Tax Review/Taxation

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Fallacy of poverty decline in Pakistan

by

*Dr Talat Anwar**

Finance Minister Ishaq Dar on April 8, 2016 with the technical support of the World Bank announced a new official poverty line of Rs 3030 per capita per month in terms of cost of basic need. The government accordingly claims that poverty has declined from 51% in 2004-05 to 29.5% in 2013-14.This claim is misleading and unsupported by the deteriorating economic conditions in the country since 2008. In this context, it is important to evaluate poverty trends and determine whether the poverty decline is consistent with underlying economic realities in Pakistan.

The new official poverty line is not only arbitrary but also ignores the consumption patterns of the poorest 10% households in the country. The poverty decline as measured by the new official poverty line is not consistent with rising malnutrition and declining social and economic indicators. This is mainly due to the fact that under the official methodology, the government uses Consumer Price Index (CPI) which underestimates the inflation rate. Thus, any underestimation of inflation will result in a misleading decline in poverty. A deeper look into the rate of change in CPI, Food Inflation and Sensitive Price Indicator (SPI) suggests that CPI inflation rate remained significantly lower than Food Inflation and SPI between 2002 and 2011. Changes in CPI were significantly lower at 21% compared with 28% in Food Inflation and SPI between 2001-02 and 2004-05. Similarly, CPI suggests lower price changes at 30.3% compared with 38%in Food Inflation and SPI between 2004-05 and 2007-08. In the most recent period 2007-08 and 2010-11, changes in CPI were much lower at 53.7% compared with 65.3% in Food Inflation and SPI indicating an increasing level of underestimation of CPI over time. Thus, underestimation of inflation as measured by CPI is causing a fallacious decline in poverty. On the other hand, high Food Inflation has been hurting the poor severely since they spend more than 70% of their total income on food items.

It is noteworthy that a rapidly declining poverty level to an unacceptable level from 34% in 2001 to 8% in 2013-14 under the old methodology forced the government to realise the flaws and revise its method of measurement of poverty. But the government once again failed to address the real issue of underestimation of CPI for political reasons. Instead of correcting this downward bias and revising CPI upward, it has announced a new official poverty line with the support of the World Bank. Though the new official poverty line of Rs 3030 per capita per month is higher than the previous official poverty line, this step does not address

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the fundamental issue of underestimation of inflation. Thereby, neglecting the questions of efficacy and evaluation of various government policies under donors' program during the past years and their impact on the poor.

Ignoring the issue of underestimation of inflation does not explain the persistent decline in poverty and lead to drawing fallacious conclusions about the government policies. This has been contended by the Members of Technical Group on Poverty including the writer being a member of the group at the Planning Commission in the same meeting on April 8, 2016 that the GDP growth rate declined from an average 6-7 percent per annum during 2004 to 2007 to 3 percent per annum since 2008, unemployment increased and inflation remained high and therefore a rapid decline in poverty from 51% in 2004-05 to 29.5% in 2013-14 is not possible during this period. Notably, this period is accompanied with sluggish economic activities, low growth, and increased food and energy prices and unemployment in the country.

The writer has now tried to correct this downward inflationary bias by using SPI inflation rate and updated the official poverty line by SPI instead of CPI as against the government. The results indicate that poverty did not decline to 29.5% and the poverty level was at 47.5% in 2013-14.The number of poor in the country has increased from 76.1 million in 2004-05 to 89.4 million in 2013-14 suggesting that deteriorating economic conditions coupled with food and energy crisis has adversely affected the poor and vulnerable groups until recently.

It is noteworthy that in past a growth trajectory of 6% per annum reduced the poverty in Pakistan. Therefore, recently achieved growth rate of 3-4%cannot reduce poverty during the last few years. This is supported by the declining exports, rising unemployment and reduced allocation for social sector (health and education) compared with huge allocation on roads and highways. Thus, if government wants to reduce poverty, it needs to undertake reforms to increase growth rate to 6%per annum and initiate projects that benefit the poor. The projects like metro bus and orange line are expensive and will divert spending from pro-poor areas to other less priority areas, which will not only increase poverty but also increase the gap between the rich and the poor.

United States

IRS defers Obamacare reporting deadlines

The US Internal Revenue Service (IRS) has issued Notice 2016-70 extending the due dates for certain 2016 information reporting requirements under the Affordable Care Act (ACA).

Within the provisions of the ACA, most Americans are required to maintain "minimum essential" health insurance coverage, and employers will be encouraged to offer that health coverage. Those individuals and employers who do not comply with these mandates – the "employee mandate" and "employer mandate" – are to make "shared responsibility" payments, or tax penalties, to the IRS.

The new Notice extends the due date for insurers, self-insuring employers, and certain other providers of minimum essential coverage to provide information forms to the IRS and to individuals under section 6055 of the Internal Revenue Code (IRC) from January 31 to March 2, 2017 (30 days). These returns are used by the IRS to administer – and by individuals to show compliance with – the employee mandate.

In addition, the IRS has noted that, because of the extension granted under the Notice, some individual taxpayers may not receive the information they need (for example, to show compliance with the employee mandate or to determine eligibility for the ACA's premium tax credit) by the time they are ready to file their 2016 tax return.

The agency confirmed therefore that taxpayers may rely on other information received from their employer or other coverage provider for filing their returns, and do not need to wait to receive the forms (which, if received later than tax-filing, should be retained and not sent to the IRS).

In addition, the information reporting requirements for applicable large employers under section 6056 of the IRC have been similarly extended. This information is used by the IRS to administer the employer mandate.

The IRS explained that it has granted the 2016 reporting extensions as it has found that a substantial number of employers, insurers, and other providers of minimum essential coverage need additional time beyond January 31, 2017, to gather and analyze data and prepare the 2016 forms. It does not anticipate extending this transition relief to reporting for 2017. – *Courtesy tax-news.com*

China

China opens international tax service hotline

On November 18, China launched an international tax service hotline at the 12366 Shanghai international tax service center, created in January this year with the aim of assisting Chinese businesses to meet new international tax standards.

At its opening ceremony, the Director of the State Administration of Taxation, Wang Jun, said that the center and hotline will support China's Belt and Road Initiative, its free trade zones, and Chinese enterprises investing overseas.

Wang added that, to contribute to more transparent and open tax services, the Shanghai center will support China's efforts to cooperate more deeply with other territories on international tax developments from the OECD, such as in the area of base erosion and profit shifting. – *Courtesy tax-news.com*

South Africa

SARS issues guide on film finance tax break

The South African Revenue Service has published a guide providing general guidance on the exemption from normal tax for income derived from the exploitation rights of a film.

South Africa had provided an incentive aimed at stimulating the production of films within South Africa. It previously provided an upfront tax deduction, or in some circumstances a deduction which was spread over 10 years, for certain production or post-production costs actually incurred by the taxpayer.

That incentive was repealed and replaced, with effect from January 1, 2012, by an exemption from normal tax on income derived from the exploitation rights of approved films. The exemption applies to all receipts and accruals of approved films if principal photography commenced on or after that date but before January 1, 2022.

The income derived from the exploitation rights of a film are exempt from tax under if the National Film and Video Foundation has approved the film as a local production or a co-production; if the income is received by or accrues to an investor acquiring the exploitation rights before the completion date of the film; and only to the extent that the income is received or accrues within a 10-year period after the film's completion date.

Taxpayers may also claim a net loss on a film in a year of assessment commencing at least two years after the completion date of the film. The deduction of a net loss results in a taxpayer being unable to claim the tax exemption on the particular film in the future.

The guide also confirms that any grant under the Department of Trade and Industry film production incentive received by a special purpose corporate vehicle responsible for the production of a film will be exempt from normal tax. In certain cases, if the grant is passed on to an investor, the investor will also qualify for the exemption. – *Courtesy tax-news.com*

FBR approves Audit Policy 2016

The new Audit Policy 2016, approved by the Federal Board of Revenue (FBR) here on Wednesday for selection of taxpayers for audit, would also include those cases in parametric selection process which were earlier selected for audit last year.

Sources told here on Wednesday that the FBR approved new Audit Policy 2016 during meeting of the Board-in-Council held at the FBR House here on Wednesday. A major policy shift in the new audit policy is that the exclusions from audit selection have been reduced under the new Audit Policy 2016. Certain categories which were excluded from audit last year, have now been included in the parametric selection process for audit.

For example, if a case has been selected during the last year, the same may again be picked for audit this year under parametric audit selection. The old case could again be picked for audit.

It has been decided that the parametric audit selection of cases would be carried out under new Audit Policy 2016.

Under the last year's audit policy, certain exclusions were identified and approved by the Board which pertain to cases where audit was not required.

The exclusions from audit for tax year 2014 included:

Income Tax Corporate Returns: All person(s) whose entire income is exclusively subject to Final Taxation under the provisions of law as mentioned in sub-section (4) of Section 115 of the Income Tax Ordinance, 2001; all cases where no business is stated to have been conducted for the relevant tax year and no sales/ receipts have been declared; all cases already selected for audit for Tax Year 2013 by the Board U/S 214C; all cases already selected for audit by the CIRs for Tax Year 2014 under section 177(1) of the Income Tax Ordinance, 2001 and all cases qualifying for exemption from audit under clause (88) of Part IV of the Second Schedule to the Income Tax Ordinance, 2001 (notwithstanding the omission of said clause through Finance Act, 2014).

Income Tax Non-Corporate Returns: All person(s) whose entire income is exclusively subject to Final Taxation under the provisions of law as mentioned in sub-section (4) of Section 115 of the Income Tax Ordinance, 2001; all cases where no sales/ receipts have been declared; taxable income from salary only; taxable income from share from AOP only; cases of pensioners drawing exempt income from pension; cases declaring foreign remittances only; all cases already selected for audit for Tax Year 2013 under section 214C of the Income Tax Ordinance, 2001; all cases already selected for audit by the CIRs for Tax Year 2014 under section 177(1) of the Income Tax Ordinance, 2001; all cases qualifying for exemption from audit under clause (88) of Part IV of the Second Schedule to the Income Tax Ordinance, 2001 (notwithstanding the omission of said clause through Finance Act, 2014) and case(s) of persons(s) where one or more of the above exclusions apply.

Sales Tax Corporate: Null Return filers, federal, provincial and Local Government Departments; all cases of Steel Melters, and Steel Re-rollers who are paying sales tax under the Sales Tax Special Procedure Rules, 2007; all cases of Commercial importers only having no business other than commercial import business and who are paying 3% value added sales tax; all cases already taken up for audit for Tax Period(s) July 2013 to June ,2014 under section 25 ,and 38 of the Sales Tax Act , 1990 and all cases already selected for audit for Tax Period(s) July 2012 to June, 2013 under section 72B of the Sales Tax Act, 1990.

Sales Tax Non-Corporate: Null Return filers; Federal, Provincial and Local Government Departments; all cases of Steel-Melters, and Steel Re-rollers who are paying sales tax under the Sales Tax Special Procedure Rules, 2007; all cases of Commercial importers only having no business other than commercial import business and who are paying 3% value added Sales Tax; all cases already selected for audit for Tax Period(s) July 2013 to June ,2014 under section 25 ,and 38 of the Sales Tax Act , 1990 and all cases already selected for audit for Tax Period(s) July 2012 to June, 2013 under section 72B of the Sales Tax Act, 1990.

FED Corporate/ Non-Corporate Returns: Null Return filers; federal, provincial and Local Government Departments; all cases already taken up for audit for Tax Period(s) July 2013 to June, 2014 under section 46 of the Federal Excise Act,2005 Act ; all cases already selected for audit for Tax Period(s) July 2012 to June, 2013 under section 42B of the Federal Excise Act, 2005.

The scope of exclusions provided was restricted to cases to be selected for audit u/s 214C of the Income Tax Ordinance, 2001, Section 72B of the Sales Tax Act, 1990 and 42B of the Federal Excise Act, 2005. – *Courtesy Business Recorder*

Senate informed: CNIC number can be used as NTN number for tax return

The Senate was informed on Wednesday that any Pakistan citizen, having Computerised National Identity Card, can now file tax returns, using CNIC number as his/her National Tax Number (NTN) while the criterion will remain the same under section 114 of the Income Tax Ordinance 2001.

Speaking on behalf of the Minister of Finance, during the question-hour, Federal Law Minister Zahid Hamid said that rules have been amended as announced by Finance Minister Ishaq Dar in his budget speech in June this year.

"It is very good news...now every citizen is bound to file his tax returns," remarked Senator Nauman Wazir of Pakistan Tehreek-e-Insaf (PTI), who had asked whether or not as announced by the minister, all CNICs had been converted into NTNs or it was merely a political gimmickry.

In response to questions by Senators Mian Attique of Muttahida Qaumi Movement (MQM), Nauman Wazir and Muhammad Azam Swati of PTI, the law minister said that tax forms are being simplified and things are moving towards E-filing and scores of companies have already done so, being a continuous exercise.

In a written reply to a question by Senator Sirajul Haq, Ishaq Dar said that total number of federal government pensioners stands at 1,849524, consisting of personnel of civil armed forces, armed forces and civilians paid out of defence.

Taking notice of various questions the answers of which were not provided by the respective government departments, Chairman Senate Raza Rabbani cautioned to either pass strictures or ruling, if this trend continues any more.

"Replies must be furnished and shared with the Senate Secretariat, as question hour is one form of the government's accountability," he remarked.

To a question by PTI's Senator Mohsin Aziz, Dar said that transgender population would be captured in the current census as a separate category and noted that use of tablets in the census process is suggested by the stakeholders.

However, he added, at this stage with 42.5 million intelligence character recognition (ICR) already got printed, it was found not feasible.

He added in addition, the infrastructure for scanning of ICR forms and data processing, use of computer technology in aid of traditional method was under consideration.

"A separate code will be assigned to the transgender population under the column titled 'sex'. Necessary amendments have been made in the manual of instructions of Form 2, 2-A and Form REN-2," he noted.

To the surprise of many senators and those sitting in the visitors galleries, Minister for Industries Ghulam Murtaza Jatoi revealed in response to a question by MQM's Tahir Hussain Mashhadi that there has been no case of corruption in his ministry during the last over three years. He added there might be such cases in autonomous bodies and departments.

The senators welcomed the Commonwealth Parliamentary Association delegation, consisting of Secretary General Akbar Khan and Lucy Pickles in the Visitors' Gallery by thumping desks when Rabbani made the announcement about the presence of the visitors.

On finding incomplete information in response to her question, PPP Senator Sehar Kamran urged the Chair for deferring the question. The Chair deferred it. She had sought details of targets fixed under Vision 2025, details of achievements made so far and information about those targets, which were required to be achieved so far but have missed their timelines indicating also the reasons for the same.

Later, Ishaq Dar came to the House with a big smile on face, and broke the news of a significant increase in salaries of the lawmakers that was approved in a meeting chaired by the Prime Minister.

He said that after hectic efforts he managed to increase the salaries of the fellow lawmakers. He also gave the details of the salaries.

Chairman Senate Raza Rabbani sent back a report of the House Standing Committee on Defence on a bill (for reconsideration) to amend the National Command and Authority Act, 2010, saying apparently, the proposed piece of legislation hit the key constitutional provisions, including the one on fundamental rights.

Rabbani contended that the state could not take away fundamental rights of employees, like the freedom of association.

He also explained that the bill prima facie struck Articles 4, 8, 17 and 25 of the Constitution.

He made this observation when on behalf of Senator Mushahid Hussain Sayed, who heads the committee, PML-N Senator Muhammad Javed Abbasi rose to present the committee's report on the proposed amendment in NCAA.

The Chairman Senate pointed out that a particular amendment appeared to be hitting the employees' fundamental rights. Therefore, he said the standing committee might reconsider the bill, adding there were as many as 52 judgements of the Supreme Court regarding this matter.

"But it does not mean, the legislature can't legislate but the proposed amendment needs to be carefully reviewed," he noted.

He reminded that besides airing recommendations or proposals, if any, it was also the duty of the committee to ensure nothing in contravention to the Constitution should be approved by it.

Replying to a question by Senator Taj Haider of PPP, Finance Minister Muhammad Ishaq Dar said that to date 98 industrial units, including seven automobiles, 15 cement, 13 chemical, seven engineering, six fertiliser, 23 ghee, 15 Roti plants and four textile units had been privatised and of these 19 were functional.

The minister noted that 18 industrial units had paid taxes amounting to Rs852.589 million, whereas 42 paid no taxes at the time of their privatisation while data pertaining to 38 units was not available at the FBR. – *Courtesy Business Recorder*

Officials of RTOs: performance evaluation to be assessed on basis of recovery pace

The performance evaluation of the Chief Commissioners and senior officials of Regional Tax Offices (RTOs) would also be assessed on the basis of pace of recovery and enforcement action in big tax evasion/concealment cases, involving billions of rupees detected by the Directorate General of Intelligence and Investigation Inland Revenue (IR).

Sources told here on Wednesday that the Directorate General of I&I IR has referred mega tax evasion cases to the RTOs for recovery of the evaded amount from tax evaders and tax dodgers. In many cases, accurate taxes have been worked out on the basis of actual income/profits and investments of individuals/companies.

The process involves detailed investigation by the agency based on data/information, which has been timely communicated to the RTOs for recovery of evaded amount of taxes. It is necessary for the field formations to timely take action on the agency's reports, but recovery of the evaded amount on the said reports is not satisfactory.

In this regard, the Director General I&I IR has drafted a Standard Operating Procedure (SOP) for the relevant directorates of the agency. The intelligence arm of the FBR has also implemented a tracking and monitoring system for status of cases forwarded to the RTOs for compliance and recovery. The recovery of evaded amount based on directorate's findings would result in helping the FBR in achievement of the assigned revenue collection target for 2016-17.

According to sources, it is a matter of concern for the FBR that the field formations are not properly pursuing mega cases, detected by the agency. Despite the fact that the FBR Member IR Operations is also assisting the agency to recover the unpaid amount of taxes by the evaders but action on many cases is yet to be taken by the field formations.

One of the parameters to judge the performance evaluation of the Chief Commissioners and other officials in the field formations would be the action taken on the reports of the Directorate General of I&I IR. Among other evaluation criteria for transfers/postings and even promotions, the feedback would be taken from the relevant departments about recovery action in mega cases of tax frauds and evasion on the reports of the Directorate General of I&I IR.

Besides, other performance evaluation criteria for transfers and postings etc, the action on the agency's reports would also be considered as a positive contribution by the Chief Commissioners.

The agency is also taking feedback of the RTOs about the fate of a number of reports of the Directorate General of I&I IR, pending with the field formations. – *Courtesy Business Recorder*

2016 TRI 545 (H.C. Punjab.)

HIGH COURT OF PUNJAB AND HARYANA AT CHANDIGARH

S.J. Vazifdar, Chief Justice and Deepak Sibal, J.

Haryana State Road & Bridges Development Corporation Ltd.
v.
Commissioner of Income Tax, Panchkula and another

FACTS/HELD

S. 37(1): While expenditure for purchase of a capital asset is capital expenditure, guarantee commission to acquire the asset on installment terms is revenue expenditure

1. Expenditure incurred for the purchase of the machinery was undoutedly capital expenditure; for it brought in an asset of enduring advantage. But the guarantee commission stands on a different footing. By itself, it does not bring into existence any asset of an enduring nature; nor did it bring in any other advantage of an enduring benefit. The acquisition of the machinery on installment terms was only a business exigency. If interest paid on a credit purchase of machinery could be held to be revenue expenditure, we fail to see how guarantee commission paid to a bank for obtaining easy terms for acquisition of the machinery could be regarded as capital payments (Sivakami Mills Ltd. Vs Commissioner of Income Tax, [1979] 120 ITR 211 approved in Commissioner of Income Tax Vs Sivakami Mills Ltd. [1997] 227 ITR 465 followed. Chhabirani Agro Industrial Enterprises Ltd. Vs Commissioner of Income Tax [1991] 191 ITR 226 is not good law)

Appeals accordingly disposed of.

ITA-85-2016 (O&M).

Decided on: 29th September, 2016.

Present at hearing: Salil Kapoor, Rishabh Kapoor, Saurabh Kapoor and Sumit Lalchandani, Advocates, for Appellant. Yogesh Putney, Advocate, for Respondents.

JUDGMENT

S.J. Vazifdar, C.J. (ORAL)–

This is an appeal against the order of the Tribunal dated 16.10.2015 in respect of the assessment year 2010-2011 confirming the order of the CIT (Appeals) which in turn had confirmed the disallowance of certain deductions.

2. The assessee filed its return on 15.10.2010 declaring a loss and a revised return on 25.03.2011 declaring the same income. The assessment was completed under Section 143(3) of the Income Tax Act, 1961 (for short the Act) after issuing the necessary notices.

3. The assessee claimed an amount of ` 96,91,000/- as a deduction under Section 37 of the Act being the commission paid by it to the State of Haryana in respect of a guarantee issued by the State of Haryana at the appellant's request in favour of the Housing Urban Development Corporation Limited (HUDCO).

4. The Assessing Officer disallowed the expenditure treating the same as capital expenditure. The Assessing Officer also disallowed an amount of ` 4,03,129/- under Section 40(a)(ia) on the ground that the appellant/assessee had failed to deduct tax at source in respect of certain payments.

5. The appeal is admitted on the following substantial questions of law:–

> *"(a) Whether "Guarantee Fee" can be allowed deduction under Section 37 of the Income Tax Act?*
>
> *(b) Whether in view of the facts and circumstances of the case, the Tribunal has erred in law and on facts in upholding the order of the assessing officer in disallowing Rs. 4,03,129/- u/s 40(a)(ia) of the Act when the same expenses have been paid by the appellant?"*

6. The other questions of law raised in the appeal are part of these questions and are dealt with accordingly.

<u>Re: Question (a)</u>

7. The question that falls for consideration is whether the commission paid in respect of a guarantee is on revenue account or on capital account. In our view, this question is to be answered in favour of the assessee in view of a judgement of the Supreme Court upholding the judgement of the Madras High Court on this issue.

8. In *Sivakami Mills Ltd. vs Commissioner of Income Tax*, [1979] 120 ITR 211, the Madras High Court held:–

> *"The expenditure incurred for the purchase of the machinery was undoutedly capital expenditure; for it brought in an asset of*

enduring advantage. <u>But the guarantee commission stands on a different footing</u>. By itself, it does not bring into existence any asset of an enduring nature; nor did it bring in any other advantage of an enduring benefit. The acquisition of the machinery on installment terms was only a business exigency. If interest paid on a credit purchase of machinery could be held to be revenue expenditure, we fail to see how guarantee commission paid to a bank for obtaining easy terms for acquisition of the machinery could be regarded as capital payments."

(emphasis supplied)

9. The Supreme Court in *Commissioner of Income Tax vs Sivakami Mills Ltd.* [1997] 227 ITR 465 held:-

"Civil Appeal No. 6488 of 1983

1. Heard learned counsel for the parties.

2. The short question that arises for our consideration in this appeal is whether the guarantee commission paid by the assessee is a revenue expenditure and hence allowable as deduction in computing the total income in the Assessment Year 1968-69. The High Court answered the question in favour of the assessee. It was held that the guarantee commission paid by the assessee was a revenue expenditure and hence allowable as a deduction in computing the total income. The Revenue has come in appeal.

3. A similar question arose before the Andhra Pradesh High Court in CIT V. Akkamba Textiles Ltd. The Court held that the expenditure incurred is revenue in nature and so allowable as deduction. Civil Appeal No. 2832 of 1977 preferred against the said decision was dismissed by this Court. In view of the aforesaid decision we see no force in this appeal.

Accordingly, this appeal is dismissed. There will be no order as to costs.

Civil Appeal No. 9542 of 1995

4. The question is regarding the deduction of interest on deferred payment and guarantee commission paid to the Bank. The High Court followed its earlier decision in Sivakami Mills Ltd. v. CIT and answered the question in favour of the assessee. It was held that both the payments are of revenue nature. We have dismissed the appeal preferred against the decision of the High Court rendered in Sivakami Mills Ltd. in Civil Appeal No. 6488 of 1983. In view of the said decision, this appeal is also dismissed. There will be no order as to costs."

10. It is clear, therefore, that the Supreme Court held that the guarantee commission paid by an assessee is a revenue expense and,

therefore, allowable as a deduction in computing the total income. It is important to note that even in that case, the Madras High Court came to the conclusion that the purchase of machinery was a capital expenditure, but the guarantee commission stands on a different footing. We will assume that in the case before us also the guarantee was issued in respect of loans taken for acquiring capital assets. In view of the judgement of the Supreme Court, it would make no difference as far as the guarantee commission is concerned. As we mentioned earlier, the guarantee was issued by the State of Haryana at the assessee's request in favour of HUDCO.

11. Mr. Putney, however, relied upon the judgement of the Patna High Court in *Chhabirani Agro Industrial Enterprises Ltd. vs Commissioner of Income Tax* [1991] 191 ITR 226. This judgement was prior to the judgement of the Supreme Court in *Commissioner of Income Tax vs Sivakami Mills Ltd.* The Patna High Court dissented from the view taken by the Madras High Court in *Sivakami Mills Ltd. vs Commissioner of Income Tax*. In that case also, the ITO disallowed the expenditure relating to the bank guarantee commission on the ground that it was a capital expense. Mr. Putney relied upon the following observations of the Division Bench of the Patna High Court:-

> *"At first, I would like to deal with the disallowance of the bank guarantee commission. Admittedly, this commission was paid to the Bank of Baroda in respect of its cost for securing their guarantee to the manufacturers of vanaspati plant. Therefore, the incurring of this expenditure is solely attributable to the acquisition of the plant as an asset of enduring benefit. In the case of Challapalli Sugars Ltd. v. CIT [1975] 98 ITR 167, at page 175, it has been held by the Supreme Court that:*
>
> *"The accepted accountancy rule for determining the cost of fixed assets is to include all expenditure necessary to bring such assets into existence and to put them in working condition."*
>
> *Since the bank guarantee commission in question was paid for the purpose of acquiring the plant, it has to be treated as an integral part of its cost.*
>
> *Learned counsel for the company has placed reliance on a decision of the Madras High Court in the case of Sivakami Mills Ltd. v. CIT [1979] 120 ITR 211 in support of his contention that the bank guarantee commission is a revenue expenditure. In this case, the assessee-company had purchased some machinery on deferred payment terms and had obtained a guarantee from a bank in favour of the sellers of the machinery, in lieu whereof the bank charged certain commission. The High Court took the view that the payment of guarantee commission*

> *was a revenue expenditure. The reasons assigned are, (i) it is the option of the assessee to evolve the mode of capitalising the cost of the capital asset, (ii) the rule of determining the cost of the capital assets laid down in Challapalli's case [1975] 98 ITR 167 (SC) will apply only for the period prior to the commencement of production, (iii) the bank guarantee commission was paid only, as a business exigency and as such was an integral part of the conduct of the business, and (iv) the guarantee commission per se does not itself bring into existence any asset of enduring nature.*
>
> *With respect, I find myself unable to agree with this view. In view of the law laid down by the Supreme Court in Challapalli's case [1975] 98 ITR 167, laying down the mode of determining the cost of a capital asset, it is now no more open to evolve new principles in this regard. Once it has been authoritatively held that "all expenditure necessary to bring such assets into existence and put them in working condition" wil form part of the cost of the asset, it is wholly irrelevant whether the asset was acquired prior to the commencement of business or subsequent to such commencement. It is also fallacious to say that it is still at the option of the assessee to capitalize or not to capitalize the expenses directly incidental to the acquisition of such assets. I may also indicate here that all the expenses made for acquisition of a capital asset are always related to the conduct of the business, nonetheless such expenses are capital in nature.*
>
> *In the present case, the bank guarantee commission was paid as an unavoidable incidence of bringing into existence the plant in question; therefore, this is necessarily an integral part of the cost of the capital asset in question. A similar view has been taken by the Gujarat High Court in the case of CIT v. Vallabh Glass Works Ltd. [1982] 137 ITR 389. With respect, I entirely agree with this view. Consequently, I hold that the instant bank guarantee commission is a capital expenditure and is not admissible under section 37(1) of the Act."*

The Patna High Court, therefore, disagreed with the view taken by the Madras High Court in *Sivakami Mills Ltd. vs Commissioner of Income Tax*. However, thereafter, the Supreme Court upheld the view taken by the Madras High Court in *Commissioner of Income Tax vs Sivakami Mills Ltd*. We are bound by the view taken by the Supreme Court in *Commissioner of Income Tax vs Sivakami Mills Ltd*.

12. Question (a) is, therefore, answered in favour of the assessee. The appeal to that extent is allowed.

Re: Question (b)

13. If indeed the assessee was bound to deduct tax at source and did not do so, the assessment order disallowing the expenditure relating to the relevant payments must be upheld.

14. The assessee, however, alleges to have discovered later that it had in fact deducted the tax at source and paid the same to the government treasury. The assessee relies upon a challan in that regard and has produced the same in this appeal as Annexure A-9. The assessee sought to produce the same before the Tribunal, but the Tribunal did not permit it to do so. In our opinion, this was a fit case for the Tribunal to have exercised its powers under Rule 29 of the Appellate Tribunal Rules, 1963 requiring the production of the challan evidencing the payment of the tax deducted at source in the government treasury. All that was required was to direct the authorities to examine whether the challan was genuine and whether the amount was paid into the government treasury or not in accordance with law. The ends of justice certainly required the same. Even if the assessee had contended before the Assessing Officer and the CIT (Appeals) that the amount was not payable, it would make no difference, if, in fact, the amount had been paid.

15. In these circumstances, question (b) is decided by quashing the order of the Tribunal refusing to allow the appellant to adduce additional evidence. On this issue, however, the Assessing Officer shall examine the challan and determine whether the requisite amount of tax was deducted at source and paid over to the government treasury or not in accordance with law. If the same has been done, the assessee shall be entitled to the deductions. If not, the disallowance shall stand.

16. The appeal is accordingly disposed of.