Principal Commissioner Of Income Tax, ... vs M/S Gujarat Narmada Valley Fertilizer ... on 29 April, 2019

Author: Bhargav D. Karia

Bench: Harsha Devani, Bhargav D. Karia

IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

R/TAX APPEAL NO. 1360 of 2018

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PRINCIPAL COMMISSIONER OF INCOME TAX, VADODARA 3

Versus

M/S GUJARAT NARMADA VALLEY FERTILIZER AND CHEMICALS LTD

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Appearance:
MR.VARUN K.PATEL(3802) for the Appellant(s) No. 1
MR JP SHAH, SENIOR ADVOCATE with MR MANISH J SHAH for the Opponent(s) No. 1

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CORAM: HONOURABLE MS.JUSTICE HARSHA DEVANI
and
HONOURABLE MR. JUSTICE BHARGAV D. KARIA

Date : 29/04/2019

ORAL ORDER

(PER : HONOURABLE MR. JUSTICE BHARGAV D. KARIA)

1. The Revenue has preferred this appeal under section 260A of the Income Tax Act, 1961 (hereinafter referred as "the Act") challenging the order dated 17.5.2018 passed by the Income Tax Appellate Tribunal, Surat Bench, Surat (hereinafter referred as "the Tribunal") in ITA No.1363/Ahd/2013/SRT for assessment year 2009-10 raising the following questions of law, stated to be substantial questions of law:-

> "(a) Whether in the facts and in circumstances of the case, the learned ITAT has erred in law and on facts in deleting addition on account of disallowance of expenses on consumption and replacement of stores and spares of C/TAXAP/1360/2018 ORDER Rs.2,55,82,153/- treated as capital expenditure by the A.O. without appreciating the

findings recorded in the assessment order ?

(b) Whether in the facts and in circumstances of the case, the learned ITAT has erred in law and on facts in deleting addition on account of loss on allotment of fertilizer bonds at Rs.18,52,04,574/-

by holding that the loss offered on allotment cannot be considered as capital loss but has to be allowed as business loss u/s. 28 read with section 37 of the Act without appreciating that merely because the market value of bonds on the date of allotment of bonds was less than actual value of bonds received by way of subsidy, it could not be said that the assessee had incurred business loss on allotment of fertilizer bonds, since consequent upon allotment of fertilizer bonds, the assessee did not sell it but held it as investment?

(c) Whether in the facts and in circumstances of the case, the learned ITAT has erred in law and on facts in deleting addition on account of loss on actual sale of fertilizer bonds of Rs.3,77,73,348/- by holding it as business loss u/s. 28 read with section 37 of the Act without appreciating that the fertilizer bonds received by the assessee was a capital asset within the meaning of section 2(14) of the Act and therefore, any loss on sale of capital asset would be a capital loss and not a C/TAXAP/1360/2018 ORDER business loss?

(d) Whether in the facts and in circumstances of the case, the learned ITAT has erred in law and on facts in deleting the addition on account of loss on allotment of fertilizer bonds and loss on sale of fertilizer bonds without appreciating that these fertilizer bonds were held by the assessee as investment and were not held as stock-in-trade of the business carried on by the assessee and consequently the said losses cannot be termed as business loss?

(e) Whether on the facts and in circumstances of the case, the learned ITAT has erred in law and on facts in deleting the disallowance u/s. 40(a)(ia) in respect of commission payment to dealers of Rs.2,95,05,335/-?"

2. With regard to question (a), brief facts are as under:-

2.1 The respondent assessee filed its e-return of income for assessment year 2009-10 declaring total income of Rs.289,02,59,060/-. The Assessing Officer framed the assessment order under section 143(3) of the Act on 30.12.2011. While passing the assessment order, the Assessing Officer disallowed an amount of Rs.255,82,153/- of expenses on consumption and replacement of stores and spares and treated the same as capital expenditure.

2.2 The assessee being aggrieved by the said disallowance preferred an appeal before the CIT (Appeals) who by C/TAXAP/1360/2018 ORDER order dated 27.2.2013 allowed the appeal of the assessee on this count.

2.3 The revenue being aggrieved by the aforesaid findings of fact given by the CIT (Appeals) preferred Appeal No. 1363 of 2013 before the Tribunal. The Tribunal after considering the facts and findings given by the CIT (Appeals) as well as the assessment order passed for the year 1999-2000 dismissed the appeal filed by the revenue on this ground.

3. Learned advocate Mr. Varun K Patel for the revenue submitted that the Assessing Officer while making disallowance of the expenditure of the spare parts claimed as a revenue expenditure has observed that on the basis of the details furnished by the assessee, average life span is five years or more and in one item the life span is twenty years and, therefore, the expenditure is not allowable under section 37. Therefore, the Assessing Officer allowed the depreciation of 15% of such expenditure and disallowed the remaining expenditure of Rs. Rs.2,55,82,153/- /- and disallowed the addition on that score.

4. It emerges from records that the manufacturing facility of the appellant included fertilizers and chemical plants complex wherein fertilizers like Urea and Ammonium Nitrophosphate and chemicals like Ammonia, Formic Acid, Acetic Acid, Weak Nitric Acid, Concentrated Nitric Acid and Methanol were manufactured. Various plants and equipment were in continuous operation in corrosive C/TAXAP/1360/2018 ORDER and acidic atmosphere. It was found that no new assets were created in the process of replacement of worn out parts. There was no capacity addition. The replacement of components of old machinery was made to bring to its original state of efficiency so that the entire integrated manufacturing unit which was considered as a profit making apparatus functions efficiently to its capacity and produces quality products. The CIT (Appeals) after perusing the paper book which contains the details like name of the main plant or machinery to which the replaced component pertains, cost of replaced component, cost of total plant and past history of disallowance and appellate decision in past in respect of similar components and the facts which were explained with the help of diagram/process chart showing that replaced component is part of the main plant. The CIT (Appeals), therefore found from the details of additions to that the fixed assets that addition of independent machinery has already been capitalised and claim is made only for depreciation. Thereafter, the CIT (Appeals) on the above facts found that the expenditure claimed as revenue expenditure is in respect of components of the machinery which cannot be treated as the independent machinery in itself as they are not capable of functioning independently. It was further held that the chemical and fertilizer plant was very large plant within which again there are large machines and within the machine there are components requiring replacement due to wear and tear, that was different plants within the fertilizers and chemical plant. Reference was also made to past history of disallowance wherein the Tribunal had set aside the C/TAXAP/1360/2018 ORDER issue to the Assessing Officer for the assessment years 1998-99 to 2002-03, who in turn accepted the explanation furnished by the appellant in de novo assessment proceedings and no additions were made. On perusal of the facts noted by the CIT

(Appeals) as well as affirmed by the Tribunal, it is clear that question (a) raised by the revenue is a pure question of fact and in the absence of any perversity being pointed out in the concurrent findings of fact recorded by the Tribunal, does not give rise to any question of law.

5. With regard to questions (b) to (d) which are relatable to deleting addition on account of loss on allotment of fertilizer bonds at Rs.18,62,04,574/- and addition on account of loss on actual sale of fertilizer bonds of Rs.3,77,73,348/-, the Assessing Officer has found as under:-

5.1 The assessee company is engaged in the manufacturing of fertilizers. The Government of India (GOI) provides various kinds of subsidies on agriculture related fertilizers. Since the subsidy payments had overshot the budgeted estimates, GOI came up with cashless settlement of the subsidy in innovative circumvention of cash payment and introduced a scheme of issuance of 8.30% and 7.95% Government of India Special Bonds 2023 and 2026 respectively in lieu of payment of fertilizer subsidy in cash. As per the said scheme, the assessee company received fertilizer bonds directly credited to Subsidiary General Ledger account and the bonds so received by the assessee company in lieu of C/TAXAP/1360/2018 ORDER subsidy being part of sale price have been shown as current assets. These bonds are issued in lieu of debt which the company's books disclose as due from the Government as subsidy. However, when the company received the bonds, the market value was less than the face value. Accordingly, effectively the assessee company has realised the lower value of subsidy to the extent of difference in the face value and the market value of the date of the issue of bonds and the said difference in value was claimed as a loss on the date of allotment, which was disallowed by the Assessing Officer, amounting to Rs.1862.04 lakhs.

5.2 Being aggrieved by the said disallowance, the assessee preferred an appeal before the CIT (Appeals), which was allowed.

5.3 Being aggrieved, the revenue filed appeal before the Tribunal. The Tribunal confirmed the findings of fact and affirmed by the order of the CIT (Appeals) and dismissed the appeal of the revenue.

6. Learned advocate Mr. Varun K Patel for the revenue submitted that merely because the market value of the bond on the date of allotment was less than the value of the bond received by way of subsidy, it cannot be said that the assessee incurred business loss as consequent upon the allotment of bond the assessee did not sell it but held it as investment, the Tribunal, therefore, erred in allowing such loss. The learned advocate further submitted that the loss on actual sale of the bonds C/TAXAP/1360/2018 ORDER amounting to Rs.3,77,73,348/- was held by the assessee as a capital asset within the meaning of section 2(14) of the Act and, therefore, loss on sale of capital asset would be a capital loss and not the business loss

and, therefore, such loss could not have been allowed under section 28 read with section 37 of the Act.

7. The Tribunal, on appreciation of facts and considering the history of allotment of bonds by the Government of India in lieu of subsidy amount, held that the finding of the Assessing Officer that from the date of allotment when the market value of the bond is less then it is the notional loss, is not correct. It was also found that as a matter of fact that in assessment year 2008-09, the Assessing Officer has already allowed such loss of Rs.7,71,16,280/-

as revenue loss.

8. It emerges from records that on the date of allotment the bonds were received in lieu of subsidy which was the additional sale price receivable from GOI. The assessee had offered to tax the subsidy receivable as part of sale price. The realization of additional sales price by way of subsidy in the form of fertilizer bond does not make bonds an investment because the bonds were never acquired by the assessee as investment or capital but as debt and also shown as current assets. Therefore, the loss suffered on allotment of bonds and actual sale of the bonds cannot be considered as capital loss but has to be allowed as business loss under section 28 or section 37 of the Act.

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9. With regard to the loss suffered on allotment of bonds and actual loss on sale of bonds amounting to Rs.377,73,348/- is concerned, the contention of the Assessing Officer was that after allotment the assessee company continued to hold bonds and, therefore, it takes characteristic of investment. However, holding period does not decide nature of bonds as investment. In view of the background of facts of getting bonds it clearly indicates that the bonds were not acquired as investments. The CIT (Appeals) as well as the Tribunal held that the bonds were received in lieu of subsidy which was additional sale price received from the Government of India and the assessee company had offered such amount to tax accordingly as part of the sale price and, therefore, the realisation to the additional sale price by way of subsidy in the form of fertilizer bonds does not make bond an investment, because such bonds were never acquired by the assessee as investment for capital but the same were received as debt and also shown as current assets. Accordingly, the loss on actual sale of the bonds cannot be considered as capital loss but the same was required to be allowed as business loss.

10. The Tribunal followed its earlier decision in ITA No.339/Ahd/2012 for assessment year 2008-09 in the case of Gujarat State Fertilizer and Chemicals Ltd. wherein similar issue had arisen. Being aggrieved by the same, the revenue preferred Tax Appeal No.900 of 2018 and this court by order dated 31.7.2018 dismissed the appeal by holding that the fertilizer bonds were issued C/TAXAP/1360/2018 ORDER by the Central Government in lieu of the subsidy. It is not disputed that the subsidy income cannot be said to be a business income. Therefore, in the facts of the case, the fertilizer bonds which were given by the Central Government in lieu of the subsidy when the same was sold at a lower price and the assessee suffered loss, the same was required to be allowed as

business loss incurred and it cannot be treated as capital. In view of the aforesaid decision of this court dismissing the appeal of the revenue on the very same ground on account of loss arising on sale of bonds, no question of law can be said to have arisen out of the order of the Tribunal.

11. With regard to the question (e) as to disallowance u/s.

40(a)(ia) in respect of commission payment to dealers of Rs.2,95,05,335/- .

11.1 The Assessing Officer disallowed of sales made to dealers on the ground of treating the same as discount by way of commission which ought to have been subjected to Tax Deducted at Source under section 194H of the Act.

11.2 The assessee, therefore, being aggrieved by the said disallowance preferred an appeal before the CIT(A) who allowed the appeal of the assessee.

11.3 The revenue, therefore, preferred an appeal before the Tribunal. The Tribunal affirming findings of the CIT (Appeals) dismissed the appeal of the revenue.

C/TAXAP/1360/2018 ORDER 11.4 The Assessing Officer while considering the tripartite agreement between the respondent assessee and the dealer who is the second purchaser found that in sale made by the assessee company, the consumers and dealers are informed of the terms of conditions of sales, discounts etc. and the material is directly transferred to the consumer. The dealer does not have any control over the price at which the product would be sold to consumer and, therefore, it is acting like a commission agent. The Assessing Officer after distinguishing between the dealer and commission agent and analysing the tripartite agreement between the assessee, the dealer and the consumer, was of the opinion that price is decided by the assessee and the person stated to be dealer is receiving consideration from the consumer and paying to the assessee. Assessing Officer invoked clause (i) of the Explanation to section 194H of the Act on the ground that as the so-called dealers have rendered services in the course of buying or selling goods like collecting the sale proceeds from the customers and making payment to the assessee, such services would falls within the definition of commission or brokerage.

11.5 The CIT (Appeals), however, after analysing the tripartite agreement held that the relation between the assessee company and the dealer is of Principal to Principal and the assessee company makes sales of the goods to the dealer. The appellant company and the dealer are mutually liable for fulfilling all the terms and conditions of the sale. Property in the goods passes to the dealer along with delivery of the goods and, therefore, discount C/TAXAP/1360/2018 ORDER given by the assessee company to the dealer is not a commission. The Tribunal affirmed the decision of the CIT (Appeals).

12. It was contended on behalf of the revenue that for sales made through dealers there were tripartite agreements between the assessee, the dealer and the ultimate purchaser. That in the case of sales under such tripartite contract, consumers and the dealers are informed about the price, discounts and other terms and conditions of sales and the material is transferred directly to the

consumer. Therefore, the dealer does not have any control over the price at which the product would be sold to the consumer and, therefore, it was submitted that the dealer is acting like commission agent. Further the major distinguishing point of dealer and commission agent would be whether the person has any flexibility in charging price from the customer. It was submitted that a commission agent would be facilitating the sale and the price would be fixed by the principal. Further in the facts of the case, the price to be paid by the consumer is fixed by the assessee itself and, therefore, it was submitted that the dealers are nothing but commission agents and hence, the discount which is offered by the assessee company to the dealer is nothing but a commission and, therefore the assessee company is liable to deduct tax under section 194H of the Act and as the assessee company did not deduct such tax, the Assessing Officer was justified in disallowing the amount on the ground of such commission under section 40(a) (ia) of the Act.

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13. On a perusal of the findings given by both the CIT (Appeals) as well as the Tribunal, it is not in dispute that the transaction of sale between the assessee company and the dealer is on principal to principal basis. Such supplies are made in the accounts of the dealers only. All accounts are maintained in favour of the dealer. The dealer makes the payment to the assessee for such supplies. All credit notes, debit notes, if any, for the agreed terms are issued by the assessee in favour of the dealers only and for all practical purposes, dealer is debtor of the company. On the facts of the case, when the assessee sells goods to its dealers, it is the dealer who makes the payment to the assessee and there is no payment made by the assessee to the dealer and, therefore, the question of deducting any tax under section 194H of the Act does not arise. The relevant extract of section 194H reads as under:-

> "194. Any person, not being an individual or a Hindu undivided family, who is responsible for paying, on or after the 1st day of June, 2001, to a resident, any income by way of commission (not being insurance commission referred to in section 194D) or brokerage, shall, at the time of credit of such income to the account of the payee or at the time of payment of such income in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rate of five per cent:
>
> Provided that no deduction shall be made under this section in a case where the amount of such income or, as the case may be, the aggregate of the amount of such income credited or paid or likely to be credited or paid during the financial C/TAXAP/1360/2018 ORDER year to the account of, or to, the payee, does not exceed fifteen thousand rupees:
>
> ... .
>
> Explanation - For the purposes of this section, -

> (i) "commission or brokerage" includes any payment received or receivable, directly or indirectly, by a person acting on behalf of another person for services rendered (not being professional services) or for any services in the course of buying and selling of goods or in relation to any transaction relating to any asset, valuable article or thing, not being securities."

14. On a perusal of the aforesaid provision of section 194H, it is clear that any person, not being an individual or Hindu undivided family, who is responsible for paying by way of commission or brokerage shall, at the time of credit of such income to the account of the payee or at the time of payment of such income in cash whichever is earlier, is liable to deduct tax. Explanation (1) to section 194H defines "Commission or Brokerage" which includes any payment received or receivable, directly or indirectly by a person acting on behalf of another person for services rendered (not being professional services) or for any services in the course of buying and selling of goods or in relation to any transaction relating to any asset, valuable article or thing, not being securities. On the facts of the present case, as per the tripartite agreement entered into between the assessee and the dealer, there is no service provided by the dealer to the assessee in the course of buying or selling goods, inasmuch as, the assessee directly sells goods to the dealer and the dealer C/TAXAP/1360/2018 ORDER makes the payment after collecting it from the consumers and, therefore, it is a transaction on principal to principal basis and, therefore, the payment made by the dealer is not liable for any deduction of tax by the assessee company. Therefore, in the facts of the case, the provisions of section 40(a)(ia) of the Act cannot be applied as the dealer cannot be said to be a commission agent of the assessee company.

15. In the light of the aforesaid discussion, it is not possible to state that the Tribunal has committed any legal error so as to warrant interference. No question of law, as proposed or otherwise, much less, substantial question of law, can be stated to arise out of the impugned order of the Tribunal. The appeal is, accordingly, dismissed with no order as to costs.

(HARSHA DEVANI, J) (BHARGAV D. KARIA, J) Z.G. SHAIKH