of the decision of the Bombay High Court in *SI Group India Ltd. vs. ACIT* (supra), wherein it is stated that the liability of the assessee to pay sales tax was a trading liability. The issue before the court was whether there is remission or cessation of the sales-tax liability when the amount paid by the assessee to SICOM towards prepayment of the deferred sales-tax liability is not accepted by the Sales-tax authorities as a proper payment of the said sales-tax liability. The Court held that since the sales-tax authorities have not accepted the payment to SICOM as discharging the sales-tax liability; there was no remission or cessation thereof. Decision of the court is to be read for what it expressly decides and not as deciding something not before the learned Judges or what the learned Judges wanted to decide [See *Goodyear India Ltd. vs. State of Haryana* (188 ITR 402) (SC)]. He further submits that the issue whether the receipt was at inception a capital receipt or a trading receipt was not before the High Court and the assessee proceeded on the footing that even if at inception the amount was a trading receipt, section 41(1) could not apply as the sales tax liability survived. Moreover, the question of whether any benefit arises or not has been expressly kept open. In fact, the judgment only decides that section 41(1) does not apply because there was no remission of liability. Therefore, the decision cannot be regarded an authority sales-tax deferral liability is a trading receipt.

52. He further submits that the Id. DR also contended that under section 43B deduction was allowed as per CBDT Circular No.496 dated 25.9.1987 and 674 dated 29.12.1993, which is a deeming fiction and therefore the Department has not accepted that payment is actually made. He submits that the deeming fiction is to be carried to its logical conclusion. In fact, the CIT(A) at page 16 has himself canvassed the proposition that a deeming fiction must be carried to its logical

conclusion. In any event, since the receipt is a capital receipt at inception, there was no question of including it in the sales. Therefore, there was no debit to the profit and loss account of the amount of sales-tax or obtaining deduction in respect of the same under section 43B. Since deduction has not been obtained for the sales-tax, section 41(1) of the Act does not apply.

53. He further submits that the Id. DR contended that the conversion cannot be regarded as having been done for the following reasons:

- 1) The assessee applied for conversion in October 2002 and made the prepayment of sales-tax liability in December 2002 thereby not allowing the Sales-tax authorities sufficient time to issue the modified Entitlement Certificate.
- 2) The assessee has not complied with several steps which are required to be taken for conversion of sales-tax liability into a loan. In this connection, the various steps mentioned at page 233 onwards were pointed out, with the submission that these steps were not complied with by the assessee.
- 3) The assessee in its correspondence with the sales-tax authorities has referred to the deferred sales-tax liability, and not a loan, as having been prepaid.

He submits that the aforesaid contentions of the Id. DR are misconceived.

54. The Id. DR's next contention was that several steps which were envisaged under the scheme for conversion of liability into loan were not taken and in this context reference was made to the various steps at page.233 onwards. There was no question of complying with paras 6.13 onwards as a formal modified Entitlement Certificate as per para 6.12 was not forthcoming.

55. The Id. DR also stated that the assessee in its correspondence with the Sales-tax authorities has referred to the liability as deferred sales tax liability and not as a loan. It is submitted that the distinction between

deferred sales-tax liability and loan is relevant from the perspective of the Income-tax Act in view of the provisions of section 41(1). It is for this reason that the reference in the prepayment related correspondence is to deferred sales-tax liability.

56. The decision of the Hon'ble Bombay High Court in the case of Solid Containers Ltd. Vs. Dy.CIT (2009) 178 Taxman 192(Bom.) is distinguishable from the assessee's case. The Hon'ble High Court was concerned with a loan which was obtained for trade purposes and which was presently payable. The question was regarding assessability of the waiver of the loan. The Bombay High Court followed the decision of the Supreme Court in T.V. Sundaram Iyengar's case 222 ITR 344. In the said case, certain deposits which were received from regular customers in the course of trading orders placed by them with the assessee, Sundaram Iyengar, which have not been claimed by the customers were written back to the profit and loss account. The Supreme Court held that since the deposits represented trade advance payments which were to be adjusted against future trade transactions, any surplus on such account must be regarded as a trade surplus and assessable as business income on a common sense approach. The Bombay High Court has followed the said decision and held that the surplus arising from the waiver of loan was assessable as business income mainly because the loan was utilized for trading purposes of the assessee. The decision of the Bombay High Court in Mahindra & Mahindra's case 261 ITR 501 has been distinguished on the ground that in that case the loan was utilized for capital purposes. In Solid Containers case the assessment was upheld on the basis of section 41(1) being applicable. He further submits that this decision is wholly distinguishable. In the present case, the amount is sought to be assessed u/s.41(1). The common sense approach which has been applied by the Bombay High Court in Solid Container's case following Sundaram Iyengar's case is not applicable to sec.41(1). It is well settled that but for

the deeming fiction in sec.41(1), remission of a liability cannot be considered as amounting to income. Reliance was also placed on the decision of the Hon'ble Supreme Court in the case of Commissioner of Agricultural Income tax vs. Kerala Estate Moorad Chalapuram 27 Taxman 339 (SC), wherein the Supreme Court has held that in absence of a deeming provision such as section 41(1) of the Act in the Kerala Agricultural I.T. Act, 1950, the remission of liability cannot be regarded as agricultural income of the assessee. In any event, the loan in the present case has been utilized for a capital purpose, namely, for fixed capital investment for setting up the unit in a backward area. Therefore, the decision of the Bombay High Court in Solid Container's case does not apply since the loan in that case was utilized for trading purpose. In this connection, reference was also made to the following decisions of the Tribunal wherein the decision in Solid Container's case has been distinguished on the ground that the loan was utilized for capital purposes:

Accelerated Freez & Drying Co. Ltd. 31 SOT 442 (Cochin)

Cipla Investments Ltd. vs. ITO 33 SOT 317 (Mum)

57. He further submits that the Id. DR also contended that if the liability was converted into a loan, then the assessee could not have prepaid it since the 4th proviso does not speak of prepayment of loan but only provides for prepayment of deferred sales-tax liability. According to him 4th proviso applies to all cases where "certificate has been granted for availing the incentives by way of deferment." Therefore, it is wide enough to cover case of deferment whether the same has been converted into a loan or not. If it is not so regarded it would mean that in a case where the liability has been converted into a loan the assessee would be worse off than where the liability has not been converted into a loan. It is to be noted that in 1995 the fourth proviso was inserted and provided for

prepayment of the loan into which the deferred sales-tax liability was converted. Circular No.20-T/1995 dated 10.10.1995 issued by the State Government clarified that such converted loans could be prepaid and "the Economic principle for recovery of future debts at the Net Present Value suggests that they are in the interest of revenue." In 2002, the fourth proviso was substituted to provide for prepayment of the deferred tax by an amount equal to the Net Present Value of deferred tax. The substituted fourth proviso widens the scope of permitted prepayments and cannot be interpreted to mean that the person who had diligently converted the deferred tax is not entitled to avail the benefit. The Finance Minister's speech also emphasizes the right to prepay which would include both converted loans and outstanding deferred tax. Accordingly, the Department's argument that the prepayment by the assessee was of deferred tax as allowed by the substituted 4th proviso which shows that the amount had not been converted into a loan is not correct.

58. He further submits that the Id. DR has placed reliance on the decision in CIT vs. Abhishek Industries (286 ITR 1) (P&H). The exact nature of the Scheme is not referred. It was certainly not a pre-payment case. Page 25 of the Report clearly brings out that the assessee has not placed any material relevant in support of its contention that the benefit was in capital field. Therefore, it is not applicable to the facts of the assessee's case.

59. Reliance has also been placed on the decision of the Tribunal in the case of Cosmo Films (28 SOT 353)(Del). That case dealt with a totally different fact-situation, namely, the liability to pay the deferred sales tax was assigned to a private party. The Tribunal took the view that this resulted in the liability of Cosmo to pay the deferred sales tax liability coming to an end. Reliance was placed on Explanation 1 to section 41(1)

to hold that a unilateral write off would result in remission of the liability. It should be noted that this was not a case of pre-payment to the concerned authority and a credit was taken in the profit and loss account. Para 16 of the order also shows that the assessee appeared to have accepted that there was a benefit but only contended that it should be spread over the period of repayment.

60. In *Wolkem (p) Ltd. vs. CIT* (259 ITR 430) (Raj) cited by the Department the excise duty was refunded on the assessee succeeding in appeal. It was indisputable that such an amount would be assessable as the assessee had obtained an amount for which deduction had been allowed earlier. This was not a case of sales tax deferral and, therefore, reference was made to *Chowringhee's* case as holding that the sales tax is a collection of revenue account. Such is not the position where sales tax is collected under an incentive scheme and which has to be repaid later, hence not applicable.

61. Similarly, in *Mysore Thermo Electric (P). Ltd. vs. CIT* (221 ITR 504) (Kar) there was a refund of the excise duty Collected which squarely falls within section 41(1). The argument was that the excise duty had not been specifically claimed as a deduction and kept a separate account was not accepted. Again in *Express Newspapers Pvt. Ltd. vs. CIT* (227 ITR 325) (Mad) cited by the Id. DR, an interest which was earlier allowed, was settled by paying a lesser sum. It was not a case of pre-payment of a future liability at its net present value which is the present case. To similar effect is the decision of the Supreme Court in *Polyflex vs. CIT* (257 ITR 343)(SC) again cited by the Id. DR. The assessee became entitled to refund of excise duty. It was held that sec.41(1) would apply as it was a case of the assessee having obtained an amount in respect of what was earlier allowed as a deduction even though the Revenue's appeal in the matter urging that the excise duty had been correctly collected was

pending. It was not a case of sales tax deferral or pre-payment and hence, the aforesaid decisions relied on by the Id. DR are not applicable to the facts of the assessee's case. He, therefore, reiterates that the addition made by the Assessing Officer and sustained by the Id. CIT(A) is not sustainable in law and the same be deleted.

62. We have carefully considered the submission of the parties and perused the material available on record. We find that the material facts are not in dispute. The assessee company obtained incentive by way of sales tax deferral scheme under the package scheme of incentive 1983 (the 1983 scheme) and package scheme of incentive 1988, (the 1988 scheme) notified by the Government of Maharashtra. Under 1983 scheme the assessee's Unit at Kondhapuri, Tal Shirur Dist. Pune which at the relevant time a notified backward area was entitled to defer the payment of sales tax collected during the period 1.11.1989 to 31.10.1996 (7 years) upto the maximum of Rs.666.94 lacs being 85% of the fixed capital investment of Rs.784.64 lacs. The assessee collected sales tax in 7 years Rs. 3,29,93,863/- which was to be repaid after 12 years in 6 equal annual instalments. Under the "1988 scheme", which is similar to "1983 scheme", the amount of tax actually deferred under the "1988 scheme" was Rs.4,22,07,515/-. Thus aggregate deferral amount under 1983 and 1988 schemes was Rs.7,52,01,338/- (Rs.3,29,93,863/- + Rs.4,22,07,515/-). We further find that it is also not in dispute that the sales tax collected by the assessee during the aforesaid period was allowed by the Assessing Officer u/s.43B as actually paid in view of the CBDT Circular No.496 dated 25.09.1987. We further find that there was an amendment made under the Bombay Sales Tax Act, 1959, (the Sales tax Act) by insertion of the third proviso to sec.38(4) of the Sales Tax Act, wherein SICOM or the relevant Regional Development Corporation or the District Industries Centre concerned was to convert the deferred sales tax into a loan and thereafter as per 2002 amendment, fourth proviso to

sec.38(4) of the Sales tax Act by which the earlier 4th proviso was substituted, which provides that where the NPV of deferred tax as may be prescribed was paid, the deferred tax was deemed, in public interest, to have been paid. We further find that the assessee following the aforesaid amendment under the Bombay Sales Tax Act, 1959 has made repayment of loan of Rs.3,37,13,393/- (Rs.1,76,02,272/- of 1983 scheme + Rs.1,61,11,121/- of 1988 scheme) on 30.12.2002 as per NPV of the deferred tax as prescribed under Circular No.39T of 2002 of Trade Circular dated 12.12.2002 appearing at Pg.174-186 to the assessee's paper book. The assessee claimed Rs.4,14,87,985/- being the difference between the deferred sales tax Rs.7,52,01,378/- and its Net Present Value amounting to Rs. 3,37,13,393/- as capital receipt, credited in the books of account of the assessee in the capital reserve account. However, the Assessing Officer keeping in view that the assessee has obtained the benefit of payment of whole amount of Rs.7,52,01,378/- as deduction u/s.43B of the Act in view of CBDT Circular No.496 dated 25.09.1987, therefore, he brought the difference of Rs. 4,14,87,985/- to tax u/s.41(1) of the Act. The Id. CIT(A) on an appeal filed in this regard has also upheld the addition made by the Assessing Officer.

63. In order to better appreciate the controversy involved, it would be convenient to extract section 41(1) of the I.T. Act, as follows:

"Section 41(1) Where an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee (hereinafter referred to as the first mentioned person) and subsequently during any previous year.

(a) the first mentioned person has obtained, whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained by such person or the value of benefit accruing to him shall be deemed to be profits and gains of business or profession and accordingly chargeable to income tax as the income of that previous year, whether the

business or profession in respect of which the allowance or deduction has been made is in existence in that year or not;"

64. We have refrained from reproducing the rest of the section which is not relevant for the purpose of the present controversy, before us.

65. We feel that it is worthwhile to state the various principles set out by Hon'ble Supreme Court and High Courts while considering the provision of section 41(1) of the Act.

66. In *Polyflex (India) (P) Ltd. vs. CIT* (2002) 257 ITR 343 (SC), it has been observed by their Lordships that section 41(1) applies if the following conditions and circumstances are satisfied:

"In the assessment for the relevant year an allowance or deduction has been made in respect of any loss, expenditure or trading liability incurred by the assessee. This is the first step. Coming to the next step the assessee must have subsequently (i) obtained any amount in respect of such loss or expenditure or (ii) obtained any benefit in respect of such trading liability by way of remission or cessation thereof. In case either of these events happen, the deeming provision enacted in the closing part of sub-s.(1) comes into play. Accordingly, the amount obtained by the assessee or the value of benefit accruing to him is deemed to be profit and gains of business or profession and it becomes chargeable to income-tax as the income of that previous year."

67. In *Wolkem (P) Ltd. vs. CIT* (2003) 259 ITR 430 (Raj), it has been observed that Sec.41 enacts adjustment provisions whereby the Revenue takes back what it has already allowed, if certain conditions come to pass and the assessee recoups something for which an allowance had already been made and deducted from his business income. The provision also fixes the year in which the recoupment, etc., is to be taxed. The first part of sub-sec.(1) contemplates loss, expenditure or trading liability in some former year for which allowance or deduction had been made in a bygone Assessment Year. The second part of sub-s.(1) contemplates recoupment

of such loss or expenditure or benefit in respect of such trading liability by way of remission or cessation thereof in some subsequent year. The word "such" appearing in the second part of sub-s.(1) signifies that the recoupment or benefit must be in respect of the loss, expenditure or trading liability mentioned in the first part of sub-s.(1). The payment with respect to the sales-tax or excise duty is normally an allowable item of business expenditure.

68. In CIT vs. Bharat Iron And Steel Industries (1993) 199 ITR 67 (Guj.) (FB) The Hon'ble Gujarat High court while considering the section 41(1) of the Act, held as under (head note):

"The key words in section 41(1) of the Income-tax Act, 1961, are "the assessee has obtained, whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof ". It is the obtaining in "cash or in any other manner whatsoever, any amount . . . or some benefit in respect of such trading liability . . ." which is contemplated by the Legislature when it used the words "has obtained". Section 41(1) introduces a fiction by which where an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee and subsequently during any previous year the assessee has obtained, whether in cash or in any other manner whatsoever any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained by him or the value of benefit accruing to him shall be deemed to be profits and gains of the business or profession and, accordingly, chargeable to income-tax as income of that previous year, whether the business or profession in respect of which the allowance or deduction has been made is in existence in that year or not. The fiction is an indivisible one. It cannot be enlarged by importing another fiction, namely, that if the amount was obtained or was receivable during the previous year, it must be deemed to have been obtained or received during that year. The amount may be actually received or it may be adjusted by way of an adjustment entry or a credit note or in any other form when the cash or the equivalent of cash can be said to have been received by the assessee. But it must be the obtaining of the actual amount which is contemplated by the Legislature when it used the words "has obtained, whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure in the past". In the context in which these words occur, no other meaning is possible."

69. Recently in SI Group India Ltd. (supra) the Hon'ble Jurisdictional High Court has observed the following: (Placitum -8, page- 121 of 326 ITR):

"In order that the provisions of sub-sec.(1) should be attracted the first requirement is that an allowance or deduction must have been made in the assessment for any year in respect of a loss, expenditure or trading liability incurred by the assessee. The liability of the assessee to pay sales tax is undisputedly a trading liability in respect of which an allowance or deduction had been made u/s.43B. However, under clause (a) of sub-sec.(1) it is inter alia required that the assessee ought to have obtained "some benefit in respect of such trading liability by way of remission or cessation thereof". This postulates that there must be a remission or cessation of the trading liability and that consequently a benefit must enure to the assessee....."

70. Thus to invoke the provisions of sec.41(1), the following conditions must be fulfilled.

- i. In the assessment of the assessee, an allowance or deduction has been made in respect of loss, expenditure or the trading liability incurred by the assessee.
- ii. The assessee must have subsequently (i) obtained any amount in respect of such loss or expenditure or (ii) obtained any benefit in respect of such trading liability by way of remission or cessation thereof. In case either of these events happen, the deeming provision enacted in closing part of sub-sec.1 comes into play.
- iii. The amount obtained by the assessee or the value of benefit accruing to him is deemed to be profit and gains of the business or profession and it becomes chargeable to income tax as an income of that previous year.

71. Further on a plain reading of sec.41(1) of the Act, it is also clear that the provisions contained in sec.41(1) does not make any distinction between any contractual trading liability or any statutory trading liability. Even if any statutory liability is remitted or ceased of, or any amount, whether in cash or in any other manner, has been obtained in respect of the expenditure incurred by way of statutory liability, the same would be deemed to be the profit and gains of the business of the assessee and would accordingly chargeable to income-tax as the income of that year in which such benefit or amount is obtained.

72. At this stage it is also necessary to take note of the provisions of sec.38 of the Bombay Sales Tax Act, 1959, applicable at the relevant time:

38. Payment of tax and deferred payment of tax, etc.

(1) Tax shall be paid in the manner herein provided, and at such intervals as may be prescribed.

(2) A Registered dealer furnishing returns as required by sub-sec.(1) of section 32, shall first pay into a Government treasury, in such manner and at such intervals as may be prescribed, the amount of tax due from him for the period covered by a return along with the amount of penalty or interest or both] payable by him u/s.36

(3) A Registered dealer furnishing a revised return in accordance with sub-section (3) of section 32, which revised return shows that a larger amount of tax than already paid is payable, shall first pay into a Government treasury the extra amount of tax.

(4) (a) The amount of tax-

(i) due where returns have been furnished without full payment thereof, or

(ii) assessed or reassessed for any period u/s.33 or section 35 less any sum already paid by the dealer in respect of such period,

(iii) assessed under sub-sec.(3) of section 41, and

(b) the amount of penalty or interest or both (if any) levied u/s.36 or 37 and

(c) the sum (if any) forfeited to the State Government u/s.37, and

(d) the amount of fine (if any) imposed under sub-sec.(3) of section 53 and

[(e) any other dues under this Act:

Shall be paid by the dealer or the person liable therefore into a Government treasury within thirty days from the date of service of the notice issued by the Commissioner in respect thereof:

Provided that, the Commissioner may, in respect of any particular dealer or person and for reasons to be recorded in writing extend the date of payment or allow him to pay the tax or penalty or interest (if any) or the sum forfeited, by instalments but such extension or grant of instalment to pay tax shall be without prejudice to the levy of penalty, interest, or both;

provided further that, the Commissioner may, in respect of a dealer to whom an Eligibility Certificate has been granted extend the date of payments or grant a moratorium for payment of the dues or provide for payment of the dues thereafter in instalments, subject to such conditions as may be prescribed:

Provided also that, notwithstanding anything contained in this Act or in the rules made thereunder but subject to such conditions as the State Government or the Commissioner may by general or special order specify, where a dealer to whom incentive by way of deferment of sales tax or purchase tax or both under the 1979 Scheme, the 1983 Scheme or, as the case may be the Electronic Scheme falling under the Package Scheme of Incentives designed by the State Government or of the tax under the 1988 or the 1993 Package Scheme of Incentives designed by State Government have been granted by virtue of Eligibility Certificate, and where a loan liability equal to the amount of any such tax payable by such dealer has been raised by the SICOM or the relevant Regional Development Corporation or the District Industries Centre Concerned then such tax shall be deemed in the public interest, to have been paid.

Provided also that, notwithstanding anything to the contrary contained in the Act or in the rules or in any of the Package Scheme of Incentives or in the Power Generation Promotion Policy 1998, the Eligible Unit to whom an Entitlement Certificate has been granted for availing of the incentives by way of deferment of sales tax, purchase tax, additional tax, turnover tax or surcharge, as the case may be, may in respect of any of the periods during which the said certificate is valid, its option, prematurely pay in place of the amount of tax deferred by it an amount, equal to the net present value of the deferred tax as may be prescribed , and on making such payments, in the public interest, the deferred tax shall be deemed to have been paid.

(5)”

73. On the plain reading of above provisions of sec.38(1), (2),(3),(4), it provides the manner as to how the payment of tax, penalty and interest , as prescribed, may be made. The first proviso states that the Commissioner may in respect of any particular dealer or person for the reason to be recorded in writing extend the date of payment or allow him to pay such amount by instalments without prejudice to the levy of penalty, interest or both. The second proviso provides that commissioner may in respect of a dealer to whom and Eligibility Certificate has been granted extend the date of payments or grant a moratorium for payment of dues or provide instalments subject to such conditions as may be prescribed. The third proviso says that the State Government or the Commissioner may by general or special order where

a dealer to whom incentive by way of deferment of sales tax or purchase tax or both under 1979 scheme, 1983 scheme or 1988 scheme or the case may be electronic Scheme or 1988 scheme or 1993 packaging scheme of incentive, have been granted by virtue of Eligibility Certificate and where a loan liability equal to the amount of any such tax payable by such dealer has been raised by the SICOM or other designated authorities, then such tax has been deemed, in the public interest, to have been paid. The fourth proviso provides that where an Entitlement Certificate has been granted to the eligible unit for availing of the incentives by way of deferment of sales tax etc. such eligible unit may in respect of the periods during which the said certificate is valid, at its option, prematurely pay in place of the amount of tax deferred by it an amount equal to the **net present value** of the deferred tax as may be prescribed and on making such payments, in the public interest, the deferred tax shall be deemed to have been paid.(Emphasis supplied).

74. Here it is also considered necessary to take note of the dictionary meaning of the net present value (NPV).

75. According to Business Dictionary.com, submitted by the Id. DR, the definition of NPV reads as under :-

"Difference between the present value (PV) of the future cash flows from an investment and the amount of investment. Present value of the expected cash flows is computed by discounting them at the required rate of return (also called minimum rate of return). For example, an investment of \$1,000 today at 10 percent will yield \$1,100 at the end of the year; therefore, the present value of \$1,100 at the desired rate of return (10 percent) is \$1,000. The amount of investment (\$1,000 in this example) is deducted from this figure to arrive at NPV which here is zero (\$1,000-\$1,000). A zero NPV means the project repays original investment plus the required rate of return. A positive NPV means a better return, and a negative NPV means a worse return, than the

return from zero NPV. It is one of the two discounted cash flow (DCF) techniques (the other is internal rate of return) used in comparative appraisal of investment proposals where the flow of income varies over time.”[<http://www.businessdictionary.com/definition/net-present-value-NPV.html>]

According to Wikipedia the [present value](#) (PV) formula has four variables, each of which can be solved for:

$$PV = \frac{FV}{(1+i)^n}$$

1. PV is the value at time=0
2. FV is the value at time=n
3. i is the rate at which the amount will be compounded each period
4. n is the number of periods (not necessarily an integer)
5. Future value of a present sum

The [future value](#) (FV) formula is similar and uses the same variables.

$$FV = PV \cdot (1+i)^n$$

From the above definition and equation it is clear that the present value of a future sum is the same and if there is a difference i.e., positive NPV then the project repays original investment plus the required rate of return. In other words a positive NPV means a better return and negative NPV means a worse return, than the return from zero NPV meaning thereby the similar value of a future sum.

76. In the present case the assessee had collected total amount of Rs.7,52,01,378/- towards sales tax during the year 1989-90 to 2001-02. It was treated as a loan liability payable after 12 years in six annual/equal instalments and thus, the assessee treated the said liability as unsecured loans in its books of account.

77. Pursuant to the amendment made under sub-section(4) of section 38 of BST Act, 1959 by substituting the 4th proviso which provides for payment of Net Present Value (NPV) of deferred taxes under the package scheme of incentives which is as under :

“Provided also that, notwithstanding anything to the contrary contained in the Act or in the rules or in any of the Package Scheme of Incentives or in the Power Generation Promotion, Promotion Policy, 1998, the Eligible unit to whom an Entitlement Certificate has been granted for availing of the incentives by way of deferment of sales tax, purchase tax, additional tax, turnover tax or surcharge, as the case may be, may, in respect of any of the periods during which the said certificate is valid, as its option, prematurely pay in place of the amount of tax deferred by it an amount, equal to the net present value of the deferred tax as may be prescribed, and on making such payments, in the public interest, the deferred tax shall be deemed to have been paid.”

The State Govt. has by notification No.STR-12.02/CR-102/taxation-1 dated 16.11.2002, introduced Rule 31D in the Bombay Sales Tax Rules, 1959 (BST Rules) laying down the procedure for determination of such NPV. The procedure for determination of NPV of the amount of deferred taxes having been published, the Deferral Units may exercise the option under 4th Proviso of sub-section 4 of section 38 of the BST Act, 1959 of pre-maturely repaying at NPV, the amount of deferred taxes. The Rule 31D of the BST Rules has been provided with a table and the notes below it for determination of NPV. For example the payment of BST Rs.27,903/- and CST Rs.70,171/- due on 1.5.2003 was deposited on 30.12.2002 i.e. four months before the due date, the discounted percentage of deferred tax to be paid as NPV was prescribed in said table as 96.4955% and accordingly the NPV amount of BST and CST was worked out to Rs.26,925/ and Rs.67,712/- respectively as per certificate dated 27.12.2002 appearing at page 191 of assessee's paper book and the same was paid on 30.12.2002 as per certificate dated 25.8.2003

appearing at page 188 of assessee's paper book . This amount was paid by the assessee as per offer made by the State Govt. who appointed the State Industrial & Investment Corporation of Maharashtra Limited (SICOM) for settlement of deferred sales tax liability by an immediate one time payment. Accordingly the assessee has paid an amount of Rs.3,37,13,393/- to SICOM which according to the assessee represented the NPV as determined by SICOM. The payment was made to SICOM on 30.12.2002 as per certificates dated 25.8.2003 appearing at page 188 and 207 of assessee's paper book. The revenue has placed no material on record to show that the present value (NPV) of a future sum is not the same or in the process of calculation of present value of a future sum there is any conversion gain to the assessee. It is also not the case of the revenue that there is no such conversion provided under the BST Act, or the Table provided for determination of NPV is not applicable in the case of the assessee. In the absence thereof it is not possible for us to accept the contention of the Id. DR that there was a remission or cessation of the trading liability.

78. Now we shall refer to the cases decided by the Hon'ble Supreme Court and High Courts and relied on by the Id. DR and assessee's Counsel.

79. In Commissioner of Income-tax Vs Sahney Steel and Press Works Ltd. (1985) 44 CTR (AP) 243: (1985) 152 ITR 39(AP)(headnote):

"The assessee received refunds of sales tax on purchase of machinery and raw materials and on the sale of finished goods under a G.O. issued by the State Government of Andhra Pradesh. The G.O. had been issued with a view to speed up the industrial development of the State. The amount refunded had to be used specifically for development of the industry and could not be distributed as profits. The ITO assessed the receipts but the Tribunal held that the

development subsidy was in the nature of a capital receipt and it was not also assessable under s. 41(1). On a reference, it was contended on behalf of the assessee that the amounts were not of the nature of "income" at all and in any case it was a voluntary contributions:

Held, (i) that it was not necessary for a receipt to constitute income that it must necessarily be in the nature of return. It may be that there is no consideration for the benefits extended to the assessee in terms of the G.O. in the common law sense. But it cannot be said that it is an act of generosity on the part of the State. The State is interested in its industrial development; it wants to attract industries to enhance the employment potential, economic prosperity and the income of the State. It is to attract new entrepreneurs that the Government had come forward with the said incentives. The payments could not be considered to be voluntary contributions. The assessee and for that matter any other person setting up an industry in the State of Andhra Pradesh was entitled to the facilities and incentives provided by the said G.O. as a matter of right, which, if denied, he could enforce in a court of law. The fact that the Government reserved to itself the power to withdraw the G.O. or to amend it, did not mean that so long as the G.O. was in operation, the persons concerned did not have a right to enforce the same. The source as well as the payments were both certain and definite. The payments were inseparably connected with the business carried on by the assessee. The benefits were available only from the date the new industrial undertaking commenced production and for a period of five years therefrom. The refund or the subsidy, as it may be called, was dependent upon the industry continuing in production. There was no room or basis for disassociating the subsidy from the business of the assessee, inasmuch as the subsidy was given for development of the business and not for any other unrelated purposes. The payment was not a subsidy for setting up the plant but a subsidy given for the efficient and profitable running of the industry and its growth. The receipt was, therefore, of a revenue nature. All three items comprised in the payment constituted income of the assessee.

(ii) That the refunds of sales tax on purchase of raw materials and on sale of finished goods fell within s. 41(1) and were assessable as gains of business."

80. On further appeal before the Hon'ble Supreme Court in Sahney Steel and Press Works Ltd. Vs Commissioner of Income-tax (1997) 142 CTR (SC) 261: (1997) 228 ITR 253 (SC)(headnote pg-254) :

"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 shareholders. 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."

It has also been observed by Their Lordships (at placitum H page-267 of ITR) :

"In view of the aforesaid, it is not necessary to discuss the point relating to applicability of sec.41(1) of the Income tax Act, 1961 in this case."

81. In Commissioner of Income-tax Vs Ponni Sugars and Chemicals Ltd. (2008) 219 CTR (SC) 105: (2008) 306 ITR 392 (SC)(headnote pg-393) :

"The assessee was a co-operative society running a sugar mill. During the relevant year in question, on account of economic factors, it was not economically viable to run new sugar factories and, due to high financial costs, financial institutions did not come forward to advance loans to the entrepreneurs of new sugar factories. The tempo of establishing new sugar factories received a serious setback. A committee appointed by the Government recommended that five possible incentives for making a sugar plant economically viable could be provided for, viz., capital subsidy, larger percentage of free sale of sugar, higher levy sugar price, allowing rebate on excise duty and remission of

purchase tax. Following that report, schemes were formulated giving the following benefits : (i) incentive subsidy available only in new units and to substantially expanded units ; (ii) minimum investment for new units and expansion of existing units ; (iii) increase in free sugar sale quota. The benefit of the schemes had to be utilised only for repayment of loans. The Department and the High Court had held that the receipts from the Government under the incentive schemes were in the nature of revenue. On appeal to the Supreme Court :

Held, accordingly, reversing the decision of the High Court, on this point, that the main eligibility condition in the schemes was that the incentive had to be utilized for repayment of loans taken by the assessee to set up new units or for substantial expansion of an existing unit. The subsidy received by the assessee was not in the course of a trade but was of a capital nature.”

82. In *Dy. Commissioner of Income tax vs. Reliance Industries Ltd.* (2004) 82 TTJ (Mum)(SB) 765 : (2004) 88 ITD 273 (Mum)(SB) it has been held that the sales tax incentive given by Government of Maharashtra to assessee for setting up industries in notified areas in the form of exemption from liability to payment of sales tax for a period of 5 years with a view to being about necessary infrastructure in backward area, based on the amount of investment in fixed assets, is capital receipts not chargeable to tax.

83. *CIT vs. Reliance Industries Limited* (Bombay High Court) in Central Excise Appeal No.1299 of 2008 dated 15.4.2009 on the question of law (D) “Whether on the facts and in the circumstances of the case and in law the Hon’ble Tribunal was right in holding that sale tax incentive is a Capital Receipt?”, Their Lordships after considering the decision of the Special Bench of the Tribunal in *CIT vs. Reliance Industries Ltd.* (2004) 88 ITD 273 (Mum.) (SB) and the test as laid down by the Hon'ble Supreme Court in *CIT vs. Ponni Sugars and Chemicals Ltd.* (2008) 306 ITR 392

(SC) have held that the object of the subsidy was to set up a new unit in a backward area to generate employment, therefore, the subsidy is clearly on capital account.

84. In all the above cases relied on by both the parties the issue was whether the subsidy received by the assessee is capital receipt or revenue in nature. Whereas in the case before us the issue is entirely different i.e. the difference of deferred sales tax liability is chargeable to tax as business income u/s.41(1) being remission or cessation of trading liability or the same is exempt as capital receipt. Therefore, the above decisions relied on by the Id. DR are distinguishable and not applicable to the facts of the present case.

85. In *Polyflex (India) (P) Ltd. vs. CIT* (2002) 257 ITR 343 (SC) the facts in brief are that (headnote):

“In 1986 the assessee had paid excise duty on certain goods. Pursuant to the decision of the CEGAT a sum of Rs. 9,64,206 was refunded in September, 1988. Thereafter the excise department filed an appeal to the High Court and, on the appeal being dismissed, a petition for special leave to appeal to the Supreme Court ; but the fate of that petition was not known. For the assessment year 1989-90, the Assessing Officer brought to tax the amount by invoking section 41(1) of the Income-tax Act, 1961, but the appellate authority and the Appellate Tribunal held that there was no remission or cessation of trading liability so long as the petition for special leave to appeal was pending in the Supreme Court. The High Court, on a reference, held that the amount was assessable to tax but observed, on the basis of counsel’s argument, that the Tribunal ought to consider the question whether the excise duty was actually refunded to the assessee or not and pass proper orders in the light of its finding. The assessee preferred an appeal to the Supreme Court :

It has been held , affirming

"Held, affirming the decision of the High Court, that where a statutory levy is discharged by the assessee and subsequently the amount paid is refunded, it will be a case where the assessee "has obtained any amount in respect of such expenditure" within the meaning of section 41(1) of the Income-tax Act, 1961 ; it will not be a case of "benefit by way of remission or cessation" of a trading liability. Where expenditure is actually incurred by reason of payment of duty on goods and the deduction or allowance is given in the assessment of an earlier period, the assessee is liable to disgorge that benefit as and when he obtains refund of the amount so paid. Whether there is a possibility of the refund being set at naught on a future date is not a relevant consideration. Once the assessee gets back the amount which was claimed and allowed as business expenditure during an earlier year, the deeming provision in section 41(1) comes into play and it is not necessary that the revenue should await the verdict of a higher court or tribunal. If the higher court or tribunal upholds the levy at a later date the assessee is not without a remedy to get back the relief.

The correct way of understanding section 41(1) is to read the latter clause, "some benefit in respect of such trading liability by way of remission or cessation thereof" as a distinct and self-contained provision."

86. In Wolkem (P.) Ltd. Vs Commissioner of Income-tax (2003) 259 ITR 430 (Raj)(headnote pg-431):

"During the accounting year relevant for the assessment year 1986-87, the assessee-company received refund of excise duty amounting to Rs. 1,45,752. The assessee did not credit the said amount in the profit and loss account on the ground that the same was not taxable. It was contended that the amount collected by the assessee against the excise duty was credited to the suspense account as such it was not pertaining to the assessee and it was payable to the Central Excise Department and as such it did not constitute an income of the assessee under any provisions of the Income-tax Act. It was further submitted that part of the amount was due to different customers and as such it being a liability the addition was unjust. The Assessing Officer rejected the contention and this was upheld by the Tribunal. On a

reference a preliminary objection was raised on the ground that a similar question had been decided by the High Court :

Held, (i) that the view taken by the Division Bench of the court in the case of CIT v. Wolkem Pvt. Ltd. [1997] 228 ITR 129 was per incuriam as it was contrary to the three decisions of the Supreme Court and an earlier decision of the court.

(ii) That the amount which was collected by the assessee against the excise duty or the sales tax was on account of business and as such was a trading receipt. Thus, it would fall in the income of the assessee. A separate account would not change the character of the initial collection. The amount after collection had neither been refunded to the customers nor paid to the Government. The addition of Rs. 1,45,752 was justified."

87. In Commissioner of Income-tax Vs Abhishek Industries Ltd. (2006) 286 ITR 1 (P&H)(headnote pg-4):

"Held (ii) That the benefit under rule 4A of the Punjab General Sales Tax (Deferment and Exemption) Rules, 1991, accrued for a period of 10 years from the date of production and the quantum was fixed at 300 per cent. of the fixed capital investment for category A industries and 150 per cent. of the fixed capital investment for category B industries to be availed of within 7 years. Besides this, there was no other document or material to substantiate the assessee's contention that the sales tax subsidy of the kind under consideration should be treated as capital receipt and not a revenue receipt or to show that the kind of subsidy under consideration was given to the assessee for creation of capital assets as an aid to setting up of the unit. Rather, it was evident that the subsidy was an operational subsidy provided by the State after the industry had been set up and commenced commercial production. In the absence of material to show that the subsidy was to enable it to carry out capital investment it could not be presumed that such a subsidy was a capital subsidy."

88. In Mysore Thermo Electric (P.) Ltd. Vs Commissioner of Income-tax (1996) 221 ITR 504(Kar) (headnote pg-505):

"In the accounting years relevant to the assessment years 1976-77 to 1978-79, the assessee-company was engaged in the manufacture of battery separators. The excise authorities had levied certain dues on the assessees under the head of central excise, holding that they were liable to payment of this levy. According to the assessees, they had paid these amounts under dispute and since it was the contention of the authorities that central excise was payable on the goods, they had maintained a separate account for purposes of tendering these payments which in turn they recovered from the dealers to whom they supplied goods. According to the accounting procedure maintained by them, they desired that these amounts should not be mixed with their receipts or costs. This separate account therefore did not form part of the balance-sheet or profit and loss account and was maintained as a separate and individual head. The assessees having contested their liability as far as the levy of central excise duty was concerned in the court, and having been successful in their challenge, the authorities were directed to refund to them the aggregate amount paid under this head which the authorities did, by way of one lump sum repayment totalling Rs. 9,11,618 and the refund in question was made during the assessment year 1983-84. The assessees contended that this amount related to a separate account altogether; that they had at no point of time earlier claimed any deductions or allowances in respect of this amount, and hence, the amount was not assessable in their hands. The assessing authority accepted this position whereas, the Commissioner of Income-tax took the view that the provisions of section 41(1) of the Act would clearly apply and that, consequently, the amount was liable to be included in their taxable income. This was confirmed by the Tribunal. On a reference:

Held, that the Tribunal was justified in holding that the provisions of section 41(1) could be invoked to tax the refunds received during the accounting year relevant to the assessment year 1983-84 even when the part of excise duty was not claimed as expenditure in the profit and loss accounts of earlier years and the applicant had kept a separate account in respect of collection and payment of excise duty."

89. In *Express Newspapers Pvt. Ltd. Vs Commissioner of Income-tax* (1997) 227 ITR 325 (Mad) (headnote pg-326):

"In the course of the assessee's business as a dealer in shares, the assessee borrowed moneys from various sharebrokers. The interest provided for in the accounts in respect of such borrowals was claimed as a deduction and

was allowed as such in computing the income of the assessee in the earlier years. Subsequently, at the time of settlement of accounts with the sharebrokers, the amount due to them on account of interest was settled at a figure lower than the figure provided in the accounts. As a result, the amounts thus given up were written back in the accounts as income. These sums were brought to tax under section 41(1) of the Income-tax Act, 1961. This was confirmed by the Tribunal. On a reference:

Held, that there were two basic requirements for the application of section 41(1) of the Act. One was that there must be an allowance or deduction in the assessment for any year in respect of loss or expenditure or trading liability incurred by the assessee. The other was that subsequently during the previous year the assessee must have obtained either in cash or any other manner whatsoever an amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation, so that the remission or cessation so obtained on the value of the benefit accruing could be deemed the income of the assessee. The benefit could be by way of a book adjustment also. Admittedly though the assessee obtained benefit in the earlier years on account of the amount due to the sharebrokers in a larger amount, this was reduced to a considerable extent on account of subsequent settlement and consequently the accounts were also adjusted in this regard. It was not always necessary that the assessee should get benefit by way of cash for application of the provisions of section 41(1) of the Act. Since this was a trading liability, which was written back in the year under consideration, application of the provisions of section 41(1) was perfectly justified."

90. In Solid Containers Ltd. vs. DCIT and Another (2009) 308 ITR 417 (Bom) :

"The assessee had taken a loan of Rs. 6,86,071 for business purposes which was written back and directly credited to the reserves account, as a result of consent terms arrived at in a suit. The assessee claimed this amount as capital receipt, even though it had offered the interest on the said loan as its income by crediting the same to its profit and loss account. The Assessing Officer added the amount to the total income of the assessee as its income and this was upheld by the Tribunal. On appeal to the High Court :

Held, dismissing the appeal that it was a loan taken for trading activity and ultimately, upon waiver the amount was

retained in the business by the assessee. The amount had become the assessee's income and was assessable."

91. In CIT vs. T.V. Sundaram Iyengar & Sons Ltd. (1996) 222 ITR 344 (SC) :

"The Income-tax Officer found that for the assessment years 1982-83 and 1983-84, the assessee had transferred an amount of Rs. 17,381 to the profit and loss account of the company during the accounting period ended on March 31, 1982 (assessment year 1982-83), and an amount of Rs. 38,975 during the accounting period ended on March 31, 1983 (assessment year 1983-84). But these amounts were not included in the total income of the assessee. The sums were stated to be credit balances standing in favour of the customers of the company. Since these balances were not claimed by the customers, the amounts were transferred by the assessee to the profit and loss account. The Income-tax Officer was of the view that because the surplus had arisen as a result of trade transactions, the amounts had the character of income and had to be added as income of the assessee for the purpose of income-tax assessment. The additions were deleted by the Commissioner of Income-tax (Appeals), and this was upheld by the Tribunal.

Held, that if a commonsense view of the matter were taken, the assessee, because of the trading operation, had become richer by the amount which it transferred to its profit and loss account. The moneys had arisen out of ordinary trading transactions. Although the amounts received originally were not of income nature, the amounts remained with the assessee for a long period unclaimed by the trade parties. By lapse of time, the claim of the deposit became time-barred and the amount attained a totally different quality. It became a definite trade surplus. The assessee itself had treated the money as its own money and taken the amount to its profit and loss account. The amounts were assessable in the hands of the assessee."

92. In ACIT vs. Cosmo Films Ltd. (2009) 28 SOT 353 (Del.):

"8. In the course of assessment proceedings, it was noticed by the Assessing Officer that the sales tax deferral liabilities of Rs.532.82 lakhs was assigned by the assessee to one partnership firm, M/s. Gayatri & Annapurna (in short 'G&A') for a sum of Rs.131.41 lakhs, and the balance of Rs.401.41 lakhs was credited to the profit and loss account by the assessee company. In the original return of income filed by the assessee company, the amount so credited to the profit and loss account was offered as income being a part of the assessee's returned income. But later on, the assessee revised its return of income by excluding the said difference of Rs.401.41 lakhs on the ground that it was wrongly included. However, after considering the composition of partnership firm (Gayatri & Annapurna) and its relation to assessee company and other company of the same group, and after deliberating upon the agreement of assigning the deferred sales tax liability by the assessee to the said firm, the Assessing Officer has taken a view that discounting of liability was clearly on revenue account being covered by section 28 and also by section 41(1) of the Act, and the Assessing Officer, therefore, included the said amount in the total income determined in the assessment .

10. The CIT(A) deleted the addition and directed the Assessing Officer to amend the assessment to incorporate the additions to the extent of the amount corresponding to the payment made by M/s. Gayatri & Annapurna in the relevant year, over and above the discounted value."

The Tribunal has held vide para- 31 of 28 SOT 353 as under :-

31. To sum up we, therefore, hold that the Assessing Officer was justified in law as well as on facts in treating the sales tax deferred liability amounting to Rs.401.41 lakhs as profit and gain of business chargeable to income-tax as the income of the year under consideration in which such liability has been written off in the accounts and credited to the profit and loss account of the assessee inasmuch as the unilateral act of the assessee in writing off the said liability in its accounts by crediting the same to the profit and loss account is amounted to be a remission or cessation of the said liability within the meaning of section 41(1) of the Act read with Explanation 1 thereto.

93. In *Cartini India Limited vs. Income tax Officer* in ITA No.1051/Mum/2008 for the Assessment Year 2004-05 order dated 19.5.2009 the relevant facts are as under:

"The assessee company, during the previous year 1996-97, got registered under the 1988 package scheme of incentives as notified by the State Government of Maharashtra. Under the scheme, an eligible unit is allowed to defer the sales tax collections by converting the said sum into an unsecured loan repayable after the period of ten years from the date of conversion. It is pertinent to mention that the qualifying amount of the loan is based on the fixed capital investment in the eligible undertaking. The assessee company had applied for the benefit and was held to be entitled for the period from 1st of April 1996 to 30th of September 1997. Since the aggregate fixed capital investment of the assessee as per the certificate was Rs.12,625 thousand, as per the scheme, the assessee was entitled to defer the sale tax liability by converting it into an unsecured loan up to an amount not exceeding 15% of the capital invested, which worked out to Rs.18,93,750/-. During the year under appeal, the Government of Maharashtra introduced the "Prepayment of sales tax deferral scheme 2003", whereunder the eligible undertaking was permitted to prepay the loan amount at the rate of "Net Present Value", repayable at a future date. Taking the benefit of the scheme, the assessee company prepaid the liability and availed remission of Rs.5,48,517/-. The Assessing Officer considered the remission of the liability of Rs.5,48,517/- assessable under section 41(1) of the Income Tax Act, 1961. The CIT(A) has confirmed the action of the Assessing Officer.

It has been held by the Tribunal (para-11):-

"....We are therefore of the considered view that if the assessee has been allowed a deduction in respect of the sales tax liability, in the year the same was allowed to be converted into a loan, then the amount remitted out of that would be liable to tax in the year of remission. Though it has been stated by the CIT(A) that the assessee has been allowed a deduction in the year of liability / collection, yet in the interest of justice, we would like to restore this issue to the file of the Assessing Officer, for the limited purpose of verification in so far as in our view the assessee might have claimed the benefit of exemption or deduction on account of the establishment of industrial unit in the year of liability. Therefore, the condition of grant of deduction to the assessee in respect of sum of Rs.5,48,517/- in earlier year deserves to be verified and issue to be decided accordingly. In case it is

found that no deduction was allowed to the assessee under section 43B of Rs.5,48,517/- in earlier year(s), the addition shall stand deleted.”

94. Whereas in the case before us the entire loan amount which was payable after 12 years in six equal instalments was repaid as per present NPV as prescribed by the State Govt. and no refund was received by the assessee, therefore, the assessee did not get any benefit in respect of such trading liability by way of remission or cessation thereof, and, therefore, the decisions relied on by the Id DR are distinguishable and not applicable to the facts of the present case.

95. In the following cases it has been held that sec.41(1) is not applicable.

96. In Mahindra and Mahindra Ltd. vs. Commissioner of Income-tax (2003) 261 ITR 501(Bom.) it has been observed and held (headnote pg-502) :

“The assessee manufactured jeeps. The assessee filed its return for the assessment year 1976-77. In Part III of the return, the assessee showed an amount of Rs. 57,74,064 as cessation of its liability towards the American company. The Income-tax Officer came to the conclusion that with the waiver of the loan the credits represented income and not a liability. Accordingly, the Assessing Officer held that the sum of Rs. 57,74,064 was taxable under section 28 of the Income-tax Act, 1961. The Commissioner (Appeals) held that the sum of Rs. 57,74,064 was taxable as income under section 28(iv) of the Act as such benefit was obtained in the course of business and the monetary value of that benefit was income. Alternatively, the Commissioner (Appeals) took the view that the waiver of the loan amount of Rs. 57,74,064 amounted to remission of trading liability and, consequently, the said amount was taxable under section 41(1). According to the Tribunal, section 28(iv) was not applicable because benefit of waiver was not received by the assessee in kind. The Tribunal further took the view that even section 41(1) of

the Act was not applicable because there was no cessation of trading liability. On a reference :

Held, (i) that there were two important facts which had been overlooked by the Assessing Officer. Firstly, the assessee continued to pay interest at 6 per cent. for a period of ten years on the loan amount. The agreement for purchase of toolings was entered into much prior to the approval of the loan arrangement given by the Reserve Bank of India. Therefore, the loan agreement, in its entirety, was not obliterated by such waiver. Secondly, the purchase consideration related to capital assets. The toolings were in the nature of dies. The assessee was a manufacturer of heavy vehicles and jeeps. It required these dies for expansion. Therefore, the import was that of plant and machinery. The consideration paid was for such import. In the circumstances, section 28(iv) was not attracted. Lastly, the principal amount of loan had been forgone as a part of takeover arrangement to which the assessee was not a party. The waiver of the principal amount was unexpected. In the circumstances, such waiver would not constitute business income.

(ii) That in order to apply section 41(1), an assessee should have obtained a deduction in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee. The assessee had not obtained such allowance or deduction in respect of expenditure or trading liability. The assessee had paid interest at 6 per cent. over a period of ten years on Rs. 57,74,064. In respect of that interest, the assessee never got deduction under section 36(1)(iii) or section 37. In the circumstances, section 41(1) of the Act was not applicable. Secondly, even assuming that the assessee had got deduction on allowance section 41(1) was not applicable because such deduction was not in respect of loss, expenditure or trading liability. Lastly the toolings constituted capital assets and not stock-in-trade. Therefore, taking into account all the above facts, section 41(1) of the Act was not applicable."

97. In CIT vs. Tosha International Ltd. (2009) 176 Taxman 187 (Del.): the Assessee was engaged in the manufacturing of black and white picture tubes. The assessee-company ran into huge losses and it ultimately became a sick company and registered with the BIFR. Under the one time settlement scheme, the financial institutions and banks required the assessee to pay 60% of the amount due towards principle and waived the entire interest payment. There is no dispute with regard

to the waiver of interest payment. The only objection raised by the Assessing Officer is with regard to the waiver of the principle amount to the extent of Rs.10,47,93,857/- which the assessee had directly credited to the capital reserve account. According to the Assessing Officer the assessee had derived benefit on the basis of either depreciation or utilising the working capital which would have formed part of the earlier years income. According to the Assessing Officer since the loans ceased to exist, this amounted to cessation of liability and, therefore, it has to be treated as an income. Consequently, the Assessing Officer added the said sum of Rs.10.47 crores in the income of the assessee. On appeal the CIT(A) and the Tribunal following the decision in Mahindra and Mahindra Ltd. vs. CIT (2003) 261 ITR 501(Bom.) deleted the addition made by the Assessing Officer. On further appeal by the revenue the Hon'ble High Court did not interfere with the conclusion of the Tribunal and upheld the order passed by the Tribunal. On further appeal before the Hon'ble Supreme Court Their Lordships dismissed the Department's special leave petition against the judgment dated 23.9.2008 of the Delhi High Court in ITA No.1143 of 2008 whereby the High Court following 261 ITR 501 upheld the order of the Tribunal holding that as the assessee had not got any deduction on account of acquisition of capital assets as it had been reflected in the balance-sheet and not in the profit and loss account and the remission of the principal amount of loan obtained from the bank and financial institution had not been claimed as expenditure or trading liability in any earlier year, section 41(1) was not applicable and that the assessee company had either shown the waiver of interest as income or had not claimed it as expenditure in the computation of income filed before the lower authorities. CIT vs. Tosha International : SLP (Civil) No.18699 of 2009.[(2009) 319 ITR 7 (St.)].

98. In S.I. Group India Ltd. (formerly known as Schenectady Specialities Asia (P) Ltd.) vs. ACIT (2010) 326 ITR 117 (Bom.) the brief

facts of the case are that the assessee has an industrial unit in the district of Raigad which is a notified backward area. The Government of Maharashtra issued a package scheme of incentives in 1993 by which a scheme for the deferral of sales tax dues was announced. The assessee during the period 1 May 1999 and 31 March 2000 collected an amount of Rs.1,79,68,846/- towards sales tax. Under the scheme the amount was payable in five annual instalments commencing from April 2010 and the liability was treated as an unsecured loan in the books of account of the assessee. The State Industrial and Investment Corporation of Maharashtra Limited (SICOM) offered to the assessee an option for the settlement of the deferred sales tax liability by an immediate one time payment. The assessee paid an amount of Rs.50,44,280/- to SICOM which according to the assessee represented the net present value as determined by SICOM. The payment was made by the assessee to SICOM on 26 June 2000. The difference between the deferred sales tax and its present value amounting to Rs.1.29 Crores was treated as a capital receipt and was credited in the books of the assessee to the capital reserve account. The Assistant Commissioner of Income tax, Range 3(3), in the assessment order for Assessment Year 2000-01 brought the aforesaid difference of Rs. 1.29 Crores to tax under section 41(1) of the Act. The appeals filed by the assessee were dismissed by the CIT(A) as well as Tribunal.

On further appeal it has been held (head note at page-118 of 326 ITR):

"Held, allowing the appeals, that the Sales tax Tribunal was of the view that the decision of the assessing authority and the Deputy Commissioner of Sales Tax not to give credit to the payment made to SICOM would have to be upheld, but left it open to the assessee to procure a valid document under the scheme which would be "considered for the relevant period for the relevant deferred amount". The net result of the order of the Sales Tax Tribunal was to uphold the decision of the assessing authority declining to grant credit of the payment made by the assessee to SICOM towards discharge of the deferred sales tax liability. As a matter of fact, a notice of demand was issued under section

38 of the Bombay Sales Tax Act of 1959 to the assessee in the total amount of Rs.1,33,13,555. Having regard both to the order passed by the Sales Tax Tribunal and the notice of demand, it was not possible for the court to accept the contention that there was a remission or cessation of liability. The record before the court did not disclose that there was a remission or cessation of liability, one of the requirements spelt out for the applicability of sec. 41(1)(a). It was not necessary for the court to address itself to the wider issue as to whether the assessee, in paying the net present value of the deferred sales tax liability should be regarded as having obtained any benefit within the meaning of clause (a) of sub-section (1) of sec.41. This issue was kept open to be adjudicated upon at the appropriate stage in appropriate proceedings."

99. In DCIT vs. Sterlite Optical Technologies Ltd. and vice versa in ITA No.7136/and 7177/Mum/2004 for Assessment Year 2001-02 dated 8.1.2008 reported in (2008) 2 ITATINDIA 184 (Mum.) the brief facts are that the assessee has an industrial unit in Aurangabad district which is a notified backward area eligible to Sales tax Deferral Scheme . In this scheme, sales tax collected was deemed to have been paid to the sales tax authorities and thereafter deemed to be received from SICOM by way of a loan. The assessee company approached SICOM for pre-poning the payment of loan liability at discounted rate and vide letter dated 28.3.2001 SICOM intimated the assessee that the Govt. of Maharashtra had decided to offer discounted rate of 11.52% per annum for pre-mature repayment of loan availed by the unit. Therefore, against the liability of Rs.17,52,84,000/- the discounted rate of 11.52 percent per annum was offered and the repayment Schedule at the current discounted value was worked out at Rs.10,15.75,307/- yielding a saving of Rs.7,37,08,693/- . The Assessing Officer treated the concession granted to the assessee company by SICOM as a sales tax subsidy and taxed the same u/s.41(1) of the Act. On appeal the Id. CIT(A) after taking into consideration the ratio of the decision of Special Bench in the case of Reliance

Industries(2004) 88 ITD 273 (Mum.)(SB) held that the benefit available to the assessee is on account of concession given by the Govt. is on account of capital receipt, therefore he deleted the addition made by the Assessing Officer. On further appeal by the revenue to the Tribunal, the Tribunal after considering the decision in the case of Sahney Steel and Press Works supra, has held vide para 10.4 of the order as under :

"10.4 From the above observations of the Hon'ble Supreme Court, it is very clear that even the sales tax refund can be treated as a capital receipt in the hands of an assessee provided the same is granted to meet directly or indirectly the capital cost on the fixed assets and to help the entrepreneur in the establishment and expansion of the Industrial Unit. Thus, where the subsidy or incentive given by the government for acquisition of an asset or for buying any new assets for completion of the project, such subsidy would be of capital nature. The Special Bench of the Tribunal in the case of Reliance Industries (supra) has considered similar views of Maharashtra Scheme and had also made a comparative analysis of Andhra Pradesh scheme and Maharashtra scheme. The judgment of the Apex Court in Sahney Steel and Press Works was also taken into consideration and then after analyzing all the material, it was found that the benefit availed by the assessee was on account of capital receipt. It has been categorically held that sales tax incentive given by Maharashtra government for setting up industrial unit in the notified areas with a view to bring about the necessary infrastructure in the backward areas, is a capital receipt not chargeable to tax. The deferral benefit received by the assessee has also resulted ultimately in the form of partial exemption for sale tax liability and the said exemption was provided under an identical incentive scheme of Maharashtra government. Therefore, the benefit availed by the assessee has to be held as capital receipts not chargeable to tax."

100. In ACIT vs. M/s. Associated Capsules Pvt. Ltd. in ITA No.4818/Mum/08 for Assessment Year 2004-05 dated 20.10.2009 the Tribunal following the decision in the case of Sterlite supra, decided the issue in favour of the assessee and dismissed the ground raised by the revenue.

101. In Everest Industries Ltd. vs. ACIT in ITA No.814/Mum/2007 for the Assessment Year 2003-04 order dated 4.12.2009 the Tribunal

following the decision in the case of Sterlite supra, decided the issue in favour of the assessee.

102. In Cipla Investments Ltd. vs. ITO (2009) 33 SOT 317(Mum)(headnote):

“The assessee had taken an unsecured loan for investment in shares from its holding company and same could not be paid due to losses. The holding company had written it off as irrecoverable from the assessee, whereas, the assessee has not written back the said amount as cessation of liability u/s.41(1). Subsequently, the assessee company was dissolved. The Assessing Officer made additions to the income of the assessee of loan liability as income u/s. 41(1). The Commissioner (Appeals), while accepting that provisions of section 41(1) did not apply, held that provisions of sec. 28(iv) would apply and made additions to the profits and gains of business of the assessee on account of cessation of liability.

On Second appeal

The facts of the instant case indicated that the holding company had advanced funds to the assessee company in 1998 which was received as share application money, and later on transferred to unsecured loan. The amounts were utilised in investments and the incomes thereon were offered under the head ‘Capital gains’ and not as ‘Business income’. As was rightly held by the Commissioner (Appeals), provisions of section 41(1) invoked by the Assessing Officer did not apply. For attracting the provisions of section 41(1), the first requisite condition to be satisfied is that the assessee should have got the deduction or benefit or allowance in respect of loss, expenditure or trading liability incurred by it and, consequently, during any previous year, the assessee should have received any amount in respect of such loss, expenditure or trading liability by way of remission or cessation thereon. The remission would become income only when the assessee has claimed deduction earlier. In the instant case, the assessee had not got any deduction on account of acquisition of capital assets as the same had been reflected in the balance sheet and not in the profit and loss

account and hence, applicability of provisions of section 41(1) was not there. The Commissioner (Appeals)'s order to that extent was correct both on facts and on law. However, he had wrongly invoked the provisions of section 28(iv). It was the contention of the assessee that it had not done any trading activity nor shown any income as business income on the investments made. The finding of the Commissioner (Appeals) that the amount was received in the course of its business was against his finding given while considering the addition under section 41(1). The assessee's business activity might comprise investment in shares and securities, but as far as computation of income was concerned, the profit and loss in those transactions was said to be under the head 'capital gains' and not under 'Business income'. Hence, the gain earned by the assessee in the course of business in investment and advancement of loans was in the capital field but could not be on the revenue field. It had been held in catena of decisions that remission of a debt by the holding company which was not claimed and allowed as a deduction in any manner in any earlier previous year could not be brought to tax either under section 41(1) or under section 28(iv). There was no benefit or perquisite arising to the assessee in that regard. Moreover, the assessee had to write off the amount in the books of account and the amount was still outstanding at the end of the year. The loans availed for acquiring the capital asset, i.e., shares, when waived could not be treated as assessable income for invoking the provisions of section 28(iv). Since the original receipt was undoubtedly on account of capital nature, its waiver did not have the quality of changing the same into a revenue receipt. In view of those facts and also various principles laid down in the case laws relied upon by the assessee, it was opined that the Commissioner(Appeals) erred in treating the amount as taxable income in the hands of the assessee under section 28(iv). On the facts of the instant case, the provision of section 28(iv) did not apply and the amount was not taxable under the provisions of the Act. Accordingly, the assessee's grounds were allowed. The Assessing Officer was directed to delete the amount."

103. In Accelerated Freez & Drying Co. Ltd. vs. DCIT (2009) 31 SOT 442(Cochin)(headnote) :

The assessee –company was engaged in the business of sea food exports. It had availed term loans from three banks for the purpose of acquiring capital assets necessarily to be deployed in its manufacturing system. The assessee – company became defaulter in making the repayments of term loans along with interest due to its bad financial position. Under a scheme framed by the RBI known as 'One Time Settlement Scheme', the assessee reached an agreement with those banks for One Time Settlement (OTS) of the outstanding liabilities due to those banks in the previous year under appeal. The total loan that remained payable to the banks amounted to Rs.3486.03 lacs. The loans were settled forever on payment of Rs.2450 lacs and thereby the assessee company obtained the benefit of waiver of term loans amounting to Rs.10.36 crores. This loan amount waived off by banks was credited by the assessee in the general reserve account. For the relevant assessment year, the assessee claimed that the waiver amount was not taxable in its hands inasmuch the said amount could not be treated as its income either under section 28(iv) or under section 41(1). The Assessing Officer did not agree with the assessee and brought the said amount to tax under section 28(iv). On appeal, the Commissioner (Appeals) held that section 28(iv) enables the Assessing Officer to charge the value of benefits or perquisite to tax and, therefore, the waiver amount received by the assessee was rightly brought to tax under section 28(iv).

Held

It is a trite law that the nomenclature given by an assessee to a particular account in its books of account is not the sole test to decide the real character of that account. Therefore, the fact that the assessee had credited the loan waiver amount in its general reserve amount would not influence the process of determining the exact nature of the issue.

Section 28(iv) seeks to charge the value of any benefit or perquisite, whether convertible into money or not, arising from business or the exercise of a profession, as profits and gains of business or profession. Therefore, what is to be examined is whether the waiver of loan would amount to a perquisite so as to be taxable, as such, under section 28. The Bombay High Court in the case of Mahindra and Mahindra Ltd. Vs. CIT (2003) 261 ITR 501/128 Taxman 394,

has explained that section 28(iv) seeks to charge the value of any benefit or perquisite, meaning thereby that the benefit must be in kind; the Court further held that waiver of loan is in respect of money transaction and, therefore, would not be in nature of any benefit or perquisite as construed in section 28(iv).

For the purpose of section 28(iv), the loan waiver amount credited by the assessee in its general reserved account was covered by the judgment of the Bombay High Court in the case of Mahindra & Mahindra Ltd.(supra) and, therefore, the said waiver amount could not be held as taxable.

104. Having regard to the aforesaid law laid down by the Hon'ble Supreme Court and High Courts, we find that to invoke the provisions of section 41(1) of the Act, the first requirement is as to whether in the assessment of the assessee, an allowance or deduction has been made in respect of loss, expenditure or the trading liability incurred by the assessee. In the case of the present assessee the revenue's plea is that the assessee has obtained the benefit of deduction of sales tax liability u/s. 43 B of the Act as per CBDT Circular No. 496 dated 25.9.1987. However, we find that in the said circular it has been clearly stated vide para 5 that "...the statutory liability shall be treated to have been discharged **for the purposes of Section 43 B**"(emphasis supplied). Thus, the benefit of deduction was allowed for the purpose of section 43 B of the Act only and not under any other provisions of the Act. There is no dispute that the Assessing Officer has also applied the aforesaid Board Circular while giving the benefit of deduction u/s. 43 B of the Act. It is settled law that the circulars are binding on the department vide number of decisions of the Hon'ble Apex Court [see in Navnit Lal C. Jhaveri vs. K.K. Sen, AAC (1965) 56 ITR 198(SC), Ellerman Lines Ltd. Vs. CIT (1971) 82 ITR 913 (SC), K.P. Varghese Vs. ITO (1981) 131 ITR 597 (SC) and UCO Bank Vs. CIT (1999) 237 ITR 889 (SC)]. It is also settled law that the Court cannot add words to statute or read words into it which are not

there vide Union of India vs. Deoki Nandan Aggarwal (1992) Supp. 1 SCC 323 (80). The similar view has been reiterated recently in CIT vs. Tara Agencies (2007) 292 ITR 444 (SC). This being so we are of the view the first requirement of section 41(1) has not been fulfilled in the facts of the present case.

105. The other requirement of section 41(1) is that the assessee must have subsequently (i) obtained any amount in respect of such loss and expenditure or (ii) obtained any benefit in respect of such trading liabilities by way of remission or cessation thereof. In the case before us we find that the sales tax collected by the assessee during the years 1989-1990 to 2001-2002 amounting to Rs.7,52,01,378/- was treated by the State Government as a loan liability payable after 12 years in six annual/ equal instalments. Subsequently pursuant to the amendment made in the fourth proviso to section 38(4) of the BST Act, 1959 which provides that where an Entitlement Certificate has been granted to the eligible unit for availing of the incentives by way of deferment of sales tax etc. such eligible unit may in respect of the periods during which the said certificate is valid, at its option, prematurely pay in place of the amount of tax deferred by it an amount equal to the net present value of the deferred tax as may be prescribed and on making such payments, in the public interest, the deferred tax shall be deemed to have been paid. In the case before us the assessee has opted the offer of SICOM, an implementing agency of the State Government and repaid an amount of Rs.3,37,13,393/- to SICOM which according to the assessee represented the NPV of the future sum as determined and prescribed by SICOM. The said payment was made to SICOM on 30.12.2002 as per certificates dated 25.08.2003. It has already been demonstrated in para- 74 of this order that NPV is equivalent to Future Value of the sum. In other words, what the assessee was required to repay after 12 years in six annual/ equal instalments, the same was repaid by the assessee, in the public interest,

as NPV is equivalent to the Future Value of the sum. Further there is no iota of evidence to show that there has been any remission or cessation of liability by the State Government. Thus, one of the requirements spelt out for the applicability of section 41(1)(a) has not been fulfilled in the facts of the present case.

106. Alternatively, it was argued on behalf of department that the assessee was required to comply with procedure laid down in clauses 6.21 and 6.22 of the State Government Resolution. According to the Id. DR the assessee has admittedly, failed to do so. Therefore the question of conversion of deferred sales tax liability into interest free loan does not arise. Further, there is no modified Eligibility Certificate incorporating the change from deferred sales tax liability to interest free loan. However, we find that the assessee on the basis of letter issued by SICOM to the sales tax authority has passed necessary entries in the books of account claiming the difference of deferral amount as capital receipt. Merely because if the sales tax authorities have not issued the modified Eligibility Certificate does not mean that the payment of Rs. 3,37,13,393/- made by the assessee cannot be accepted as having been paid at NPV of the future sum of Rs.7,52,01,378/- towards discharge of full liability. It is settled law that the law does not contemplate or require the performance of an impossible act-lex non cogit ad impossibilia, vide Life Insurance Corporation of India vs. CIT(1996) 219 ITR 410 (SC). Further both the parties have submitted and agreed during the course of their arguments that the entries recorded in the books of accounts are not determinative of the nature of transaction vide Tuticorin Alkali Chemicals And Fertilizers Ltd. vs. CIT (1997) 227 ITR 172 (SC). Even assuming for the sake of argument that the assessee did not get modified Eligibility Certificate or the repayment of loan paid by the assessee at its NPV of future sum, then in that circumstances, merely because the assessee has passed necessary

entires in its books of account, it cannot be held that there is any cessation or remission of liability.

107. The Id. DR has put great emphasis on the notes to the accounts which have been reproduced by us in para-43 appearing at page-43 of this order wherein the assessee itself has used the expression 'remission' of the loan liability. However, the position in law is well settled that making of an entry or absence of an entry cannot determine rights and liabilities of parties. In other words, if the law does not lead to incurring of a liability, or does not lead to a corresponding right to insist for discharging such a liability any accounting practice (even if suggested by the Institute of Chartered Accountants of India) cannot lay down anything to the contrary. As held by the Hon'ble Apex Court in the case of Tuticorin Alkali Chemicals and Fertilizers Ltd. vs. CIT (1997) 227 ITR 172 (page 183):

"It is true that this court has very often referred to accounting practice for ascertainment of profit made by a company or value of the assets of a company. But when the question is whether a receipt of money is taxable or not or whether certain deductions from that receipt are permissible in law or not, the question has to be decided according to the principles of law and not in accordance with accountancy practice. Accounting practice cannot override section 56 or any other provision of the Act As was pointed out by Lord Russell in the case of B. S. C. Footwear Ltd. [\[1970\] 77 ITR 857](#), 860 (CA), the income-tax law does not march step by step in the footprints of the accountancy profession."

108. We have also examined this issue from another angle in the light of Indian Contract Act, 1872. Chapter IV deals with the performance of contracts. Section 63, which has been placed in Chapter IV, reads as under:

“Section 63. Promisee may dispense with or remit performance of promise. — Every promisee may dispense with or may remit, wholly or in part, the performance of the promise made to him, or may extend the time for such performance, or may accept instead of it any satisfaction which he thinks fit.

Illustrations

- (a) A promises to paint a picture for B. B afterwards forbids him to do so. A is no longer bound to perform the promise.
- (b) A owes B 5,000 rupees. A pays to B, and B accepts, in satisfaction of the whole debt, 2,000 rupees paid at the time and place at which the 5,000 rupees were payable. The whole debt is discharged.
- (c) A owes B 5,000 rupees. C pays to B 1,000 rupees, and B accepts them, in satisfaction of his claim on A. This payment is a discharge of the whole claim.
- (d) A owes B, under a contract, a sum of money, the amount of which has not been ascertained. A, without ascertaining the amount, gives to B, and B, in satisfaction thereof, accepts, the sum of 2,000 rupees. This is a discharge of the whole debt, whatever may be its amount.
- (e) A owes B, 2,000 rupees, and is also indebted to other creditors. A makes an arrangement with his creditors, including B, to pay them a composition of eight annas in the rupee upon their respective demands. Payment to B of 1,000 rupees is a discharge of B's demand.”

The above clearly shows that promisee may, inter alia, remit part of the promise or whole of the promise and even then the contract can be said to have been preformed. For example, illustrations (b) and (c) clearly show that when a large amount was due and only a smaller amount was paid, then, in view of the remission of the balance amount, the contract can still be said to have been performed and such debt would stand discharged. In the Commentary by Pollock & Mulla, Thirteenth Edition on Indian Contract Act, the Learned Authors have observed at pages 1267 & 1268 as under:

"This section does not apply to cases where the whole contract has been supplanted by a new one, but to cases where the old contract subsists, and there is a voluntary remission of performance of some promise in it, for example, the remission of part of the debt at the time it becomes payable. It does not cover a case of a binding promise to dispense with or remit performance in the future unless that waiver is made the subject of a fresh contract. Section 63 applies whether there is actual remission, ie, *in praesenti* and *in futuro*, ie, not a mere promise to remit, an agreement to remit *in futuro* clearly requires consideration, if it is to be a binding contract. This must be distinguished from a remission or dispensation which is made contingent on the happening of a future event. In such a case the remission is *in praesenti*, though it is suspended until the event occurs. The holder of a promissory note from the officers of a masonic lodge agreed in writing to make no claim 'if the... lodge building which has been burnt down is resuscitated.' He could not sue on his note after the lodge was rebuilt. It would be monstrous if he could. However, a conditional remission is not enforceable under the section, as when conditional, it is not an absolute remission and the plaintiff is not estopped from enforcing his rights in full. Where the promisee wishes his rights to continue in the event of some conditions simultaneously imposed on the promisor, he must see that the release is made dependent on the performance by the promisor of his part of the agreement."

The above again shows that remission is possible only in praesenti and not in future.

Now coming back to the case before us, the assessee was liable to pay sales tax amounts collected from 1.11.1989 to 31.10.1996, payments of which were deferred under the scheme, and the amounts were payable after twelve years in six equal annual instalments commencing from 1.05.2003, which means that the liability was payable in future. Later on, the State Government came with a scheme by which it was provided that if some dealer opts, then they could pay the future liability at a

discounted value or what we may call net present value immediately. Thus, in this situation, it cannot be construed as remission of liability; because the State Government has not waived any of the liability as given in the illustrations. Had the State Government accepted lesser amount after twelve years or reduced such instalments, then it could have been a case of remission or cessation. However, in the case before us the State Government has chosen to receive the money immediately which was receivable from 1.05.2003 to 1.05.2008. The amount of Rs.3,37,13,393/- was actually paid to SICOM on 30.12.2002. Thus, the amount which was payable from 1.05.2003 to 1.05.2008, has been paid on 30.12.2002. Thus, it does not satisfy the condition of actual remission in praesenti as opined by the Learned Authors in the above commentary. It is a simple case of collecting the amount at net present value which is due later on and even the formula for collecting the net present value was also given by the SICOM and the amounts have been paid as per that formula. Therefore, such payment of net present value of the future liability cannot be, in our opinion, classify as remission or cessation of the liability so as to attract the provisions of section 41(1)(a) of the Income Tax Act, 1961. We are fully conscious that issue before us is regarding statutory liability and the above discussion and the provisions of the Indian Contract Act referred to by us in the above para relate to contractual liability. However, we have referred to these provisions just to understand the meaning of the expression "remission" for the purpose of deciding the

case before us under the Income Tax Act and our decision is based on the provisions of the Income Tax Act, 1961.

109. For the reasons as stated above, we hold that the deferred sales tax liability Rs.4,14,87,984/- being the difference between the payment of net present value Rs.3,37,13,393/- against the future liability of Rs.7,52,01,378/- credited by the assessee under the capital reserve account in its books of account is a capital receipt and cannot be termed as remission/cessation of liability and consequently no benefit has arisen to the assessee in terms of sec.41(1)(a) of the Income Tax Act, 1961. Accordingly, the modified question as framed in para-5 of this order is answered in favour of the assessee and against the revenue.

110. The matter will now go before the regular Bench for disposing of the appeals keeping in view our decision rendered hereinabove.

111. Before parting with this order we desire to place on record our deep appreciation to both the parties for assisting the Bench.

Order pronounced in the open court on 10.11.2010.

Sd/-

(T.R. SOOD)

ACCOUNTANT MEMBER

Sd/-

(R.V.EASWAR)

PRESIDENT

Sd/-

(D.K.AGARWAL)

JUDICIAL MEMBER

Mumbai, Dated:10.11.2010.

Jv.

Copy to: The Appellant
The Respondent
Intervener
The CIT, Concerned, Mumbai
The CIT(A) Concerned, Mumbai & Pune.
The DR " E " Bench

True Copy

By Order

Dy/Asstt. Registrar, ITAT, Mumbai.