Delhi High Court
Addl Commissioner Of Income-Tax, ... vs General Industries Corporation on 18 March, 1985
Equivalent citations: 1985 155 ITR 430 Delhi
Author: Kapur
Bench: D Kapur, S Ranganathan
JUDGMENT Kapur, J.

1. The following questions have been referred to us by a common statement of case relating to assessment years 1966-67 to 1969-70 :

"1. Whether, on the facts and in the circumstances of the case, the Tribunal was legally correct in directing the ITO to dispose of the contention of the assessed regarding admissibility of depreciation and development rebate in conformity with the instruction of the Central Board of Direct Taxes as contained in their circulars relied on by the assessed ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was legally correct in directing the Income-tax Officer to include the value of machinery and plant employed in plaster of paris unit in the computation of capital employed for purposes of section 84 of the income-tax Act, 1961, in conformity with the instructions of the Central Board of Direct Taxes, contained in their circulars relied on by the assessed ?"

2. The facts of the case are quite simple. The assessed had purchased machinery under a hire-purchase agreement entered into with the National Small Scale Industries Corporation for the purpose of its plaster of paris unit. The purchase price was Rs. 3,28,020 and the agreement was on the lines of an ordinary hire-purchase agreement. Under such agreements, the property remains with the National Small Scale Industries Corporation till the last Installment is paid. The question which arose for these years was whether development rebate and depreciation were to be allowed on the amount invested in the machinery. There was an audit objection that the assessed was not entitled to depreciation and development rebate, so the ITO reopened the assessments under s. 147(b) of the I.T. Act, 1961. On reopening the assessments, the development rebate and depreciation were withdrawn, but interest payable on the hire-purchase agreement was allowed. The reopening was done for the assessment years 1966-67, 1967-68 and 1968-69. In the assessment year 1969-70, the ITO himself did not allow the development rebate or depreciation.

3. On appeal to the AAC, the contention of the assessed, viz., that the allowance was permissible under a Circular dated March 23, 1943, and a subsequent Circular dated June 26, 1959, issued by the Central Board of Direct Taxes was rejected.

4. On appeal to the Tribunal, it was held that the income-tax authorities were bound by the Circulars and some decisions of the Bombay and Calcutta High Courts were referred to. The Tribunal was of the view that the decisions of the Supreme Court in Navnit Lal C. Javeri v. K.K. Sen, AAC [1965] 56 ITR 198 and Ellerman Lines Ltd. v. CIT [1971] 82 ITR 913, left no room for doubt that the ITO was bound to follow the Circular issued by the Central Board taxes. Accordingly, a direction was given to the ITO to dispose of the contention in conformity with the instructions of the Central Board of

Direct Taxes.

5. This has led to the references before us. The main contention urged before us is that the Central Board of Direct Taxes could not issue instructions which had the effect of treating the machinery as belonging to the assessed when it was under a hire-purchase agreement. The real question is that depreciation is to be allowed when machinery belongs to the assessed and similarly in the case of development rebate. The second question is concerned with the computation of capital employed under s. 84 of the I.T. Act, 1961.

6. On a careful examination of the nature of the hire-purchase agreement, it can be said that though it is worded as a hiring agreement which matures into a sale, it can also be regarded as a sale on Installments. The property passes in such agreements on the payment of the last Installment.

7. However, during the period of hire, the purchaser is also paying the price, so virtually it is a sale on Installments. The circulars of the Central Board of Direct Taxes only serve to overcome a greater difficulty in computing how the various allowances have to be given to the assessed. If the payments towards the hire-purchase are not treated as being capital payments, they will have to be allowed as revenue payments, because the payments are certainly for business purposes and yet, if they are not treated as capital payments, they will necessarily be amounts expended towards the carrying out of the business. On the other hand, if the property passes at the time of the last Installment, then the entire revenue payment will be transformed into a capital payment at that stage. To meet this obvious difficulty, the Central Board of Direct Taxes has issued circulars at various times directing that assets purchased on hire-purchase basis should be treated as belonging to the assessed. The various documents filed along with the statement of case show that this position has been continuing for a very long time. Circular No. 9 dated March 23, 1943, issued by the Central Board of Revenue directed that the periodical payments should be treated as (a) the consideration for hire to be allowed as a revenue deduction, and (b) a payment on account of purchase to be treated as a capital layout. It is also mentioned in that circular that depreciation should be allowed on the initial value, i.e., the amount for which the hired object could be purchased in cash on the date of the agreement. The same view was reiterated by the Central Board of Revenue in its circular dated June 26, 1959. The Central Board of Revenue again reiterated its instructions in November, 1962, and again on July 15, 1963. In the technical instructions of November, 1962, it is pointed out that if depreciation is not allowed to the user, the same cannot also be granted to the owner because he is not using the object for the business, i.e., the result would be that neither the owner nor the hirer would get the allowance. This document points out that it is the person who runs the business who should get the allowance and not the formal owner.

8. As we see it, there is a real difficulty in determining who is to get the allowance and how much, which has been resolved by the circulars.

9. The judgments of the Supreme Court relied upon by the Tribunal, Navnit Lal C. Javeri v. K. K. Sen, AAC [1965] 56 ITR 198 and Ellerman Lines Ltd. v. CIT [1971] 82 ITR 913, indicate that the circulars issued by the Central Board of Revenue are binding on the income-tax authorities. We agree with the Tribunal, following the Supreme Court's judgments, that the circulars are binding

and in this case the circulars resolve a real difficulty in assessing the actual income of the assessed. The problem is common to all businesses where machinery purchased on hire-purchase is involved. So, we answer the first question referred to us in the affirmative, in favor of the assessed and against the Department.

10. As far as we can see, the second question does not arise in this form on the facts of this case, because there is no circular issued under s. 84. This provision requires a computation of the capital employed for the purpose of the business. The Tribunal has merely adopted the principle that if the machinery purchased on hire-purchase belongs to the assessed for depreciation and development rebate, then it also belongs to the assessed for the purpose of applying s. 84 of the Act. We have not been able to find any infirmity in this reasoning; so we answer the second question referred to us in the affirmative, in favor of the assessed and against the Department.

11. We have not referred to the other judgments cited on the interpretation of the provisions of the Act, but have relied only on the circulars. We leave the parties to bear their own costs.