

IT: Waiver of loan for acquiring capital assets cannot be taxed as perquisite under section 28(iv) as receipt in hands of debtor/assessee are in form of cash/money and it also cannot be taxed as a remission of liability under section 41(1) as waiver of loan does not amount to cessation of trading liability

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[2018] 93 taxmann.com 32 (SC)

SUPREME COURT OF INDIA

Commissioner

v.

Mahindra And Mahindra Ltd.*

R.K. AGRAWAL AND ABHAY MANOHAR SAPRE, JJ.†

CIVIL APPEAL NOS. 6949-6950 OF 2004 & OTHERS

APRIL 24, 2018

Section 28(iv), read with section 41(1), of the Income-tax Act, 1961 - Business income - Value of any benefit or perquisite, arising from business or exercise of profession (Waiver of loan) - Assessment year 1976-77 - Assessee had acquired certain tooling and equipments from KJC for which KJC agreed to provide loan to assessee, however, subsequently, another entity took over KJC and agreed to waive outstanding loan amount - Revenue claimed that waived amount represented income under section 28(iv) or alternatively, under section 41(1) - Assessee however, pointed out that sum waived could not be brought to tax as it represented waiver of a loan liability which was on capital account and, thus, was not in nature of income - Whether, for invoking provisions of section 28(iv), benefit received has to be in some form other than in shape of money and since waiver amount represented cash/money, provisions of section 28 (iv) were inapplicable - Held, yes - Whether further, for application of section 41(1), it is sine qua non that there should be an allowance or deduction claimed by assessee in respect of loss, expenditure or trading liability incurred, however, assessee had not claimed deduction under section 36(1)(iii) for interest on loan and loan was obtained for acquiring capital assets, hence, waiver was on account of liability other than trading liability and, thus, provisions of section 41(1) were inapplicable - Held, yes [Paras 13, 15, 16 and 17][In favour of assessee]

FACTS

- The assessee entered into an agreement on 18-6-1964 with Kaiser Jeep Corporation ('KJC') based in America wherein KJC agreed to sell the dies, welding equipments and die models to the assessee. For the procurement of the said toolings and other equipments, the KJC agreed to provide a loan to the assessee at the rate of 6 per cent interest repayable after 10 years in instalments. Subsequently, American Motor Corporation (AMC) took over the KJC and also agreed to waive the principal amount of loan advanced by the KJC to the assessee and to cancel the promissory notes as and when they got matured.
- The assessee filed its return for relevant assessment year 1976-77 and showed Rs. 57.74 lakhs as cessation of its liability towards the American Motor Corporation. The

Assessing Officer, however, held that the credit represented income taxable under section 28.

- On appeal, the Commissioner(Appeals) dismissed the appeal and upheld the order of the Assessing Officer with certain modifications.
- On further appeal, the Tribunal decided the case in favour of the assessee and set aside the order passed by the Commissioner(Appeals).
- On Reference by revenue to the High Court, the High Court confirmed findings of Tribunal in favour of assessee.
- On appeal to the Supreme Court, the revenue claimed that the waived amount represented income under section 28(iv) or alternatively, under section 41. However, the assessee pointed out that sum waived could not be brought to tax as it represented the waiver of a loan liability which was on the capital account and thus, was not in the nature of income.

HELD

- The term 'loan' generally refers to borrowing something, especially a sum of cash that is to be paid back along with the interest decided mutually by the parties. In other terms, the debtor is under a liability to pay back the principal amount along with the agreed rate of interest within a stipulated time.[Para 10]
- It is a well-settled principle that creditor or his successor may exercise their 'Right of Waiver' unilaterally to absolve the debtor from his liability to repay. After such exercise, the debtor is deemed to be absolved from the liability of repayment of loan subject to the conditions of waiver. The waiver may be a partly waiver *i.e.*, waiver of part of the principal or interest repayable, or a complete waiver of both the loan as well as interest amounts. Hence, waiver of loan by the creditor results in the debtor having extra cash in his hand. It is receipt in the hands of the debtor/assessee. The short but cogent issue in the instant case arises whether waiver of loan by the creditor is taxable as a perquisite under section 28(iv) or taxable as a remission of liability under section 41(1).[Para 11]
- On a plain reading of section 28(iv), *prima facie*, it appears that for the applicability of the said provision, the income which can be taxed shall arise from the business or profession. Also, in order to invoke the provision of section 28(iv), the benefit which is received has to be in some other form rather than in the shape of money. In the instant case, it is a matter of record that the amount of Rs.57.74 lakhs is having received as cash receipt due to the waiver of loan. Therefore, the very first condition of section 28(iv) which says any benefit or perquisite arising from the business shall be in the form of benefit or perquisite other than in the shape of money, is not satisfied in the instant case. Hence, in no circumstances, it can be said that the amount of Rs 57.74 lakhs can be taxed under the provisions of section 28(iv).[Para 13]
- On a perusal of section 41(1), it is evident that it is a *sine qua non* that there should be an allowance or deduction claimed by the assessee in any assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee. Then, subsequently, during any previous year, if the creditor remits or waives any such liability, then the assessee is liable to pay tax under section 41. The objective behind this section is simple. It is made to ensure that the assessee does not get away with a double benefit once by way of deduction and another by not being taxed on the

benefit received by him in the later year with reference to deduction allowed earlier in case of remission of such liability. It is undisputed fact that the assessee had been paying interest at 6 per cent per annum to the KJC as per the contract but the assessee never claimed deduction for payment of interest under section 36(1)(iii). In the case at hand, the Commissioner(Appeals) relied upon section 41(1) and held that the assessee had received amortization benefit. Amortization is an accounting term that refers to the process of allocating the cost of an asset over a period of time, hence, it is nothing else than depreciation. Depreciation is a reduction in the value of an asset over time, in particular, to wear and tear. Therefore, the deduction claimed by the assessee in previous assessment years was due to the deprecation of the machine and not on the interest paid by it.[Para 15]

- Moreover, the purchase effected from the KJC is in respect of plant, machinery and tooling equipments which are capital assets of the assessee. It is important to note that the said purchase amount had not been debited to the trading account or to the profit or loss account in any of the assessment years. It is to be noted that there is difference between 'trading liability' and 'other liability'. Section 41(1) particularly deals with the remission of trading liability. Whereas in the instant case, waiver of loan amounts to cessation of liability other than trading liability. Hence, there is no force in the argument of the revenue that the case of the assessee would fall under section 41(1).[Para 16]
- To sum up, the judgment and order passed by the High Court cannot be interfered with for the following reasons:
 - (a) Section 28(iv) does not apply on the present case since the receipts of Rs 57.74 lakhs are in the nature of cash or money.
 - (b) Section 41(1) does not apply since waiver of loan does not amount to cessation of trading liability. It is a matter of record that the assessee has not claimed any deduction under section 36(1)(iii) *qua* the payment of interest in any previous year.[Para 17]
- In view of above discussion, the appeals being devoid of merit are dismissed.[Para 18]

CASE REVIEW

Mahindra & Mahindra Ltd. v. CIT [2003] 128 Taxman 394/261 ITR 501 (Bom.), *Commissioner of Income-tax v. Dholgiri Industrial (P.) Ltd.* [2014] 48 taxmann.com 279 (Madhya Pradesh), *CIT v. Gujarat State Fertilizers & Chemicals Ltd.* [2013] 36 taxmann.com 557 (Gujarat) and *Commissioner of Income-tax v. Ramaniyam Homes (P.) Ltd.* [2016] 68 taxmann.com 289 (Madras) (para 18) affirmed.

CASES REFERRED TO

Mahindra & Mahindra Ltd. v. CIT [2003] 128 Taxman 394/261 ITR 501 (Bom.) (para 2).

Rameshwar Prasad Goyal, AOR, **Arijit Prasad**, Adv., **Mrs. Anil Katiyar**, AOR, **B.V. Balram Das**, AOR, **Pratap Venugopal**, Adv., **Ms. Surekha Raman**, Adv., **Ms. Niharika**, Adv., **Ms. Kanika Kalaiyarasan**, Adv., **Ajay Vohra**, Sr. Adv., **Ms. Kavita Jha**, AOR, **Udit Naresh**, Adv., **Manish K. Bishnoi**, AOR, **Rabin Majumder**, AOR, **Shantanu Sagar**, AOR, **Gunnam Venkateswara Rao**, AOR, **Amar Dave**, Adv., **P.S. Sudheer**, AOR, **Ms. Shruti Jose**, Adv., **Rishi Maheswari**, Adv., **Bharat Sood**, Adv., **Ms. Bharti Tyagi**, AOR, **Rakesh K. Sharma**, AOR, **Nishant**, Adv., **Bhargava V. Desai**, AOR, **Akshat Malpani**, Adv., **Rajat Jariwal**, Adv., **Snehal Kakrania**, Adv., **Bharat Gupta**, Adv., **Akshay Mahajan**, Adv., **Sanjeev K. Kapoor**, Adv., **A. Venayagam Balan**, AOR, **T.G. Narayanan Nair**,

AOR, **Sumit Goel**, Adv., **Ms. Sonal Gupta**, Adv., **Tanuj Agarwal**, Adv., **Ms. Tanya Chaudhry**, Adv. and **Rashmikumar Manilal Vithlani**, AOR *for the Appearing Parties*.

JUDGMENT

R.K. Agrawal, J. - Leave granted.

2. These appeals have been filed against the impugned judgment and order dated 29.01.2003 passed by the High Court of Judicature at Bombay *Mahindra & Mahindra Ltd. v. CIT* [[2003](#)] [128 Taxman 394/261 ITR 501 \(Bom.\)](#) and R.A.No.5161/B/80 whereby the Division Bench of the High Court while giving answers to the Reference Applications filed by the Respondent as well as the Revenue, confirmed certain findings passed by the Income Tax Appellate Tribunal (in short 'the Tribunal') dated 16.08.1982 in favour of the Respondent. Along with this, there are certain other connected appeals also. Since the question of law is same in all these appeals, all the appeals would stand disposed off with this common judgment.

3. Brief facts:—

- (a) For the proper appreciation of the issue in the case at hand, we deem it apposite to mention the gist of the facts. The appellant herein is the Department of Income Tax (for brevity 'the Revenue'), on the other hand, respondent herein is Mahindra & Mahindra Ltd. (for brevity 'the Respondent') - a company registered under the Companies Act, 1956.
- (b) The Respondent, way back, decided to expand its jeep product line by including FC-150 and FC-170 models. For this purpose, on 18.06.1964, it entered into an agreement with Kaiser Jeep Corporation (for short 'the KJC') based in America wherein KJC agreed to sell the dies, welding equipments and die models to the assessee. The final price of the tooling and other equipments was agreed at \$6,50,000/- including cost, insurance and freight (CIF). Meanwhile, the Respondent took all the requisite approvals from the concerned Government Departments. The said toolings and other equipments were supplied by the Kaiser Jeep Corporation through its subsidiary Kaiser Jeep International Corporation (KJIC).
- (c) However, for the procurement of the said toolings and other equipments, the KJC agreed to provide loan to the Respondent at the rate of 6% interest repayable after 10 years in installments. For this purpose, the Respondent addressed a letter dated 07.06.1965 to the Reserve Bank of India (RBI) for the approval of the said loan agreement. The RBI and the concerned Ministry approved the said loan agreement.
- (d) Later on, it was informed to the Respondent that the American Motor Corporation (AMC) had taken over the KJC and also agreed to waive the principal amount of loan advanced by the KJC to the Respondent and to cancel the promissory notes as and when they got matured. The same was communicated to the Respondent vide letter dated 17.02.1976.
- (e) On 30.06.1976 the Respondent filed its return and shown Rs. 57,74,064/- as cessation of its liability towards the American Motor Corporation. After perusal of the return, the Income Tax Officer (ITO) concluded that with the waiver of the loan amount, the credit represented income and not a liability. Accordingly, the ITO, vide order dated 03.09.1979, held that the sum of Rs

57,74,064/- was taxable under Section 28 of the Income Tax Act, 1961 (for brevity 'the IT Act').

- (f) Being dissatisfied, the Respondent preferred an appeal before the Commissioner of Income Tax (Appeals) being No. CIT(A) V/CCIV/IT/261/79-80. After perusal of the matter, learned CIT (Appeals), vide order dated 23.03.1981, dismissed the appeal and upheld the order of the ITO with certain modifications.
- (g) Being aggrieved, the Respondent as well as the Revenue preferred appeals being Nos. 2007 (Bomb.) of 1981 and 2132 of 1981 respectively before the Tribunal. The Tribunal, vide order dated 16.08.1982, set aside the order passed by learned CIT (Appeals) and decided the case in favour of the Respondent.
- (h) Being aggrieved, the Revenue filed a Reference before the High Court at Bombay. In that Reference, three applications were filed, one by the assessee and rest two by the Revenue. Vide impugned common judgment and order dated 29.01.2003, the High Court confirmed certain findings of the Tribunal in favour of the Respondent.
- (i) Hence, these instant appeals have been filed by the Revenue.

4. Heard learned senior counsel for parties and perused the factual matrix of the case.

Point(s) for consideration:—

5. The short point for consideration before this Court is whether in the present facts and circumstances of the case the sum of Rs. 57,74,064/- due by the Respondent to Kaiser Jeep Corporation which later on waived off by the lender constitute taxable income of the Respondent or not?

Rival contentions:—

6. At the onset, learned senior counsel for the Revenue submitted that the Respondent had received the amount of Rs. 57,47,064/- from the American Motor Corporation as loan waiver, which it had initially borrowed from the Kaiser Jeep Corporation as loan in order to enable it to purchase dies, tools etc. for manufacture of jeeps. The waiver of loan was done by the American Motor Corporation, who took over the Kaiser Jeep Corporation, as a measure of compensation for certain losses including goodwill, the benefit of association, and also for sudden change to the American Motor Corporation as a share holder which was credited by the Respondent to its account but was claimed as exemption from taxation being capital receipt.

7. Before concluding, it was contended that since an amount is waived off, for which the Respondent is claiming exemption, it actually amounts to income at the hands of the Respondent in the sense that an amount which ought to be paid by it is now not required to be paid. As a result, the case of the Revenue falls within the ambit of Section 28(iv) and, alternatively within Section 41 of the IT Act. Hence, the decision of the High Court is liable to be set aside.

8. Conversely, learned senior counsel for the Respondent submitted that the Kaiser Jeep International Corporation (KJIC) supplied the toolings and the loan was given by the Kaiser Jeep Corporation (KJC), hence, these transactions were independent transactions. The only relationship, which survived after the supply of toolings, was that of a lender and borrower. The purchase of toolings was not a transaction for the purchase of goods on credit in the ordinary course of business nor could it be equated to unpaid purchase consideration to be liquidated over a period of time.

9. Further, it was also submitted that it is very clear that the amount of \$650,000 provided by KJC was

in fact a loan on which interest was being paid regularly from time to time. It is also pointed out that in the books of account of the Respondent, this loan has been shown in the Balance Sheet under the heading "Loans-unsecured". Hence, it is submitted that the said sum could not be brought to tax as it represents the waiver of a loan liability which was on the capital amount and is not in the nature of income. Accordingly, the High Court rightly upheld the order of the Tribunal and, hence, these appeals deserve to be dismissed.

Discussion:—

10. The term "loan" generally refers to borrowing something, especially a sum of cash that is to be paid back along with the interest decided mutually by the parties. In other terms, the debtor is under a liability to pay back the principal amount along with the agreed rate of interest within a stipulated time.

11. It is a well-settled principle that creditor or his successor may exercise their "Right of Waiver" unilaterally to absolve the debtor from his liability to repay. After such exercise, the debtor is deemed to be absolved from the liability of repayment of loan subject to the conditions of waiver. The waiver may be a partly waiver i.e., waiver of part of the principal or interest repayable, or a complete waiver of both the loan as well as interest amounts. Hence, waiver of loan by the creditor results in the debtor having extra cash in his hand. It is receipt in the hands of the debtor/assessee. The short but cogent issue in the instant case arises whether waiver of loan by the creditor is taxable as a perquisite under Section 28 (iv) of the IT Act or taxable as a remission of liability under Section 41 (1) of the IT Act.

12. The first issue is the applicability of Section 28 (iv) of the IT Act in the present case. Before moving further, we deem it apposite to reproduce the relevant provision herein below:—

'28. Profits and gains of business or profession.— The following income shall be chargeable to income-tax under the head "Profits and gains of business profession",—

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(iv) the value of any benefit or perquisite, whether convertible into money or not, arising from business or the exercise of a profession;

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13. On a plain reading of Section 28 (iv) of the IT Act, *prima facie*, it appears that for the applicability of the said provision, the income which can be taxed shall arise from the business or profession. Also, in order to invoke the provision of Section 28 (iv) of the IT Act, the benefit which is received has to be in some other form rather than in the shape of money. In the present case, it is a matter of record that the amount of Rs. 57,74,064/- is having received as cash receipt due to the waiver of loan. Therefore, the very first condition of Section 28 (iv) of the IT Act which says any benefit or perquisite arising from the business shall be in the form of benefit or perquisite other than in the shape of money, is not satisfied in the present case. Hence, in our view, in no circumstances, it can be said that the amount of Rs 57,74,064/- can be taxed under the provisions of Section 28 (iv) of the IT Act.

14. Another important issue which arises is the applicability of the Section 41 (1) of the IT Act. The said provision is re-produced as under:

"41. Profits chargeable to tax.- (1) Where an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee (hereinafter referred to as the first-mentioned person) and subsequently during any previous year,-

(a) the first-mentioned person has obtained, whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained by such person or the value of

benefit accruing to him shall be deemed to be profits and gains of business or profession and accordingly chargeable to income-tax as the income of that previous year, whether the business or profession in respect of which the allowance or deduction has been made is in existence in that year or not; or

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15. On a perusal of the said provision, it is evident that it is a *sine qua non* that there should be an allowance or deduction claimed by the assessee in any assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee. Then, subsequently, during any previous year, if the creditor remits or waives any such liability, then the assessee is liable to pay tax under Section 41 of the IT Act. The objective behind this Section is simple. It is made to ensure that the assessee does not get away with a double benefit once by way of deduction and another by not being taxed on the benefit received by him in the later year with reference to deduction allowed earlier in case of remission of such liability. It is undisputed fact that the Respondent had been paying interest at 6 % per annum to the KJC as per the contract but the assessee never claimed deduction for payment of interest under Section 36 (1) (iii) of the IT Act. In the case at hand, learned CIT (A) relied upon Section 41 (1) of the IT Act and held that the Respondent had received amortization benefit. Amortization is an accounting term that refers to the process of allocating the cost of an asset over a period of time, hence, it is nothing else than depreciation. Depreciation is a reduction in the value of an asset over time, in particular, to wear and tear. Therefore, the deduction claimed by the Respondent in previous assessment years was due to the depreciation of the machine and not on the interest paid by it.

16. Moreover, the purchase effected from the Kaiser Jeep Corporation is in respect of plant, machinery and tooling equipments which are capital assets of the Respondent. It is important to note that the said purchase amount had not been debited to the trading account or to the profit or loss account in any of the assessment years. Here, we deem it proper to mention that there is difference between 'trading liability' and 'other liability'. Section 41 (1) of the IT Act particularly deals with the remission of trading liability. Whereas in the instant case, waiver of loan amounts to cessation of liability other than trading liability. Hence, we find no force in the argument of the Revenue that the case of the Respondent would fall under Section 41 (1) of the IT Act.

17. To sum up, we are not inclined to interfere with the judgment and order passed by the High court in view of the following reasons:

- (a) Section 28(iv) of the IT Act does not apply on the present case since the receipts of Rs 57,74,064/- are in the nature of cash or money.
- (b) Section 41(1) of the IT Act does not apply since waiver of loan does not amount to cessation of trading liability. It is a matter of record that the Respondent has not claimed any deduction under Section 36 (1) (iii) of the IT Act *qua* the payment of interest in any previous year.

18. In view of above discussion, we are of the considered view that these appeals are devoid of merits and deserve to be dismissed. Accordingly, the appeals are dismissed. All the other connected appeals are disposed off accordingly, leaving parties to bear their own cost.

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*In favour of assessee.

† Arising out of orders of High Court in *Mahindra & Mahindra Ltd. v. CIT* [2003] 128 Taxman 394/261 ITR 501 (Bom.), *Commissioner of Income-tax v. Dholgiri Industrial (P.) Ltd.* [2014] 48 taxmann.com 279 (Madhya Pradesh), *CIT v. Gujarat State Fertilizers & Chemicals Ltd.* [2013] 36 taxmann.com 557 (Gujarat) and *Commissioner of Income-tax v. Ramaniyam*

Homes (P.) Ltd. [\[2016\] 68 taxmann.com 289 \(Madras\)](#).