IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "E ", MUMBAI
BEFORE SHRI AMIT SHUKLA, JUDICIAL MEMBER AND
SHRI GAGAN GOYAL, ACCOUNTANT MEMBER

ITA No. 1193/Mum/2023 (A.Y.2002-03)

DCIT Cen. Cir– 8(2),
R. No. 658, 6th floor,
Aayakar Bhavan,
M. K. Road
Mumbai-400 020 ..... Appellant

Vs.

M/s Echjay Industries Pvt. Ltd.
83 Bajaj Bhavan, Bajaj Road,
Nariman Point,
Mumbai-400 020
PAN – AAACE1157B ..... Respondent

Appellant by	:	Shri H. M. Bhatt, Ld. DR
Respondent by	:	Shri B. N. Rao, Ld. AR

Date of hearing	:	03/07/2023
Date of pronouncement	:	25/08/2023

ORDER

PER GAGAN GOYAL, A.M:

This appeal by revenue is directed against the order of Ld. CIT (A)-50, Mumbai dated 17.01.2023 u/s. 250 of the Income Tax Act, 1961 (in short 'the Act') for A.Y. 2002-03. The revenue has raised the following grounds of appeal:-

"1. On the facts and circumstances of the case and in law, the Ld. CIT(A) erred in directing to allow the depreciation on plant and machinery without reducing the amount of compensation received by the assessee in AY 1999-2000 of Rs. 16,05,29,977/- (being initial year), whereas the compensation received by the assessee was in the nature of capital receipts and liable to be deducted from the WDV of plant & machinery for charging depreciation as per Income Tax Act/ Rule and the issue for AY 1999- 2000 yet to be decided by the ITAT."

2. The brief Facts of the case are that Assessee Company is engaged into the business of manufacturing of engineering products & exports. Case of the assessee originally assessed u/s. 143(3) of the Act, determining total income at Rs. 14,77,02,280/- against the returned income of Rs. 12,74,92,260/-. Against this order assessee preferred an appeal before the Ld. CIT (A) and in its first-round; matter has already travelled up to ITAT. Coordinate Bench Restored the matter back to the AO on the appeal of department pertaining to the issue of Depreciation. In compliance to the order of coordinate bench, AO again assessed the case u/s. 143(3) r.w.s. 254 of the Act by restricting the claim of depreciation to Rs. 1,23,86,490/- against the claim of Rs. 2,92,09,742/-.

3. Assessee being aggrieved with this order of AO passed u/s. 143(3) r.w.s. 254 in second round of assessment proceedings preferred an appeal before the Ld. CIT (A), who in turn reversed the order of AO and allowed the appeal of the assessee in his order u/s. 250 of the Act. Now, revenue being aggrieved with this order preferred this appeal before us. We have gone through the order of AO, Order of Ld. CIT (A) and arguments of the assessee. It is observed that assessee is involved in the business of manufacturing steel forged products using MS steel and its alloys. Production is tailor made meaning thereby that it manufactures

products to the specification and drawings given by the customers. On the issue of facts elaborately noted by the Ld. CIT (A) (both assessee and AO) as under:-

3. **Submissions/contentions of the appellant and the Ld. AO-** During the course of the present proceedings, in response to the notices issued u/s 250 of the Act, the appellant has made detailed submissions on e-proceedings from time to time including requests for early processing of this appeal. The relevant extract of the submissions made by the appellant are as under-

4. The appeal is against the AO's holding that a compensation received by the appellant from a German manufacturer supplier of a plant known as ACDR plant, compensating the inherent manufacturing defect in the plant supplied, though was capital receipt, reduced the cost/ WDV for working out depreciation allowance and thus reducing the claim of depreciation allowance claimed by the appellant. The two grounds of appeal taken before your Honour confine to this issue only.

5.0 As to facts, we submit the following:

5.1 The appellant company is in the business of manufacturing steel forged products using MS Steel and its alloys. Production is tailor made meaning thereby that it manufactures products to the specifications and drawings given by the customers. They do not manufacture any product for shelf. Major clientele are ISRO, Railways, Tramways and top automobile manufacturers like Mahindras.

5.2 The production unit of the appellant has state of the art plants. In or about 199-93-94, the appellant imported a plant known as ACDR (Axial Cold Die Rolling

plant) from Germany. The same was found to be defective by the appellant to the effect that it did not turn out to its optimum capacity production guaranteed by the manufacturer. The appellant raised a dispute on this issue and after taking up the dispute before Queen's Council in England and Conciliation Tribunal in Paris, the German Manufacturer supplier offered that their Engineers should be allowed to work on the plant in India for an agreed period and if they shall be satisfied with the claim of the appellant, it would pay a compensation. On trial by their Engineers, the appellant was proved right in its claim made and the manufacturer granted a compensation of DM 7 Million which amounted to Rs. 16,05,29,977 in the financial year 1998-99 relevant to the assessment year 1999-00.

5.3 In the course of assessment for the AY 1999-00, the AO upon inquiries in the matter, held that the compensation received was capital in nature. But, he held that the said compensation reduced the cost/WDV of the plant and machineries for the purpose of allowing depreciation allowance. He reduced the total WDV of plant and machineries as at 1.4.1998 by the amount of compensation received as under section 43(1) of the Income-tax Act. Depreciation claim of the appellant was reduced. This became the bone of contention in appeal before the CIT(A). The learned CIT(A), after considering the facts and with elaborate discussions on law applicable thereto, held, on facts of the case, that the compensation received did not reduce the cost of plant and machineries (ACDR plant) and directed the AO to allow depreciation accordingly, without reducing the WDV of the plant and machineries. He held thus vide para 6.9 of his order dated 22.05.2002 _

> *"Upon consideration of the provisions of section 43, the above noted cases and applying the ratio of the said decisions to the set of facts in the appellant's case, I am inclined to hold that (a) that a mere reference to the cost of the ACDR plant in the letter of the German supplier dated 14th April, 1998 above referred by itself does not show that the compensation was paid to meet any part of the cost. I accordingly hold that the AO was not justified in reducing the actual cost of the assets by the compensation received and reducing the claim of depreciation. I direct that the AO will re-compute the depreciation allowance accordingly without reducing any part of compensation from the WDV of assets as at 1.4.1998."*

5.4 For the said Assessment year 1999-00, the department took this issue in appeal before the Tribunal. But, the Tribunal has not passed any orders on the said

appeal. *As of date depreciation for the AY 1999-00 stands allowed without any reduction in WDV on account of the compensation received in terms of the directions by the CIT(A).* A copy of the order of the CIT(A) for the AY 1999-00 dated 22.05.2002 is attached as *Annexure-2* hereto.

5.5 The assessment for the subsequent year 2000-01 was made u/s 143(1)((a) of the Act accepting the Return of income filed. *Depreciation stands allowed on the closing WDV of the plant i.e. without WDV reduced by the compensation.*

5.6 For the assessment year 2001-02, the AO, in regular assessment, worked out depreciation on WDV as reduced by the compensation received. In appeal, the CIT(A) allowed the claim of the appellant following the decision of his worthy predecessor in respect of the AY 1999-00. The matter was taken in appeal by the Department, before the Tribunal. The Tribunal by its order dated 15.12.2008 remanded the issue to the AO to work out depreciation recording that " *We deem it fit to restore the issue back to the file of Assessing Officer to determine the WDV for the year under consideration in line with the WDV determined for the preceding years and allow the claim of the assesse as per law. A reasonable opportunity of hearing to the assessee shall be afforded." [Emphasis supplied]* A copy of the said order of ITAT for the AY 2001-02 dated 15.12.2008 is attached as *Annexure-3* hereto. This order has not been given effect to by the AO till date, for reasons unknown. *Depreciation stands allowed on WDV of the plant without reduced by the compensation.*

5.7 In respect of the subject AY 2002-03 for which the appeal is before your Honour, two cycle of appeal proceedings have already been taken between AO – CIT(A) – ITAT and this is the third cycle in which the AO has passed orders in same terms as passed in regular assessment without bringing in any further facts or legal issue. It is before your Honour in appeal for adjudication.

5.8 In the regular assessment made by the AO for the assessment year 2002-03 on 28.02.2005, he worked out depreciation on WDV as reduced by the compensation received. He went by the regular assessment order made for the AY 1999-00 and citing pendency of the issue in appeal before ITAT for the previous assessment year 1999-00. A copy of the regular assessment order is attached as *Annexure-4* hereto. In appeal, the CIT(A) allowed the claim of the appellant following the decision by the CIT(A) for the assessment years 1999-00 and 2001-02. A copy of the said order of

CIT(A) dated 29.11.2005 is attached hereto as *Annexure-5.* The issue was taken in appeal before the Tribunal by the Revenue. The Hon'ble Tribunal passed orders on 30.04.2010 setting aside the issue to the files of the AO to work out depreciation considering WDV and depreciation allowable for the previous years, following the Tribunal's order passed for the AY 2001-02. A copy of the said order is attached as *Annexure-6.*

5.9 In the second cycle, the AO reworked depreciation as done in regular assessment and passed orders giving effect to the Tribunal's order. No new facts or law issue was discussed. Depreciation was worked out on WDV of the Plant and machineries as reduced by the compensation part. A copy of the said order is attached as *Annexure7* hereto. The issue was taken up before the CIT(A), who again following the decision taken in previous assessment years and the earlier order of the CIT(A) for the same assessment year, allowed the claim of the appellant. His order passed on 9.10.2013 is attached as *'Annexure-8'* hereto. The said order was again taken in appeal by the Department before the Tribunal. Both the Department and the appellant requested the Tribunal to take up the appeal for the initial AY 1999-00 in which the issue arose for the first time also along with the appeal for the year to reach a finality on the issue. We are enclosing a copy of the submissions made to the Tribunal in that regard on 9th April, 2018 as *Annexure -9* hereto. However, the Tribunal in its order dated 28.09.2018 followed its earlier order and remanded the issue again to the AO citing the order of the Tribunal passed for the Assessment year 2001-02. They recorded as follows:

> *" .... For AY 2000-01 dated 15.12.2008, the Tribunal has remanded this issue back to the file of the AO with the following directions –*
>
> > *3. The issue in ground No. 1 & 2 raise by the Revenue is against the determination of the WDV for the year under consideration and the allowance of depreciation on the said WDV. In view of the non co-operation of the assesse in presenting the details the WDV for the year under consideration which in turn is to be adopted for working he depreciation for the year cannot be determined. In the interest of justice, we deem it fit to restore the issue back to the file fo the Assessing Officer to determine the WDV for the year under consideration in line with the WDV determined for the preceding years and allow the claim of the assesse as per law. A*

reasonable opportunity of hearing to the assesse be afforded. Accordingly, ground Nos. 1 and 2 raised by the Revenue are allowed for statistical purposes.

9. *Exactly on similar directions, we also restore this issue back to the file of the Assessing officer.....*" A copy of the order of the Tribunal dated 28.09.2018 is attached as *Annexure -10* hereto.

From the above order, your Honour will kindly see that the Tribunal did not consider taking up appeal for 1999-00 filed by the Department for any reason and they passed orders directing the AO to pass fresh order on the issue in terms of the direction given by the Tribunal for the AY 2001-02.

5.10 In terms of the directions of the Tribunal, the AO was bound to consider the depreciation allowance given to the appellant for the AY 1999-00, 2000-01 and 2001-02 and on the basis of WDV that works out as at 1.4.2001. He was to work out depreciation for the subject assessment year 2002-03. He has failed to do that way. He should have considered that for those previous three years, the appellant was granted depreciation on value of WDV as at the beginning of the year without deducting any part of compensation that it received. He mechanically computed depreciation as made in the original assessment by taking the WDV on first day of the previous year i.e. 1.4.2001, reduced the same by compensation part received and allowed depreciation on such reduced WDV of the plant and machineries. He has not brought any new facts or law issue in respect of the claim by the appellant or on his conclusion. He has not discussed the issue by any speaking order except recording (vide Para 9 of the assessment order dated 28.08.2019 that "the Hon'ble Tribunal has restored the issue to the AO by following its decision for AY 2001-02. Therefore, to keep the issue alive as the same issue is pending before Hon'ble ITA for the AY 1999-00, and no new facts brought before me in contravention to the findings of my predecessor, the depreciation on ACDR is restricted to Rs.1,23,86,490..... as determined by the Assessing officer in the original assessment proceedings u/s 143(3) ....."

5.11 The order passed by the AO is not justified on facts of the case and we request your Honour kindly to allow the claim of the assessee following the

decision of the predecessor CIT(A) for the subject assessment year and for the assessment years 1999-00 and 2001-02.

5.12 May be it is irrelevant although, we would like to submit the position of this issue of depreciation as have happened in subsequent years subsequent to AY 2002-03.

(i) Assessment years 2003-04 to 2005-06: The AO disallowed the claim and the CIT(A) in appeals have allowed the claim of the appellant. The Department went in appeal before the Tribunal. The Tribunal as in respect of 20001-02 and 2002-03, restored "the issue" to the files of the AO for determining depreciation allowance allowable considering the WDV and depreciation allowed for the previous years. The order was passed on 29.06.2011.

(ii) On or about July, 2007, there was a search action in the case. The appellant challenged the action by way of writ proceedings before the Bombay High Court. The Court has passed orders not to take any proceedings in pursuance of such search till further orders. The HC has not passed final orders although pleadings from both sides have been complete. Perhaps therefore, the Tribunal's order received and the assessments then pending for the AYs 2006-07 to 2009-10 were not taken up for any further proceedings. Depreciation allowance issue has not been taken up as related to these years.

(iii) In respect of the assessment years 2010-11 to 2014-15, the AO disallowed the claim of the appellant and reworked the allowance reducing WDV by the compensation component. The assessments were taken in appeal before the CIT(A) who on appreciating the facts of the case, held the issue in favour of the appellant following the decision by his predecessors for various assessments. A copy of the CIT(A)'s order for the AY 2014-15 passed on 18.11.2017 is attached as *Annexure -11* hereto. The Department has not taken the decision of CIT(A) in further appeal for the above said AYs 2011-12 to 2014-15 before the Tribunal, it amounting to acceptance of the decision by the Department. It means that as for as the appellant is concerned, for the

above 5 years, the depreciation allowance stands granted in terms of its claim i.e. allowing depreciation allowance without reducing any compensation component from WDV of the plant and machineries.

(iv) The assessment for AY 2015-16 has been made u/s 143(1)(a) of the Act meaning thereby the depreciation claim of the appellant stands worked out on WDV without reducing any compensation component from it.

6. With the above discussions on the issue, we relying on the decision of the CITs(A) for the Assessment years 1999-00 to 2005-06 and 2010-11 to 2014-15, request your Honour kindly to allow the appeal of the appellant and direct the AO to modify the assessment computing depreciation allowance on WDV without reducing any compensation component therefrom. We pray accordingly. A copy of the CIT(A)'s order for the Assessment year 2014-15 is attached as Annexure -12 hereto.

7. Should your Honour need any further information, clarifications and/or documents, kindly advise.

N. R. RAO
Advocate
20th January, 2021

Annexures attached.

1. Letter of authority in our favor.
2. Copy of CIT(A)'s order for the AY 1999-00
3. Copy of Tribunal's order for the AY 2001-02 dated 15.12.2008
4. Copy of the Regular assessment for AY 2002-03 dated 28.02.2005
5. Copy of CIT(A)'s order for AY 2002-03 dated 29.11.2005
6. Copy of the Tribunal's order for AY 2002-03 dated 30.4.2010
7. Copy of AO's order giving effect to the Tribunal's order dated15.12.2011
8. Copy of CIT(A)'s order on the above, dated 9.10.2013
9. Copy of submissions made before Tribunal by appellant dated 9.4.2018
10. Copy of the Tribunal's order on the above dated 28.9.2018
11. Copy of the CIT(A)'s order for the AY 2014-15 dated 18.11.2017 (Relevant Para 14, Ground No. 5 related to depreciation allowance.

n response to the latest notice u/s 250 of the Act, the appellant has reiterated and summarised the submissions made earlier vide submission made on e-proceedings on 02.01.2023, as reproduced below-

In the assessment year 1999-00, this issue arose for the first time. The AO reduced WDV of the Plant and machineries by the compensation amount received from the Supplier of ACDR plant the compensation being towards generic defects in the ACDR plant supplied. The Commissioner of Income Tax Appeals upheld the claim of the appellant. Held that WDV should not be reduced by the amount of compensation received. There is no order from the Tribunal on this issue for the year. In subsequent asst years 2000-01 claim of the appellant has become final. There was no scrutiny assessment. For Asst. year 2001-02, AO reduced WDV by the proportionate compensation and accordingly allowed depreciation. Commissioner of Income Tax Appeals allowed the claim, following his predecessor s order held compensation should not be reduced from WDV in allowing depreciation on plant and machineries. Tribunal only set aside the order to the files of AO to recomputed depreciation in terms allowed for earlier years. AO has not passed any order. For this assessment year 2002- 03, first AO disallowed the claim. Commissioner of Income Tax Appeals allowed it. Tribunal set aside the order on the issue to the AO to recompute depreciation after verifying the claim in earlier years. AO again disallowed the claim of the appellant. Commissioner of Income Tax Appeals, on appeal allowed it. Again the Tribunal set it aside to the AO with only remarks as in earlier occasion. AO passed orders again disallowing the claim of the appellant. On the same issue, it is before your Honour. Should you require any further information or particulars, please advise. Please take up the appeal for early hearing and oblige

4. Assessee received a compensation of Rs. 16,05,27,977/- (DM-7) from German Supplier M/s THYSSEN Industries AG in the assessment year 1999-2000. In that year, AO reduced this amount from the cost of plant, accordingly WDV was revised resulting into reducing the claim of depreciation. This money of compensation received is on account of defect in the machine supplied. The production unit of the appellant has state of the art plants. In or about 199-93-94, the appellant imported a plant known as ACDR (Axial Cold Die Rolling plant) from Germany. The same was found to be defective by the appellant to the effect that it did not turn out, to its optimum capacity production guaranteed by the manufacturer. The appellant raised a dispute on this issue and after taking up the dispute before Queen's Council in England and Conciliation Tribunal in Paris, the German Manufacturer supplier offered that their Engineers should be allowed to work on the plant in India for an agreed period and if they shall be satisfied with the claim of the appellant, it would pay a compensation. On trial by their Engineers, the appellant was proved right in its claim made and the manufacturer granted a compensation of DM 7 Million which amounted to Rs. 16,05,29,977 in the financial year 1998-99 relevant to the assessment year 1999-00.

5. We have gone through the order of Ld. CIT (A). He decided the matter in favour of the assessee relying on the order of his predecessor for AY 1999-2000. Although, appeal for the same year, is still pending before the Coordinate Bench. We have gone through the facts of the case and the findings of the authorities below, we find the order of Ld. CIT (A) to be correct in facts and in law. To arrive at a conclusion, we relied upon the following judicial pronouncements of Hon’ble Supreme Court and Hon’ble High Court of Calcutta as under:-

[2010] 192 Taxman 300 (SC) CIT, Gujarat *v.* Saurashtra Cement Ltd.

"It was clear from the agreement that the liquidated damages were to be calculated at 0.5 per cent of the price of the respective machinery and equipment of which the items were delivered late, for each month of delay in delivery completion, without proof of the actual damages the assessee would have suffered on account of the delay. The delay in supply could be of the whole plant or a part thereof but the determination of damages was not based upon the calculation made in respect of loss of profit on account of supply of a particular part of the plant. It was evident that the damages to the assessee were directly and intimately linked with the procurement of a capital asset, i.e., the cement plant, which would obviously lead to delay in coming into existence of the profit-making apparatus, rather than a receipt in the course of profit-earning process. Compensation paid for the delay in procurement of capital asset amounted to sterilization of the capital asset of the assessee as supplier had failed to supply the plant within time as stipulated in the agreement. The amount received by the assessee towards compensation for sterilization of the profit-earning source and not in the ordinary course of its business, was a capital receipt in the hands of the assessee. [Para 13]"

[2022] 143 taxmann.com 58 (Cal.) PCIT *v.* XPRO India Ltd.

"The next issue is with regard to the compensation received from M/s. Batenfeld, UK. The Assessing Officer was of the view that the entire amount of compensation had reduced the cost of the machinery and therefore, denied relief to the assessee. The correctness of the said finding was considered by the CIT (A) and after noting that the entire amount of compensation would not reduce the actual cost of machinery and there is no dispute to the fact that the assessee had capitalised the full invoice value of machinery in its books of accounts and accordingly, claimed depreciations and noting the decision of the Hon'ble Supreme Court in Sourashtra Cement Ltd. (supra) directed the Assessing Officer to restrict the disallowance of depreciation pertaining to 10% of the compensation received by the assessee which will go to reduce the cost of machinery, and for the remaining amount the assessee's case was accepted. With regard to the 10% of the amount which was directed to be restricted, the assessee was not an appeal before the Tribunal. The Tribunal after considering the findings recorded by the CIT (A) examined the settlement which was executed between the assessee and the UK Company which show that the compensation was given on account of non-achievement of performance parameters. After noting the relevant clauses in the settlement agreement, the Tribunal held that the condition specified in section 143 (1) of the Act for directing the actual cost from value of the machines were applicable to the compensation amount paid to the assessee. We find

there is no error in the approach of the Tribunal or that of the CIT (A) for us to interfere. Accordingly, substantial questions of law No. 7 and 8 are answered against the revenue."

6. In view of above facts and decision of Hon'ble Supreme Court on similar facts in the case of Saurashtra Cement Ltd. (supra), we hold that stand of the assessee is correct and action of AO is liable to be reversed. As assessee has incurred full cost of acquisition out of its own pocket and no part of cost has been borne by anybody else. In the given circumstances, amount of compensation received cannot be equated with "Cost bear by third party". Hence WDV of the assets cannot be adjusted by this amount of compensation received by the assessee. In the result ground raised by the revenue is dismissed.

7. **In the result, appeal of the revenue is dismissed.**

Order pronounced in the open court on 25th day of August, 2023.

Sd/- Sd/-

(AMIT SHUKLA) (GAGAN GOYAL)
JUDICIAL MEMBER ACCOUNTANT MEMBER
Mumbai, दिनांक/Dated: 25/08/2023
Sr. PS (Dhananjay)

Copy of the Order forwarded to:

1. अपीलार्थी/The Appellant ,
2. प्रतिवादी/ The Respondent.
3. आयकर आयुक्त CIT
4. विभागीय प्रतिनिधि, आय.अपी.अधि., मुबंई/DR, ITAT, Mumbai
5. गार्ड फाइल/Guard file.

BY ORDER,

//True Copy//

(Asstt. Registrar)
ITAT, Mumbai