Commissioner Of Income Tax vs Sdb Infrastructure Private Ltd on 29 November, 2016

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FORM NO.(J2)

                         IN THE HIGH COURT AT CALCUTTA
                        SPECIAL JURISDICTION (INCOME TAX)
                                 ORIGINAL SIDE


Present:
Hon'ble Chief Justice Girish Chandra Gupta
And
Hon'ble Justice Arindam Sinha

                           ITA No.233 of 2009

                     COMMISSIONER OF INCOME TAX
                             Versus
                     SDB INFRASTRUCTURE PRIVATE LTD.

                                 Advocate for the Appellant: Md. Nizamuddi
                                                             Ms. Smita Das D
                     Advocate for the Respondent :Mr. N. K. Poddar, Sr. Ad
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Mr. Ashoke Gupta, Adv.

Hearing concluded on: 11.11.2016 Judgment delivered on: 29.11.2016 GIRISH CHANDRA GUPTA, C.J.:- The appeal and the cross objection are directed against a judgement and order dated 27th March, 2009 by which the learned Income Tax Appellate Tribunal partly allowed an appeal preferred by the assesse registered as ITA No.235/Kol/2007 and dismissed a cross objection registered as ITA No.440/Kol/2007 preferred by revenue both pertaining to the assessment year 2003-04. The facts and circumstances of the case briefly stated are as follows:-

> The assesse had entered into a contract dated 21st August, 1985 with the republic of Iraq, Ministry of Local Government, Organisation for Water and Sewerage (Employer) Bagdad, Iraq for carrying out the civil construction works in respect of Hilla Water Supply Scheme and Left Bank Mosul Water Supply Scheme on deferred payment basis. While execution of the aforesaid projects was in progress, remittances from Iraq on account of project receivables were suddenly stopped since June, 1990 due to Gulf Crisis and sanctions, imposed by the United Nations against Iraq as on 31st March, 1991. US Dollars $86,69,772.20 in respect of Hilla Water Supply Scheme and US Dollars $1,43,74,818.40 in respect of Left Bank Mosul Water Supply Scheme aggregating to US Dollars $230,44,590.60 correspondingly a sum of Rs.45,05,21,747/- in Indian Currency were receivable by the assesse but nothing was recovered. The assesse wrote off the said sum of Rs.45,05,21,747/- during the assessment year 1995-96.

The stoppage of remittance from Iraq had not only affected the Indian Project Exporters but Exim Bank and other commercial banks, who had advanced credit facilities to the Indian Project Exporters against policies/counter-guarantees furnished by ECGC, were also affected. In order to resolve the deadlock, a group was constituted by the Government of India on 12th September, 2001 consisting of the representatives of Reserve Bank, Exim bank and ECGC to work out the modalities for the implementation of the decision of the Cabinet Committee on economic affairs relating to six projects executed by the Indian Project Exporters in Iraq including the assesse on deferred payment basis. Pursuant to the recommendations made by the group in its report dated 9th October, 2001, the project receivables were assigned by the assesse in favour of the President of India by and under two several Deeds of Assignment both dated 6th May, 2002. Consequent to such assignment, the Government of India issued and/or agreed to issue bonds for US Dollars $87,53,051.62 as certified by the Rafidain Bank, Iraq with respect to Hilla Water Supply Scheme and bonds for US Dollars $146,15,102.50 as certified by the Rafidain Bank, Iraq in respect of Left Bank Mosul Water Supply System. Rafidain Bank had certified in both the cases that the aforesaid sum in US dollars were payable to the assesse as on 30th September, 2001. The total sum of US Dollars $2,33,68,154.12 (87,53,051.62+146,15,102.50) included a sum of US Dollars $27,78,033.79 on account of interest according to the settlement of dues evidenced by the document appearing at page no. 49 of Volume 2 of the paper book which appears to have been issued by the Exim Bank, Mumbai.

From the Deeds of Assignment it appears that the assesse had originally agreed to accept the payment on deferred payment basis from the Iraq Govt. The agreements between the assesse and the foreign employer are not, however on the record. It has already been noticed that as on 31st March, 1991 US Dollars $2,30,44,590.60 were receivable by the assesse. Pursuant to the Deeds of Assignment dated 6th May, 2002, bonds for US Dollars $2,33,68,154.12 were received by the assesse. The assesse received an excess payment of US Dollars $3,23,563.52. The Assessing Officer was of the opinion that the US Dollars $27,78,033.79 were received by the assesse on account of interest.

Even assuming that the assesse was entitled to interest the undisputed fact is that US Dollars $3,23,563.52 were received by the assesse in excess of US Dollars $2,30,44,590.60 which were receivable as on 31st March, 1991.

Therefore, it follows that the project receivable as on 31st March, 1991 included an element of interest, if any, payable to the assesse. The assesse received additional US Dollars $3,23,563.52 with respect to which the views expressed by the learned Tribunal are as follows:-

"Further, there is also no dispute with regard to the balance project receivables in the aggregate sum of US $3,23,563.52 equivalent to Rs.63,25,667, which represented untaxed project receivables, and were not known to the assesse company earlier, on account of sudden abandonment of project activity in due to gulf war, and came to its notice only during the year under appeal on receipt of relevant information through the ECGC/Exim Bank/Rafidain Bank. The said sum of Rs.63,25,667 had also been shown by the assesse as its business income in the return filed for the assessment year 2003-04. The same has also been duly taxed by the AO, as business income, in the year under appeal."

The case of the assesse was as follows:-

(A) The sum of Rs.45,05,21,747/- written off on 31st March, 1995 was restored to the profit and loss account of the current year.

(B) US Dollars $3,23,563.52 received in excess were offered for taxation as a business receipt.

(C) The US Dollars $2,33,68,154.12 upon conversion in Indian Currency fetched a sum of Rs.83,59,80,000/-. After giving credit for a sum of Rs.45,05,21,747/- on account of money written of and a sum of Rs.63,25,667/- (equivalent to US Dollars $3,23,563.52) received in excess there remained a balance sum of Rs.37,91,32,586/- which was a long term capital gain.

The assesse, however contended that after indexation there was a long term capital loss of Rs.75,85,592/-. The aforesaid loss was arrived at as follows:-

COMPUTATION OF CAPITAL LOSS Rs. Rs.

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Exchange Fluctuation Gain                                      37,91,32,5

Add:   Amount  accounted  for   as 63,25,667
contract receipt in the year under
appeal including
                                   6246                        63,31,913
                                                               Rounding
                                              -----------      ----------
                                              ----------       ---------
                                                               38,54,64,5

Amount converted in US Dollars 80,54,001
@47.86= (38,54,64,500/47.86)
Value of US$ 80,54,001 as on
31.3.91   in    Rupee(80,54,001 X
19.55= 15,74,55,724)
INDEX VALUE - 15,74,55,724 - 182 x 447                         38,67,18,1

Less: Exchange Fluctuation Gain                                37,91,32,5

Long term Capital Loss
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75,85,592

> (D) The assessee contended that with respect to excess receipt of a sum of Rs.63,25,667/-. It was entitled to benefit under Section 80HHB.
>
> (E) There was another claim for deduction on account of bad debt of a sum of Rs.14,22,98,000/-.

The assessing officer was of the opinion that the deduction under Section 80HHB was not available to the assessee. The excess sum of Rs.37,91,32,586/- received by the assessee owing to fluctuation of exchange rates were on account of project receivables and, therefore taxable as revenue receipts. The claim for deduction on account of bad debt was disallowed by the assessing officer. In an appeal preferred by the assessee the CIT(A) reversed the order of the Assessing Officer rejecting the claim on account of bad debt of a sum of Rs.14,23,98,000/- . Rest of the order of the Assessing Officer was upheld by him. Against the order of the CIT(A), the revenue preferred an appeal against the order allowing the claim for bad debt. The assessee preferred an appeal against the order treating the receipt of the balance sum of Rs.37,91,32,586/- as a revenue receipt as also against the order refusing to allow deduction under Section 80HHB.

The learned Tribunal held that the excess sum of Rs.37,91,12,586/- received by the assessee was a capital gain and not a revenue receipt. The claim for deduction under Section 80HHB was rejected and the order allowing bad debt of a sum of Rs.14,22,98,000/- was upheld.

The revenue has come up in appeal.

The following substantial questions of law were suggested on 7th January, 2010 when the appeal was admitted.

> "(a) Whether on the facts and in the circumstances of the case the Tribunal was justified in law in deleting the addition of Rs.37,91,32,586/- with regard to the gain on account of exchange fluctuation in relation to foreign projects receivable from Iraq treating it, as Capital receipts and not revenue receipts as assessed by the assessing officer?
>
> (b) Whether on the facts and in the circumstances of the case the Tribunal was justified in law in deleting the addition on account of Bad Debt disallowed Rs.14,22,98,000/- despite the fact that the assessee failed to establish that it was engaged in the business of money lending during the year and also failed to fulfil the condition specified under Section 36(2) of the said Act?"

The assessee has filed a cross-objection and raised the following substantial questions of law:-

> "I. Whether the learned Tribunal misdirected itself in law and adopted a wholly erroneous approach in holding that the deduction under section 80HHB of the said

> Act, was not available to the Respondent/Assessee Company in respect of Rs.63,25,667/- realised by it in the form of Government of India Compensation Bonds, 2008 during the year under appeal?
>
> II. Whether the findings of the learned Tribunal to the effect that the Assessee Company did not comply with all the conditions laid down in Section 80HHB(3)(i) & (iii) of the said Act, are against the facts and evidences on record, based on irrelevant considerations, unreasonable and/or otherwise perverse?"

The learned Tribunal allowed the contention of the assessee that the excess sum received was a capital gain but did not examine the reasoning advanced by the assessing officer which was as follows:-

> "Without prejudice to the above, it may also be remarked here that the indexation carried out by the assesse while computing the Long Term Capital Loss is sans any basis. It is not at all clear as to how the assesse had taken a figure of Rs.15,74,55,724/- as the "cost of acquisition" of the "capital asset". It is beyond any comprehension as to how the assesse can attribute a "cost of acquisition" to a "capital asset" when there was no such capital asset as on 31.03.1991. Hence, even the determination of the Long Term Capital Los by the assesse has no basis at all and is, therefore, bad in law."

As a result the claim for long term capital loss put forward by the assesse was allowed without examining the views of the assessing officer. The questions which arise for determination are whether the excess sum received by the assessee is a revenue receipt as contended by the department or does it constitute a capital gain as contended by the assessee. In case the first question is answered against the revenue and in the negative the second question which arises for consideration is whether the long term capital loss computed by the assessee at a sum of Rs.76 lacs approximately is in accordance with law. For a satisfactory disposal of the appeal these two questions have to be considered. The other questions required to be considered are with regard to the allowability of claim for deduction on account of bad debt and the allowability of deduction under Section 80HHB.

Therefore, the questions for consideration are formulated as follows:-

> (a) Whether the sum of Rs.37,91,32,586/- received in excess on account of exchange gain is a revenue receipt or a capital receipt?
>
> (b) Whether the long term capital loss of Rs.75,85,592/- was computed in accordance with law?
>
> (c) Whether in the facts and circumstances of the case there was any cost of acquisition? If so what was that?

> (d) Whether in the facts and circumstances of the case the Tribunal was justified in law in upholding deletion of the addition on account of Bad Debt amounting to Rs.14,22,98,000/- despite the fact that the assesse, according to the revenue, had failed to establish that it was engaged in the business of money lending during the year and also, according to revenue, failed to fulfil the condition specified under Section 36(2) of the said Act?
>
> (e) Whether the learned Tribunal misdirected itself in law and adopted a wholly erroneous approach in holding that the deduction under section 80HHB of the said Act, was not available to the Respondent/Assessee Company in respect of Rs.63,25,667/- realised by it in the form of Government of India Compensation Bonds, 2008 during the year under appeal?
>
> (f) Whether the findings of the learned Tribunal to the effect that the Assessee Company did not comply with all the conditions laid down in section 80HHB(3) (i) & (iii) of the said Act, are against the facts and evidences on record, based on irrelevant considerations, unreasonable and/or otherwise perverse?

The reasons assigned by the learned Tribunal for disallowing deduction under Section 80HHB are as follows:-

> (A) The bonds issued by the Reserve Bank of India did not constitute convertible foreign exchange.
>
> (B) Circular No.711 dated 24th July, 1995 issued by the CBDT does not cover the instant case and separate circular was required in respect of these bonds.
>
> (C) The assessee did not comply with the conditions laid down in Section 80HHB (3)(i) and (iii).

The view that the conditions laid down in Sub-Section 3(i) of Section 80HHB were not fulfilled is belied by the observation made by the Tribunal that "the assessee maintained separate project accounts in its books." There is no finding recorded anywhere either by the Tribunal or by the assessing officer or by the CIT(A) that the Auditors' Report verifying such project accounts was not furnished.

We are, as such unable to accept the contention that the conditions laid down in Clause (i) of Sub-section 3 of Section 80HHB were not fulfilled. The rest of the objections are squarely answered by the Circular No.711 dated 24th July, 1995 issued by the CBDT. The only question required to be considered is whether the circular dated 24th July, 1995 shall be applicable to the RBI Bond, 2008 issued in favour of the assessee.

The circular dated 24th July, 1995 bearing No.711 was issued by the CBDT in order to ease the hardship "faced by project exporters who have executed projects in Iraq." The circular does not refer to any particular bond. No reasons were advanced by the learned counsel appearing for the revenue to establish that the aforesaid circular could not cover the RBI Bond, 2008 issued in favour of the assessee.

We are, as such of the opinion that the circular was very much applicable to the bonds issued in favour of the assessee. The aforesaid circular in paragraphs 4 and 5 provided as follows:-

> "The Central Board of Direct Taxes have examined the matter in consultation with the Department of Economic Affairs. Since the payments received in the shape of bonds are in lieu of foreign exchange realisation from the project exports and the foreign exchange will eventually be repatriated into India by the EXIM Bank after the lifting of the U. N. sanction, the RBI/ECGC bonds issued by way of settlement of claims of projects in Iraq will be treated as convertible foreign exchange brought into India for the purposes of section 80HHB.
>
> The request for extension of the period of six months for bringing in convertible foreign exchange into India may be liberally allowed by the Chief Commissioner/Commissioner of Income-tax."

We are, as such, of the opinion that the deduction under Section 80HHB is admissible in this case. The question No. (e) is thus answered in favour of the assessee. In that view of the matter, the question No. (f) need not be answered. We now take up the question as regards the allowability of the deduction on account of bad debt of a sum of Rs.14,22,98,000/-.

The submission advanced by Mr. Nizamuddin assailing the concurrent views of the CIT and the learned Tribunal allowing the claim for bad debt is that the loan had been advanced to the sister concerns. The sister concerns in their turn had advanced moneys to various parties. When the former failed to recover the same they assigned the same in favour of the assessee. The assessee did not provide for any interest in its books of accounts on the loans which were assigned to it by its debtors who are no other than the sister concerns. Paragraph 83 of the impugned judgement has been relied upon by Mr. Poddar which reads as follows:-

> "As regards the contention of ld. CIT DR to the effect that the Assessee did not provide any interest in its books of accounts on the debts taken over by it from the loanee companies in terms of the Deeds of Assignments appearing at pages 14-29 of Volume - II of the Paper Book filed on behalf of the Assessee before us, we find that the assessee had provided interest year after year on the loans advanced by it in course of its money lending business to each of the three companies viz. Som Datt Enterprise Ltd., Datt Enterprise Ltd. And Khaneja Consolidated Co. Ltd. The interest on all these loans had been taxed in its hands as business income in the earlier asstt. Years. The debts written off, during the year under appeal, are those, which had been taken over by the Assessee from each of the said loanee companies, on assignment of debts in its favour under the Deeds of Assignments. The assignments took place in the earlier years viz. 1998 to 2000. On such assignment, the assigned debts, as per

> list appearing at pages 12-14, 17, 20, 23 & 26 of Paper Book, Volume - II, were entered by the Assessee in its own books of accounts, as debts/loans forming part of its continuing money lending business. These entries had been passed in the financial year 1998-99 itself corresponding to the assessment year 1999-2000, long before the year under appeal. There is no material on record to suggest that any of the parties, whose debts had been assigned in favour of the Assessee were connected or related to the Directors/shareholders of the Assessee."

From the aforesaid finding of the learned Tribunal it appears that the assessee provided interest year after year on the loans advanced by it to the three sister concerns. These three sister concerns appeared to have assigned debts payable to them to the assessee.

The point is whether the assesse is obliged to show that it had charged interest on the loans assigned to it by its sister concerns. Contention raised before the learned Tribunal was that the assesse is unable to show that any such interest was charged.

Mr. Nizamuddin has also reiterated the point before us. For a satisfactory answer we need to notice the requirement contained in Clause - (i) of Sub- Section 2 of Section 36 of the Income Tax Act, 1961, which provides as follows:-

> "no such deduction shall be allowed unless such debt or part thereof has been taken into account in computing the income of the assesse of the previous year in which the amount of such debt or part thereof is written off or of an earlier previous year, or represents money lent in the ordinary course of the business of banking or money-lending which is carried on by the assesse;"

It would appear that charging of interest in the previous year is not the only pre-condition. This is one of the pre-conditions. There are alternatives. The alternative condition is that the amount sought to be written off represents money lent in the ordinary course of business of banking or money lending carried on by the assesse. In this case, admittedly the assignment took place "in the earlier years namely viz. 1998 to 2000".

The order of the learned Tribunal for the assessment year 1997-98 passed on 27th December, 2002 contains the following finding:-

> "From the record, we find that in addition to the construction activity, the assesse-company was also engaged in the business of money lending which comprises of loans against shares, L.C. Discounting and other financial transactions. This money lending division of the assesse company was also earning huge revenue over the last several years and the interest income arising from the money lending business during the relevant assessment year under consideration was Rs.6.02 crores as against interest income of Rs.12.24 crores in the immediately preceding year."

It appears, that between the assessment years 1998-99 and 2003-04 the assesse had shown the following income from interest, from paragraph 18 of the impugned judgement which we have quoted above.

Assessment Year	Interest Income included in Column II (Amount in Thousand)
1998-1999	69,786
1999-2000	21,049
2000-2001	16,386
2001-2002	17,768
2002-2003	25,016
2003-2004	89,532

It appears that the learned Tribunal found that the assesse in the current year had continued its money lending business. Therefore, the alternative pre- condition stood satisfied. Even with regard to the first condition, the learned Tribunal relied upon a judgement of the Supreme Court in the case of CIT -Vs- Veerabhadra Rao Koteswar Rao & Co. reported in (1985) 155 ITR 152 (SC) wherein their Lordships observed as follows:-

> "It seems to us that even if the debt had been taken into account in computing the income of the predecessor firm only and had subsequently been written off as irrecoverable in the accounts of the assesse, the assesse would still have been entitled to a deduction of the amount written off as a bad debt. It is not imperative that the assesse referred to in sub cl. (a) must necessarily mean the identical assesse referred to in sub cl. (b). A successor to the pertinent interest of a previous assesse would be covered within the terms of sub cl. (b). The successor assesse, in effect, steps into the shoes of his predecessor. Accordingly, we hold that the assesse in the instant case was entitled to the deduction as a bad debt of the sum of Rs.15,100/- written off by it in its accounts of the previous year as irrecoverable."

It is not in dispute that the assignors of the loan had charged interest against the debts assigned to the assesse. On that basis the first condition appearing in Clause - I of Sub-Section 2 of Section 36 of the Income Tax Act stood satisfied. An alternative argument was also advanced on the basis of Section 29 of the Income Tax Act drawing an analogy with Section 10(1) of the 1922 Act. Mr. Poddar relied upon a judgement in the case of Badridas Daga -Vs- Commissioner of Income Tax reported in (1958) 34 ITR 10 wherein the following views were taken:-

> "Although the Act nowhere in terms authorises the deduction of bad debts of a business, such a deduction is necessarily allowable. What are chargeable to income-tax in respect of a business are the profits and gains of a year; and in assessing the amount of the profits and gains of a year account must necessarily be taken of all losses incurred, otherwise you would not arrive at the true profits and gains."

The next judgement relied upon by him is in the case of Ramchandar Shivnarayan -Vs- CIT reported in (1978) 111 ITR 263 wherein the following views were expressed:-

> "Under section 10(1) of the Indian Income-tax Act, 1922, hereinafter called the 1922 Act, the assesse was required to pay tax in respect of the profits or gains of any business carried on by him. The corresponding provision in the 1961 Act is to be found in section 28. Sub-section (2) of Section 10 of the 1922 Act prescribed the method for computation of profits or gains after making the allowances enumerated in the various clauses of that sub-section. The corresponding section 29 of the 1961 act says: "The income referred to in section 28 shall be computed in accordance with the provisions contained in sections 30 to 43A."

In terms no specific provision is to be found in either of the two Acts for allowing deduction of a trading loss of the kind we are concerned with in this case. But it has been uniformly laid down that a trading loss not being a capital loss has got to be taken into account while arriving at the true figures of the assessee's income in the commercial sense. The list of permissible deductions in either of the Acts is not exhaustive. We may just refer to section 10(2)(xv) of the 1922 Act corresponding to section 37 of the 1961 Act. The relevant words of the said provision, namely, "any expenditure... not being in the nature of capital expenditure or personal expenses of the assesse laid out or expended wholly and exclusively for the purpose of such business..." occurring in either of the two provisions has not been able to take within its ambit loss of property or money by theft or dacoity as it is not an expenditure which has an element of volition, but a forced loss. The cases have laid down that such a loss is a trading loss in the commercial sense and has got to be taken into account for ascertainment of true taxable profits."

We need not take any assistance of Section 29, nor we need any express opinion with regard thereto. We are of the opinion that the assesse, in this case, on the basis of the finding recorded by the Tribunal has fulfilled the alternative condition.

Relying on the judgement of the Supreme Court in the case of Birvadra (supra), it can also be said that the first condition of Section 36 (2)(i) has also been fulfilled. Therefore, we are of the opinion that the bad debt was rightly allowed by the learned Tribunal.

We are, as such, unable to find any illegality in allowing the claim for bad debt. The question No.(d) is, thus answered in favour of the assessee. Now we take up the question as to whether the excess sum of Rs.37.91 crores approximately received by the assessee consequent to exchange gain is a revenue receipt or a capital receipt.

As on 31st March, 1991 an aggregate sum of Dollars $2,30,44,590.60 equivalent to Rs.45,05,21,747/- was receivable by the assesse in Indian currency which was written off on 31st March, 1995, that is to say during the assessment year 1995-96.

The RBI Bonds of 2008 were received by the assesse for the US Dollars $2,33,68,154.12 in the current year out of which US Dollars $3,23,563.52 have already been offered for the taxation leaving thereby balance US Dollars $2,30,44,590.60. At the time when the write off was claimed and allowed, the value of the aforesaid Dollars was Rs.45,05,21,747/- whereas value thereof in Indian currency during the current year was Rs.83,59,80,000/- in the Indian currency. The question is whether the differential amount of Rs.37.91 crores after offering Rs.63,25,667/- for taxation on account of project receivables is a revenue receipt or a capital receipt.

In the case of CIT -Vs- Canara Bank Ltd. reported in (1967) 63 ITR 328(SC) an identical question arose. The facts and circumstances of the case were as follows:-

> "The respondent-bank had opened a branch in Karachi on November 15, 1946. After the partition of India in 1947, the currencies of the two Dominions of India and Pakistan continued to be at par until there was a devaluation of the Indian rupee on September 18, 1949. On that date the respondent had a sum of Rs. 3,97,221 at the Karachi branch belonging to its head office. As Pakistan did not devalue its currency the parity between the Indian rupee and the Pakistan rupee ceased to exist. The exchange ratio between the two countries was not determined until February 27, 1951. The bank did not carry on any business in foreign currency - and even after it was permitted to carry on business in Pakistan currency on April 3, 1951, it carried on no foreign exchange business. The Appellate Tribunal found that the money was lying idle in the Karachi branch and was not utilised in any banking operation even within Pakistan. The State Bank of Pakistan granted permission on July 1, 1953, and two days later the bank remitted the amount to India and in view of the difference in values of the currencies made a profit of Rs.1,73,817 The question was whether this amount was a revenue receipt."

Their Lordships answered the question as follows:-

> "We shall assume in favour of the appellant that the money was "stock-in-trade" of the bank. But it does not necessarily follow that the increment due to the fluctuation in the exchange rate was due to trading operations in the carrying on of the banking business. On the contrary, it has been found by the Appellate Tribunal that the amount of Rs.3,97,221 was "a blocked" and "sterilised" balance and the bank was unable to deal with that amount or use it for any banking purpose between September, 1949, and July 1953, when it was finally remitted to India. In our opinion, the money changed its character of "stock-in-trade" when it was "blocked' and "sterilised" and the increment in its value owing to the exchange fluctuation must be treated as a capital receipt. It has also been found by the Appellate Tribunal that the said amount of Rs.3,97,221 was not utilised for internal banking operations within Pakistan and it is hence not possible to draw an inference that the bank realised any profit in the carrying out of its business. We accordingly hold that Mr. Hazarnavis is unable to make good his argument on this aspect of the case and the High Court was right in reaching the conclusion that the exchange difference of Rs.1,70,746 was not assessable to income-tax."

In the case of Sutlej Cotton Mills Ltd. -Vs- CIT reported in (1979) 116 ITR 1 (SC) an identical issue arose, though in that case consequent to fluctuation in the rate of exchange the assessee had suffered a loss. The facts and circumstances of the case were as follows:-

> "The appellant company, which had its head office in Calcutta, had a cotton mill situated in West Pakistan where it manufactured and sold cotton fabrics. During the financial year ending March 31, 1954, relevant to the assessment year 1954-55, the appellant made large profits amounting to Indian Rs.1,68,97,232 converted at the then prevailing rate of exchange of 100 Pakistani rupees to 144 Indian rupees. On August 8, 1955, Pakistan devalued its rupee restoring the parity between the Indian rupee and the Pakistani rupee. Thereafter, during the accounting periods relevant to the assessment years 1957-68 and 1959-60, the appellant obtained permission of the Reserve Bank of Pakistan and remitted to India Rs.25 lakhs and Rs.12 ½ lakhs, respectively. The appellant claimed that on remittance the appellant suffered respectively a loss of Rs.11 lakhs and Rs.5 ½ lakhs but the claim was rejected by the department and the Tribunal sustained the disallowance. On a reference, the High Court held that no loss was sustained by the appellant on remittance of the amounts from West Pakistan and that, in any event, the loss could not be said to be a business loss because it was not a loss arising in the course of the business of the appellant but was one caused by devaluation which was an act of State."

Their Lordships answered the question as follows:-

> "What is necessary to be considered is the true nature of the transaction and whether in fact it has resulted in profit or loss to the assesse. Here, it is clear that the assessee earned Rs.36 lakhs and Rs.18 lakhs in terms of Indian rupees in the assessment year 1954-55 and retained them in West Pakistan in Pakistani currency and when they were subsequently remitted to India, the assessee received only Rs.25 lakhs and Rs.12,50,000 and thus suffered loss of Rs.11 lakhs and Rs.550,000 in the process of conversion on account of alteration in the rate of exchange. It is, therefore, not possible to accept the view of the High Court that no loss was suffered by the assessee on the remittance of the two sums of Rs.25 lakhs and Rs.12,50,000 from West Pakistan. This view which we are taking is clearly supported by the decision of this Court in CIT v. Tata Locomotive and Engineering Co. Ltd. [1966] 60 ITR 405 (SC), which we shall discuss a little later.
>
> That takes us to the next and more important question whether the loss sustained by the assesse was a trading loss. Now, this loss was obviously not an allowable deduction under any express provision of s.10(2), but if it was a trading loss, it would be liable to be deducted in computing the taxable profit of the assesse under s.10(1). This indeed was not disputed on behalf of the revenue but the serious controversy raised by the revenue was whether the loss could at all be regarded as a trading loss. The argument which found favour with the High Court was that the loss was caused on account of devaluation of the Pakistani rupee which was an act of the sovereign

power and it could not, therefore, be regarded as a loss arising in the course of the business of the assesse or incidental to such business. This argument is plainly erroneous and cannot stand scrutiny even for a moment. It is true that a loss in order to be a trading loss must spring directly from the carrying on of business or be incidental to it as pointed out by Venkatarama Aiyar J., speaking on behalf of this court in Badri Das Daga v. CIT [1958] 34 ITR 10 (SC), but it would not be correct to say that where a loss arises in the process of conversion of foreign currency which is part of trading asset of the assesse, such loss cannot be regarded as a trading loss because the change in the rate of exchange which occasions such loss is due to an act of the sovereign power. The loss is as much a trading loss as any other and it makes no difference that it is occasioned by devaluation brought about by an act of State. It is not the factor or circumstance which causes the loss that is material in determining the true nature and character of the loss, but whether the loss has occurred in the course of carrying on the business or is incidental to it. If there is loss in a trading asset, it would be a trading loss, whatever be its cause, because it would be a loss in the course of carrying on the business. Take for example the stock-in-trade of a business which is sold at a loss. There can be little doubt that the loss in such a case would clearly be a trading loss. But the loss may also arise by reason of the stock-in-trade being stolen or burnt and such a loss, though occasioned by external agency or act of God, would equally be a trading loss. The cause which occasions the loss would be immaterial: the loss, being in respect of a trading asset, would be a trading loss. Consequently, we find it impossible to agree with the High Court that since the loss in the present case arose on account of devaluation of the Pakistani rupee and the act of devaluation was an act of sovereign power extrinsic to the business, the loss could not be said to spring from the business of the assesse. Whether the loss suffered by the assesse was a trading loss or not would depend on the answer to the question, whether the loss was in respect of a trading asset or a capital. asset. In the former case, it would be a trading loss but not so in the latter. The test may also be formulated in another way by asking the question whether the loss was in respect of circulating capital or in respect of fixed capital. This is the formulation of the test which is to be found in some of the English decisions. It is, of course, not easy to define precisely what is the line of demarcation between fixed capital and circulating capital, but there is a well~ recognized distinction between the two concepts. Adam Smith in his Wealth of Nations describes "fixed capital" as what the owner turns to profit by keeping it in his own possession and "circulating capital" as what he makes profit of by parting with it and letting it change masters. Circulating capital" means capital employed in the trading operations of the business and the dealings with it comprise trading receipts and trading disbursements, while "fixed capital" means capital not so employed in the business, though it may be used for the purposes of a manufacturing business, but does not constitute capital employed in the trading operations of the business. Vide Golden Horse Shoe (New) Ltd. v.Thurgood [1933] 18 TC 280 (CA). If there is any loss resulting from depreciation of the foreign currency which is embarked or adventured in the business and is part of the circulating capital, it would be a trading loss, but depreciation of

> fixed capital on account of alteration in exchange rate would be a capital loss. Putting it differently, if the amount in foreign currency is utilised or intended to be utilised in the course of business or for a trading purpose or for effecting a transaction on revenue account, loss arising from depreciation in its value on account of alteration in the rate of exchange would be a trading loss, but if the amount is held as a capital asset, loss arising from depreciation would be a capital loss."

In the case of Indo-Burma Petroleum Co. Ltd. -Vs- CIT reported in (1982) 136 ITR 251 (Cal) an identical question arose in the facts and circumstances of the case as follows:-

> "The assesse-company, a subsidiary of Steel Bros. of the U.K. was resident in India. It was incorporated at a time when Burma was part of India. It owned oil fields in Burma and carried on the business of prospecting for, winning and trading in oil. The oil fields were destroyed during the war. In 1950, it received the sterling equivalent of Rs.97,01,124 from the Govt. of U.K. by way of ex gratia grant for the rehabilitation of its war-damaged industry. This amount was credited by the company to its capital reserve account. This reserve, subject to certain subsequent adjustments, had been permanently reflected in the company's investments in U.K. Govt. securities, Burma Oil Co. (1954) shares and U.K. Municipal Corporation deposits. These amounts lying in the U.K. were not easily encashable nor could they be utilised by the assesse except with the permission of the Reserve Bank of India (RBI). In 1956, the company entered into an arrangement with Steel Bros. for prospecting for oil in the U.K. and for this the company obtained the Reserve Bank's approval to retain a sum of $1,50,000 in the U.K. As the company's total funds in the U.K. was much higher, the RBI from time to time instructed the assesse to repatriate funds to India and this was duly effected by the assesse. As a result of these instructions the company repatri9ated, shortly after the devaluation of the Indian rupee in June, 1966, $20,204 being the balance fund lying in the U.K. on 30th June, 1966, after retaining moneys from commitments of U.K. Drillings and a sum of $1,796 towards other expenses. As a result of the remittance and on account of the devaluation, the assesse realised an extra amount of Rs.1,68,157/- in terms of Indian currency. The Tribunal held that this amount was assessable as a revenue receipt. The appreciation in value of the amount retained in the U.K. in terms of Indian currency as a result of the devaluation of the Indian rupee was also held to be business profit."

This Court answered the question as follows:-

> "The basic fact remains that these amounts lying in the U.K. were not easily encash-able or intended easily to be utilised by the assessee, save and except with the permission of the Reserve Bank. If that is the position, then, not having taken this aspect into consideration, in our opinion, the Tribunal had committed an error, which a man of prudence, in law, could not have arrived at, and if that is the position, then such a finding could properly be characterised as a perverse finding in law....

The true nature of an amount must be found out by discovering the true nature of the amount in question and if the consequences of the funds being not permitted to be utilised save and except with the permission of the Reserve Bank make the funds sterilized or blocked, as was adverted to by the Supreme Court in the case of Canara Bank referred to hereinbefore, then the fact that the assessee had treated this amount as current assets on revenue account or the fact that the assessee offered a part of the amount on revenue account for assessment would not be decisive or conclusive. In support of this proposition reliance may be placed on the observations of the Supreme Court in the case of CIT v. India Discount Co. Ltd., [1970] 75 ITR 191 (SC), and on the observations of Bhagawati J. in the decision in the case of Sutlej Cotton Mills Ltd. v. CIT, [1979] 116 ITR 1 (SC), a decision with which we shall have to deal in greater detail later on; on various aspects. For the reasons, as we have indicated before, in our opinion, the Tribunal committed an error of law in its finding, an error which resulted in an erroneous finding, which can be properly described as a perverse finding in law. In the premises, question No. 1 must be answered in the affirmative and in favour of the assessee.

But this finding by itself would be of little academic interest. This finding or this question is really a step into the other main question, viz., question No. 3, that is to say, whether the sum of Rs. 1,68,157 had been correctly taxed as part of the assessee's trading profits? We now proceed to deal with this aspect of the matter.

We have set out the reasons and the basis on which the Tribunal came to the finding that the amount in question was taxable. We have also set out the origin of this amount. On behalf of the assessee, it was contended that the Tribunal proceeded on the basis that as the said amount had been held to be circulating capital, any profit or accretion resulting therefrom would be in the nature of a revenue transaction and if profit accrued out of such transaction, such profit would be taxable on revenue account. The distinction, as we have mentioned before, between circulating capital and fixed capital is well known in law and in economics. Adam Smith in "Wealth of Nations" described "fixed capital" as for the owner's profit by keeping it in his own possession and "circulating capital" as that he makes profit out of it by parting it and letting it circulate. "Circulating capital", therefore, means capital employed in the trading operations of the business and dealings which comprise of trading receipts and trading disbursements, while "fixed capital" means capital not so employed in the business; though it may be utilised for the purpose of manufacturing business, yet does not constitute capital employed in the trading operations. (See, in this connection, the observations in the case of Golden Horse Shoe (New) Ltd. v. Thurgood, [1933] 18 TC 280 (CA)......

The true test was whether the accretion arose as a result of any trading operation carried on by the assessee not on the nature of the asset and the Division Bench in that case found that it was not possible to hold that the accretion had occurred as a result of any operation carried on by the assessee. This decision, as we have

> mentioned before, was affirmed by the Supreme Court in the case of CIT v. Canara Bank Ltd., [1967] 63 ITR 328 (SC). There, the Supreme Court observed at page 332 as follows:
>
> "We shall assume in favour of the appellant that the money was 'stock-in-trade' of the bank. But it does not necessarily follow that the increment due to the fluctuation in the exchange rate was due to trading operations in the carrying on of the banking business. On the contrary, it has been found by the Appellate Tribunal that the amount of Rs. 3,97,221 was a 'blocked' and 'sterilised' balance and the bank was unable to deal with that amount or use it for any banking purpose between September, 1949, and July, 1953, when it was finally remitted to India. In our opinion, the money changed its character of 'stock-in-trade' when it was 'blocked' and 'sterilised' and the increment in its value owing to the exchange fluctuation must be treated as a capital receipt. It has also been found by the Appellate Tribunal that the said amount of Rs.3,97,221 was not utilised for internal banking operations within Pakistan and it is hence not possible to draw an inference that the bank realised any profit in the carrying out of its business. We accordingly hold that Mr. Hazarnavis is unable to make good his argument on this aspect of the case and the High Court was right in reaching the conclusion that the exchange difference of Rs.1,70,746 was not assessable to income-tax."

Incidentally, it may be mentioned that this was a decision rendered by a Bench composed of three learned judges of the Supreme Court and it was held, as it was necessary to hold in that case, that the fact of appreciation of the money did not arise in the course of any trading operation and assuming the amount, with which the Supreme Court was concerned, was originally the stock-in-trade, when it was blocked and sterilised by the bank, the assessee was unable to deal with that amount. It ceased to be the stock-in-trade and the increase in its value, because of the fluctuation in the rate of exchange, was a capital receipt. It was further observed that if by virtue of exchange operations profits were made during the course of the business and in connection with business transactions, the excess receipts on account of conversion of one currency to another would be revenue receipts, but if the profit arises by virtue of exchange operations, and not by way of business of the assessee, it would be a capital receipt. If that ratio is applied to the facts of this case, then, in our opinion, there is no finding that this appreciation in value, even if the money in respect of which the appreciation accrued was held on revenue account, was as a result of any operation arising out of or in the course of the business of the assessee. It is nobody's case that the assessee carried on any business or dealt in foreign exchange, in the facts of the case, even if the amount held in foreign currency had been held on revenue account." In the case of CIT -Vs- Bombay Burmah Trading Corporation reported in (1986) 161 ITR 386 (SC) the assesse was a lessee in respect of forest land. The Government took over the rights of the assesse with respect to the lease including elephants, cattle, stores, buildings, dwelling houses etc. and in lieu thereof the Government agreed to hand over to the assesse 50,000 tonnes of teak logs of specified qualities. The Government made over 43,806 tonnes of logs which were sold from time to time during the year 1949-52 and a sum of Rs.1,35,55,611/- were realised which was allocated to the four years on an agreed basis.

The cost incurred for getting these logs was determined at Rs.225 per tonne. The question arose whether the sale proceeds were revenue receipts. The High Court answered the question in the negative. In an appeal the Supreme Court held as follows:-

> "It is, therefore, necessary as mentioned hereinbefore to examine whether the acquisition of forest leases by assessee were acquisitions of capital assets. Though we will refer to some of the decisions to which our attention was drawn and which were referred to by the High Court, it is well to bear in mind the basic principles. These are: if there was any capital asset, and if there was any payment made for the acquisition of that capital asset, such payment would amount to a capital payment in the hand of the payee. Secondly, if any payment was made for sterilisation of the very source of profit making apparatus of the assessee, or a capital asset, then that would also amount to a capital receipt in the hand of the recipient. On the other hand if forest leases were merely stock-in-trade and payments were made for taking over the stock-in-trade, then no question of capital receipt comes. The sum would represent payments of revenue nature or trading receipts. Whether in a particular case, for the contracts of the type with which we are concerned, payments were capital receipts or not would depend upon the facts and circumstances of the case. In this connection it is important to bear in mind that normally in trade there are two types of capital, one circulating capital and the other fixed capital. Fixed capital is what the owner turns to profit by keeping it in his own possession; circulating capital is what he makes profit of by parting with it and letting it change hands. Therefore, circulating capital is capital which is turned over and in the process of being turned over, yields profits or loss. It is well settled as the High Court observed in the judgment under appeal that what is capital assets in the hands of one person may be trading assets in the hands of the other. The determining factor is the nature of the trade in which the asset was employed. Compensation received for immobilisation, sterilisation, destruction or loss, total or partial of a capital asset would be capital receipt. If a sum represented profit in a new form then that was income but where the agreement related to the structure of assessee's profit making apparatus and affected the conduct of the business, the sums received for cancellation or variation of such agreement would be capital receipt."

From the aforesaid judgements two points clearly emerge: (a) An amount held on revenue account may lose its character if the same is sterilised or blocked. Any return arising out of the sterilised or blocked fund would be a capital receipt.

(b) The relevant question to be asked in each case is "whether the receipt arose in the course of trading operation or an operation incidental thereto?" If an answer to the question is in the affirmative the receipt is clearly a revenue receipt. Viewed in the aforesaid light there can be no doubt that the project receivables as on 31st March, 1991 remained blocked for about 11 years. There was no chance of its recovery. Therefore, the project receivables, bearing the character of revenue, lost their character and became a capital investment. Only thing that happened during the period between 31st March, 1991 and the current year is that during the assessment year 1995-96 the assesse wrote off the debt. By writing off the debt the assesse did not cease to be a creditor of the Iraq Government. Therefore, when the money was realised it partook the character of a capital receipt.

We are, as such of the opinion that the view taken by the learned Tribunal is a correct view.

The decision cited by Mr. Nizamuddin in the case of Ircon International Ltd. - vs- Deputy Commissioner of Income Tax reported in (2015) 377 ITR 503 (Del) does not help him. He relied on paragraphs 16, 17 and 18 which we shall quote in our judgement, wherein the Delhi High Court expressed the following views:-

> "16.This Court is of the opinion that both the cases are of no assistance to the assessee. The Iraqi debts were appropriately part of the profits which arose or accrued to the assessee. Concededly, the assessee follows a mercantile method. The fact that it could not realise those amounts for a considerable period which resulted in the Indian Government intervening and negotiating protocols and eventually taking over the debts and issuing bonds instead, did not in any manner transform or alter the nature or character of the amount receivable. The analogy drawn on the basis of the two decisions is neither sound nor appropriate. In neither case did the Supreme Court hold that the increase in value of the Indian Rupee, amounts to a gain as is being urged here. All that was said was that the isolated transactions in both cases, i.e Canara Bank (supra), the exchange fluctuation resulting in gain on account of devaluation of Pakistani Rupee-was an intrinsic part of the bank's operation; and in Universal Radiators (supra), the settlement of the insurance claim as compensation, the receipts were in the true sense not "real income" but capital and unintended accruals. Here, however, the debts payable were not on account of any advances given to the Iraqi Government by the assessee but rather as consideration for the services provided. In fact, for some of the years, part consideration was paid through Iraqi Dinars. It was the balance - payable in hard currency which could not be repatriated due to external factors and economic sanctions.
>
> 17. A fact which did not go unnoticed by the Revenue is that the assessee's statutory auditors in note 6 of their debt report dated 28.06.1995 commented adversely that the credit balance appearing in the Foreign Exchange Fluctuation Reserve Account (FEFR A/c) relating to the debts released till 31.03.1995 - a sum of Rs. 1,261,252/- was not credited to the P&L account thereby understating the profit to the said extent. This was sought to be explained by the assessee that income, if any, due on account of FEFR on discharge of the Iraqi debts would accrue only in the year in which the bonds would be paid by the Central Government. The assessee further sought to elaborate by stating that the deed of assignment dated 10.03.1995 resulted in the Central Government purchasing its right to realize the amount in hard currency from the Iraqi Government. The bond amount was to mature in 2001. Consequently, the assessee contended that the income would be shown when the bonds mature. However, the lower authorities rejected that explanation. During the

> pendency of the assessment proceedings, on 7.5.1996, the CBDT had issued a circular that income, if any, arising out of the receipts of the bonds would be taxable in AY 1995-96.
>
> 18. In this Court's opinion, the holding of amounts in foreign currency for diverse reasons by itself cannot be determinative of its character. As held in Sutlej Cotton (supra), appreciation or depreciation in foreign currency value upon conversion would be either trading profit or trading loss. However, the exception to this is that if foreign exchange currency is kept as capital asset or fixed capital - in such event, the gain or loss would be of capital nature. In the present instance, the amounts as indicated earlier were payable for services provided by way of projects executed by the assessee in Iraq. The Iraqi Government's inability to pay due to sanctions imposed by it and the subsequent Central Government's negotiating an arrangement for its payment through bonds that were to mature in future - with interest did not in any way alter their character or convert them into capital assets as the assessee argues. Rather, this Court is also of the opinion that the analogy of bad debts and their reduction from the revenue receipts in a given year and its converse treatment - by virtue of Section 36(1)(vii) is apt to the circumstance of the case. The assessee's claim of capital loss, based on indexed treatment of capital gain is therefore insubstantial and unfounded on any principle."

We are of the opinion that the view taken in the aforesaid judgement is patently contrary to the view taken by the Supreme Court and this Court which we have discussed above.

Mr. Nizamuddin also relied upon a judgement in the case of Calcutta Jute Agency Pvt. Ltd. -Vs- CIT, West Bengal reported in 117 ITR 741 (Cal) wherein it was held that the fact that the fund became frozen or immobilised does not make any difference. This judgement was rendered without considering the views expressed by the Apex Court in the case of Canara Bank (supra). We are, as such of the opinion that this judgement is of no assistance to the revenue. This question No. (a) is answered, accordingly, in favour of the assesse. The next question which arises for determination is whether the capital receipt of a sum of Rs.37.91 crores is liable to capital gains. The assesse himself admitted that the same is liable to taxation by way of capital gains. The assesse however has contended that it is not liable to pay any capital gain tax on the basis that if the aggregate of the excess project receivables amounting to Rs.38,54,64,500/- are divided by a sum of Rs.47.86/- which was the exchange rate of Dollars in the current year, the same would work out to 80,54,000 US Dollars, which at the prevailing exchange rate as on 31st March, 1991 would have fetched a sum of Rs.15,74,55,724/-. The assesse contends that the aforesaid sum of Rs.15,74,55,724/- is to be treated as cost of acquisition which after indexation would work out to a sum of Rs.38,67,18,179/- whereas the exchange fluctuation gain after deducting the amount offered for taxation would be a sum of Rs.37,91,32,587/-. There shall, as such be a long term capital loss of Rs.75,85,592/-. The Assessing Officer did not accept this contention. The views of the assessing officer were upheld by the CIT. The learned Tribunal did not examine the matter at all and disposed of the matter simply by holding that the receipt was of a capital nature. The correctness of the contention of the assesse as regards the cost of acquisition was not at all examined. Mr. Poddar contended that if it is to be held that when the project receivables were written off in the year 1995-96 the cost of acquisition became zero then in that case the cost of acquisition revived once the amount written off in the assessment year 1995-96 was written back in the current year. Mr. Poddar contended that the historical cost of acquisition could not have become zero because the debt was written off by the assesse. According to him when the money was realised two entries were passed in the books of accounts which were as follows:-

> (a) The account of the debtor was debited and the P/L account was credited at historical cost.
>
> (b) Compensation bond account was debited for the entire sum of Rs.83 crores approximately and the corresponding credit entries were split in two parts.
>
> (i) The account of the debtor was credited by a sum of Rs.45 crores and the (ii) balance 38 crores was credited to capital reserve.

He contended that the historical cost plus indexed value thereof is the cost of acquisition. We need not take notice of this argument of Mr. Poddar. Because this was not the case presented by him before the assessing officer. The case presented by him before the assessing officer has already been discussed by us. Realising his difficulty he has now come up with a new case which was not there before the assessing officer or the CIT or even the learned Trial Court. He cited the following judgements in support of his contentions: CIT -Vs- B. C. Srinivasa Setty reported in AIR 1981 SC 972 wherein it was held that goodwill generated in a newly commenced business could not be described as an asset within the terms of Section 45 and, therefore, if transferred is not subject to Income Tax under the head capital gains.

The aforesaid view was taken on the following basis:-

> "This inference flows from the general arrangement of the provisions in the Income-tax act, where under each head of income the charging provision is accompanied by a set of provisions for computing the income subject to that charge. The character of the computation provisions in each case bears a relationship to the nature of charge. Thus the charging section and the computation provisions together constitute an integrated Code."

There may not be any quarrel with the proposition that the charging Section and the computation provisions together constituted an integrated Code. But, in this case the facts and circumstances are not the same as that of goodwill. At the relevant point of time when the aforesaid judgement was rendered profit arising out of transfer of goodwill was not taxable which is now taxable. The second judgement relied upon by Mr. Poddar is in the case of CIT, Calcutta -Vs- Satya Paul reported in (1984) 148 ITR 21 (Cal) a Division Bench of this Court in that case held as follows:-

> "If that is the position, then in our opinion, by the well settled principle as laid down in the latest decision of the Supreme Court in the case of CIT v. B.C. Srinivasa Setty

> [1981] 128 ITR 294, where it has been held that the asset which did not cost the assesse anything nor was it capable of being estimated a cost could never be subjected to taxation under the scheme of capital gains tax under the I.T. Act, 1961, or the Indian I.T. Act, 1922."

The next judgement is in the case of CIT -Vs- Magnum Export (P) Ltd. reported in (2003) 262 ITR 10, in both the aforesaid judgements the same view was expressed as in the case of Satya Paul. Admittedly, in this case the excess receipt of a sum of Rs.38 crores approximately was on account of fluctuation in the exchange rates which ordinarily would be a receipt of a revenue character as rightly contended by Mr. Nizamuddin.

We, however, have accepted the contention of Mr. Poddar that the debt due from the Iraqi Government had become frozen due to outbreak of war and, therefore, it acquired a character of capital though originally it was a project receivable and thus was held on revenue account.

Mr. Poddar cannot be heard to say (a) that after the debt was written off the assesse continued to own the debt as a capital asset and (b) upon recovery the debt revived. If the debt revived then it would partake the character of a revenue receipt in spite of the fact that it had been written off. According to us, the assesse continued to remain a creditor in a sum of Rs.45 crores approximately though the cost of acquisition in his books of accounts had become zero by virtue of writing off the debt. The right to recover was transferred as a consequence whereof profit to the tune of Rs.38 crores accrued. In the circumstances, all that he had to do was to refund, the benefit of bad debt received by him, under Section 41(4) of the Income Tax Act and to offer the balance sum on account of long term capital gain.

The judgements cited by him are not applicable because goodwill and the other related cases were essentially self-generating assets which at the relevant time were not taxable. In this case, the income could not have accrued to the assesse if the debt was not due from the Iraqi Government. We are, as such of the opinion that the entire balance sum of Rs.38 crores approximately are taxable as long term capital gain without deduction of any cost of acquisition because the cost of acquisition had become zero by having been written off. The accounting entry which the assesse might have made is altogether irrelevant.

The question No.(c) is accordingly answered. The question No. (b) is answered in the negative. Question No. (a) is answered by holding that the receipt was a capital gain liable to tax in its entirety.

The appeal preferred by the revenue thus, partly succeeds. The cross objection succeeds fully.

Parties shall bear their own costs.

(GIRISH CHANDRA GUPTA, C.J.)

I agree. (ARINDAM SINHA, J.)