

**IN THE HIGH COURT OF DELHI AT NEW DELHI**

Date of Decision: October 29, 2007

ITR No. 113 of 1986

**COMMISSIONER OF INCOME TAX** ..... Petitioner

Through: Mr. J.R.Goel, Advocate.

versus

**M/S ALL INDIA FILMS CORPN.** .... Respondent

Through: Mr. P.N. Monga, Advocate.

2. ITR No. 114 of 1986

**M/S ALL INDIA FILMS CORPN.** ..... Petitioner

Through: Mr. P.N. Monga, Advocate.

versus

**COMMISSIONER OF INCOME TAX** ..... Respondent

Through : Mr. J.R.Goel, Advocate.

and

3. ITR No. 115 of 1986

**M/S ALL INDIA FILMS CORPN.** ..... Petitioner

Through: Mr. P.N. Monga, Advocate.

versus

**COMMISSIONER OF INCOME TAX** ..... Respondent

Through : Mr. J.R.Goel, Advocate.

**CORAM:**

**HON'BLE MR. JUSTICE MADAN B. LOKUR**

**HON'BLE DR. JUSTICE S. MURALIDHAR**

Dr. S. MURALIDHAR, J.

1. A question that frequently engages the attention of our tax courts has been referred for our opinion by the Income Tax Appellate Tribunal, Delhi Bench "D", New Delhi ('Tribunal') under Section 256(1) of the Income Tax Act, 1961 ('the Act') for the Assessment Years 1975-76 and 1980-81 arising out of the Tribunal's order dated 20th April, 1985 in ITA No. 5404 and 5405 (Del)/1983.

While ITR No. 113 of 1986 is a reference at the instance of the Revenue, ITR Nos. 114 and 115 of 1986 are references at the instance of the Assessee. That question is whether a sum received by an Assessee should be treated for the purposes of the Act as a capital receipt or a revenue receipt. The large volume of precedents of the High Courts and the Supreme Court on the point underscores the difficulty in easily answering what appears to be a fairly simple question.

The precedent volume grows larger with this judgment.

2. First, the facts. The Assessee took on lease two cinema halls, "Capital" and "Minerva" at Ambala. Since 1952 it was exhibiting films in them and earning a part of its income from that activity. The cinema halls were owned by one Lala Beli Ram Sarin. The last time the lease was renewed was in 1968 for a term of six years and three months from 1st December, 1968 to 28th February, 1975 on a consolidated sum of Rs.72,000/- per year. From a copy of the lease deed which has been included in the paper book it appears that the lease was of not only the cinema halls. It included the stalls, godowns and cinema equipments. The lease deed acknowledged that the Assessee had renovated the cinema halls and that future repairs would be at the cost of lessee subject to the condition that the lessee would inform the lessor in advance of his proposal to carry out repairs, renovations and additions. The lessee was to hand over peaceful possession of the cinema halls along with its equipments to the lessor on the expiry of the lease. The lessee was prohibited from transferring or sub-letting the leasehold rights to any third party except for the stalls where contractors could be appointed.

3. On 1st December, 1975 the owner of the two cinema halls, Lala Beli Ram Sarin, wrote to the Assessee reminding it that the lease was to expire on 28th February, 1975 but that the lessor was willing to extend the period of lease for another five years commencing from 1st March, 1975 and ending on 28th February, 1980 at a consolidated rent of Rs.10,000/- per month. However it appears that during the further negotiations that took place, the parties agreed that the Assessee would hand over possession of the cinema halls to the lessor on or before 28th February, 1975 and to treat the letter dated 1st February, 1975 written by the lessor as cancelled. The terms of this arrangement were reduced to writing in a letter dated 21st February, 1975 written by the landlord to the Assessee which, inter alia, stated that the lessor would pay the lessee a sum of Rs.1,24,000/- in lieu of the loss of business and by way of compensation for handing back the possession of the two cinema halls. It was further agreed that apart from this, the lessor would pay the lessee a further

sum of Rs.2,00,000/- in five equal instalments of Rs.40,000/- each ending with 28th February, 1980.

4. The relevant portion of the aforementioned letter dated 21st February, 1975 written by the landlord to the Assessee reads as under:

“I write this to confirm my agreement that in consideration of your agreeing to treat my said letter dated 1st February, 1975, as cancelled and the said extension of lease as revoked and agreeing to hand back the possession of both the cinemas to me on or before and as on 28th February, 1975, I have agreed to pay to you a sum of Rs.1,24,000/- (Rupees one lac twenty four thousand) in lieu of your loss of business and by way of compensation for handing back the possession of the said two cinemas as on the 28th February, 1975, and also a sum of Rs.40,000/- (Rupees forty thousand) for every year of the extended lease period of five years as under:-

- 1.Rs.40,000/- for period from 1st March, 1975 to 28th Feby. 1976.
- 2.Rs.40,000/- for period from 1st March, 1976 to 28th Feby. 1977.
- 3.Rs.40,000/- for period from 1st March, 1977 to 28th Feby. 1978.
- 4.Rs.40,000/- for period from 1st March, 1978 to 28th Feby. 1979.
- 5.Rs.40,000/- for period from 1st March, 1979 to 28th Feby.1980.”

5. It was further undertaken by the landlord as under:

“In case I do not pay this money to you on or before 1st April, 1975, you are at liberty to file a suit for its recovery in the Courts at Delhi. I agree to give you proper receipt for all the machinery, equipment, furniture, etc. and also receipt for having taken possession of the said cinema premises. I confirm that with the signing of the said receipt for the machinery, equipment, furniture etc., I have no claim against you for anything whatsoever and this handing over of the cinemas in the manner provided above is in full and final settlement.”

6. It is not in dispute that during the Assessment Year 1975-76 the sum of Rs.1,24,000/- was in fact paid to the Assessee and the balance of Rs.2,00,000/- was paid in five equal instalments in the succeeding years i.e. from the Assessment Year 1976-77 onwards. In the accounts prepared for the year ending on 28th February, 1975 the Assessee showed the sum of Rs.1,24,000/- in the credit side of the Profit and Loss Account ('PandL Account') under the heading “compensation for premature closure of the cinema halls at Ambala”. In the accounts for each of the subsequent years beginning from 1976-77 and ending with the Assessment Year 1980-81, the Assessee showed the sum of Rs.40,000/- payable to it by Lala Beli Ram Sarin on the credit side of its PandL Account. Therefore for the Assessment Year 1975-76 a sum of Rs. 1,24,000/- was offered by the Assessee for taxation as a revenue receipt whereas for the Assessment Year 1980- 81, Rs. 40,000/- was offered for taxation.

7. In the Assessment Order dated 29th September, 1977 the Income Tax Officer ('ITO') assessed the entire sum of Rs.3,24,000/- as a revenue receipt in the hands of the Assessee for the Assessment Year 1975-76 on accrual basis.

Aggrieved by the order of the ITO, the Assessee filed an appeal before the Commissioner of Income Tax (Appeals) ['CIT(A)']. It was the Assessee's case that no part of the sum of Rs.3,24,000/- was chargeable to tax since this constituted compensation received for the loss of the profit or income yielding apparatus and therefore the sum received as compensation for the extinguishment of such right would only be a capital receipt. By an order dated 15th September, the CIT(A) accepted this plea and allowed the appeal of the Assessee. The CIT (A) held that the sum of Rs.3,24,000/- was a capital receipt and therefore not taxable.

8. The Revenue then appealed to the Tribunal. Relying on the decision of the Supreme Court in Commissioner of Income Tax v. Shamsheer Printing Press (1960) 39 ITR 90 (SC), the Revenue contended that the sum of Rs. 1,24,000/- was only a revenue receipt since admittedly the sum was given to the Assessee as compensation for the loss of business. The case of the Assessee was that the mere fact that the Assessee had offered Rs.1,24,000/- for tax ought not to be seen as a concession by it that the said sum constituted a revenue receipt.

9. The Tribunal by its judgment dated 20th April, 1985 reversed the order of the CIT(A) and directed that Rs.1,24,000/- be included in the Assessee's taxable income for the Assessment Year 1975-76. It further directed that an addition of Rs.40,000/- should be made to the Assessee's taxable income for the Assessment Year 1980-81. This order has given rise to the present references to this Court.

10. The question that has been referred to us at the instance of the Revenue, is: "Whether on the facts and in the circumstances of the case the Tribunal was justified in holding that even though Rs.3,24,000/- was a revenue receipt, the entire of it did not become assessable in the assessment year 1975-76 only Rs.1,24,000/- became assessable and that the remaining sum of Rs.2,00,000/- accrued to the assessee company to terms of the aforesaid agreement at the expiry of the following accounting periods:-

- (i) For the period from 1st March, 1975 to 28th Feb., 1976  
Rs.40,000
- (ii) For the period from 1st March, 1976 to 28th Feb., 1977  
Rs.40,000
- (iii) For the period from 1st March, 1977 to 28th Feb., 1978  
Rs.40,000
- (iv) For the period from 1st March, 1978 to 28th Feb., 1979  
Rs.40,000
- (v) For the period from 1st March, 1979 to 28th Feb., 1980  
Rs.40,000"

11. The two questions referred to us at the instance of the Assessee are:

"(i) Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that the sum of Rs. 3,24,000/- realised by the assessee by way of compensation for the termination of the lease of the two cinemas namely Minerva and Capital at Ambala by the lessor constituted a revenue receipt

thereby resulting in the income of Rs.1,24,000/- chargeable to tax in the assessment year 1975-76?

(ii) Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that the sum of Rs. 3,24,000/- realised by the assessee by way of compensation for the termination of the lease of the two cinemas namely Minerva and Capital at Ambala by the lessor constituted a revenue receipt thereby resulting in the income of Rs.40,000/- chargeable to tax in the assessment year 1980-81?"

12. Appearing for the Revenue Mr. J.R.Goel, learned senior standing counsel submitted that the sum of Rs.3.24 lakhs received by the Assessee from the lessor for loss of business was a revenue receipt as the entire income had accrued during the Assessment Year 1975-76 itself. In other words, as per the mercantile system of accounting, which the Assessee undoubtedly followed, the said income had accrued in this very year notwithstanding the fact that the sum of Rs.1.24 lakhs was received in the previous year and the remaining sum of Rs.2 lakhs was received in five equal instalments of Rs.40,000/- each in the subsequent years. He further submitted that the extinguishment of the lease of the cinema halls did not bring the entire business of the Assessee to a halt. The Assessee was exhibiting films in cinema halls in other places and earning income and therefore the compensation received for extinguishment of the lease of the two cinema halls at Ambala cannot be treated as a capital receipt. He placed reliance on a decision of the Supreme Court in *Shamsher Printing Press* to contend that the compensation received for termination of lease is not liable to be treated as a capital receipt in the facts of the present case.

13. Mr. P.N.Monga, learned counsel appearing for the Assessee on the other hand contended that the profit making apparatus of the Assessee had been totally crippled and the source of income had been rendered sterile. Relying on the decisions in *Chunduri Venkata Reddi v. Commissioner of Income-Tax, Madras* (1959) 35 ITR 87 (AP), *Commissioner of Income-Tax, Mysore v. Canara Bank Ltd.* (1967)63 ITR 328 (SC), *Lakshmi Insurance Co. (P.) Ltd. v. Commissioner of Income-Tax, New Delhi* (1971) 80 ITR 575 (Del), *Bombay Burma Trading Corp. Ltd v. CIT, Bombay* (1971) 81 ITR 777 (affirmed by the Supreme Court in (1986) 161 ITR 386), *Bawa Shivcharan Singh v. CIT, Delhi* (1984) 149 ITR 29 (Del), *B.G.Shah v. CIT* (1986) 162 ITR 23 (Bom), *H.L.Sidappa v. CIT* (1980) 126 ITR 641 (Kar) and *K.Eapen Jacob v. Commissioner of Income Tax* (1987) 166 ITR 199 (Mad), Mr. Monga contended that the sum of Rs.3,24,000/- had to be necessarily treated as a capital receipt which is not taxable. According to Mr.Monga, the mere fact that there were other cinema halls elsewhere from which the Assessee was earning income by exhibiting films did not change the character of the compensation received by the Assessee; it continued to remain a capital receipt.

14. Without prejudice to the above contention, Mr.Monga submits that the sum of Rs.1,24,000/- alone is liable to be treated as revenue receipt in the hands of the Assessee for the relevant Assessment Year 1975-76. He points to the letter dated 21st February, 1975 in which it is clearly indicated that it is

only the sum of Rs.1,24,000/- which has been offered as compensation for the business loss and that the remaining sum of Rs. 2 lakhs was payable in five equal instalments of Rs.40,000/- each in the years following the Assessment Year 1975-76. In fact, the Assessee did offer for tax the said sum of Rs.40,000/- in the subsequent Assessment Years. The stand of the Revenue that the entire sum of Rs.3.24 lakhs should be taxed in the Assessment year 1975-76 is contrary to what it submitted to the Tribunal. Referring to the judgment in Shamsheer Printing Press Mr. Monga points out that if the case of the Revenue were to be accepted and the entire amount of Rs. 3.24 lakhs is brought to tax in the Assessment Year 1975-76, the component of Rs.2 lakhs which has already been subjected to tax in the subsequent Assessment Years will again have to be taxed in the Assessment Year 1975-76 which is contrary to the settled legal position that no income can be subjected to tax twice over.

15. The first question that requires to be answered is whether the sum of Rs.3,24,000/- constituted a revenue receipt thereby resulting in the income of Rs. 1,24,000/- being chargeable to tax in the Assessment Year 1975-76 and the sum of Rs.40,000/- being chargeable to tax in the Assessment Year 1980-81.

16. Among the early decisions in which the question whether a sum received by way of compensation was a revenue receipt or a capital receipt was considered was that handed down by the Privy Council in Commissioner of Income-tax v. Shaw Wallace and Company AIR 1932 PC 138. The question there was whether a sum of Rs.9,83,361/- which had been included in the total income of the Assessee and received as compensation for cessation of the agency or loss of office was a capital receipt or a revenue receipt. In holding that it was a capital receipt, the Privy Council observed (AIR, p.141):

“If the business had been sold “ even if that somewhat indeterminate asset known as the “goodwill” had been assigned to the employing companies, as the High Court seems to have thought it had “ it is conceded that the price paid would not have been taxable. But why” Plainly because it could not be regarded as profit or gain from carrying on the business, and their Lordships think that the same reasoning must apply when the sum received is in the nature of a solatium for cessation.”

What weighed with the Privy Council was whether there was a complete cessation of business. That would determine whether the compensation received was a capital receipt or a revenue receipt.

17. In Commissioner of Income Tax v. South India Pictures Ltd. (1956) 29 ITR 910 (SC), the Assessee was carrying on the business of distribution of films. For this purpose it had entered into three agreements for advancing moneys to certain motion picture producers towards production of three films and acquiring the rights of distribution thereof. After the Assessee had exploited to a certain extent its right of distribution of three films, the agreements were cancelled and the producers paid an aggregate sum of Rs.26,000/- to the Assessee towards commission. In the relevant accounting year the Assessee had distribution rights in respect of 11 films including 3 films for which it had advanced moneys to the producers. The question then arose whether the sum

of Rs.26,000/- was a revenue receipt in the hands of the Assessee. By a 2:1 majority, the Supreme Court held that the sum paid to the Assessee was in the ordinary course of business and that the termination of the agreement did not radically affect or alter the structure of the Assessee's business. It clarified that the amount was not received by the Assessee as the price of any capital asset sold or surrendered or destroyed. It was held that the decision in Shaw Wallace would not apply in such a case. Again, what appears to have weighed with the Supreme Court in South India Pictures Ltd. was that there was no total cessation of the Assessee's business and that the termination of the agreements "did not radically or at all affect or alter the structure of the Assessee's business." This then appears to be the critical test for determining whether the amount received by way of compensation is a revenue receipt or a capital receipt.

18. The question was again addressed by the Supreme Court in Shamsheer Printing Press. The Assessee had for the purposes of his business housed a printing press in a premises which came to be requisitioned by the Government in September 1943 for the duration of war. This compelled the Assessee to shift and restart its business in another place. A sum of Rs.57,435/- was paid by the Government towards the claim made by the Assessee "on account of the compulsory vacation of the premises, disturbance and loss of business." The Supreme Court held that the compensation received was not towards loss of goodwill. It noted that the claim of the Assessee was under three distinct heads:

(a) compulsory vacation of premises (b) disturbance of business and (c) loss of business.

The Supreme Court then concluded as under (ITR, pp.93-94):

"It seems to us for the reasons aforesaid that the sum of Rs.57,435/- had not been received by the respondent for any injury to any of its capital assets. In our view, the sum was received as compensation for loss of profits for the period during which, it was imagined, the respondent's business would remain stopped before it could be re-started at a new premises. That being so, it was clearly a revenue receipt; it has not been disputed that if the amount in question was paid as compensation for loss of profit, it would be a revenue receipt and liable to tax."

19. It appears to us that the facts in Shamsheer Printing Press are not very different from the facts on hand. The slight difference is that here the Assessee has been compensated by the landlord towards the business loss resulting from it having to vacate premises which did not belong to it but which was in its possession pursuant to a lease. Coupled with this is the undisputed fact that the Assessee had been carrying on the business of distribution and exhibition of films in other cinema halls located in the cities of Jagraon, Yamuna Nagar and Moga. In the circumstances, following the dictum in Shamsheer Printing Press it must be held that the compensation amount received by the Assessee towards the business loss was in fact a revenue receipt.

20. Reliance was placed by the learned counsel for the Assessee on the decision of the Andhra Pradesh High Court in Chunduri Venkata Reddi. It was held by the High Court in that case that the test for determining whether a sum of money is a capital receipt or a revenue receipt was as under (ITR, p.96):

“The amount should have been paid for parting with something which could be described as an enduring asset of the business. The cessation of the business or the cancellation of the agreement should affect the profit-making structure. To quote the words “it should materially destroy or cripple the structure of the profit-making apparatus.”

The decision in Chunduri Venkata Reddi, apart from reiterating the well settled law does not particularly help the case of the Assessee since it is distinguishable on facts. Unless the Assessee here is able to demonstrate that there was a compulsory cessation of Assessee's business and that the source of income was rendered sterile, it will not be able to succeed in its contention that the sum paid by the landlord was a capital receipt.

21. Reliance was also place on the decision of the Supreme Court in Canara Bank Ltd. The facts in that case were that the Respondent Assessee had opened the branch of its Bank in Karachi on 15th November, 1946. After the partition of India in 1947 the currencies of the two countries i.e. India and Pakistan, continued to be at par until 18th September, 1949 when there was a devaluation of the Indian rupee. On that day the Assessee had a sum of Rs.3,97,221/- at the Karachi branch which belonged to its Head Office. The exchange ratio between the two countries was not determined until 27th November, 1951. The Bank in any event did not carry on any business and in particular foreign exchange business.

The State Bank of Pakistan granted permission on 1st July, 1953 to the Assessee to remit the amount to India. In that process, the Assessee made a profit of Rs.1,73,487/- in view of the difference in the value of the currencies. It was held on those facts that the realisation of the profit was not in the course of any trading operation. It was a capital receipt since even if the amount represented stock-in-trade, it was blocked and sterilised. It was clarified that if the profit was earned by exchange operations and “not by way of business of the Assessee, the profit would be capital.” In the instant case however the Assessee had received sum as compensation for business loss and therefore the receipt of the said sum is clearly only a revenue receipt.

22. The question that arose in Lakshmi Insurance Co. (P.) Ltd. was whether the sum of Rs.56,028/- paid as compensation by the Central Government to the Assessee Company which conducted a life insurance business was a revenue receipt in its hands. This Court held that on the facts of that case there was a complete cessation of the activity of the management and that “the divesting of its management was really divesting the assessee-company of its property, the compensation paid was, therefore, was for a loss of a capital asset.” It was therefore held that “compensation paid to the Assessee company is not income.”

The contention of the Revenue that the continuation of the business of the Assessee company would disable it from claiming the sum received as capital receipt was negated by the Court. It was observed as under (ITR, p.581):

“The significant point to be noticed is that there was no complete cessation of the business of the assessee even upon the termination of the two agencies of the assessee. Therefore, even if the revenue is right in saying that the business of the assessee-company in the present case continued despite the divesting of its management as a result of the said Ordinance and the said Act, it is to be seen whether the compensation paid was income or whether it was for the divesting of a part of its profit-making apparatus. The compensation paid cannot be said to be in respect of the profits or gains of any business carried on by the assessee-company nor can it be profit earned by a process of production according to the test laid down by the Privy Council.”

The above decision was peculiar to the facts of the case. The important distinguishing feature in the present case is that the correspondence between the parties itself indicates that the sum paid by way of compensation was clearly for the loss of business.

23. The facts in K.Eapen Jacob were that the sum was paid under a compromise and as compensation for the Assessee surrendering the source of his income namely, the share in the partnership. In those circumstances since the very source of the income of the Assessee was rendered sterile, the Madras High Court held that the amount received by way of compensation was only a capital receipt. Again, the said decision is clearly distinguishable in the applicability to the facts of the present case.

24. Mr. Monga sought to place reliance on the decision of this Court in Bawa Shivcharan Singh where the Assessee received a sum of Rs.30,000/- for surrendering tenancy rights of the first floor of the premises under its occupation. This Court sought to distinguish the type of payment received by the Assessee. It was observed by this Court as under (ITR, p.33):

“The consideration for a lease may be “of a price paid or promised, or of money, a share of crops, service or any other thing of value, to be rendered periodically or on specified occasions to the transferor by the transferee.”

Normally, the initial amount paid for the acquisition of the leasehold right is “premium” “pagri”, “salami” or by whatever name it may be called. This is in consideration for being let in possession. The consideration for relinquishment of the tenancy rights may again be a lump sum called “pagri”. The periodical payment in terms of money for the use and occupation of the premises is called rent or lease money. What distinguishes rent from “premium” is that the latter represents money paid as a price or a consideration for being let in possession. “Pagri” is a consideration for the cessation or surrender of the property or the relinquishment of the leasehold rights.”

As far as the present case is concerned it bears repetition that the

compensation received was not so much for the loss of premises but for the business loss that would ensue therefrom. Moreover, the Assessee was exhibiting films in other cinema halls and therefore there was no permanent cessation of its business.

25. This Court is of the considered view that there was no complete cessation of the Assessee's business activity. It cannot be said that any part of the profit-making apparatus of the Assessee had been extinguished so as to render the amount of compensation received for the said purpose a capital receipt. The sum of Rs.1,24,000/- received by the Assessee in the Assessment Year 1975-76 was a revenue receipt and not a capital receipt. The two questions referred at the instance of the Assessee are therefore answered in the affirmative, that is, in favour of the Revenue and against the Assessee.

26. We take up next for discussion, the question referred at the instance of the Revenue: whether the entire sum of Rs.3,24,000/- became assessable to tax in the Assessment year 1975-76 as contended by the Revenue or only a sum of Rs.1,24,000/- should be assessed to tax since that was the amount received during the Assessment Year”

27. The correspondence between the landlord and the Assessee unambiguously states that a sum of Rs.1,24,000/- has been paid towards his loss of business. The further sum of Rs.2 lakhs does not bear any such particular description in order to determine whether such sum accrued in that very Assessment Year 1975- 76. This coupled with the fact that the Assessee had in fact offered to tax the sum of Rs.40,000/- in every succeeding Assessment Year including 1980-81 indicates that there is no attempt by the Assessee to avoid payment of tax in those Assessment Years. If the said sum of Rs.2 lakhs is brought to tax in the year 1975-76 it will doubtless amount to double taxation of the same amount since admittedly a sum of Rs.40,000/- has been offered to tax by the Assessee in each of the succeeding Assessment Years as a revenue receipt.

28. In that view of the matter this Court is of the view that the question posed at the instance of the Revenue should be answered in the affirmative, that is, in favour of the Assessee and against the Revenue.

29. The reference petitions are accordingly disposed of.

S. MURALIDHAR, J

MADAN B. LOKUR, J

October 29, 2007