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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Judgement reserved on: 06.12.2023

% *Judgement pronounced on 23.01.2024*

\+ **ITA 392/2014**

COMMISSIONER OF INCOME TAX-IV ..... Appellant
versus
M/S INDO RAMA TEXTILES LTD. ..... Respondent

\+ **ITA 393/2014**

COMMISSIONER OF INCOMETAX-IV ..... Appellant
versus
M/S INDO RAMA SYNTHETICS (I) LTD. ..... Respondent

\+ **ITA 394/2014**

COMMISSIONER OF INCOME TAX-IV ..... Appellant
versus
M/S INDO RAMA SYNTHETICS (I) LTD. ..... Respondent

\+ **ITA 395/2014**

COMMISSIONER OF INCOME TAX-IV ..... Appellant
versus
M/S INDO RAMA TEXTILES LTD. ..... Respondent

\+ **ITA 396/2014**

COMMISSIONER OF INCOME TAX-IV ..... Appellant
versus
M/S INDO RAMA SYNTHETICS LTD. ..... Respondent

\+ **ITA 397/2014**

COMMISSIONER OF INCOME TAX-IV ..... Appellant

versus

M/S INDO RAMA SYNTHETICS LTD. ..... Respondent

\+ **ITA 443/2022**

PRINCIPAL COMMISSIONER OF INCOME TAX, DELHI-4 ..... Appellant

versus

M/S INDO RAMA SYNTHETIC (INDIA) LTD. ..... Respondent

\+ **ITA 496/2022**

PRINCIPAL COMMISSIONER OF INCOME TAX, DELHI-4 ..... Appellant

versus

M/S INDO RAMA SYNTHETIC (INDIA) LTD. ..... Respondent

\+ **ITA 398/2014**

COMMISSIONER OF INCOME TAX-IV ..... Appellant

versus

M/S INDO RAMA SYNTHETICS LTD. ..... Respondent

Present: Mr Shailendera Singh, Sr Standing Counsel with Ms Anuja Pethia, Ms Dacchita Shahi, Standing Counsel and Mr Rishabh Nigam, Adv. for appellant in ITA No.398/2014.

Mr Aseem Chawla, Sr Standing Counsel with Ms Pratishtha Chaudhary, Ms Nivedita, Mr Aditya Gupta and Mr Naveen Rohila, Advs. for the appellant in ITA Nos.443/2022 & 496/2022.

Mr Shlok Chandra, Sr Standing Counsel with Ms Madhavi Shukla and Ms Priya Sarkar, Standing Counsels along with Mr Ujjwal Jain and Ms Saumya Pandey, Advs. for appellant in ITA Nos.392/2014, 393/2014, 394/2014, 395/2014, 396/2014 & 397/2014.

Mr Ajay Vohra, Sr Adv. with Mr Rohit Jain, Adv., Mr Aniket D Agarwal, Adv and Mr Samarth Chaudhari, Adv for the respondent in ITA Nos.393/2014, 394/2014, 396/2014, 397/2014, 443/2022, 496/2022 & 398/2014.

CORAM:

HON'BLE MR JUSTICE RAJIV SHAKDHER
HON'BLE MR JUSTICE GIRISH KATHPALIA

RAJIV SHAKDHER, J.:

Prefatory Facts:

1. These appeals concern Assessment Year (AY) 1997-98 [ITA No.393/2014], AY 2005-06 [ITA Nos.392/2014 & 395/2014], AY 2006-07 [ITA Nos.394/2014 & 397/2014], AY 2008-09 [ITA Nos.396/2014 & 398/2014], AY 2013-14 [ITA No.496/2022] and AY 2014-15 [ITA No.443/2022].

2. At the outset, we would note that the counsel for the parties agreed in the course of the hearing in the above-captioned appeals that the issue raised on behalf of the appellant/revenue is common, and therefore, the facts of one of the appeals could be taken up for discussion to arrive at the end result.

3. Bearing this in mind, we would be referring to the facts insofar as they are relevant to the issue at hand obtaining in ITA No.393/2014, which, as indicated above, concerns the earliest AY, i.e., AY 1997-98.

4. The common question of law, which was framed in the above-captioned appeals, reads as follows:

> *"Whether the Income Tax Appellate Tribunal was right in holding that the subsidy received in the form of sales tax incentive under the Resolution dated 07th May, 1993 under the Package Scheme of Incentives Scheme, 1993 was [a] capital receipt and not revenue in nature?"*

5. Thus, the central issue which arises for consideration in the appeals concerns the nature of the benefit received by the respondent/assessee. The benefit which the respondent/assessee has obtained from the Government of Maharashtra, in the AYs in issue, is a sales tax subsidy in the manner and form prescribed under the scheme titled "Dispersal of Industries Package of Incentives, 1993" [hereafter referred to as "1993 Scheme"].

6. The moot point which arises for consideration is whether the sales tax subsidy received by the respondent/assessee is a capital receipt or, as contended by the appellant/revenue, a revenue receipt.

Backdrop:

7. Thus, before we proceed further to conclude one way or the other concerning the aforementioned issue, the following broad facts are required to be noticed:

7.1 The 1993 Scheme referred to hereinabove was notified by the Government of Maharashtra *via* Resolution dated 07.05.1993.

7.2 It appears that the Government of Maharashtra, to achieve the dispersal of industries outside the Bombay [now Mumbai]-Thane-Pune belt and to incentivise the setting up of new and expanded units in underdeveloped and developing areas had in 1964, forged a scheme titled "Package Scheme of Incentives".

7.3 The Package Scheme of Incentives introduced in 1964 underwent changes from time to time. The 1993 Scheme we are concerned with is rooted in the Package Scheme of Incentives put in place by the Government of Maharashtra, as indicated above, in 1964.

7.4 Seeking to take advantage of the 1993 Scheme, the respondent/assessee set up industrial units in Butibori, Nagpur and

Takhalghat, Nagpur. The production in the Butibori unit commenced on 01.05.1994, while in the expanded Takhalghat unit, it commenced on 01.09.1996.

7.5 Upon an application being made, the respondent/assessee was issued two eligibility certificates dated 13.12.1994 and 15.10.1996 by the designated authority, i.e., the State Industrial and Investment Corporation of Maharashtra Limited [hereafter referred to as "SICOM"].

7.6 On 29.11.1997, the respondent/assessee filed its Return of Income [hereafter referred to as "ROI"] for AY 1997-98, wherein it declared a loss amounting to Rs.205,02,97,503/-.

7.7 The respondent/assessee was subjected to scrutiny assessment. The Assessing Officer (AO) passed an order on 28.03.2000, whereby the loss declared by the respondent/assessee was scaled down to Rs.180,95,99,757/-.

7.8 In the appeal preferred by the respondent/assessee with the Commissioner of Income Tax (Appeals) [hereafter referred to as "CIT(A)"], the order passed by the AO was reversed. Thus, CIT(A), via order dated 10.09.2002, in effect, accepted the loss, as declared by the respondent/assessee in its ROI.

7.9 This resulted in the appellant/revenue approaching the Income Tax Appellate Tribunal [hereafter referred to as "Tribunal"] against the order dated 10.09.2002 passed by the CIT(A). The respondent/assessee lodged cross-objections with the Tribunal regarding the issue concerning sales tax subsidy.

7.10 The Tribunal, insofar as the issue pertaining to sales tax subsidy was concerned, restored the matter to the AO to examine whether the 1993 Scheme (under which incentives had been granted to the

respondent/assessee) was similar to an earlier avatar of the scheme, i.e., 1979 Scheme, which was considered by its special bench of the Tribunal in the matter of ***DCIT v. Reliance Industries Ltd*** (2004) 88 ITD 273 (Mum) (SB). This direction was issued by the Tribunal on 01.02.2006.

8. Upon remand by the Tribunal, submissions were advanced before the AO qua the matter concerning sales tax subsidy on 28.12.2007.

8.1. The AO, however, was not persuaded by the arguments advanced on behalf of the respondent/assessee and, accordingly, via order dated 31.12.2007, concluded that the sales tax subsidy had to be treated as a revenue receipt.

8.2. The respondent/assessee assailed the assessment order dated 31.12.2007 before the CIT(A). The CIT(A), via order dated 19.09.2011, overturned the conclusion arrived at by the AO that the sales tax subsidy had to be treated as revenue receipt. The CIT(A) observed that the 1993 Scheme was identical to the 1979 Scheme considered by the unique bench of the Tribunal in the matter of ***DCIT v. Reliance Industries Ltd.***

8.3 In reaching this conclusion, the CIT(A), among other things, considered the order dated 26.03.1998 passed by his counterpart concerning the respondent/assessee *qua* AY 2003-04. Since, in the said order, there was an elaborate discussion about the similarities and differences that obtained between not only the 1979 Scheme but also the 1983 Scheme, when compared with the scheme forged by the Andhra Pradesh State Government [which was the subject matter of the decision rendered by the Supreme Court in ***Sahney Steels and Press Works Ltd. v. CIT,*** (1997) 228 ITR 253 SC], the order passed was extracted in extenso.

8.4. For convenience, the relevant part of the said order passed by the

CIT(A) concerning AY 2003-04 is set forth hereafter:

> *"(c) In the background of the facts above, and directions of the ITAT, the appellant's case for AY 97-97 that the case of the appellant for claim of sales tax subsidy as exempt being a capital receipt be examined in the case of DCIT vs Reliance Inds. ltd 88 ITD 273 (Mumbai Special bench), the relevant grounds of appeal are required to be considered. My analysis and findings are as under*
>
> *(i) The sales tax subsidy is said to pertain to the appellant's unit at Butibori. Butibori is and [sic, an] industrial area developed by [the] Maharashtra Industrial-Development Corporation in 1994. The appellant in 1995 set up its integrated polyester complex at Butibori for [the] production of POY and PSF.*
>
> *(ii) In the scheme formulated by [the] Govt of Maharashtra (Industries, Energy and Labour Department) under resolution No. IDL1093/(8889)IND-8 under the nomenclature "Dispersal of Industries -New Package Scheme of Incentives. 19931" Butibori falling in Nagpur Division is a group "D" area, where the quantum of sales tax incentives in accordance with para 5.1 (IS) would be 9 years or earlier, if the ceiling of 90% of fixed capital investment is reached in case of non-pioneer unit or 11 years or earlier if the ceiling of 110% of fixed capital investment is reached, in case the appellant is regarded as a pioneer unit. Thus if the appellant is otherwise eligible to sales tax incentive by way of exemption under the 1993 New Package Scheme of Incentive of GOvt. of Maharashtra, the fact that the unit is at Butibori, a category "D" area as per classification, and the unit being setup up in 1995, the percentage of fixed capital investment as per the stipulation for a period of 9 to 11 year. Since the appellant has setup up its unit in 1995, it is otherwise covered for the tax incentive for the year under appeal.*
>
> *(iii) The Tribunal in the appellant's case for AY 1997-98 has set aside for verification the issue as regards applicability of the DCIT" Vs Reliance Industries Ltd. 88 ITD 273 (Mumbai Special Bench)" to the case of appellant undertaking its business of production of PSF and POY at an area classified under the Maharashtra Incentive. Scheme 1993 for its coverage for grant of sales tax incentive. In the case before the Bombay Tribunal, the issue relate to classifying the character of the subsidy obtained under the 1979 package scheme of incentives of the Maharashtra Government, and whether subsidy could be treated as revenue receipt as per the decision of the Tribunal in the case of Bajaj Auto LTd (IT reference no. 49 and 110) (Bombay) of 1991 dated 31.12.2002). in the case of DCST vs Reliance Industries Ltd (supra) it was held at para 28 and 29 of the order that the thrust of the Maharashtra Scheme was industrial development of the backward districts as well as generation of employment, thus establishing, a direct-nexus with the investment in fixed capital assets. In the preamble to 1993 scheme, there is sufficient pointer that the incentive under the scheme is given encourage the setting up of industrial*

units during a particular period n certain backward areas of Maharashtra as well as for dispersal of the Industries. At para 17 of the order, the Tribunal referring to Sahney Steel & PressWorks ltd 228 ITR 253 (SO holds that the nature of the receipt would depend upon the scheme under which a subsidy is given. The Special Bench gave a finding that in the earlier order of Reliance Industries ltd for 1985-86 (IT appeal no. 1418 (Bom) of 1988 and 75554 of 1989) the Tribunal examined the 1979 scheme of the Govt of Maharashtra tracing the background of the subsidy from 1965 when it was first given, and each and every scheme thereafter and proceeded to compare the 1979 scheme with the Andhra Pradesh Scheme. The Andhra Pradesh Scheme was the subject matter of judgment in Sahney Steel & Press Works Ltd (Supra).The Special Bench observed that the Tribunal after detailed analysis of the schemes came to the conclusion that the Maharashtra scheme Was materially different from the Andhra Pradesh and Madhya Pradesh scheme (the latter was the subject in Ousad industries 162 STR 784 (M.P.) The Tribunal on and analysis of the 1979 package scheme came to the conclusion that the thrust of the scheme was that the assessee would become entitled that the object of the incentive even before the commencement of the business which implied that object of the incentive was to finance a part of the cost of setting up of the factory in the notified backward area. According to the Tribunal, the Scheme was for industrial development of the backward districts as well as generation of employment and hence there was direct nexus with investment in fixed capital assets. The sales tax incentive had been envisaged as an "alternative, to disbursement and by its very nature would be available to the assesses only after the production has commenced. The Special Bench, after appreciating the ratio of the previous decision in Reliance Industries case (IT Appeal No. 1418/1988 and 7544/89) held that the observation of the Tribunal in Bajaj Auto case (IT reference -No 49 and 11-01) (Born) of 1991) was not supported by any reason as to why it was felt that the earlier order of the Tribunal in Reliance Industries case referred only to the form of the Scheme and not their substance in para 108 of the order in Reliance Industries case, the Tribunal found that in Andhra Pradesh Scheme, the object was to stimulate rapid industrialization throughout the state, whereas under the Maharashtra Scheme, the aim was to disperse the industries outside the Bombay, Thana - Pune belt and to speed up the pace of industrialization in the developing regions of the state. Under the Maharashtra Scheme, no incentive was available to industries in the developed regions of the state. The second point of difference related to the quantum of the sales tax incentive which was uniform to "all eligible units under the Andhra Pradesh Scheme, but not so under the Maharashtra scheme, under which the quantum depended on the area in which the industry is located. The third point of distinction was that in the Andhra Pradesh scheme incentive, was in the form of refund of sales tax subject to maximum of equity capital, whereas under the Maharashtra scheme, it was either in form of sales tax exemption and interest free unsecured loans. Further the incentives in the Maharashtra Scheme were subject to monetary limits directly related to fixed-capital investment. Another

distinction is the period f (sic: of) eligibility, which stood at 5 years for all units under Andhra Pradesh scheme, whereas, it varied depending upon whether the unit was new or existing or a pioneer unit or a resource based unit. The period of eligibility could also be curtailed if the investment was likely to fail short of sales tax liability. Another pint of distinction was that under the A. P. scheme, the units were required to apply every year for the subsidy after being II set up and going into production, whereas under the Maharashtra scheme, an intending entrepreneur after taking initial effective steps such as taking possession, of land, making application for registration, could also make an application without waiting for the completion of the setting up of the unit for the purposes of availing the incentives, although the final eligibility certificate from SICOM and the letter f (sic: of) entitlement from the Commissioner of sales tax could be granted only after the commencement of production, in that manner, the ratio of the decision in Bajaj Auto Ltd case has been overruled in 1988 ITO 273 (Mumbai).

In Bajaj Auto Ltd. case the assessee availed of the benefit of the 1983 package scheme of incentives. This is comparable to the 1993 scheme of incentives. The preamble and object of both 1983 and 1993 schemes are identical i.e. setting up or expansion of the units in the developing under developed regions of Maharashtra . ***The basis for classification of areas under the 1993 scheme, and the 1983 scheme are identical. The effective steps to be taken for claiming approval under the 1993 scheme are similar to the one used in the 1983 scheme. The quantum of sales tax incentives under para 5.1 (1((I) of the scheme 193, is directly linked to the amount of capital investment in the unit. The exemption under the package scheme of 1993 as in the 1983 scheme are therefore in direct production to the investment in fixed assets.***

I hold therefore that following the over ruling of the order in the case of Baja] Auto Ltd (IT reference No.49 and 1101 Bombay) of 1991 dated 31.12.2002) vide the special bench Bombay's order vs DCIT vs Reliance Industries Ltd 88 lTD 273 (mum) and the fact that the 1983 scheme of Govt of Maharashtra is identical in its application to those contained in the 1993 package scheme of incentives, the appellant is entitled to claim as capital receipt of the notional sales tax liability. *The AD is directed to allow upon verification the quantum of notional sales tax liability computed at Rs. 77,89,99,7437- as per the CAs certificate. Subject to the verification above, the ground is allowed.*

(d) I also hold that pursuant to introduction of Explanation (10) in section 43(1) w.e.f 01.04.99, any subsidy intended to meet the cost of assets should go to the reduce the actual cost for the purposes of allowance of depreciation u/s 32 of the act. Hence, the amount of sales tax exemption is also to be proportionately reduced from the w.d.v. of the respective block of asset on the

basis of cost of project indicators given in the eligibility certificate issued by SICOM. Thus I direct that the amount of sales tax incentives held a capital receipt in an earlier part of this order be considered as a reduction form the block of asset at the admissible amount of depreciation. The AD would give effect accordingly."

[Emphasis is ours]

9. Being dissatisfied, the appellant/revenue preferred an appeal with the Tribunal. *Via* the impugned order dated 22.06.2012, the Tribunal sustained the order passed by the CIT(A).

10. Against this backdrop, the appellant/revenue has preferred an appeal to this court.

Submissions of counsel:

11. The submissions on behalf of the appellant/revenue were advanced by Mr Shlok Chandra, learned senior standing counsel, while Mr Ajay Vohra, learned senior counsel, advanced arguments on behalf of the respondent/assessee.

11.1 Mr Chandra's arguments can broadly be paraphrased as follows:

(i) The 1993 Scheme was a production-linked incentive scheme that kicked in only after the eligible unit had commenced production. To buttress this submission, the following aspects of the scheme were emphasised:

(a) Firstly, although the main objective of the 1993 Scheme was to disperse industries outside the Bombay [now Mumbai]-Thane-Pune belt, the eligibility certificate was issued once commercial production had commenced. Significantly, the 1993 Scheme did not envisage land grants or interest-free capital.

(b) Secondly, under the 1993 Scheme, the eligible units were those that, among other things, possessed the land, registrations from different

governmental bodies, and industrial licenses declaring the commencement of commercial production. The said requirements were captured in the 1993 Scheme under the sub-headings "Initial Effective Steps" and "Final Effective Steps".

(c) Thirdly, the 1993 Scheme provided various incentives, including sales tax incentives by way of exemption, deferral and interest-free unsecured loans.

(ii) The 1993 Scheme, thus, did not assist in setting up the industry but helped make the industrial units viable by increasing their working capital. [See paragraphs 3.1 and 3.3 of the 1993 Scheme].

(iii) The 1993 Scheme improved liquidity by providing sales tax incentives; it did not provide for any direct or indirect payment for setting up the industrial unit. The sole purpose of the 1993 Scheme was to alleviate hardship and handhold such industrial units. [See ***Sahney Steel & Press Works Ltd. v. Commissioner of Income Tax*** (1997)228 ITR 253 (SC)]

(iv) The 1993 Scheme was not intended to contribute towards the capital outlay of the industrial unit. The sales tax subsidy provided to the respondent/assessee only assisted in carrying on business operations and, thus, was in the nature of a revenue receipt. [See ***Commissioner of Income Tax v. Rassi Cements Ltd. (***2013) 351 ITR 169 (Andhra Pradesh); ***Wardex Pharmaceuticals (P.) Ltd. v. Assistant Commissioner of Income Tax*** (2008) 307 ITR 387 (Madras) and ***Commissioner of Income Tax v. Steel Authority of India Ltd.*** (2002) 257 ITR 241 (Delhi)]

(v) Since the incentive concerned sales tax, the receipt inherently can only be construed as a revenue receipt.

(vi) The judgments rendered in ***PCIT-04 v. Nestle India Ltd.,*** 2023:

DHC:4438-DB; ***CIT v. Ponni Sugars and Chemicals Ltd.***, (2008) 306 ITR 392 (SC) and ***CIT v. Chaphalkar Brothers,*** [2018] 400 ITR 279 (SC), are distinguishable on facts. In paragraph 16 of the judgment rendered in ***Ponni Sugar's*** case, the Supreme Court noted that the facts found in ***Sahney Steel*** were different. It was noticed that Ponni Sugar, i.e., the appellant, was free to use the money received in its business activity as per its requirements. Likewise, in ***Chaphalkar Brothers,*** the subsidy was given to offset the burden of the substantial capital expenditure required for setting up multiplex cinema theatres.

(vii) On the other hand, the 1993 Scheme does not impact the capital expenditure component, which would remain the same or even less if the eligible industrial unit moved to a less developed or underdeveloped area. What the 1993 Scheme does is improve the profitability and viability of the eligible industrial unit.

(viii) The mere factum of setting up a new unit in a particular geographical region would not be sufficient to treat the sales tax incentive as a capital receipt. Thus, the subsidy would have to be treated as a revenue receipt in the instant case.

11.2 Mr Vohra, on the other hand, apart from taking us through the contours of the 1993 Scheme, which, according to him, in sum, was put in place to disperse and attract industries to underdeveloped and developing areas in the State of Maharashtra, gave granular details about the investment made by the respondent/assessee in setting up the new units in Butibori area as reflected in the eligibility certificates dated 13.12.1994 and 15.10.1996:

Particulars	**EC dated 13.12.1994 [Annexure 'A']**	**EC dated 15.10.1996 [Annexure 'B']**

	[refer Addenda V @ pp.61-63 below]	[refer Addenda IV @ pp.88-89 r/w 109 below]
Quantum of investment	Rs.411.12 crores	Rs.924.29 crores
Eligibility Period	14 years [01.01.1995 to 31.12.2008]	13 years & 11 months [15.10.1996 to 14.09.2010]
Maximum entitlement [refer pp. 0100 below]	Rs.452.23 crores (110% of investment)	Rs1010.71 crores (110% of investment)
Nature of incentive availed	Sales Tax Incentives by way of Exemption	

11.3 Mr Vohra emphasised that the court while ascertaining the nature of the sales tax subsidy received by an assessee, had to employ the "purpose test".

11.4 According to Mr Vohra, if the purpose is ascertained, which, under the 1993 Scheme, was to both disperse and attract industries to underdeveloped and developing areas of the State, the manner and the point at which the assessee received the sales tax subsidy was of little relevance.

11.5 In sum, the submission was that merely the fact that the sales tax subsidy under the 1993 Scheme was received based on the eligibility certificate issued after the commencement of the production would not render the receipt as one on capital account.

11.6 In support of his submission, Mr Vohra relied upon the following judgments:

(i) Sahney Steel and Press Works Ltd. v. CIT [1997] 228 ITR 253 (SC)

(ii) CIT v. Ponni Sugars and Chemicals Ltd. [2008] 306 ITR 392 (SC)

(iii) CIT v. Chaphalkar Brothers [2018] 400 ITR 279 (SC)

(iv) Shree Balaji Alloys v. CIT [2011] 333 ITR 335 (J&K) [approved in [2016] 287 CTR 459 (SC)]

(v) DCIT v. Munjal Auto Industries Ltd. [2013] 218 Taxman 135 (Guj) [approved by Hon'ble Apex Court vide order dated 08.05.2018]

(vi) CIT v. Maruti Suzuki India Ltd. ITA No.171 of 2012 (order dated 07.12.2017)

(vii) CIT v. Johnson Matthey India (P) Ltd. ITA No. 193 of 2015 (order dated 13.03.2015)

(viii) CIT v. Bougainvillea Multiplex Entertainment Centre (P.) Ltd. [2015] 373 ITR 14 (Del)

(ix) CIT v. Rasoi Ltd. [2011] 335 ITR 438 (Cal)

(x) Sunbeam Auto (P.) Ltd. v. PCIT [2018] 402 ITR 309 (Del)

(xi) PCIT v. Nestle India Ltd. [ITA 303 of 2023 (Order dated 04.07.2023)]

Analysis and Reasons:

12. We have heard the learned counsel for the parties and perused the record.

13. As would be evident from the narration of facts and the submissions recorded hereinabove, the nature of subsidy in the hands of an assessee is fact-centric.

13.1 What has uniformly emerged upon perusal of the case law cited by both sides is that the courts have applied the "purpose test" for concluding one way or the other as to whether the subsidy received should be treated one on capital or revenue account. The principles enunciated by the Supreme Court in ***Sahney Steel's*** case have been uniformly applied in all cases which followed that decision.

14. In the ***Sahney Steel*** case, the Supreme Court dealt with an incentive scheme forged by the Government of Andhra Pradesh. The incentives were given in the form of refund of sales tax on raw materials, machinery and finished goods, subsidy on power consumed for production, exemption from payment of water rate on water drawn from sources which were not maintained at the cost of the government or any local body, refund of water rate in respect of water drawn from a government source or source maintained by any local body but returned after purification, limitation *qua*

liability on account of assessment of land revenue or taxes on land use for the establishment of any industry and additional incentives to new industrial units set up in designated areas.

14.1 Although the aforesaid incentives were provided, their disbursement was linked to the commencement of production. Thus, an assessee became entitled to incentives only after the industrial unit began production.

14.2. The scheme framed by the Government of Andhra Pradesh did not envisage a direct or indirect disbursal of incentives for setting up the industry.

14.3 The Supreme Court, thus, based on its examination of the scheme, concluded that the incentives received by the assessee in that case were akin to an operational subsidy. In other words, the court concluded that the incentives/subsidies had to be treated as trade or supplementary trade receipts. Notably, a specific observation was made by the court concerning the refund of sales tax on the purchase of machinery, while repelling the argument made on behalf of the assessee that since a part of the refund was linked to a capital asset, it had to be necessarily treated as a capital receipt.

14.4 The observations made by the court in this context being significant and perhaps apposite in unravelling the predicament in which one can get caught while deciphering as to how the incentives received by the assessee in a given case should be treated, for convenience, are extracted hereafter:

> *"18. Mr. Ganesh's further argument was that the three types of refunds contemplated in the scheme, the refund of sales tax on purchase of machinery must be treated as capital. The payment for the purchase of machineries must be of capital nature and the entire payment of sales tax must have been treated as capital expenditure of the Company. If any refund of sales tax paid on purchase of capital goods is made the refund will partake of the character which it had originally borne. Such refunds cannot in any circumstances be treated as trade receipts or supplementary trade*

receipts. This argument overlooks the basic principle laid down in the cases discussed above. ***It is not the source from which the amount is paid to the assesses which is determinative of the question whether the subsidy payments are of revenue or capital nature. The first proposition stated by Viscount Simon in Ostime's Case (supra) is that if payment in the nature of subsidy from public funds are made to the assessee to assist him in carrying on his trade or business, they are trade receipts. The sales tax upon collection forms part of the public funds of the State. If any subsidy is given, the character of the subsidy in the hands of the recipient-whether revenue or capital- will have to be determined by having regard to the purpose for which the subsidy is given. If it is given by way of assistance to the assessee in carrying on of his trade or business, it has to be treated as trading receipt. The source of the fund is quite immaterial****.*

19. For example, if the scheme was that the assessee will be given refund of sales tax on purchase of machinery as well as on raw materials to enable the assessee to acquire new plants and machinery for further expansion of its manufacturing capacity in a backward area, the entire subsidy must be held to be a capital receipts in the hands of the assessee. It will not be open to the revenue to contended that the refund of sales tax paid on raw materials or finished products must be treated as revenue receipts in the hand of the assessee. ***In both the cases , the Government is paying out of public funds to the assessee for definite purpose. If the purpose is to help the assessee to set up its business or complete a project as in Seaham Harbour Dock Company's Case(supra), the monies must be treated as to have been received for capital purpose. But if monies are given to the assessee for assisting him in carrying out the business operation and the money is given only after and conditional upon commencement of production, such subsidies must be treated as assistance for the purpose of the trade***."

[Emphasis is ours]

15. As noted hereinabove, this principle, i.e., the purpose test, has been applied in subsequent judgments rendered both by the Supreme Court as well as by various High Courts [See ***Ponni Sugars and Chemicals Ltd.; Chaphalkar Brothers*** and ***Nestle India Ltd.***]

16. Therefore, what the court requires to examine while applying the purpose test to the incentive/subsidy received by an assessee are the following aspects:

(i) First, does it assist in setting up an industry, as opposed to carrying out trade or business operations?

(ii) Second, is the incentive/subsidy given to operate the industrial unit profitably and not for setting it up?

(iii) Third, while employing the purpose test, the court is not concerned with the source, the timing or the mode and manner in which the subsidy is measured and paid. In other words, the quantification of the subsidy/incentive (whether it is linked to turnover or the cost of a capital asset) would not be a determinative factor in concluding the nature of the receipt. The purpose and the object with which the benefit/incentive/subsidy is extended would determine its character in the hands of the recipient, i.e., the assessee.

17. Against the backdrop of the aforesaid principles, it will be helpful to advert to the purpose and object of the 1993 Scheme. The purpose and object of the 1993 Scheme is best illustrated by referring to the preamble of the 1993 Scheme:

> *"**In order to achieve dispersal of industries outside the Bombay-Thane-Pune belt and to attract them to the underdeveloped and developing areas of the State, Government has been giving a Package of Incentives to New/Expansion Units set up in the developing region of the State since 1964 under a Scheme popularly known as the Package Scheme of Incentives**.*
> *The Package Scheme of Incentives, introduced in 1964, was amended from time to time. The last amended Scheme, commonly known as the 1988 Scheme was operative from 1st October, 1988 to 30th September, 1993.*
> *The question of revising the 1988 Scheme to rationalise the scope of incentives, various scales and mode of release of incentives **to intensify and accelerate the process of dispersal of industries from the developed areas and for development of the underdeveloped regions of the State, particularly those farther away from the Bombay-Thane-Pune belt, had been under consideration of the Government**. In the light of the experience gained in implementation of the earlier Schemes, particularly*

the 1988 Scheme, and in the changed circumstances of the liberalised industrial policy of the Government of India, and ***with a view to achieving the objectives outlined above, the Government has decided to revise the 1988 Scheme and bring into force a New Scheme, viz., the Package Scheme of Incentives, 1993*** *(hereinafter referred to as "the 1993 Scheme").*"

[Emphasis is ours]

17.1 A careful perusal of the preamble would show that the 1993 Scheme was forged to achieve three broad objectives.

(i) First, to disperse industries outside the Bombay[now Mumbai]-Thane-Pune belt and to attract new and expanded units to developing and underdeveloped areas of the State.

(ii) Second, to rationalise incentives accorded by intensifying and accelerating the dispersal of units from developed to underdeveloped/developing areas.

(iii) Third, the development of underdeveloped regions of the State, particularly those which were at some distance from the Bombay [now Mumbai]-Thane-Pune belt.

17.2 Thus, the central theme, object and purpose of the 1993 Scheme was to industrialise underdeveloped and developing areas which fell outside the Bombay [now Mumbai]-Thane-Pune belt by incentivising the setting up of new and expanded units.

18. A closer look at the 1993 Scheme would show that the following incentives were envisaged as captured in paragraph 5 of the said scheme:

"5. INCENTIVES

The incentives under the 1993 Scheme will be admissible to a New Unit/Pioneer Unit/Prestigious Unit, and will be in the nature of-

(i) Sales Tax Incentive by way of Exemption/Deferral/Interest-Free Unsecured Loan,
(ii) Special Capital Incentive for SSI Units,
(iii)Refund of Octroi/Entry Tax (in lieu of Octroi),
(iv) Refund of Electricity Duty,

(v) Concession in the Capital Cost of Power Supply, and
(vi) Contribution towards the Cost of Feasibility Study."

19. Each of the incentives referred to above was made admissible to either one or more of the following units categorised as new/pioneer or prestigious.

19.1 A perusal of the definition of new unit/pioneer unit/prestigious unit would show that there is a common denominator: a brand-new unit had to be set up. The only difference was that insofar as the pioneer unit was concerned, it included a large-scale new unit or a large-scale fixed capital investment made by an existing unit. In other words, there was an expansion of an existing unit.

19.2 Insofar as the prestigious unit was concerned, its definition is almost similar to a pioneer unit; the only difference being that it had to be set up in a specific district, i.e., Gadchiroli District. It is common knowledge that Gadchiroli is a problematic area for more than one reason; therefore, setting up an industry in that area is challenging.

20. Besides this, the scheme also refers to a sick unit, which, as per the definition provided in paragraph 3.17 of the scheme, includes a small-scale industrial unit.

21. Therefore, the common thread running through various incentives provided under the scheme (to which we have referred above) was the setting up a new unit or large-scale investment in fixed capital. The fact that the eligibility certificate was to be issued by the agency implementing the scheme after the commencement of commercial production by the eligible unit appears to have been incorporated in the 1993 Scheme to ensure that the object and the purpose of the 1993 Scheme, which was to industrialise underdeveloped and developing areas was fulfilled.

22. Thus, in our opinion, the argument advanced on behalf of the appellant/revenue that a perusal of paragraphs 3.1 and 3.3 of the 1993 Scheme would show that the incentives were tied in with production is untenable. The complete focus of the 1993 scheme was to achieve the object, as noticed above, engrafted in its preamble.

23. As noticed hereinabove, the respondent/assessee was entitled to avail of sales tax subsidy/incentive under two eligibility certificates dated 13.12.1994 and 15.10.1996 [as amended] for 14 years and 13 years & 11 months, respectively, subject to a maximum entitlement of 110% of capital investment made in setting up of the industrial units.

23.1 Investment in capital assets such as land, buildings, plant and machinery was only a measure adopted for calculating the sales tax subsidy/incentive [which in this case was availed by the respondent/assessee by retaining the sales tax it had levied on its goods].

23.2 A perusal of the eligibility certificate dated 13.12.1994 would show that it was issued for setting up a “new unit”, while the eligibility certificate dated 15.10.1996 was given to a "pioneer unit" which had undertaken expansion.

24. Therefore, the argument that the sales tax subsidy/incentive was granted to assist in carrying on business operations and thereby help make the industries more profitable, both on facts and in law is untenable.

25. At the risk of repetition, it must be stated that the sole purpose of the 1993 Scheme was to set up new units and/or expand existing units in underdeveloped and developing areas; an aspect which also emerges on perusal of classification of areas given in paragraph 1.3 of the 1993 Scheme.

25.1 In the categorisation, a clear distinction has been drawn between

developed areas [Group A] and those where some development has taken place [Group B] or are less developed than those falling under Group B [Group C], those which are the least developed areas of the State not covered under Group A/Group B/Group C [Group D] and areas which are least developed lacking basic infrastructure and not covered under Group A, Group B, Group C and Group D [Group D+].

26. The fact that the 1993 Scheme is different from the scheme which the Andhra Pradesh Government framed [which was considered in ***Sahney Steel***] is evident upon perusal of the order passed by the CIT(A). The finding of fact returned by the CIT(A) is that the 1993 Scheme is akin to the 1979 Scheme considered in ***DCIT v. Reliance Industries Ltd***.

26.1 Even though the appellant/revenue did not inform us as to whether the decision of the special bench of the Tribunal rendered in ***DCIT v. Reliance Industries Ltd*** was carried further in appeal, we are of the opinion that the frame of the 1993 Scheme clearly indicates that it was mainly envisaged to industrialise underdeveloped and developing areas and not to improve the production capability or profitability of industrial units, which may have been incidental benefits of the said scheme.

27. Apart from the ***Sahney Steel*** judgement, Mr Shlok Chandra, on behalf of the appellant/revenue, has also cited the decisions rendered in ***Commissioner of Income Tax v Rassi Cements Ltd*** by the Andhra Pradesh High Court, ***Wardex Pharmaceuticals (P.) Ltd v ACIT*** by the Madras High Court and lastly, a judgement of this court in ***Commissioner of Income Tax v Steel Authority of India Ltd***. A close perusal of these judgements would show that they are distinguishable on facts.

27.1. In ***Rassi Steel***, the court was called upon to decide whether the power

subsidy received by the assessee under an incentive scheme framed by the State of Andhra Pradesh was a revenue receipt. The court concluded that the power subsidy received by the assessee [albeit after the commencement of production] was based on actual power consumption and, hence, had nothing to do with investment subsidy for establishing industries in backward areas. It is in this context that the court ruled that the power subsidy received was a trading receipt and, hence, taxable.

27.2. The ***Wardex*** case concerned financial assistance received by an assessee from the Government of West Bengal under a scheme titled "West Bengal Industrial Promotion (Assistance to Industrial Units) Scheme, 1994". The scheme brought registered dealers within its sway who manufactured specified goods in West Bengal via SSI units. The scheme also provided that for obtaining assistance, one of the parameters which was operable was that the registered dealer should not have discontinued manufacturing activities for fifteen (15) days. It was only when these requirements stood fulfilled that the assessee was extended financial assistance equivalent to 90% of the sales tax paid by him for a quarter.

27.3 The court noted that there was no provision in the scheme that financial assistance would be given to invest in a fixed asset or establish a new unit. Given these peculiarities, the court concluded that the financial assistance obtained by an assessee would have to be treated as a revenue receipt. Clearly, the facts obtaining in the said case are distinguishable from those that arise for consideration in the aforementioned appeals.

27.4 Insofar as ***Steel Authority of India Ltd*** is concerned, it must be noted that it is a cryptic order in which the court notes that the assessee had received a grant-in-aid from the Central Government for operations and not

to bring into existence a new asset. Based on the purpose test evolved in ***Sahney Steels Ltd,*** the court answered the question of law as framed in favour of the revenue. In other words, the court held that the grant-in-aid was a revenue receipt. Once again, we must emphasise that the facts mentioned in the judgement suggest that the aid received was on the revenue account.

Conclusion:

28. Given the foregoing discussion, we are not inclined to interfere with the impugned order dated 22.06.2012 passed by the Tribunal concerning AY 1997-98. The question of law, as framed in ITA 393/2014, is answered in favour of the respondent/assessee and against the appellant/revenue. The sales tax subsidy/incentive received by the respondent/assessee under the 1993 Scheme was a capital receipt.

29. Since, as noticed at the outset, the issue is common to the remaining appeals, the decision in those appeals can be no different. Consequently, in the remaining appeals as well, the question of law as framed is answered in favour of the respondent/assessee and against the appellant/revenue.

30. The appeals are disposed of in the aforesaid terms.

(RAJIV SHAKDHER)
JUDGE

(GIRISH KATHPALIA)
JUDGE

January 23, 2024
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