

(2002) 05 RAJ CK 0101

In the Rajasthan High Court

Case No : IT Ref. No's. 2, 3 and 24 of 1989 28 May 2002 A.Y. 1979-80 and 1980-81

Jai Drinks (P) Ltd.

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 28-05-2002

Acts Referred:

Income Tax Act, 1961 — Section 256, 32, 41, 43

Citation : (2002) 178 CTR 42

Hon'ble Judges : Rajesh Balia, J;F.C. Bansal, J

Bench : Full Bench

Advocate : N.M. Ranka, for the Assessee and J.K. Singhi, for the Revenue, for the Appellant;

Judgement

Rajesh Balia, J.

These two Income Tax references arise out of a common order passed by the Tribunal, Jaipur Bench, Jaipur in ITA No. 708/709(Jp)1984 for successive assessment years 1979-80 and 1980-81 and common questions arise in these two reference applications except difference in the amount in question in each assessment year. The facts in the context of which these questions have been raised remain the same, therefore, they are being heard and decided together .

2. The assessee-company was manufacturing and selling soft drinks under a licence issued by M/s Coca-Cola Export Corporation, USA. For the manufacture of the soft drinks, the concentrate was provided by the Coca-Cola Export Corporation. The arrangement of providing concentrate by the company was disrupted for reasons, which are not germane. As a result of which the bottles with marking of "Coca-Cola" and "Fanta" the two products, in which soft drink was marketed earlier remained with the assessee. As a result of disruption of this arrangement, a letter was issued by M/s Coca-Cola Export Corporation through its office in India dealing with the stocks of Coca-Cola and Fanta bottles remaining with the assessee.

As the entire contention is based on the contents of this letter, which is marked as Annexure-C, along with the statement of the case, we deem it proper to reproduce the same full in its entirety :

"Ref : 402 49-17-22

2-2-1978

M/s Jai Drinks (P) Ltd.,

Jawaharlal Nehru Marg,

Jaipur - 302004.

Dear Sir,

(1) The Coca-Cola Export Corporation does not accept any legal obligation to purchase stocks of Coca-Cola and Fanta bottles in your possession.

(2) However, in response to appeals from several of the bottlers who find themselves in dire financial straits as a result of the non-availability of Coca-Cola, the Corporation is prepared to make an ex gratia offer of compensation to assist the bottlers through this different period treating all bottlers on an equal basis.

(3) As your Coca-Cola and Fanta bottles are not usable and now have no commercial value in India, and in order to prohibit their misuse (which will be resisted, in any event, by vigorous action through the courts), it is proposed that after being counted in your plant, the bottles will be destroyed by your staff under the supervision of our personnel or appointed agents. The Corporation will not accept responsibility for the resultant cullet which the bottlers will be free to dispose of as they wish.

(4) The compensation to be paid to each bottler on depreciation as mentioned above, would be on a basis pro rata to sales reported throughout 1976, the last full year of operation in India. In respect of your plant in Jaipur, the maximum quantity of "Coca-Cola"/"Fanta" bottles to which this offer of compensation will apply is - 27,500 cases.

(5) For each case of 24 "Coca-Cola"/"Fanta" bottles thus destroyed in the presence of our appointee, and up to the maximum quantity calculated under the pro-ration plan (as amended in para 4 above) the Corporation will pay to the bottler the sum of ten rupees less any tax or other levy which may be applicable to the transaction in law.

(6) As it is in our mutual interest to complete this exercise with the minimum of delay, this offer is open for acceptance until 15-2-1978 and if no response is received by the Corporation by 5.00 p.m. on that date it will be assumed that the offer is not acceptable to you. In token of your acceptance please sign the duplicate copy of this letter enclosed herewith and return the same by registered post or hand delivery so as to reach this office before 5.00 pm. on 15-2-1978.

Yours faithfully,

Sd/-

(BIPIN MATHUR)

Resident Manager"

In pursuance of this letter stocks of Coca-Cola and Fanta bottles which had remained with the assessee company were destroyed. As a result of this, the assessee-company received Rs. 2,75,000 in the previous year relating to assessment year 1979-80 and Rs. 38,500 were received in the previous year relating to assessment year 1980-81.

3. IT Ref. No. 24/89 relates to assessment year 1979-80 and IT Ref. No. 23/89 relates to assessment year 1980-81.

4. In the two assessment years the assessee has claimed that the aforesaid amount received from M/s Coca-Cola Export Corporation was an ex gratia payment and was in the nature of capital receipt, which was not includible in the taxable income of the assessee. However, the assessing officer considered the amount received by the assessee on destruction of the bottles as revenue receipts chargeable to tax, on the ground that the cost of bottles, which were plant of the assessee had earlier been subjected to deductions under the provisions of Income Tax Act while computing taxable income of such earlier years.

According to the assessing officer, the aforesaid amount received by the assessee was the amount paid to him in respect of plant, which was destroyed and such receipt was liable to be taxed u/s 41(2) as it was prevalent in the assessment year in question.

5. The assessee was unsuccessful before the Commissioner (Appeals) and in second appeal learned JM and the AM had difference of opinion on this issue. While the JM agreed with the conclusion reached by the Income Tax Officer and affirmed by the Commissioner (Appeals), the AM held it to be a capital receipt in the hands of the assessee and the question was referred to the President of the Tribunal.

The President agreed with the JM by holding that the amounts of Rs. 2,75,000 and Rs. 38,500 received by the assessee from M/s Coca-Cola Export Corporation were liable to be includible in taxable income of the assessee for the two assessment years in question on u/s 41(2) of the Income Tax Act, 1961.

6. On an application made in this behalf by the assessee u/s 256(1) of the Income Tax Act, 1961, following question has been referred in each case :

IT Ref. No. 24/29

"Whether the learned Tribunal was right in law in holding that the amount of Rs. 2,75,000 received by the assessee-company from M/s Coca-Cola Export

Corporation was liable to be taxed as income within the meaning of section 41(2) of the Income Tax Act, 1961 ?"

IT Ref. No. 23/29

"Whether the learned Tribunal was right in law in holding that the amount of Rs. 38,500 received by the assessee- company from M/s Coca-Cola Export Corporation was liable to be taxed as income within the meaning of section 41(2) of the Income Tax Act, 1961 ?"

7. We have heard learned counsel for the parties.

It has been urged by the learned counsel for the assessee Mr. Ranka that from the tenor of letter dated 2-2-1978, reproduced hereinabove, it is apparent that M/s Coca-Cola Export Corporation was under no obligation to buy the bottles in question from the assessee and, therefore, it had no obligation to pay any amount in respect of these bottles to the assessee. It was only by way of rendering some assistance to its dealers in India, which were facing financial difficulties because of the non-availability of Coca-Cola concentrate for the bottling for which the plants were settled in India that an ex gratia offer of compensation was made to the bottlers in India. The measure of ex gratia assistance extended to its dealers in India by the Corporation was related to the stocks of bottles of Coca-Cola and Fanta remaining with the bottlers subject to maximum ceiling of Rs. 2,75,000. Except for rendering financial assistance no other consideration prevailed for paying the ex gratia sum to the bottlers by the Corporation. The principle of measuring such compensation cannot be raised to the height of treating it to be payment for the bottles remaining with the bottlers or compensation for its destruction so as to invite operation of section 41(2) of the Income Tax Act, 1961, to bring balancing charge to tax.

An analogy was sought to be drawn by the learned counsel with the principle on which subsidy extended by the government in the interest of economic growth to different industries, which were not considered as a measure of reducing capital cost of establishing industries where subsidies are extended. Nonetheless, the amount of subsidy to be disbursed, is measured with reference to capital investment made by the industry in the shape of fixed capital assets. He relied on the decisions in Commissioner of Income Tax, Hyderabad Vs. M/s. P.J. Chemicals Ltd., , Commissioner of Income Tax, Bombay City Vs. Bombay Burmah Trading Corpn., Bombay, and Commissioner of Income Tax Vs. Bengal Assam Steamship Co. Ltd.,

8. On the other hand, it was contended by the learned counsel for the revenue that the amount received by the assessee is directly relatable to his plant in the form of Coca-Cola and Fanta bottles on account of destruction of such bottles. The bottles were his business assets in respect of which deductions have been claimed by the assessee. Any amount received by him whether by sale of such plant or on account of destruction of such plant the same was liable to be included in taxable income u/s 41(2) of the Income Tax Act to the extent, it does

not exceed the cost of such assets. Any amount received in excess of actual cost can be considered as capital gains arising out of the transfer of capital assets, if it can be considered to be transferred. He urged that tenor of letter dated 2-2-1978, leaves no room of doubt that the amount was paid to the assessee by the M/s Coca-Cola Export Corporation solely for the purpose of destroying the bottles in question and to safeguard its own business interest by ensuring that such Coca-Cola and Fanta bottles do not find their way in the market, which is liable to be considered as misuse of the bottles.

9. Having considered the rival contentions and closely considering contents of letter Annexure-C, we are of the opinion that only one conclusion is possible to reach that this amount paid by the Corporation to the assessee was for compensating for destroying the brand bottles remaining with the assessee. The Corporation was not inclined to purchase the bottles, but it offered the alternate to seek their destruction by the assessee in order to prohibit the misuse of the bottles. The Corporation could itself have purchased the bottles and use the same or destroyed the same, if was not willing to use them, or could prevent its misuse by seeing that the same are destroyed by the stockist.

The very first paragraph of the letter discloses the real intent and object of the transaction offered. It termed that the Corporation was not prepared to purchase bottles remaining in possession with the assessee, however it also accepted that bottlers were facing financial constraints because of the non-availability of Coca-Cola concentrate. It cannot be doubted that special type of bottles with the print of brand name was acquired by the assessee solely for the purpose of business of bottling and selling Coca-Cola and Fanta.

According to learned counsel himself the agreement required that on closure of the transaction the bottles would not be purchased by the Corporation. Apparently, when investment was made by the assessee, for building the plant and for carrying on business became part of his business asset, on closure of the business he could have sold the bottles in the market.

Mechanism devised for dealing with such bottles, which may ensure the security of the Corporation business interest and the assessee's interest by not placing the burden of carrying assets without its authority to market that the assessee destroyed all those bottles and for such destruction the Corporation paid him certain amount.

10. Clauses (3) and (4) of the letter leaves no room of doubt. It deals with the contract between the Corporation and the assessee and the real object for the transaction was devising a mechanism to secure destruction of bottles by making payment thereof. No amount was payable, if bottles were not destroyed. The amount was not payable as subsidy de hors the requisite conditions to be fulfilled by the assessee. If that be conclusion, which we have reached, the payment received by the assessee as a result of destruction of business asset in respect of which deduction as depreciation u/s 32 has been allowed to the assessee, same

was liable to be taxed u/s 41(2) of the Income Tax Act.

11. On the first conclusion the consequence to follow is not seriously disputed by the learned counsel for the assessee, also. Section 41(2) as it existed during assessment years in question, clearly postulates that where any building, machinery, plant or furniture which is owned by the assessee and which was or has been used for the purposes of business amongst other things is demolished, discarded or destroyed, and moneys payable in respect of such building or plant or machinery or furniture together with the amount of scrap value, if any, exceeds written down value, so much of the excess as does not exceed the difference between the actual cost and the written down value is to be charged to Income Tax as income of the business of the previous year in which money payable for such building or plant or machinery or furniture sold, discarded, demolished or destroyed became due. The relevant assessment years are 1979-80 and 1980-81. The original provisions of section 41(2) relevant part of it as it stood prior to its amendment by Finance (No. 2) Act of 1980 with effect from 1-4-1981, and governs the present case, reads as under :

"Section 41(2) : Where any building, machinery, plant or furniture which is owned by the assessee and which was or has been used for the purposes of business or profession is sold, discarded, demolished or destroyed and the moneys, payable in respect of such building, machinery, plant or furniture, as the case may be, together with the amount of scrap value if any, exceed the written down value, so much of the excess as does not, exceed the difference between the actual cost and the written down value shall be chargeable to Income Tax as income of the business or profession or the previous year in which the moneys for the building, machinery, plant or furniture became due."

12. From the facts found by the Tribunal it is clear that the bottles in question were plant owned by the assessee and were used by him for his business. During the two relevant years the said bottles were destroyed and in respect of destroying of such bottles the moneys became payable to assessee from M/s Coca-Cola Export Corporation and the same were received by the assessee. The assessee has claimed deduction on account of depreciation in respect of such plant. The assessee was entitled to retain cullet of the destroyed bottle and en cash the same by selling it.

All the ingredients inviting applicability of section 41(2) are present in the case. Therefore, moneys receivable by the assessee along with scrap, value of cullet, if any, was chargeable to Income Tax as income of the assessee for the previous year relevant to assessment years 1979-80 and 1980-81 respectively during which the amount has become due.

13. The decisions relied on by the learned counsel are of little help to him. In CIT v. P.J. Chemicals Ltd. (supra), the question related to what should be actual cost to the assessee of the capital assets within the meaning of section 43(1) on which depreciation is to be calculated.

The contention was raised on behalf of revenue that the subsidy is paid by the government to reduce the cost of acquisition of capital assets in the hands of the persons to whom subsidy is granted. The real question posed by this court was whether the subsidy is intended as an incentive to encourage entrepreneurs to move to backward areas and establish industries. The court concluded after referring to various decisions of High Courts in India that :

"the government subsidy, it is not unreasonable to say, is an incentive not for the specific purpose of meeting a portion of the cost of the assets, though quantified as or geared to a percentage of such cost. If that be so, it does not partake of the character of a payment intended either directly or indirectly to meet the "actual cost"."

With this conclusion the court approved the decision of Andhra Pradesh High Court in Commissioner of Income Tax Vs. Godavari Plywoods Ltd., and Gujarat High Court in Commissioner of Income Tax Vs. Grace Paper Industries Pvt. Ltd., Whitco Ltd., Amit Stampings and Narendra M. Lakhadia, . In the process, the court approved the principle that the cost of acquisition of asset is the amount the assessee pays for acquisition of such assets and it does not involve consideration wherefrom he arranges the finance for it. This decision, in our opinion, is of little relevance to the controversy raised in this case. We are not concerned here that what is the cost of acquisition that has already been determined when the assessee claimed deduction in respect thereof.

The question raised in this case is whether on destruction of bottles the amount paid by the Corporation to the assessee was a receipt in respect of the asset for which he has claimed by way of depreciation or is related to some other purpose.

14. As discussed above, it is apparent that payment made to the assessee has direct nexus with the destruction of the capital or business asset in respect of which he has claimed depreciation/cost deduction and is not for the purpose of conferring any other benefit to the assessee, except to recover above part of the cost which the assessee had acquired for running business of Coca-Cola and Fanta and which has been disrupted on account of non-supply of concentrate by the Corporation. In these circumstances where Corporation was not willing to accept the bottles by purchase, but at the same time in the agreement the bottles could not be sold in open market by assessee also, therefore, the destruction of capital assets was brought about at the instance of the Corporation on a compensation payable by it. It is very akin to the compensation recovered from insurance company on destruction of depreciable assets.

15. Another decision on which reliance was placed by the learned counsel in CIT v. Bombay Burmah Trading Corporation (supra) also does not assist the cause of the assessee. It was a case in which on account of premature determination of the forest lease granted by the Government of Burma because of the situation arisen as a result of IIInd World War and the timber logs, which were received by the assessee thereafter, was considered to have been received in lieu of loss of

its business running machine and was considered that in exchange of the loss of lease which was a capital asset for the assessee, the timber received also partake the character of capital asset and amount arising out of sale of such logs was not a revenue receipt, therefore, the application of principle of balancing charge could not be made applicable to transaction of sale of plant.

In the aforesaid circumstances, the case is clearly distinguishable both on facts and the controversy which had arisen before the court.

16. The decision in CIT v. Bengal Assam Steamship Co. Ltd. (supra) by the Calcutta High Court depended on the distinction drawn by it whether destruction of the business asset was accepted on account of some voluntary act of the assessee or its destruction was caused by act during the hostilities between India and Pakistan and was indemnified under the scheme.

Without dwelling on the validity of the distinction which weighed with the Calcutta High Court, on the principle evolved by said High Court, the assessee's contention must fail. The destruction of the bottles in the present case has been caused on behalf the assessee voluntarily. The offer was made to the assessee. It was on the volition of the assessee to have accepted this offer to destroy the bottles and claim compensation or to leave it. The ratio of Calcutta High Court clearly goes to show that the concept of sale or discard involved exercise of volition on the part of the assessee to the provisions of section 41(2) . In the facts of this case the decision on principle helps the revenue than the assessee.

17. On the aforesaid discussion, we answer the question referred to us in each case in affirmative that is to say in favour of the revenue and against the assessee and hold that the amount received by the assessee-company from M/s Coca Cola Export Corporation as a compensation for destruction of Coca-Cola and Fanta bottles, was liable to be taxed as income of the previous year relating to assessment years in which such amount was received u/s 41(2) of the Income Tax Act as it was existing during the relevant assessment years. There shall be no order as to costs.

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