आयकर अपीलीय अधिकरण, अहमदाबाद न्यायपीठ "डी", अहमदाबाद ।
IN THE INCOME TAX APPELLATE TRIBUNAL
"D" BENCH, AHMEDABAD

श्री टी.आर. सेन्थिल कुमार, न्यायिक सदस्य एवं
श्री मकरंद वसंत महादेवकर, लेखा सदस्य के समक्ष।

BEFORE SHRI T.R. SENTHIL KUMAR, JUDICIAL MEMBER &
SHRI MAKARAND V. MAHADEOKAR, ACCOUNTANT MEMBER

Sl. No(s)	आयकर अपील सं/ ITA No(s)	निर्धारण वर्ष/ Assess-ment Year(s)	Appeal(s) by :	
			अपीलार्थी / Appellants	बनाम/vs. प्रत्यर्थी / Respondents
1.	784/Ahd/2013	2003-04	M/s.Munjal Auto Industries Ltd. 187, GIDC Estate Waghodia, Baroda 391 760 (Assessee) PAN: AAACG8588 L	The Income Tax Officer Ward-4(1) Baroda (Revenue)
2.	2007/Ahd/2007	2004-05	The DCIT Circle-4(1),Baroda	By Assessee
3.	1619/Ahd/2008	2005-06	-do-Revenue	By Assessee
4.	1382/Ahd/2009	2003-04	-do-Revenue	By Assessee
5.	1383/Ahd/2009	2006-07	-do-Revenue	By Assessee

Assessee by :	Ms. Amrin Pathan, AR
Revenue by :	Shri Waghe Prasadrao, Sr.DR

सुनवाई की तारीख/**Date of Hearing** : **27 /02/2025**
घोषणा की तारीख /**Date of Pronouncement:** **25 /03/2025**

आदेश/O R D E R

PER BENCH:

These appeals, filed by the assessee and the revenue, pertain to Assessment Years (AYs) 2003-04 to 2006-07 and arise from separate orders passed by the Commissioner of Income Tax (Appeals)-III, Baroda [hereinafter referred to as "CIT(A)"]. Since the facts and issues involved in these appeals

are interconnected, they have been heard together and are being disposed of by this consolidated order.

Background of the case:

2. The present set of appeals arises from disputes regarding the tax treatment of sales tax subsidies received by M/s. Munjal Auto Industries Ltd., the assessee, from the State Governments of Punjab and Haryana. The core issue pertains to whether the sales tax subsidy should be treated as a capital or revenue receipt, and its subsequent impact on depreciation computation and Minimum Alternate Tax (MAT) liability under Section 115JB of the Income Tax Act, 1961 [hereinafter referred to as "the Act"].

2.1. The Co-ordinate Bench had earlier adjudicated these appeals for Assessment Years 2003-04 to 2006-07 vide its order dated 21.12.2011. The appeals included:

- ITA No. 1382/Ahd/2009 & ITA No. 1420/Ahd/2009 – Cross appeals for A.Y. 2003-04.
- ITA No. 2007/Ahd/2007 – Appeal for A.Y. 2004-05.
- ITA No. 1619/Ahd/2008 – Appeal for A.Y. 2005-06.
- ITA No. 1383/Ahd/2009 – Appeal for A.Y. 2006-07.

2.2. During the first round of litigation, the Assessing Officer [hereinafter referred to as "AO"] treated the sales tax subsidy as a revenue receipt, making it taxable. The CIT(A) held it to be capital in nature, providing relief to the assessee. However, the Co-ordinate Bench while confirming the capital nature of the subsidy, held that the subsidy must be reduced from the cost of fixed assets, thereby reducing depreciation. Consequently, the issue was

restored to the AO for re-computation of depreciation. Following this, both the assessee and the Revenue filed appeals before the Hon'ble Gujarat High Court, challenging different aspects of order of Co-ordinate Bench.

2.3. On 28-01-2013 Hon'ble Gujarat High Court first adjudicated the Revenue's appeal in Tax Appeal No. 450, 451 and 453 of 2012, which challenged the ITAT's decision of treating the sales tax subsidy as a capital receipt. Following question of law was framed before the Hon'ble High Court-

> *"Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the sales tax incentive is a capital receipt without considering the fact that subsidy in the form of sales tax deferment was given by the Government of Haryana to the assessee company much after the commencement of business to augment the normal business running of Binola Unit and not for setting up of business and should, therefore, have been treated as a revenue receipt?"*

2.4. The Hon'ble High Court dismissed Revenue's appeals, holding that the Tribunal was correct in treating the subsidy as capital in nature.

2.5. Subsequently, in another judgement dated 12.02.2013, the Hon'ble Gujarat High Court ruled on the assessee's appeal in Tax Appeal Nos. 342 to 345 of 2012. Following substantial questions of law were adjudicated by the Hon'ble High Court –

> *"(i) Whether on the facts and in the circumstances of the case, the Tribunal was within its rights in giving a direction to the Assessing Officer that he must allow the depreciation on the actual cost reduced by the amount of such subsidy under sec.43(1) of the Income Tax Act, 1961?*
>
> *(ii) Even if the reply to the above question is in the affirmative, whether the Tribunal was right in law in holding that the portion of the actual cost is met directly or indirectly by the above subsidy as required by section 43(1), and therefore, the Assessing Officer must allow depreciation on such reduced cost (actual cost less subsidy)?"*

2.6. The Hon'ble High Court set aside the order of the Co-ordinate Bench on second issue and remanded the matter back to the Tribunal for reconsideration, directing the ITAT to decide the issue afresh in light of the concluded nature of the subsidy by virtue of the judgement dated 28-01-2013. While doing so the Hon'ble High Court concluded on the first question of law affirming the power of Tribunal to direct the Assessing Officer. Following are the relevant paras from the judgement of the Hon'ble High Court relating to second question of law –

> *"7. Though ordinarily, it may be true that the subsidies, which are in the nature of capital receipts given for covering the capital details for acquisition of fixed assets such as plants, machineries, land and building etc., may go on to reduce the cost of acquisition of such assets and resultantly, may have an effect of reducing the depreciation available on the assets on such investment, nevertheless, this cannot be held to be a rule of universal application without examination of relevant facts. In this respect, we had noticed several decisions of this Court cited by counsel for the assessee and noted by us in earlier order dated 08.01.2013.*
>
> *8. Though applicability of the proposition canvased by the Tribunal itself was open to argument on the basis of facts on record, in our opinion, the Tribunal committed an error in giving directions 1) without availing opportunity of hearing to the assessee and 2) without discussion of facts on record or law applicable to it. The relevant observation of the Tribunal is only discussed to throw light on this aspect of the matter.*
>
> *9. Under the circumstances, we request the Tribunal to consider the issue afresh bearing in mind the nature of subsidy, purpose for which the same was made available and all other relevant factors bearing in mind the case laws cited before us and which may further be argued before the Tribunal by both the sides. For this limiter purpose, the question is placed before the Tribunal for afresh consideration and disposal in accordance with law.*
> *10. We clarify that we express no opinion on merit or demerit of rival contentions raised before the Tribunal."*

2.7. While these matters were pending, the issue concerning the taxability of sales tax subsidy was escalated to the Hon'ble Supreme Court in Civil Appeal Nos. 6226 and 6227 of 2013, wherein the Revenue contested the ruling of the Hon'ble Gujarat High Court in assessee's own case, which had classified the subsidy as a capital receipt. Vide order dated 08.05.2018, the Hon'ble Supreme Court dismissed the Revenue's appeal, thereby affirming the classification of the sales tax subsidy as capital in nature.

2.8. In light of the Apex Court's ruling, the characterisation of the subsidy stands conclusively determined. The only substantive issues remaining for adjudication before us pertain to the treatment of the subsidy in relation to the cost of fixed assets, its impact on depreciation computation under Section 43(1) of the Act, and its implications for the determination of book profits under Section 115JB.

2.9. Following appeals have now been reconstructed and listed for adjudication -

ITA No.	**Assessment Year**	**Appellant**	**Amount in Dispute (Rs.)**
784/Ahd/2013	2003-04	Assessee	Not quantified
2007/Ahd/2007	2004-05	Revenue	62,38,589/-
1619/Ahd/2008	2005-06	Revenue	56,33,154/-
1382/Ahd/2009	2003-04	Revenue	88,89,959/-
1383/Ahd/2009	2006-07	Revenue	19,48,517/-

2.10. The respective relevant grounds of appeal raised by assessee and revenue are:

Assessee's appeal in ITA No. 784/Ahd/2013 for A.Y. 2003-04

All the grounds of appeal in this appeal are mutually exclusive and without prejudice to each other.

1. The learned CIT(A) erred in fact and in law in confirming the action of the Assessing Officer in recomputing the book profit u/s. 115JB of the Act.

2. The learned CIT(A) erred in fact and in law in holding that the amount of sales tax subsidy is required to be reduced from the cost of fixed asset and thereby depreciation is to be recalculated for the purpose of computing book profit u/s 115JB of the Act.

3. The learned CIT(A) erred in fact and in law in holding that the accounts of the Appellant have not been prepared in accordance with Part II and III of Companies Act, 1956.

4. Your Appellant craves the right to add to or alter, amend, substitute, delete or modify all or any of the above grounds of appeal.

Revenue's appeal in ITA No.2007/Ahd/2007 for AY 2004-05

1) The Ld. CIT(A) has erred in law and on facts in deleting the amount of Rs.62,38,589/- being subsidy given by State Government in the form of sales tax deferment being the amount added by Assessing Officer treating it as revenue receipt for the reason that subsidy was not for fixed assets but was to augment the normal business running of Binola Unit which had been established years back so question of setting up of new industrial unit does not arise as per finding of the AO.

Revenue's appeal in ITA No.1619/Ahd/2008 for AY 2005-06

1. The Ld. CIT (A) has erred in law and on facts in deleting the amount of its 56,33,154/- being subsidy given by State Government in the form of sales tax deferment being the amount added by Assessing Officer treating it as revenue receipt for the reason that subsidy was not for fines assets but was to augment the normal business running of Binola Unit which had been established years back, so question of setting up of new industrial watt does not arise as per finding of the AO.

Revenue's appeal in ITA No.1382/Ahd/2009 for AY 2003-04

1. On the facts and in the circumstances of the case, the learned CIT(A) erred in deleting the amount of Rs.88,89,959/- being subsidy given by State Government in the form of sales tax deferment being the amount added by the Assessing Officer treating it as revenue receipt for the reason that subsidy was not for fixed assets but was to augment the normal business running of Binola Unit and was not for setting up of new industrial unit.

Revenue's appeal in ITA No.1383/Ahd/2009 for AY 2006-07

1. On the facts and in the circumstances of the case, the learned CIT(A) erred in deleting the revenue receipt of Rs.19,48,517/- being subsidy given by Haryana State Government in the form of sales tax and VAT incentive, the objective of which was not for encouraging or setting up of new industrial unit but was to augment the normal business of Binola Unit, which was patently against the principle laid down by the apex court in the case of Sahney Steel & Press Works Ltd. etc. V/s CIT 228 ITR 253 (SC).

3. During the course of hearing the Departmental Representative (DR) made a detailed submission before us, focusing on the applicability of Explanation 10 to Section 43(1) of the Income-tax Act, 1961, and the correct computation of book profits under Section 115JB of the Act.

3.1. On this background, we now first deal with Revenue's Grounds of appeals. Before delving into the core issue, the DR pointed out that there is no dispute that the subsidy is capital in nature. The DR relied on Explanation 10 to Section 43(1) of the Act, which was amended by inserting Explanation 10 w.e.f. 01.04.1999. As per Explanation 10, if a portion of the cost of an asset is met, directly or indirectly, by the government in the form of a subsidy, grant, or reimbursement, such portion must be reduced from the actual cost of the asset for the purpose of depreciation. The proviso to Explanation 10 clarifies that even if the subsidy is not directly linked to a specific asset, it must still be proportionately allocated and deducted from the total asset cost.

4. The Authorised Representative (AR) of the assessee contended that the incentive received by the assessee in the form of sales tax deferment does not fall within the ambit of Explanation 10 to Section 43(1) of the Act. The AR submitted that Explanation 10 requires a direct or indirect nexus between the subsidy and the cost of acquisition of fixed assets for it to be reduced from the cost of such assets. However, in case of assessee, the sales tax deferment scheme does not provide any direct financial assistance for acquiring fixed assets. Instead, it is a mechanism introduced by the State Government for industrial development, wherein the assessee was required to collect sales tax, deposit it in a reserve account, and later pay 50% of the collected amount to the government while retaining the remaining 50% as a subsidy.

4.1. The AR emphasized that the incentive was granted post-commencement of production, meaning that it was not meant to subsidise the cost of acquiring fixed assets but rather to assist in the operation of the business. The AR stated that this fact has been acknowledged by both the AO and the CIT(A), who accepted that the subsidy was not received for meeting the cost of assets.

4.2. To further substantiate the claim, reliance was placed on the judgment of the Hon'ble Bombay High Court in the case of *Pr. CIT vs. Welspun Steel Ltd.* [(2019) 264 Taxman 252], where it was held that subsidies granted for the development of industries, without any direct linkage to the cost of acquisition of fixed assets, cannot be deducted from the cost of such assets.

4.3. The AR submitted that in the present case as well, since the subsidy was not granted for acquiring plant and machinery but was instead linked to post-commencement operations, the same should not be reduced from the cost of fixed assets.

4.4. The AR also referred to the Hon'ble Gujarat High Court's decision in *CIT vs. Grace Paper Industries Pvt. Ltd.* [183 ITR 591] and *CIT vs. Swastik Sanitary Works Ltd.* [286 ITR 544], as well as the Hon'ble Supreme Court's ruling in *CIT vs. P.J. Chemicals Ltd.* [(1994) 210 ITR 830], where similar principles were upheld. Additionally, the AR argues that the revenue's reliance on Explanation 10 to Section 43(1) is misplaced, as this provision applies only when a subsidy or grant is directly linked to the acquisition of an asset.

4.5. The AR concluded that the incentive received by the assessee does not satisfy the conditions prescribed under Explanation 10 to Section 43(1) and, therefore, should not be deducted from the cost of fixed assets for the purpose of computing depreciation.

5. The DR referred the observations of this Bench in its order passed in ITA No.1382 and 2007/Ahd/2007 and 3 others dated 21.12.2011, where it was held the subsidy received for fixed assets is required to be deducted from the actual cost of fixed assets, and depreciation must be recalculated accordingly. For the sake of clarity, the same is reproduced here –

> *"11. We have considered rival submissions and have perused the material on record and gone through the orders of the authorities below. We find that in the course of the assessment proceedings, it was stated by the AO in the show cause notice issued to the assessee on 17.11.2006 that the assessee was requested to show cause as to why*

the amount of capital subsidy should not be reduced from the cost of respective assets for the purpose of calculating depreciation. In reply dated 27.11.2006, it was submitted by the assessee before the AO that the amount of sales-tax incentives received by the assessee of Rs.62,38,589/- was included in the schedule-2 of reserves and surplus and the amount was not subsidy for the fixed assets. It was submitted that the incentive is with reference to the sales made after the fixed assets were put to use and hence, this was not a case in which portion of cost of fixed assets was met by the Government and therefore, this amount was not required to be deducted from the cost of fixed assets. In view of this reply of the assessee, now it emerges that when the AO considered this receipt of subsidy as capital receipt and asked for reduction of the same from the cost of fixed assets for the purpose of calculating depreciation allowable to the assessee, it was the submission of the assessee before the AO that this incentive is with reference to sales made after the fixed assets were put to use and therefore, it was not a capital receipt meant for cost of fixed assets. When the AO treated the amount of subsidy as revenue receipt, the case of the assessee is that it is a capital receipt. The decision of the Special of the Tribunal rendered in the case of Reliance Industries (supra) has been relied upon by the learned CIT(A) to hold that this receipt as capital receipt, however, there is no finding given by the learned CIT(A) as to whether the subsidy is required to be reduced from the cost of fixed assets for the purpose of calculating depreciation allowable to the assessee. Once it is accepted that the subsidy receipt by the assessee is with reference to the fixed assets and therefore, capital receipts and not includible in the total income of the assessee as revenue receipt, the natural consequence is this that the same is required to be reduced from the cost of fixed assets for the purpose of calculating depreciation as per the provisions of section 43(1) of the Act. On this aspect, the decision of the Special Bench of the Tribunal is silent. Similarly, in the case of Ponni Sugars & Chemicals (supra) also, this issue was not before the Hon'ble Apex Court as to whether the subsidy received by the assessee and treated as capital receipt is required to be reduced from the cost of fixed assets for the purpose of computation of depreciation allowed to the assessee. In the present case, this was the first proposition put forward by the AO in the course of assessment proceedings and although in the ground of the appeal before us by the Revenue, this contention is not put forward in so many words, but this is the ground of the Revenue that the learned CIT(A) is wrong in holding that the AO was wrong in treating the subsidy as revenue receipt for the reason that subsidy was not for fixed assets. Hence, as per this ground of the revenue, it comes out that if it is held that the subsidy is for fixed assets, then the natural consequence as per the law should follow and if it is held that it is not for fixed assets, then the same should be required to be added to the income of the assessee as revenue receipt. On this aspect, as to whether the subsidy receipt by the assessee is revenue or capital receipt, we feel that this aspect is covered in favour of the assessee by the decision of the Special Bench rendered in the case of Reliance Industries (supra) and also by the judgment of the Hon'ble Apex Court in the case of Ponni Sugar & Chemicals Ltd. (supra) and hence, we decide this issue in favour of the assessee. But at the same time, we direct the AO to consider the receipt as subsidy received by the assessee for fixed assets and therefore, the AO should recalculate the depreciation as per the law after

reducing the amount of subsidy from the cost of fixed assets as per the provisions of section 43(1) of the Act. Before doing so, the AO should provide reasonable opportunity of being heard to the assessee and thereafter he should pass necessary order as per the law on these aspects."

5.1. The DR also pointed out the stand taken by the assessee in its grounds of appeal and also the submission of the assessee during the assessment and appellate proceedings which put forward the argument that the subsidy was granted as an incentive for sales rather than for purchasing fixed assets. The DR refuted this and stated that the subsidy was directly linked to fixed capital investment and that the manufacturing unit could not be set up without purchasing fixed assets and the quantum of subsidy was determined based on a prescribed percentage of fixed capital investment. The DR emphasized that the subsidy was calculated based on sales made after the assets were put to use, but its eligibility was tied to capital investment and therefore it falls squarely within the ambit of Explanation 10 to Section 43(1), requiring a proportionate reduction from cost of assets. The DR further demonstrated that the subsidy was conditional upon fixed capital investment.

5.2. The DR stressed that if the assessee had not invested in fixed capital, it would not have been eligible for the subsidy, irrespective of sales turnover, which proved that the subsidy was inherently a reimbursement of capital cost, even if it was calculated post-commencement. The DR explained that granting subsidies after production commencement ensures that industries actually operate rather than misusing upfront incentives. Thus, the timing of subsidy receipt does not alter its capital nature, and it must still be deducted from fixed asset costs under Explanation 10 to section 43(1) of the Act. The assessee had contended that there was no direct link between the subsidy and

fixed asset acquisition since the subsidy was granted based on sales after the assets were put to use. The DR countered this by stating that the subsidy was for putting the fixed assets to use, the quantum of subsidy was capped by the amount spent on fixed capital and thus, the nexus between subsidy and fixed assets was clearly established.

6. The AR placed reliance on the judgment of Hon'ble Bombay High Court in the case of Welspun Steel Ltd. (supra) to argue that the sales tax subsidy received by the assessee should not be deducted from the cost of fixed assets for depreciation purposes. The DR countered by arguing that the Bombay High Court's decision was based on case laws that predate the insertion of Explanation 10 and, therefore, cannot override the statutory provisions. The DR pointed out that the Hon'ble Bombay High Court while holding that 'No question of law, therefore, arises in this respect" in respect of issue of reduction of capital subsidy from the cost of the fixed assets, has relied upon the following three judgements:

- CIT v. Grace Paper Industries (P.) Ltd. [1990] 183 ITR 591/52 Taxman 18 (Guj HC).
- CIT v. Swastik Sanitary Works Ltd. [2006] 286 ITR 544 (Guj HC).
- CIT v. P. J. Chemicals Ltd., [1994] 210 ITR 830 (Supreme Court).

7. The DR argued that the Hon'ble Bombay High Court's ruling in Welspun Steel Ltd. is ultimately based on the ratio laid down in P.J. Chemicals Ltd. and other pre-1999 cases, without analysing the impact of Explanation 10 to section 43(a) o. The AR further argued that Hon'ble Supreme Court's ruling in P.J. Chemicals Ltd. (1994) did not consider

Explanation 10, therefore, any reliance on it without accounting for the statutory amendment is misplaced.

7.1. The DR placed reliance on Kinfra Export Promotion Industrial Parks Ltd. vs. Joint Commissioner of Income Tax (OSD), Kerala High Court (ITA No. 62 & 65/2018, judgment dated 07.04.2022), which explicitly held that the financial assistance received without reference to a specific purpose, still by application of proviso to Explanation 10 of section 43(1) of the Act, is apportioned and reduced from the cost of the assets of the assessee for the purpose of computation of depreciation. The DR highlighted that before the Hon'ble Kerala High Court, the Senior Advocate representing the assessee had specifically relied on the Welspun ruling, but the High Court rejected its applicability, emphasizing that financial assistance received without reference to a specific purpose must still be apportioned and deducted from the cost of the asset under Explanation 10 of section 43(1) of the Act.

8. During the course of hearing before us, the AR contended that in the case of Kinfra Export Promotion Industrial Parks Ltd., the Hon'ble Kerala High Court had held that proportionate reduction of the subsidy from the cost of the asset could be against the assets which received the financial assistance under ASIDE and therefore only so much of the amount should be apportioned from the cost of foxed asset which was actually utilized from the amount of financial assistance received. The AR further contended that since no fresh funds were infused in the form of grant and on the contrary, the sales tax collected was kept as reserve and on satisfaction of conditions prescribed used as subsidy. In this regard, the DR submitted that the contention raised by the AR is misplaced and has no relevance to the present case. The DR

further submitted that the decision of the Hon'ble Kerala High Court was based on the specific contention of the assessee in that case, which was that the subsidy received was utilised for the purchase of a specific asset (such as capacity building of the water and power distribution infrastructure) and in that context, the Hon'ble Kerala High Court had directed the Assessing Officer to consider the assessee's argument and reduce the subsidy from the actual cost of the asset for which it had been specifically utilised.

9. The DR also placed reliance on the decision of Co-ordinate Bench in case of Pargo Frozen Foods Pvt. Ltd. Vs. ITO in ITA No. 1076/Chd/2018 for A.Y. 2014-15 where it was held that when a portion of the cost of an asset has been met directly or indirectly by the government in the form of a grant or subsidy, such amount must be reduced from the actual cost of the asset while computing depreciation.

10. We have heard the rival contentions and perused the material available on the records. Before addressing the specific contentions raised, it is pertinent to reiterate that there is no dispute regarding the capital nature of the subsidy. The core issue in the present appeal revolves around whether the sales tax deferment incentive received by the assessee qualifies for reduction from the actual cost of assets under Explanation 10 to Section 43(1) of the Income-tax Act, 1961. The said explanation reads as follows:

> *"Where a portion of the cost of an asset acquired by the assessee has been met directly or indirectly by the Central Government or a State Government or any authority established under any law or by any other person, in the form of a subsidy or grant or reimbursement (by whatever name called), then, so much of the cost as is relatable to such subsidy or grant or reimbursement shall not be included in the actual cost of the asset to the assessee:*
> *Provided that where such subsidy or grant or reimbursement is of such nature that it cannot be directly relatable to the asset acquired, so much of the amount which*

bears to the total subsidy or reimbursement or grant the same proportion as such asset bears to all the assets in respect of or with reference to which the subsidy or grant or reimbursement is so received, shall not be included in the actual cost of the asset to the assessee."

10.1. Explanation 10 to section 43(1) of the Act introduced w.e.f. 01.04.1999, mandates that if a portion of the cost of an asset is met, directly or indirectly, by the Government in the form of a subsidy, grant, or reimbursement, such portion must be deducted from the actual cost of the asset for the purpose of computing depreciation. The proviso to Explanation 10 to section 43(1) of the Act further clarifies that even if the subsidy is not directly linked to a specific asset, it must still be proportionately allocated and deducted from the total cost of the block of assets.

10.2. We find that the mode of settlement of a subsidy or financial assistance can be either through direct payment or by allowing the retention of statutory liabilities. In both cases, the benefit accrues to the assessee, and the economic effect remains the same. Non-payment of a government-mandated liability is tantamount to an additional inflow of funds, and therefore, such incentives fall squarely within the ambit of Explanation 10 to section 43(1) of the Act. Further, it is well established that once an asset is merged into the block of assets, its individual identity is lost. The depreciation scheme under the Act operates on the principle that the cost of an asset ceases to have a standalone significance once it is added to the block. Thus, even if a financial incentive is not linked to a specific asset, it must still be adjusted against the cost of the entire block. The method of receipt, whether in cash or through liability retention, does not alter this principle.

10.3 The AR submitted that the sales tax deferment scheme availed by the assessee does not fall within the purview of Explanation 10 to section 43(1) of the Act, as it does not constitute direct financial assistance towards the acquisition of fixed assets. It was argued that the scheme was implemented as a post-commencement incentive for industrial development and lacked any direct nexus with the cost or acquisition of fixed assets. To support this argument, reliance was placed on the judgment of the Hon'ble Bombay High Court in *Pr. CIT vs. Welspun Steel Ltd.* [(2019) 264 Taxman 252], wherein it was held that subsidies granted for industrial development, without a direct link to the acquisition of plant or machinery, cannot be reduced from the cost of such assets.

10.4. We are unable to accept the contention advanced by the AR. On a close examination, it is evident that the Hon'ble Bombay High Court's ruling in *Welspun Steel Ltd.* was based on judicial precedents, such as *CIT vs. P.J. Chemicals Ltd.* [(1994) 210 ITR 830 (SC)], that predate the insertion of Explanation 10 to section 43(1) of the Act, which came into effect from 01.04.1999. Explanation 10 is a statutory amendment that overrides any earlier judicial interpretation rendered without considering its scope and effect. It explicitly provides that any subsidy or grant, whether received directly or indirectly, and even if not linked to a specific asset, must be reduced from the cost of the asset. Accordingly, reliance on pre-1999 case law, without appreciating the overriding effect of Explanation 10, is misplaced. Therefore, we are of the view that the assessee's contention does not withstand the test of law post-insertion of the said Explanation.

10.5. We find that the sales tax incentive availed by the assessee, as noted in Part-II of Schedule-16 of the Notes on Accounts, was fundamentally linked to its fixed capital investment. The eligibility for this incentive was contingent upon the investment in fixed assets, as the scheme itself was framed to support industrial development. While the quantum of subsidy was ultimately determined based on post-commencement sales, the nature of the incentive remained a capital subsidy, as it was later converted into a capital reserve. Furthermore, as explicitly stated in the financial statements, the subsidy would become payable to the government if specified conditions were not met, reinforcing its conditional and capital nature. If the assessee had not undertaken the required fixed capital investment, it would not have been eligible for the subsidy, regardless of its sales turnover. The fact that the incentive was structured as a deferment of statutory liability, later converted into a capital reserve, does not alter its fundamental nature. Non-payment of a statutory liability is functionally equivalent to a direct inflow of funds, making the subsidy fall squarely within the ambit of Explanation 10 to Section 43(1) of the Act. Consequently, the subsidy must be deducted from the cost of fixed assets for the purpose of depreciation computation. We also take note of the ruling in Kinfra Export Promotion Industrial Parks Ltd. vs. Jt. CIT (ITA No. 65 of 2018, reported in [2022] 137 taxmann.com 379, Kerala HC), where it was held that even financial assistance without reference to a specific asset must be apportioned and deducted from the cost of the assets under Explanation 10 to section 43(1) of the Act.

10.6. In light of the above discussion, we hold that the sales tax deferment incentive received by the assessee qualifies for reduction from the actual cost of assets under Explanation 10 to Section 43(1) of the Act. The fact that the

subsidy was received after the commencement of production does not alter its fundamental character, as its eligibility was directly tied to the assessee's fixed capital investment.

10.7. We reject the assessee's contention that the mode of receipt determines the applicability of Explanation 10. The statutory liability retained by the assessee is equivalent to an inflow of funds, and thus, the benefit derived from it must be adjusted against the asset cost. Once the asset is merged into the block of assets, its individual character is lost, making the proportionate reduction of subsidy from the block cost mandatory.

10.8. We also find strength in the observations made by the Co-ordiante Bench in its order in ITA No. 1382 and 2007/Ahd/2007, dated 21.12.2011, where it was held that a subsidy received for fixed assets must be deducted from the actual cost of fixed assets, and depreciation must be recalculated accordingly. The assessee had contended that the sales tax incentive was linked to sales made after the fixed assets were put to use and not meant for asset acquisition. However, once it was accepted that the subsidy was in reference to fixed assets and was a capital receipt, the natural consequence under the law was that it must be reduced from the cost of fixed assets for the purpose of calculating depreciation. The Co-ordinate Bench in that case had also directed the AO to recalculate depreciation after reducing the amount of subsidy from the cost of fixed assets, in accordance with Section 43(1). This earlier decision of the Co-ordinate Bench reaffirms the principle that once a subsidy is categorised as capital in nature, its treatment must align with Explanation 10, mandating a proportionate deduction from the cost of fixed assets.

10.9. In its grounds of appeal, the Revenue has contended that the CIT(A) erred in holding that the sales tax subsidy is capital in nature and should be deducted from the cost of fixed assets. However, we find no merit in this ground, as the capital nature of the subsidy is undisputed, and once classified as such, its reduction from the cost of fixed assets follows as a natural consequence under Explanation 10 to section 43(1) of the Act.

10.10. In view of the above findings and conclusions, we direct the AO to recalculate depreciation in accordance with Explanation 10 to Section 43(1). The AO shall reduce the proportionate amount of subsidy from the actual cost of fixed assets, in line with the findings of the Co-ordinate Bench and re-compute depreciation on the revised cost of assets, following the provisions of Section 32 of the Act.

10.11. In light of the above discussions, the **appeals filed by the Revenue are dismissed**, and the directions issued to the AO by the Co-ordinate Bench for re-computation of depreciation are upheld.

11. Now we deal with the assessee's appeal in ITA No.784/Ahd/2013 for A.Y. 2003-04. This arises from the order passed by the AO under Section 143(3) r.w.s. 147 of the Act, on 20.11.2008, wherein an addition of Rs. 62,38,589/- was made to the total income of the assessee under normal provisions by treating the sales tax subsidy as revenue in nature. Additionally, the AO made an adjustment to the Book Profit under Section 115JB of the Act. Aggrieved, the assessee filed an appeal before the CIT(A), who deleted the addition of sales tax subsidy under normal provisions.

However, one of the grounds raised by the assessee regarding the adjustment of sales tax subsidy while computing Book Profit under Section 115JB was not adjudicated by CIT(A). Subsequently, the matter reached this Bench, where the assessee contended that the CIT(A) erred in not directing the AO to reduce the sales tax subsidy from the Book Profit under Section 115JB. The Co-ordinate Bench, vide its order in ITA No. 1420/Ahd/2009 dated 21.12.2011, restored the matter to the file of CIT(A) for fresh adjudication of the issue related to Section 115JB. In compliance with the Tribunal's directions, the CIT(A) vide order dated 24.02.2012 examined the issues raised by the assessee concerning the treatment of sales tax subsidy and its impact on book profit computation under Section 115JB of the Act and concluded that once a subsidy is accepted as a capital receipt, it should be adjusted against the cost of the asset. Regarding the re-computation of book profit under Section 115JB, the CIT(A) held that the AO could not arbitrarily add back the subsidy amount, as book profit is to be computed as per net profit disclosed in the Profit & Loss Account. However, since the subsidy affects depreciation, which in turn affects the net profit, the AO was directed to recompute depreciation and then revise the book profit accordingly.

12. Aggrieved by the decision, the assessee has preferred the present appeal before us, challenging the CIT(A)'s finding.

13. During the course of hearing before us, the AR submitted that the appellant had received sales tax subsidy for its Binola Unit, Haryana, under the Sales Tax Deferment Scheme granted by the State of Punjab & Haryana. The assessee had treated the sales tax subsidy as a capital receipt and credited the same to the Capital Reserve Account in its books of accounts.

13.1. The AR further submitted that since book profits are computed as per the Companies Act, 1956, the treatment given by the assessee was correct. The AR emphasized that the Co-ordinate Bench had already decided that the sales tax subsidy is a capital receipt and, therefore, should not be included in the book profit. The AO's action of adding it back was incorrect as per Supreme Court ruling in Apollo Tyres Ltd. v. CIT (2002) 255 ITR 273 (SC), which held that the AO has no power to alter the book profits unless the accounts are not prepared as per the Companies Act.

13.2. The AR submitted that the assessee is a public company, and its Profit & Loss Account is prepared in accordance with Part II & III of Schedule VI of the Companies Act, 1956. There was no allegation that the accounts were not prepared in compliance with the Companies Act. The statutory auditors had certified the accounts, and the shareholders had approved them in the AGM. Therefore, the AO had no authority to alter the net profit unless there was misrepresentation, fraud, or non-compliance with Schedule VI of the Companies Act.

13.3. As per Section 211(3C) of the Companies Act, 1956, the AR further argued that every company is required to prepare its accounts in accordance with Accounting Standards (AS) issued by ICAI. The AR relied on AS-12 (Accounting for Government Grants), which provides that government grants in the nature of promoters' contribution should be credited to capital reserve and not routed through the Profit & Loss Account. The AR referred to para 10.1 of AS-12, which states that where government grants are given

with reference to total investment in an undertaking, such grants are treated as capital reserve and not as deferred income.

13.4. Regarding the direction of the Co-ordinate Bench to reduce the subsidy from the cost of fixed assets, the AR submitted that this direction would not adversely affect the assessee's case. The sales tax subsidy was not granted for specific fixed assets and, therefore, should not be reduced from the cost of assets for depreciation purposes. The AR referred to para 14 of AS-12, which states that only government grants related to specific fixed assets should be shown as a deduction from the gross value of the asset. In the present case, the subsidy was a general grant under the Sales Tax Deferment Scheme and was not for any particular asset. Therefore, it was correctly credited to capital reserve, and no adjustment was required in book profits.
On the assessee's grounds relating to re-computation of book profits in accordance of section 115JB of the Act, the DR submitted that as per the Explanation [1] to Section 115JB of the Income-tax Act, 1961, "book profit" means the net profit as shown in the profit and loss account for the relevant previous year, prepared under sub-section (2), as increased by "the amounts carried to any reserves, by whatever name called, other than a reserve specified under section 33AC." (as per Clause (b) of the explanation). The DR contended that the assessee did not route the sales tax collected through the profit and loss account but directly credited it to the "Sales Tax Capital Reserve." This was despite the fact that there was no change in the accounting method employed by the assessee in preceding years, as per Form No. 3CD, Column No. 11(6).

14. The DR further argued that the sales tax so collected but not remitted assumes the character of income, and the act of creating a Sales Tax Subsidy effectively results in the amount being carried to a reserve by debiting an equivalent amount of unpaid sales tax. It was submitted that this action of the assessee falls within the purview of Clause (b) of the Explanation to Section 115JB of the Act and, therefore, the addition made by the AO was justified.

14.1. The DR also referred to the assessee's submission before the Ld. CIT(A) regarding the unpaid sales tax constituting a subsidy and contended that the said amount ought to have been added to the book profit under Clause (c) of the Explanation to Section 115JB of the Act. The DR pointed out that in Para 13 of the Ld. CIT(A)'s order dated 11.12.2012, the following submission of the assessee was recorded:

> *"We may also like to mention that in the case of the appellant, the scheme is a Sales Tax Deferment Scheme and not an exemption scheme. The appellant is required to collect the sales tax and retain it for a certain number of years. If during these years, the appellant stops production or fails to fulfil certain conditions, the appellant has to pay the entire amount of sales tax collected under the scheme of the government. The sales tax collected is therefore a liability and, therefore, on this count also, the same cannot be credited to the profit and loss account."*

14.2. It was submitted that the assessee itself admitted that the sales tax collected would become payable to the Government if certain conditions were not met. According to the DR, this clearly demonstrates that the unpaid sales tax (debited) may, depending on the fulfillment or non-fulfillment of conditions, either constitute a liability towards the Government or create a Sales Tax Subsidy, which is also in the nature of a liability.

14.3. The DR contended that by creating the Sales Tax Capital Reserve, the assessee effectively set aside an amount to meet uncertain liabilities—

whether towards the Government or towards the Sales Tax Subsidy. Since the exact nature of the liability was uncertain at the time of creating the reserve, such an amount clearly falls within Clause (c) of the Explanation to Section 115JB, which mandates an increase in book profit by the amount set aside as provisions for meeting liabilities, other than ascertained liabilities.

15. We have carefully considered the submissions made by the AR and the DR, as well as the orders of the lower authorities. The primary issue before us is whether the sales tax subsidy, which has been accepted as a capital receipt, should be included in the computation of book profit under Section 115JB of the Act.

15.1. At the outset, we note that the Co-ordinate Bench of ITAT in ITA No. 1420/Ahd/2009 dated 21.12.2011 had already adjudicated the nature of the sales tax subsidy and held it to be a capital receipt. This finding has attained finality and, therefore, there remains no dispute that the subsidy does not form part of taxable income under normal provisions. However, the CIT(A) and AO adjusted the same while computing book profits under Section 115JB, of the Act on the ground that the subsidy impacts depreciation and thus affects net profit.

15.2. The DR contended that the assessee, by crediting the subsidy directly to the Sales Tax Capital Reserve instead of routing it through the Profit & Loss Account, effectively carried an amount to a reserve, and as per Clause (b) of Explanation 1 to Section 115JB of the Act, such an adjustment is justified. The DR further submitted that even if the subsidy is a capital receipt, the creation of a reserve effectively increases book profits, as per the deeming provisions

of Section 115JB of the Act. We have also duly considered the contention of the DR that the assessee, by not routing the sales tax subsidy through the Profit & Loss Account, adopted a treatment inconsistent with the income approach prescribed under Accounting Standard (AS)-12 – Accounting for Government Grants. The DR argued that the subsidy ought to have been recognized as income, and its direct credit to the Sales Tax Capital Reserve amounted to an impermissible deviation from the standard accounting treatment, thereby justifying its addition while computing book profit under Section 115JB of the Act. However, we find this contention without merit. A plain reading of AS-12, particularly paragraphs 10.1 and 14, makes a clear distinction between government grants related to specific fixed assets and those which are in the nature of promoters' contribution or linked to the overall investment in an undertaking. AS-12 explicitly states that subsidies received as promoters' contribution, or those not relatable to specific fixed assets, are to be credited directly to the capital reserve, and not recognised as income in the profit and loss statement. In the present case, the assessee has consistently treated the sales tax subsidy as a capital receipt not linked to any specific asset, and has therefore credited it directly to the capital reserve, in accordance with AS-12 and the provisions of the Companies Act, 1956. Consequently, the income approach under AS-12 is not applicable in the facts of the present case.

15.3. We find merit in the argument of the AR that the AO has no power to tinker with the book profits unless the accounts are not prepared in accordance with Part II & III of Schedule VI of the Companies Act, 1956. The Hon'ble Supreme Court in Apollo Tyers Ltd. v. CIT (2002) 255 ITR 273 (SC) has categorically held that the AO has no authority to alter the book profit

unless there is a violation of accounting standards or provisions of the Companies Act.

16. The AR has further referred to Accounting Standard (AS) 12 – Accounting for Government Grants, which states that capital grants should be credited to the capital reserve and not routed through the Profit & Loss Account. The assessee's treatment of the subsidy is, therefore, in compliance with AS-12 and the Companies Act, 1956. The contention of the DR that the subsidy should be included in book profit due to its impact on depreciation is not supported by any express provision in Explanation 1 to Section 115JB.

16.1. Thus, once the subsidy is held to be a capital receipt, it cannot be added back to book profit, as the mere credit to reserves does not fall under the specific additions required under Explanation 1 to Section 115JB. The statutory language is clear that amounts specified in clauses (a) to (i) are to be added only if they are debited to the statement of profit and loss. Explanation 1 explicitly states that **"if any amount referred to in clauses (a) to (i) is debited to the statement of profit and loss or if any amount referred to in clause (j) is not credited to the statement of profit and loss, then such amount shall be added or reduced, as the case may be."** Since the sales tax subsidy was directly credited to the capital reserve and was never debited to the Profit & Loss Account, the AO was not justified in making an addition to book profit under Section 115JB. The AO's adjustment in this regard is not justified, and **we allow the first ground in favor of the assessee.**

17. We have discussed and decided in the earlier part of this order while dealing with the Revenue's appeal that once it has been accepted that the

subsidy pertains to fixed assets and is capital in nature, the natural consequence under Explanation 10 to Section 43(1) is that it must be reduced from the cost of fixed assets for the purpose of calculating depreciation. In light of the findings and decision, **Ground No. 2 of the assessee's appeal is dismissed.**

17.1. The CIT(A) has observed that the accounts of the assessee were not prepared in accordance with Part II & III of Schedule VI of the Companies Act, 1956 because the subsidy was not appropriately accounted for in book profits. The AO, based on this observation, sought to re-compute book profit under Section 115JB of the Act. We note that the assessee is a public company whose financial statements have been certified by statutory auditors, approved by shareholders in the AGM, and filed with the Registrar of Companies. The Hon'ble Supreme Court in Apollo Tyers (supra) has held that once the accounts are certified by the auditors and approved by shareholders, the AO cannot make adjustments unless there is fraud, misrepresentation, or non-compliance with Schedule VI of the Companies Act. There is no finding in the CIT(A)'s order that the accounts were not in accordance with the Companies Act, apart from the difference in accounting treatment of the subsidy. A mere difference in accounting interpretation cannot be a reason to modify book profits under Section 115JB. Therefore, we hold that the accounts of the assessee were correctly prepared, and the AO's adjustment was beyond his jurisdiction. We allow the Ground number 3 in favor of the assessee.

18. In the combined result, the appeals filed by the Revenue are dismissed, as we uphold the directions issued to the AO by the Co-ordinate Bench for

re-computation of depreciation after reducing the amount of subsidy from the cost of fixed assets, in line with the provisions of Section 43(1) of the Act. With respect to the assessee's appeal, we partly allow the same.

pronounced in the Open Court on 25th March, 2025 at Ahmedabad.

Sd/-	**Sd/-**
(T.R. SENTHIL KUMAR)	**(MAKARAND V. MAHADEOKAR)**
JUDICIAL MEMBER	**ACCOUNTANT MEMBER**

अहमदाबाद/Ahmedabad, दिनांक/Dated 25/03/2025
टी. सी. नायर, व. नि. स. / T.C. NAIR, Sr. PS

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. संबंधित आयकर आयुक्त / Concerned CIT
4. आयकर आयुक्त (अपील) / The CIT(A)-III, Baroda
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण ,राजोकट/DR, ITAT, Ahmedabad,
6. गार्ड फाईल /Guard file.

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सहायक पंजीकार (Asstt. Registrar)
आयकर अपीलीय अधिकरण, ITAT, Ahmedabad