

FGP Ltd vs. Commissioner of Income-tax

High Court of Bombay

IT Appeal No. 69 of 2008

June 26, 2008

F.I. Rebello and K.U. Chandiwal, JJ.

Counsels appeared

Subhash Shetty and A.K. Jasani for the Appellant. A.D. Kango for the Respondent.

JUDGMENT

F.I. Rebello, J. - Admit on the following questions:

"(1) Whether on the facts and in the circumstances of the case and in law, the Tribunal was right in coming to the conclusion that the royalty of Rs. 1.35 crores accrued to the appellant during the year in question.

(2) In view of the principles laid down in the decision of this Hon'ble High Court in the case of *CIT v. Smt. Vimla D. Sonawane* 212 ITR 489 and the Supreme Court decision in the case of *Godhra Electricity Co. Ltd. v. CIT* [1997] 225 ITR 746, whether on the facts and in the circumstances of the case and in law, the Tribunal was justified in coming to its impugned conclusion.

(3) On the facts and in the circumstances of the case and in law, whether the Tribunal was justified in coming to the conclusion that impugned royalty accrued to the appellant even though UPT, the party from whom the said amount is due had filed a suit in this Hon'ble Court denying its liability to make any payment under the said agreement."

2. The assessee had a royalty agreement with M/s. UP Twiga Fibre Glass Limited (UPT) under which certain amounts were payable to the assessee. The record would, however, indicate that no income has been received by the appellant till date pursuant to the royalty agreement as there is dispute between the parties and arbitration proceedings are being proceeded with. It is pointed out that when the parties have been referred to arbitration pursuant to suit filed by UPT before this court, seeking relief that no amount was due and payable by them to the assessee herein.

3. The learned CIT had held in favour of the appellant that no real income had accrued in favour of the assessee relying on the judgment in *Godhra Electricity Co. Ltd. v. CIT* [1997] 225 ITR 746 (SC). The revenue aggrieved, preferred an appeal. The assessee relied on the judgment of the Supreme Court in *Godhra Electricity Co. Ltd.'s case (supra)*. The Tribunal distinguished the said judgment on the ground that on the facts it was not applicable and consequently allowed the appeal preferred by the revenue by holding that

once the assessee adopted the mercantile system even if the amount is not received, it will be taxable in assessment year for which it were payable. Hence, the present appeal.

4. The Apex Court in *Godhra Electricity Co. Ltd.'s case (supra)* has laid down the test to assessee income in the hands of an assessee. The assessee therein was also following the mercantile system of accounting and had made entries in the books regarding electrical charges for the supply made to the consumers, however, no real income had accrued to the assessee company. The Tribunal had held that it represented hypothetical income and the Assessing Officer was not right in assessing it to tax. Before the Supreme Court it was urged that even in case of mercantile system of accounting, tax can only be imposed if there is real income and Income-tax cannot be imposed on hypothecated income. The Court held even in mercantile system what has to be seen is whether income can be said to have really accrued to the assessee company. The Court referred to the judgment of the Court in *H.M. Kashiparekh & Co. Ltd. v. CIT* [1960] 39 ITR 706(Bom.) which view was approved by the Supreme Court in *CIT v. Birla Gwalior (P.) Ltd.* [1973] 89 ITR 266. What can therefore, be assessed is real income as Income-tax is a tax on income. The test therefore, before income can be taxed is whether there is real accrual of income. In our opinion, the ratio of that judgment fully applies to the facts of the present case.

5. In the instant case, there is no real accrual of income. There is dispute between the parties for the relevant assessment year which was pending in arbitration. It is only on the arbitral proceedings coming to an end and award being passed and income received by the assessee, will it be liable to be assessed.

Considering the above, question Nos. 1, 2 and 3 are answered against the revenue. Appeal accordingly allowed.