

Earnest money forfeited by HSIDC on surrender of industrial plot allotment was capital loss not deductible

Summary – The High Court of Delhi in a recent case of ICS Systems (P.) Ltd., (the Assessee) held that Loss incurred in transactions of purchase of plot due to forfeiture by State Industrial Development Corporation of part of advance deposit would be capital loss

Facts

- The assessee, a company carrying on manufacturing activities, applied for allotment of an industrial plot and had deposited 10 lakhs with Haryana State Industrial Development Corporation (HSIDC) being 25 per cent of the cost of the plot.
- A plot was allotted to appellant but the assessee-company did not accepted it as it was not properly measured. Therefore, the assessee asked for a refund of Rs. 10.87 lakhs. HSIDC refunded Rs. 6.94 lakhs and the balance amount of Rs. 3.93 lakhs was forfeited.
- The Assessing Officer held that the amount deposited with HSIDC was for acquiring a capital asset and, hence, the amount deducted by HSIDC on surrender of the industrial plot would be capital loss and could not be allowed as revenue expenditure.
- On appeal, the Commissioner (Appeals), however, allowed the appeal preferred by the appellant-assessee, observing that deposit of money while bidding for the industrial plot did not partake character of a capital asset and, therefore, forfeiture of earnest money cannot be treated as a capital loss. The appellant-assessee had neither acquired any capital asset nor the assessee had obtained any benefit of enduring nature. Forfeiture of earnest money was incidental to the business of the appellant-assessee and hence in the nature of a revenue loss.
- On second appeal, the Tribunal confirmed conclusion of Assessing Officer.
- On appeal to the High Court:

Held

- The principle as laid down in *Empire Jute Co. Ltd. v. CIT* [\[1980\] 124 ITR 1/3 Taxman 69 \(SC\)](#) reads that the question must be viewed in the larger context of business necessity or expediency. If the outgoing expenditure is so related to the carrying on or the conduct of the business that it may be regarded as an integral part of the profit-earning process and not for acquisition of an asset or a right of a permanent character, the possession of which is a condition of the carrying on of the business, the expenditure may be regarded as revenue expenditure.
- On the application of the said principle, forfeiture of Rs. 3.93 lakhs would be a capital expenditure or loss as it was a loss incurred not for the purpose of, or as an integral part of the profit-earning process, but for acquisition of an asset or a right of permanent character.
- The Supreme Court, in *Oberoi Hotels (P.) Ltd. v. CIT* [\[1999\] 236 ITR 903/103 Taxman 236](#) has held that the amount received by the assessee for giving up its right to purchase and/or to operate the

property or for getting it on lease, before it was transferred and let out to other persons, was in the nature of a consideration. It would not be for settlement of rights under a trading contract. The injury inflicted was on the capital asset of the assessee. Giving up a contractual right on the basis of the agreement that had resulted in loss of source of the assessee's income would be a capital receipt.

- In the instant case the loss incurred was in the transaction relating to and for acquisition of a capital asset. For some reason, the attempt made by the appellant-assessee to acquire land/plot as a capital asset did not fructify. Hence, the appellant-assessee had asked for refund of the amount, which was paid for acquisition of the capital asset. Forfeiture or deduction made by the HSIDC while refunding the amount would be a capital loss and not a revenue expenditure.