Sbw

IN THE HIGH COURT OF JUDICATURE AT BOMBAY

ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX REFERENCE NO.364 OF 1997

The Commissioner of Income Tax,
Bombay City-I, Bombay. ..Applicant
Versus
M/s. Hoechst India Limited
Hoechst House, Nariman Point,
Bombay-400 021. ..Respondent

....

Mr. Suresh Kumar a/w Ms. Samiksha Kanani for the Applicant.
Mr. J. D. Mistri, Senior Counsel, a/w Mr. Sameer Chitnis i/b. Cr. Bayley & Co. for the Respondent.

....

CORAM: M. S. SANKLECHA &
A. K. MENON, JJ.

DATE : 5th JULY, 2016

P.C.:

1. This Reference under Section 256(1) of the Income Tax Act, 1961 (the Act) made by the Income Tax Appellate Tribunal (the Tribunal) seeks our opinion on the following substantial questions of law:-

> *"(i) Whether on the facts and in the circumstances of the case, the Tribunal was right in law in confirming the order of the Commissioner of Income Tax (A) (CIT(A)) directing that the disallowance under Rule 6D should be worked out on the basis of total trips of each executives during the year instead of each trip?*

(ii) Whether on the facts and in the circumstances of the case, the Tribunal was right in law in upholding the order of the (CIT(A)) deleting the addition of Rs.1,10,84,000/- being the amount realised under the Drug Price Control order?

(iii) Whether on the facts and in the circumstances of the case, the Tribunal was right in law in upholding the order of (CIT(A)) allowing investment allowance on telephone lines, canteen equipments and fire extinguishers?"

2. Regarding Question No.1:-

(a) It is an agreed position between the parties that the issue raised herein stands concluded in favour of the Applicant-Revenue and against the Respondent-Assessee by the decision of this Court in ***CIT v/s. Aorow India Ltd. 229 ITR 325.***

(b) Accordingly, question no.1 is answered in the negative i.e. in favour of the Applicant-Revenue and against the Respondent-Assessee.

3. Regarding Question No.2:-

(a) The Respondent-Assessee is a manufacturer of drugs. During the subject assessment year, a Drug Price Control Order 1979 (DPCO) was in force. In terms of the DPCO, inter alia, sale price of certain drugs manufactured by the Respondent-Assessee was fixed. The DPCO, inter alia, provided that in case the drugs are sold at a price higher then that fixed by the DPCO, the excess recovered by the drug manufacturer would be paid over to the Government of India.

(b) The Respondent-Assessee sold its drugs at prices higher than that fixed by the DPCO and did not pay over to the Government of India the price recovered in excess of the cap provided by the DPCO. This was for the reason they challenged the DPCO by filing a Writ Petition in the Delhi High Court. This Writ was admitted and by an interim order the Government of India was restrained from collecting the amounts in excess of the DPCO price cap received by the Respondent-Assessee on sale of its drugs.

(c) Notwithstanding the stay of the Delhi High Court the Respondent-Assessee not only included the excess amounts received in excess of the DPCO price as its income but also claimed the same as an expenditure being a liability which has to be discharged in terms of the DPCO by paying over to the Government. The Assessing Officer in the subject assessment year disallowed the amount of Rs.1,10,84,000/- being received in excess over and above the price fixed by the said DPCO as an expenditure and brought it to the tax. This for the reason that there was a stay of the obligation to hand over the excess of the amount received to the Government under the DPCO by the Delhi High Court.

(d) In appeal, the CIT(A) allowed the Respondent-Assessee's appeal by deleting the addition of Rs.1,10,84,000/- by following its own order for the A.Y. 1982-83. Being aggrieved, the Revenue carried the issue in appeal to the Tribunal. The Tribunal by an order dated 6th March, 1992 dismissed the Revenue's appeal by following its order rendered in the case of the same Respondent-Assessee for A.Y. 1982-83. The aforesaid order dated 6th March, 1992 of the Tribunal does not contain any discussion on the aforesaid issue.

(e) Mr. Suresh Kumar, the learned counsel for the Revenue states that inspite of an extensive search carried out by the officer of the Revenue they are unable to make a statement whether or not a Reference had been filed for the A.Y. 1982-83. In these circumstances, Mr. Suresh Kumar tendered a copy of the order of the Tribunal for the A.Y. 1982-83 across the bar and invited our attention to the reasoning given therein.

(f) On reading the order of the Tribunal for A.Y. 1982-83, we find that while upholding the order of the CIT(A) it observed that there was no bar against the assessee selling its drugs at a price higher than that fixed by the DPCO. However, the only obligation on such a manufacturer under the DPCO was to pay over the excess realisation to the Government as a part of the Drug Price Equalization Fund. This obligation to pay over the excess to the Drug Price Equalization Fund continued even though the the Delhi High Court had admitted the respondent-assessee's Writ Petition and granted a stay of the same till its final disposal. This on the ground that the amounts retained by the Respondent-Assessee consequent to the Delhi High Court interim order was subject to final order of Delhi High Court and only if it quashed DPCO then that excess amount would vest in the respondent-assessee to be offered for tax. Further the Tribunal held that the obligation to pay the amount received in excess of the DPCO to the Price Equalization Fund arose as soon as the sale of the drugs at price higher than that fixed by the DPCO took place. It held that mere securing of a stay from the Delhi High Court would not obliterate that liability.

(g) Mr. Suresh Kumar, the learned counsel for the Revenue submits that the liability to pay the amounts in excess of the price fixed by the DPCO is a contingent liability during the subject assessment year. The liability according to him would only be crystallized as and when the challenge by the Respondent-Assessee before the Delhi High Court would be negatived. At the relevant time the liability was contingent upon the decision of the

Delhi High Court as the payments to the Government had been stayed. It is submitted that the contingent liability would not constitute an expenditure allowable for the purposes of income tax. In support of the aforesaid submission reliance is placed upon the decision in ***CIT v/s. Indian Smelting & Refining Co. Ltd. 230 ITR 194.***

(h) On the other hand, Mr. Mistri, the learned Senior Counsel appearing for the Respondent-Assessee points out that the entire issue is concluded in favour of the Respondent-Assessee by the decision of the Apex Court in ***Kedarnath Jute Mfg. Co.Ltd. v/s. Commissioner of Income Tax (Central), Calcutta 82 ITR 363.*** This is particularly so as we are dealing with the period prior to the introduction of Section 43B of the Act w.e.f. 1st April, 1984 which made deduction of expenditure on account of statutory levy, only on payment.

(i) In Kedarnath Jute Mfg. Co.Ltd. (supra) the assessee had claimed expenditure of the amounts payable to the sales tax authorities in respect of the sales made during the course of the assessment year. At the same time, the assessee therein had contested the sales tax liabilities in appeal. Nevertheless, as it was following the mercantile system of accounting it claimed deduction of the sales tax liabilities from the profits and gains of its business activity. The Calcutta High Court upheld the orders of the authorities under the Act to the effect that the liability on account of sales tax which was payable by the assessee therein would only be crystallized on a final decision being taken on the assessee's challenge to the demands raised under the Sales Tax Act.

However the Apex Court held the deduction claimed on account of sales tax liability from the profits and gains of business by the assessee was allowable by observing as under:-

> *"An assessee who follows the mercantile system of accounting is entitled to deduct from the profits and gains of the business such liability which had accrued during the period for which the profits and gains were being computed. It can again not be disputed that the liability to payment of sales tax had accrued during the year of assessment even though it had to be discharged at a future date. In Pope The King Match Factory v. Commissioner of Income-tax, a demand for excise duty was served on the assessee and though he was objecting to it and seeking to get the order of the Collector of Excise reversed, he debited that amount in his accounts on the last day of his accounting year and claimed that amount as a deductible allowance on the ground that he was keeping his accounts on the mercantile basis. The Madras High Court had no difficulty in holding that the assessee had incurred an enforceable legal liability on and from the date on which he received the Collector's demand for payment and that his endeavour to get out of that liability by preferring appeals could not in any way detract from*

or retard the efficacy of the liability which had been imposed upon him by the competent excise authority. In our judgment, the above decision lays down the law correctly."

(j) In the present facts also admittedly the Respondent-Assessee follows the mercantile system of accounting and the liability to pay the amount of Rs.1,10,84,000/- into the Drug Price Equalization Fund arose as soon as the drug was sold at a price higher than the cap provided in DPCO during the subject assessment year. This liability of Rs.1,10,84,000/- was statutory and determined liability. It was not contingent upon the decision of the Court on the Writ Petition filed by the Respondent-Assessee. There is in fact no dispute with regard to the aforesaid amount of Rs.1,10,40,000/-. In the above view, it was an enforceable legal liability but the same had been kept in abeyance because of the interim order of the Delhi High Court. However, such order of stay by the Delhi High Court would not in any event efface the liability which was payable under the DPCO. At the highest the collection of the same, was postponed. Thus the decision of the Apex Court in Kedarnath Jute Mfg. Co.Ltd. (supra) would apply to the present facts and the view taken by the Tribunal is in accordance with the principles laid down by the Apex Court.

(k) The reliance by the Revenue upon the decision of this Court in

Indian Smelting & Refining Co. Ltd. (supra) is inappropriate. In the above case, the liability was contingent as the Excise Authorities had only issued a show cause notice which was contested by the Assessee. Thus there was no ascertained liability. The ascertaining of liability, if at all, would be on disposal of the show cause notice issued by the excise authorities to the prejudice of the assessee. This for the reason that it is very likely that the authorities under the Excise Act on being satisfied with the response of the assessee therein may withdraw the show cause notice. Thus, it was in the above fact situation that this Court held that the liability in such case would be a contingent liability upon the decision on the show cause notice. Therefore it could not be allowed as deduction from the profits and gains of the business till a decision is taken on the show cause notice. It has no application to the present facts.

(l) Therefore, as we are dealing with a period prior to introduction of Section 43B of the Act, the decision of the Apex Court in Kedarnath Jute Mfg. Co.Ltd. (supra) would apply to the present facts. In the above view, question no.2 is answered in the affirmative i.e. in favour of the Respondent-Assessee and against the Applicant-Revenue.

4. <u>Regarding Question No.3:-</u>

(a) It is an agreed position between the parties that the issue stands concluded against the Applicant-Revenue and in favour of the Respondent-Assessee by the decision of this Court in ***CIT v/s. Tata Chemicals Ltd. 162 ITR 662*** and the decision of the Himachal Pradesh High Court in ***CIT v/s. Mohan Meakin Breweries Ltd. 122 ITR 203.***

(b) In the above view, question no.3 is answered in the affirmative i.e. in favour of the Respondent-Assessee and against the Applicant-Revenue.

5. In the above view, our answers to the questions posed for our opinion are answered as under:-

Question No.1 – in the negative i.e. in favour of the Appellant-Revenue and against the Respondent-Assessee,

Question No.2 – in the affirmative i.e. in favour of the Respondent-Assessee and against the Appellant-Revenue, and

Question No.3 – in the affirmative i.e. in favour of the Respondent-Assessee and against the Appellant-Revenue.

6. Reference is disposed of in above terms. No order as to costs.

(A. K. MENON, J.) **(M. S. SANKLECHA, J.)**

wadhwa