

**IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION
INCOME TAX APPEAL NO. 997 OF 2008**

The Commissioner of Income Tax-IV

.. Appellant

vs

The Solapur Dist.Coop Milk Producers
and Process Union Ltd

.. Respondent

**WITH
INCOME TAX APPEAL (Lodging) NO.290 of 2006**

The Commissioner of Income Tax (Central)

.. Appellant

vs

The Kolhapur Zilla Sahakari Dudh Utpadak
Sangh Ltd

.. Respondent

..

Mr.P.S.Sahadevan with Mr.Vimal Gupta for
Appellant
Mr.S.N.Inamdar for Respondent

..

**CORAM : F.I.REBELLO AND
R.S.MOHITE, JJ**

**JUDGMENT RESERVED ON: 18th March, 2009
JUDGMENT PRONOUNCED ON: 4th April, 2009**

JUDGMENT (Per F.I.Rebello, J)

1. These appeals are being disposed of by this common order as they involve the same questions of law which is framed as under :

. " Whether on the facts and

circumstances of the case and in law, the Hon'ble Tribunal was justified in deleting the addition of Rs.1,55,81,519/- by holding the said amount represented rate difference payment in the purchase of milk paid by the assessee even though the said payment of Rs.1,55,81,519 was paid at the end of the previous year. "

A few facts may now be set out from the case of

' The Solapur District Cooperative Milk Producers

and Process Union Ltd.' The facts in the other

case are also same or similar except to the extent

of supply of milk by non-members also.

2. The assessee-societies are federal milk societies and its members are primary milk co-operative societies and the business of the assessee is to purchase milk from its members and other producers of milk at the rate i.e. similar to both the members and outside milk producers and sell the milk to various parties. The difference in purchase price and sale price after the normal expenses is the profit of the assessee- societies which is liable to tax. This profit in turn is distributed to the member primary milk

co-operative societies.

3. The rate of purchase price is fixed by the board of the assessee-societies. The purchase price is linked to the fat content of milk and also varies according to seasons like the rate for purchase of milk in the lean season is different from the flush season.

4. The respondents fixes the rate of processing of milk at the beginning of the year on the basis of the price declared by the Government of Maharashtra and price which other buyers pay to the vendors. These rates are revised from time to time. It is made always clear that the rates are provisional to the final milk rate difference which is determined in the month of March every year and paid subsequently in the following year. It is ascertained and verified that the primary milk society also in turn makes payment of final rate difference to the individual milk producers around Diwali. The respondents are apex district societies of primary milk societies; Individual

milk producers are members of these primary societies. Individual producers supply milk to the primary milk co-operative milk societies. The milk so collected is brought to the processing unit of the assessee society and payment to member cooperative societies/non-member cooperative societies is made on the basis of quality of fat and SNF content. Milk is also supplied by non-members to the primary milk societies. The processed milk is supplied to the "Mahananda i.e. Maharashtra Rajya Co-op Dudh Sangh, a state milk federation. The assessee before the end of the financial year depended on its books, makes a final rate difference to the primary society who in turn pay the difference to members and non-members who supply milk.

5. The learned A.O. refused to exclude the final rate difference paid from the total amount paid by

the respondents on the ground that :

(a) It was not linked to the quality of the milk like fat content or source of milk, quality of milk, period of milk procurement.

(b) It was paid only to member societies and not to other suppliers;

(c) It was not linked to the price paid by government or other cooperative societies;

(d) It was made on the basis of the accrued profits of the year and hence the amounted to distribution of profits;

6. Against the order of the A.O. an appeal was preferred by the assessee. The C.I.T. (Appeals) affirmed the claim of the assessee that the prices fixed provisionally were not found supported by any documentary evidence. The C.I.T. (Appeals) also observed that the assessee's arguments that such payment are made to keep an edge over its competitors and attract more and more members to supply milk to the assessee is without any merit. It was also held that the assessee has been unable to establish that the final market rate difference was paid at a fixed price per litre irrespective of the quality of the milk fat and its content. The C.I.T. (Appeals) substantially agreed with the reasoning of the A.O. and accordingly dismissed the appeal.

7. The assessee aggrieved preferred an appeal to the I.T.A.T. in respect of the findings recorded by the A.O. which we have reproduced earlier and which is affirmed by the C.I.T.(Appeals), the tribunal recorded as under :

(i) The basic price itself was based on quality, any increase in basic price which was provisional was automatically linked with quality e.g. if price paid on the basis of fat and SNF content was X & Y final rate difference of say 25 paise & Y +25 increased the price as X+ 25 paise & Y +25 paise.

(ii) The supply by non-members was miniscule and that too only for two years. Therefore, non payment of final rate difference to outsiders does not convert the payments to members in respect of milk as appropriation of profits. Here, we may mention the case of Solapur District Cooperative Milk Producers and Process Union Ltd, a finding has been recorded that payment is made to members as well as non-members.

(iii) The government only fixes minimum price to be paid. The board has authority under bye laws to fix the price of the milk purchased from time to time. In view of the cooperative principles, assessee tend to pass on the maximum price to its member societies. Similar situation was obtaining in Mehsana Districts case 282 ITR 24 wherein Gujrat High Court has answered similar issue in favour of the assessee.

(iv) The resolution to pay final rate difference were always passed in the month of March every year i.e. before the end of previous year and only the resolution to disburse the amounts were passed after the year end. Rate difference was paid only on the basis of quantity of milk supplied during year not in proportion of shareholding so as to amount to distribution of profits. The dates on which the resolutions is to pay the final milk rate difference are recorded before the end of the year. It accordingly allowed the appeal and allowed deductions of final rate.

8. At the hearing of these appeals, on behalf of

the revenue, learned counsel submits that there is material on record to show that the final rate difference was paid after accrual of the net profits and out of the net profits. The transactions which were recorded and noted during the course of survey shows that the final milk rate difference was paid after accrual of net profit and payment of final milk rate difference was not included in the total per litre production of cost of milk. This was corroborated in the statement recorded of the Finance Manager of the society. It is also set out that the resolution of final rate difference in the same case was passed after expiry of the relevant financial year. There was no legal obligation on the assessee society to make payment of final rate difference to member cooperative societies. Our attention is drawn to the fact that the C.I.T.(Appeals) has recorded a finding that in some cases the assessee paid commercial purchase price by even excluding the amount of final rate difference to milk producers as compared by the purchase price of milk to government and some other cooperative societies. It is submitted that there is also a finding of C.I.T.(Appeals), that in some cases the apex societies purchased milk

under consideration at a fixed purchase price and not at provisional price. For these reasons, the appeals ought to be dismissed.

9. The entire argument sought to be advanced on behalf of the revenue is that what in fact is paid to the milk suppliers whether they be members or non-members is out of the profits of the society; The resolution to pay may be passed before the accounts are approved, but nevertheless, it is out of profits. That being the case the order of the A.O. as affirmed by the C.I.T.(Appeals) was justified. Apart from supporting the order of the ITAT, it is also submitted, that the profits were arrived at after debiting the expenditure by way of market rate difference and there was no allocation of the profits and this fact has remained uncontroverted.

In the case of **C.I.T. vs Shri Sarvaraya Sugars Ltd, (1987) 163 ITR 429 and Addl.C.I.T.Kanpur vs MP Sugar Mills (P) Ltd (1984) 148 ITR 203,** it has been held that the liability for additional price of sugar cane under price linking formula in the year the sugarcane is purchased and arises on receipt of goods and additional price paid relates

back to such receipts. If this test is applied to the assessee's case, it would be squarely covered. Payment is made not in proportion to shareholding but, based on quality of milk and quantity supplied. The tribunal has further held that " If in the final accounts certain amounts are taken as liability for purchase of goods, quantified on the basis of quality or quantity of goods purchased then it cannot be said that the payment amounts to appropriation of profits.

10. Is the price difference paid out of the profits ? Firstly, the profits have to be ascertained. If there be profits they attract tax at that point of time. The word 'profit' as observed by Lord Chancellor Halsbury in *Gresham Life Assurance Society of Styles* (1982) A.C.309 is to be understood in its natural and proper sense - in a sense in which no commercial man would misunderstand. When an individual or a company has in that proper sense ascertained what are the profits of his business or trade the destination of profits charged on those profits by previous agreements or otherwise is immaterial. The profits are to be determined considering two points of time and they can be determined only

after all expenses incurred for the business are deducted from the gross income. As held by the Supreme Court in **CIT vs Travancore Sugars and Chemicals Ltd (1973) 88 ITR** the amount paid by reference to profit can either be that, - (i) it is paid after the profits become deductible or (ii) the amount is payable prior to such distribution to be computed by reference to notional profits or what in certain cases termed as approved net profits. In the first instance, it will be distributed out of profits and not deductible in computation of profits as expenditure.

10. Section 64 of the Maharashtra Cooperative Societies Act, 1960 (M.C.S.Act) sets not that no part of the funds other than the dividend equalisation or bonus equalisation funds as may be prescribed or the net profits of the society shall be paid by way of bonus or dividend or otherwise distributed among its members. Under section 65 the society shall construct its relevant annual financial statements and arrive at its consequent net profit or loss in the manner prescribed. The proviso explains that no part of the profits shall be appropriated except with the approval of the

annual general meeting and in conformity with the Act, rules and bye-laws. From a reading of this provision, it is apparent that the net profits have first to be determined and then only can be appropriated after the approval of the annual general meeting. The net profits do not accrue from day to day or from month to month and profits have to be ascertained by comparison at two stated points of time. The assessee when it decided to pass a resolution to pay the price difference had not ascertained the net profits nor was a resolution passed at its A.G.M. to distribute the profits as by way of higher price difference. In the instant case, admittedly the decision to pay the additional purchase price was based on the resolution of the Board of Directors, approved at the general meeting.

11. From the facts on record and arguments

advanced what emerges is as under :

- 1) That the price difference paid in the case of Kolhapur society to its members and in case of Solapur society to both members and non-members ;
- 2) Payment is made only to members who are suppliers;

3) Payment is made to suppliers not on the basis of the shares held by them but, on the amounts of the milk supplied and on the basis of the fat content of the milk ;

4) The resolution to pay additional price is taken before the end of the financial year i.e. before the profits can be said to accrue though payment is made in the subsequent financial year;

5) The profits are only payable in terms of section 65 of the Maharashtra Cooperative Societies Act, 1960.

12. A similar question had come up for consideration before the Gujrat High Court. The Gujrat High Court was considering in case of **Commissioner of Income Tax vs Mehasena District Cooperative Milk Producers Union Ltd (2005) (195) CTR 385,** as to whether a claim for deduction was allowable either under section 28 or section 37 (1). There also an additional payment was made towards the price of the milk. The A.O. disallowed the same on the ground of profit adjustment. The C.I.T.(Appeals) affirmed the order of the A.O. The tribunal allowed the assessee's claim. Various contentions were sought

to be canvassed before the learned High Court. The learned bench noted the legal position as to when accrual of profits can be said to have accrued. It considered the case of **C.I.T. vs Ashokbhai Chimanbhai (1965) 56 ITR 42 (SC)** and noted that the words "accrue" and "arise" are used to contradistinguish the word 'receive'. Income is said to be received when it reaches the assessee. When the right to receive the income becomes vested in the assessee, it is said to accrue or arise. Dealing with profits, this is what the learned Court said:

" Profits do not accrue from day to day or even from month to month and have to be ascertained by a comparison of assets at two stated points. Unless the right to profits comes into existence there is no accrual of profits and the destination of profits must be determined by the title thereto on the day on which they arise. "

Applying the test, the learned Court held that because the board resolved to fix the final purchase price and pay on the last day of the accounting period it would not amount to

application of profits. The Court also noted that the profits to be assessed have to be the "real profits" and are required to be determined on the ordinary principles of commercial trading and commercial accounting. The Court further noted as

under :

a) The expenditure in question cannot be termed to be application of income in absence of any evidence as to accrual of profits in light of settled legal position;

(b) The payment of additional/final price made on the last day of the accounting year is allowable under section 28 of the Act being a necessary deduction for ascertaining the real profits on principles of commercial accounting and ;

(c) The payment in question is alternatively allowable under section 37 of the Act having been incurred wholly and exclusively for the purpose of business carried on by the assessee in light of the evidence which has come on record ;

13. Coming to our case, (as we have noted this is not the case of distribution of profits) as the amount to be paid was not out of the profits ascertained at the annual general meeting. It is not paid to all shareholders. The amount which is the subject matter is paid to members who supply milk and in some case also to non-members. The payment is for the quantity of milk supplied and

in terms of the quality supplied. The commercial expediency for payment of this price are the market conditions, and the need to procure more milk from the members and non-members to the assessee. To our mind, therefore, the amount paid by no stretch of imagination can be said to be dividend to the members or shareholders or payment in the form of bonus as bonus also has to be paid from the accrued profits.

14. In the light of our discussion, we are in agreement with the views taken by the tribunal and the question at present has to be answered in the affirmative in favour of assessee and against the the revenue. Appeals dismissed.

{ R.S.Mohite, J }

{ F.I.Rebello, J }