IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCHES : "H" NEW DELHI

BEFORE SHRI J.SUDHAKAR REDDY, AM
AND
SHRI C.M. GARG, JM

ITA no. 2610/Del/2012
Assessment Year 2008-09

ACIT, Circle 16(1) New Delhi	vs.	Tirupati Udyog Ltd. 8-2-629/1/A/3, MLS's Colony A 3, 2nd floor, Vishal Bhawan Road no.12, Banjara Hills Hyderabad PAN: AABCT 3941 R
(Appellant)		(Respondent)

Appellant by:-Sh. Amit Goel, FCA
Respondent by:- Sh. AK Mishra, CIT, D.R.

O R D E R

PER J.SUDHAKAR REDDY, AM

This is an appeal filed by the Revenue directed against the order of the Ld.Commissioner of Income Tax (Appeals)-XIX, New Delhi dated 26.3.2012 pertaining to the Assessment Year 2008-09.

2. Facts in brief:- The assessee is a Company and is engaged in the business of manufacturing and trading of facilities of sponge iron from iron ore, steel melting section for manufacturing of MS ingots from sponge iron and MS scrap, a rerolling mill for manufacturing of constructional and structural steels from MS ingots/billets.

3. The facts of the issue that arises for our consideration are brought out by the Ld.Commissioner of Income Tax (Appeals) at para 25 which is extracted for ready reference.

"25. The assessee company entered into the Memorandum of Understanding (MOU) with Shri R.Charuchandra Prop. Of M/s Shree Nidhi Mines on 03.01.2004 for developing of mines, production/extraction of ore etc. for a period of 5 years from the date of renewal of mining lease that was extendable for further period. The area of the mines in question was of 45 hectares of land situated at survey no.1 of Kallahalli Village Hospet Taluk. The mines was closed due to orders from Forest Department since 1997. The permission for mining operation was granted on 30.11.2004 to Shri Charu Chandra in respect of Shrree Nidhi Mines, Kallahalli, Hospet. Shri Charu Chandra had been making contravention of the agreement time and again. The assessee company came to know that Shri R.Charuchandra entered into a fresh contract with M/s Raj Shree Mineral, Bangalore in the year 2007 for extraction and screening of iron ore in without taking the permission of the assessee and without resolving the issue of assessee company's right. The assessee company filed suit against Shri R.Charuchandra and his concerns which ultimately resulted into out of court settlement and as a result of which the assessee company received compensation of Rs.12,80,00,000/-. A sum of Rs.1,12,12,446/- was outstanding receivable in the assessee's books from the party from whom the compensation was received. Since the amount of Rs.1,12,12,446/- was not recovered, the appellant adjusting this amount of Rs.1,12,12,446/- from the compensation of Rs.12,80,00,000/-, showed/credited the net amount of Rs.11,67,87,854/- in the P&L a/c."

4. The assessee, on the ground that the compensation received was for loss of "source of income" disclosed the same in its return of income as a capital receipt. The Assessing Officer, after considering the submissions of the assessee, treated this compensation received as a revenue receipt. While doing so, the Ld.AO placed reliance on the following case laws.

i. CIT vs. Eastern Book Co. (2010) 322 ITR 605 (All)

ii. Kailashnath & Associates vs. ITO (2009) 121 ITD 563 (Del) (SB)

5. The assessee had relied upon the following decisions before the Ld.AO.

i. CIT vs. Saurashtra Cements Ltd. (2010) 192 Taxman 300(S.C.);

ii. Oberoi Hotels P.Ltd. vs. CIT (1999) 103 Taxman 236 (S.C.).

6. The Assessing Officer did not make any effort in his Assessment Order to distinguish the case laws relied upon by the assessee. The A.O. rejected the claim of the assessee. Aggrieved the assessee carried the matter in appeal.

7. The First Appellate Authority considered the terms of the MOU and thereafter applied the decisions of the Hon'ble Supreme Court in the case of Kettlewell Bullen & Co. vs. CIT (Cal.) 53 ITR 261 and the decision in the case of Oberoi Hotels P.Ltd. vs. CIT (1999) 236 ITR 903 (S.C.) and held that the receipt in question is a capital receipt and hence not taxable.

8. Aggrieved the Revenue is in appeal before us on the following grounds.

"1. On the facts and in the circumstances of the case and in law the Ld.Commissioner of Income Tax (Appeals) erred in deleting the addition of Rs.12,80,00,000/- made on account of receipt of compensation treating the same as revenue receipts.

1.1. On the facts and in the circumstances of the case and in law the Ld.Commissioner of Income Tax (Appeals) erred in holding that the receipt of Rs.12,80,00,000/- was in the nature of capital receipt.

2. On the facts and in the circumstances of the case and in law the Ld.Commissioner of Income Tax (Appeals) erred in deleting an addition of Rs.1,12,12,446/- which was made on account of the fact that the amount receivable was written off without any rhyme and reason.

3. The appellant craves leave for reserving the right to amend, modify, alter, add or forego, any grounds of appeal at any time before or during the hearing of appeal."

9. The Ld.D.R. Mr.A.K.Mishra submitted that all the grounds raised by the Revenue are inter related and pertain to the same issue. He submitted that the sole issue that has to be adjudicated by the Tribunal is whether the compensation received by the assessee from R.Charu Chandra is a capital receipt or a revenue receipt. He referred to the facts of the case as well as the MOU and submitted that as on the date of MOU i.e. 03.01.2004, Mr.R.Charu Chandra did not have required permission from the Forest department for undertaking mining operations. He pointed out that the permission was received only on 30.11.2004 and under those circumstances, he cannot decide that the assessee has source of income by virtue of this MOU. He submitted that the MOU was terminated in the year 2005 and there was an out-of-Court settlement and the assessee received compensation in the FY 2007-08 relevant to the Assessment Year 2008-09. He submitted that on the facts and circumstances of the case the receipt in question is a Revenue receipt as rightly held by the Assessing Officer. While relying on the case laws mentioned by the Ld.AO in his assessment order, the Ld.CIT, D.R. relied on the following case laws.

i. CIT vs. Chari & Chari Ltd. Judgement dt. 9.4.1965 (1966) AIR 54 1965 SCR(3) 692;
ii. CIT vs. M/s Best & Co. 1965, AIR 1325, 1966 SCR 2 430 judgement dt. 2nd November,1965.

He took this Bench through both these case laws and submitted that generally the type of receipt would be a capital receipt but there is an exception as pointed out by the Hon'ble Supreme Court in both these cases. He submitted that the assessee has multiple businesses and one agreement is terminated with the restrictive covenant, not to carry on business, then the compensation received would become a revenue receipt.

10. On ground no.2, he submitted that it is consequential to the decision in ground no.1.

11. The Ld.Counsel for the assessee Shri Amit Geol on the other hand relied on the order of the Ld.Commissioner of Income Tax (Appeals). He submitted that the compensation received was for loss of "source of income" and hence it was a capital receipt. He contended that this is not a case of "loss of profit". He further contended that the cancellation of contract has impaired the very business structure of the company. He pointed out that neither the Ld.Assessing Officer nor the Ld.D.R., have disputed the fact that the compensation has been received for "loss of source of income". He distinguished the case laws relied upon by the Ld.Assessing Officer as well as Ld.Commissioner of Income Tax (Appeals). He further relied on the following case laws.

i. Oberoi Hotels P.Ltd. vs. CIT (1999) 236 ITR 903 (S.C.)
ii. Khanna and Annadhanam vs. CIT (ITA no.1286/2008, judgement dt. 29.1.2013(Del)
iii. CIT vs. Prabhu Dayal (1971) 82 ITR 804 (SC)
iv. CIT vs. Saurashtra Cement Ltd. (2010) 192 Taxman 300 (SC)
v. Godrej & Co. vs. CIT (1959) 37 ITR 381 (SC).

12. He emphasized that the argument of the Ld.D.R. that all activities of the assessee have to be looked at, for claiming that the receipt in question is capital receipt, is against the propositions laid down by the Hon'ble Supreme Court. On facts he pointed out that the assessee company never had any business of mining either in the past or in the future and it was only vide this MOU, the assessee had obtained mining rights.

13. Ground no.2, he submitted that it is a case of double addition and that the Ld.CIT(Appeals) has rightly deleted the same.

14. On the contention of the department that Mr.R.Charu Chandra had no mining rights Mr.Amit Goel submitted that Mr.R.Chaur Chandra always had mining rights and it was only a case of forest department permission to commence mining operations, that was in issue.

15. Rival contentions heard. On a careful consideration of the facts and circumstances of the case and on a perusal of the papers on record as well as the orders of the authorities below and case laws cited, we hold as follows.

16. The relevant terms and conditions of the MOU dt. 3.1.2004 have been brought out at page 17 and 18 of the Ld.Commissioner of Income Tax (Appeals)'s order which is extracted for ready reference.

"The second party has agreed to carryout the development of work of mines, production of ore by mining in a scientific and systematic manner at the expense of the second party for which this mutual agreement has been executed upon with the various terms and conditions herein under"

"WHEREAS the second party herein has assured the First Party that he would perceive the renewal of mining lease application pending for consideration with

the competent authorities and seek the renewal for and on behalf of the first party."

"The second party has also agreed to complete all the formalities of forest clearance as prescribed under Indian Forest Act with reference to Mines Act and has also undertaken to invest money for the purpose of clearing on behalf of the First Party."

"All the dues, levies and all such other sums that are found due with reference to the renewal of mining lease, Forest clearance, environment and pollution control clearance etc in this behalf has agreed to invest substantiate sum of money which has to be adjusted over a period of time as enumerated in the following paras of this agreement between the parties hereunder:"

"The second party has assured the first party that he does produce a minimum quantity of 30,000 MT per month i.e. 3,60,000 MT of Iron Ore per annum. In the event of failure to produce the same by the second party, the second party shall compensate the shortage to the first party by paying the assured Royalty for 30,000 MT per month that very month. In the event of the second party exceeding the agreed production of 3,60,000 MT of Iron Ore per annum, the amount compensated for the shortage of production shall be refunded duly retaining the agreed Royalty for 3,60,000 MT per annum."

"Both the parties herein have agreed that the period of the mutual agreement is for five (5) years only from the date of Renewal of mining lease. The period can be extended on mutual consent for a further period subject to satisfactory performance, relationship and dealing by the 2nd party."

"The second party herein has agreed to pay the First Party a sum of Rs. 70 per MT of Iron Ore Lumps/mined & moved out of mines every month within 1st week. The amount of Royalty fixed is based on the maximum rate M/s MMTC has fixed for Iron Ore fines as on 1.1.2004 which is Rs. 880/- for Iron Ore fines of 65% Fe grade. The present rate of Royalty i.e. Rs. 70 per MT shall continue till 31.12.2004. Any raise in the rate by M/s MMTC after 31 st December of 2004, a proportional raise of 7% shall be raised in the Royalty rate payable by the second party to the first party."

"In consideration for the services rendered by the second party, the first party has agreed to supply the entire quantity of ore produced to the second party or his assignee @ Rs. 140 per MT. All the expenses such as transportation, wages,

crushing, screening including sales tax, ESIC, EPF etc should be borne by the second party only. In this respect out of Rs. 140/- Rupees 70/- will be counted as Royalty to the 151 Party as mentioned in the above. The balance amount of Rs. 70/- will be deducted by the second party towards charges for mining, crushing, screening, wages, transportation including sales tax, ESIC and EFP etc. Incase of any increase in Royalty then the selling rate is counted as Rs. 70/- (mining charges) + the applicable royalty rate from time to time. For ego Present mining charge Rs. 70 + Royalty Rs. 70/- = Total Rs. 140/-"

17. The assessee, as recorded by the Ld.Commissioner of Income Tax (Appeals), had incurred expenditure in pursuance to MOU. The expenditure incurred up to 31.3.2006 was Rs.1,12,12,446/-. This amount was not claimed as a revenue expenditure by the assessee.

18. The essence of the MOU is to enable the assessee to carry on the business of mining. As already pointed out the assessee was not in this line of business and was in the business of manufacturing and trading. The assessee chose to enter into a new line of business by way of this MOU.

19. The undisputed fact is that the assessee received compensation on termination of this MOU from Mr.R.Charu Chandra, the owner of the mines.

20. We now consider the various case laws on the issue.

21. The Ld.AO relied upon the following case laws.

i. CIT vs. Eastern Book Co. (2010) 322 ITR 605 (All)
ii. Kailashnath & Associates vs. ITO (2009) 121 ITD 563 (Del) (SB)

22. In the case of CIT vs. Eastern Book Co. (2010) 322 ITR 605 (All) the assessee was a publisher firm and had received a sum for infringement of copy rights. The Hon'ble Allahabad High Court held as under.

"Coming to the facts of the present case, it may be noted that the assessee-firm is publisher of law books and journals. It received certain amount of compensation for infringement of its copyright in the relevant books. The assessing authority has recorded that the assessee's copyright in the relevant books has not been affected and has remained fully intact as capital asset. Certain publishers unauthorisedly infringed the copyright of the assessee and the injuries received on account of such publishers have been redressed by paying compensation for the damages caused to the assessee's business of publication. On this factual scenario we are of the view that compensation amount received by the assessee is not towards the loss of capital but is towards the loss of its income. This being so, the Tribunal was not justified in holding otherwise. Our view also finds support from the judgment of the apex court in the case of Sirpur Paper Mills Ltd. [1978] 112 ITR 776."

Thus this case is relevant, only in a factual scenario, where the receipt is towards loss of income and not loss of capital. The undisputed fact is that, the copyright remained fully in tact as a capital asset. Only the injury by way of infringement was received as compensation. The facts of the assessee's case are different. The mining lease which is a capital asset is terminated. The capital asset in this case is not in tact. Hence this case law does not apply to this case.

23. The decision in the case of Kailashnath & Associates vs. ITO (supra) we find that the issue whether the amount received is capital or revenue has not been discussed and what was discussed is the year of taxability. The Tribunal has specifically said that it was not going into the merits of the matter. Thus this case law does not apply.

24. Coming to the judgement of Hon'ble Supreme Court relied upon by the Ld.D.R. in the case of CIT vs. Chari & Chari Ltd. (supra), the facts are that the assessee company was carrying on business in tobacco and other commodities

and also acted as a managing agent for the 'N' company and two other companies. The managing agency agreement with the 'N' company was terminated when the State Government acquired the undertaking of 'N' company. In those circumstances the Hon'ble Supreme Court held as follows:-

"(ii). Ordinarily, compensation for loss of office or agency is regarded as a capital receipt; but this rule is subject to an exception that payment received even for termination of an agency agreement, where the agency is one of many which the assessee holds, and the termination of the agency does not impair the profit making structure of the assessee, but is within the frame work of the business, it being a necessary incident of the business that existing agencies may be terminated and fresh agencies may be taken, is revenue and not capital. However, in the absence of evidence as to what effect the determination of the managing agency of the N company had upon the business of the respondent, the mere circumstance that the respo9ndent had managing agencies of two other companies without more would not bring the present case within the exception (698 H, 699 A-c), Kelsal Parsons & Co.vs. Commissioners of Inland Revenue, 2 ITC and Kettlewell Bullen & Co.vs CIT, Calcutta (1964) 8 SCR 93 3xplained and distinguished." (Emphasis ours)

A perusal of the above case demonstrates that the Hon'ble Supreme Court held that as there was no evidence as to what effect the determination of the managing agency of 'N' company, had upon the business of the assessee, it stated that mere circumstances that the respondent's is the managing agents of two other companies without more will not suffice. The facts of the case on hand are different. The effect of the termination of the mining elase is known.

25. In the case of M/s Western Company (supra), it was a case of multi agency concern, where one of the agencies was terminated and compensation was received. The Hon'ble Court stated that the assessee gave up one of its innumerable agencies in different lines, without any protest presumably

because it was in its normal course of business, and it continued to do business without any mishap. Hence factually this judgement is distinguishable for the case on hand.

26. Now we discuss the case laws relied upon by the assessee.

27. In the case of Oberoi Hotels P.Ltd. 236 ITR 906 (S.C.), the Hon'ble Court was considering a case where the assessee was operating a number of hotels belonging to third parties for the fees. As per the agreement the assessee was having fixed period for operating the hotels. It also had a right of option to purchase the hotel, if other party owner desired to transfer the hotel during the current year of the agreement. The assessee had subsequently gave up its right to exercise the option of purchase of hotel, by way of a supplementary agreement and in lieu thereof, the assessee received certain amounts. The questions before the Hon'ble Supreme Court was whether the amount received was a capital receipt or a revenue receipt. The Hon'ble Court at para 6 observed as follows:-

"6. Applying the aforesaid test laid down by this Court in the present case, in our view, the Tribunal was right in arriving at a conclusion that it was a capital receipt. Reason is that as provided in article XVIII of the first agreement, the assessee was having an option or right or lien, if owner desired to transfer the hotel or lease all or part of the hotel to any other person, the same was required to be offered first to the assessee (operator) or its nominee. This right to exercise its option was given by a supplementary agreement which was executed in September, 1975 between the receiver and the assessee. It was agreed that the receiver would be at liberty to sell or otherwise dispose of the said property at such price and on such terms as he may deem fit and was not under any obligation requiring the purchaser thereof to enter into any agreement with the operator (assessee) for the purpose of operating and managing the hotel or otherwise and in its return, agreed consideration was as stated above in clause X. On the basis of the said agreement, the assessee has received the amount in

question. <u>The amount was received because the assessee, had given up its right to purchase and or to operate the property. Further, it is loss of source of income to the assessee and that right is determined for consideration. Obviously, therefore, it is a capital receipt not a revenue receipt."</u> (Emphasis ours)

In this jdugement, the decision in the case of Chari & Chari Ltd.(supra) was also considered.

At para 10 and 11, the Hon'ble Court has held as follows.

"10. After analyzing number of cases, the Court observed that following satisfactory measures of consistency in the principle is disclosed:
"………………..Where on a consideration of the circumstances, payment is made to compensate a person for cancellation of a contract which does not affect the trading structure of his business, nor deprive him of what in substance is his source of income, termination of the contract being a normal incident of the business, and such cancellation leaves him free to carry on his trade (freed from the contract terminated) the receipt is revenue: Where by the cancellation of an agency source of the assessee's income, the payment made to compensate for cancellation of the agency agreement is normally a capital receipt."

11. The aforesaid principal is relied upon in the case of Karam Chand Thapar & Bros.P.Ltd. case (supra). Considering the aforesaid principles laid down as per article XVIII of the principal agreement, the amount received by the assessee is for the consideration for giving up his right to purchase and/or to operate the property or for getting it on lease before it is transferred or let out to other persons. It is not for settlement of rights under trading contract but the injury is inflicted on the capital asset of the assessee and giving up the contractual right on the basis of principal agreement has resulted in loss of source of the assessee's income."

This judgement in our considered view applies on all force to the facts of this case. The cancellation of the agreement in question deprives the assessee of what is a substantive source of income from mining. It is a loss of source of income from mining. Hence a capital receipt.

28. In the case of Khanna & Anandam ITA 1286/2008 judgement dt. 29.1.2013, the Hon'ble Delhi High Court at paras 7 and 8 held as follows:-

"7. We may refer to one more judgment of the Supreme Court which is reported as Oberoi Hotesl P.Ltd. vs CIT(1999) 236 ITR 903. There the assessee was operating, managing and administering several hotels across the globe such as Cairo, Colombo, Kathmandu, Singapore etc. Its agreement with Hotel Oberoi Imperial, Singapore, which it was operating from 2.11.1970 was terminated and the assessee received a sum of Rs.29,47,500/- from the receiver of the Singapore Hotel. The Supreme Court held that the amount was received because the assessee had given up its right to purchase or operate the property and thus it was a loss of a source of income. The receipt was accordingly held to be capital in nature. It was observed, after a review of the earlier cases, that ordinarily compensation for loss of office or agency is to be regarded as a capital receipt and the only exception where the payment received for termination of an agency agreement could be treated as revenue was where the agency was one of many which the assessee held and its termination did not impair the profit making structure of the assessee, but was within the frame work of the business, it being a necessary incident of the business that existing agencies may be terminated and fresh agencies may be taken. It is somewhat difficult to conceive of a professional firm of chartered accountants entering into such arrangements with international firms of chartered accountants, as the assessee in the present case had done, with the same frequency and regularity with which companies carrying on business take agencies, simultaneously running the risk of such agencies being terminated with the strong possibility of fresh agencies being taken. In a firm of chartered accountants there could be separate sources of professional income such as tax work, audit work, certification work, opinion work as also referred work. Under the arrangement with DHS there was a regular inflow of referred work from DHS through the Calcutta firm in respect of clients based in Delhi and nearby areas. There is no evidence that the assessee firm had entered into similar arrangements with other international firms of chartered accountants. The arrangement with DHS was in vogue for a fairly long period of time 13 years and had acquired a kind of permanency as a source of income. When that source was unexpectedly terminated, it amounted to the impairment of the profit making structure or apparatus of the assessee firm. It is for that loss of the source of income that the compensation was calculated and paid to the assessee. The compensation was thus a substitute for the source. In our opinion, the Tribunal was wrong in treating the receipt as being revenue in nature.

8. On behalf of the revenue our attention was drawn to another judgement of the Supreme Court in CIT vs. Best & Co.P.Ltd. (1966) 60 ITR 11. This judgement was rendered by the same bench which had earlier rendered the judgement in Kettlewell Bullen & Co.Ltd.(supra).
The decision was however in favour of the revenue. The earlier judgement in Kettlewell Bullen & Co.Ltd.(supra) was referred to in the judgement but the Supreme Court observed that the application of the principle laid down in Kettlewell Bullen & Co.Ltd.(supra) must depend on the facts of each case. Their Lordships distinguished the facts and held that in the case of Best&Co.(supra) the assessee had innumerable agencies in different lines and it only gave up one of them and continued to do business without any apparent mishap and that the correspondence showed that the assessee gave up the agency without any protest "presumably because such termination of agencies was part of the normal course of its business." It was on account of this distinction that the ultimate decision went in favour of the revenue. The facts of the case before us, as noted earlier, are not in pari material with those in Best&Co.(supra). In our view the facts are more akin to the case of Kettlewell Bullen & Co.Ltd.(supra) and, therefore, the ratio laid down in that case is more appropriate to be applied to the present case."

In this judgement the decisions of Best & Co.(supra) was distinguished on the ground that the facts are not relevant. The distinction brought out applies to the facts of this case also. This is not a case where termination of an agency was part of the normal course of business. In the case on hand the profit making structure or apparatus of the assessee, which in this case was the mining lease was impaired. It was a loss of source of income.

29. In the case of CIT vs.Prabhu Dayal, 82 ITR 804, the Hon'ble Supreme Court held that when, compensation was a price paid for surrendering the right, which was a capital asset, the receipt has to be considered as a capital receipt.

30. In the case of CIT,Gujarat vs. Saurashtra Chemicals Ltd. 325 ITR 422 (S.C.) it was held that the amount received by the assessee towards

compensation for sterilization of a profit earning source and not in the ordinary course of its business was a capital receipt in the hands of the assessee. This proposition applies to the facts of the assessee's case, as the cancellation of the contract has resulted in sterilization of profit earning source to the assessee i.e. income from mining. Compensation received for such sterilization of the profits earning source is to be considered as a capital receipt.

31. In view of the factual matrix and the well settled propositions of law, we are of the considered view that the order of the First Appellate Authority that the receipt in question is a capital receipt has to be upheld and the ground of Revenue is dismissed.

32. In the result ground nos. 1 and 1.1 of the Revenue is dismissed.

33. Both parties submitted that ground no.2 is a consequential ground to ;ground no.1. Hence this is also to be dismissed for the reason that it is consequential to our decision in ground no.1. Admittedly it was a case of double addition.

34. Ground no.3 is general in nature.

35. In the result the appeal of the Revenue is dismissed.

Order pronounced in the Open Court on 20th June, 2013.

Sd/-	Sd/-
(C.M. GARG) JUDICIAL MEMBER	(J.SUDHAKAR REDDY) ACCOUNTANT MEMBER

Dated: the 20th June, 2013

*manga

Copy of the Order forwarded to:

1. Appellant; 2.Respondent; 3.CIT; 4.CIT(A); 5.DR; 6.Guard File

By Order

Dy. Registrar

1. Date of Dictation:
2. Draft placed before the Author on:
3. Draft proposed and placed before Second Member on:
4. Draft discussed/approved by the Second Member on:
5. Approved draft came to Sr.P.S. on:
6. Date of Pronouncement :
7. File sent to Bench Clerk on :
8. Date on which file given to Head Clerk on:
9. Date of dispatching the Order on: