

## Compensation received from 'Coca Cola' for breaching contract for bottling soft drinks was capital receipt: HC

**Summary – The High Court of Bombay in a recent case of Parle Soft Drinks., (the Assessee) held that where under master agreement between Coca Cola and Parle group, assessee-subsiary was to be formed for bottling soft drinks for coca cola and as a result of breach of contract by Coca Cola assessee's fundamental right for starting bottling business was taken away, compensation received by assessee from Coca Cola would be treated as capital receipt**

**Sale proceeds of old soft drinks bottles would reduce value of relevant block and depreciation was to be allowed accordingly**

### Facts

- The assessee, a Parle Group of Companies, was engaged in the business of manufacturing, bottling and distribution of soft drinks and beverages under several popular brands.
- The Assessing Officer observed during the assessment that the assessee had received a sum of Rs. 16.06 crores from Coco Cola Company of USA (TCCC), which was claimed to be exempt from tax on account of it being a capital receipt. This compensation was claimed to have been received as compensation related to the 'right of first refusal for bottling rights given to the assessee' in the city of Pune.
- A reference was made to the master agreement with Coca Cola company of September, 1993 for transfer of intellectual property rights in the nature of trademarks, knowhow, franchisee rights etc. in respect of various brands of beverages/soft drinks owned by the Parle Group. After the transfer of trademark, as per the master agreement, wherein the Parle Group of Companies along with two persons RC & PC was the seller and TCCC was the buyer along with Coco Cola South Asia Hoding (Inc.) as the confirming party, bottling of soft drink was to be continued by RC and PC through Parle Bottling Company having bottling rights in Pune while LFFL, having bottling rights in the territory of Bangalore. In the said agreement itself, a draft of right of first refusal regarding bottling rights was also elaborated. However, later on, TCCC took strategic policy decision to set up its own bottling plant at Bangalore. This led to breach of obligation by TCCC in respect of the 'right of first refusal given to Parle Group' in the master agreement and led to dispute between Parle Group and TCCC. This dispute was ultimately settled with TCCC agreeing to pay the assessee Rs. 16.06 crore.
- The Assessing Officer disallowed Rs. 16.06 crore on protective basis.
- On appeal, the Commissioner (Appeals) passed an order holding that the sale proceeds relate to capital assets and hence, the same was to be reduced from the block assets.
- On the revenue's appeal, the Tribunal held that the compensation received by the assessee from Coca-Cola was the capital receipt and since there was no transfer for extinguishment of any rights, there was no question of capital gain and accordingly, the Tribunal dismissed the revenue's appeal.
- On appeal:

#### Held

- Under the master agreement, the right of first refusal was vested with LFFL to carry out the bottling activities in the territory of Bangalore. There was a clear indication that there would be formation of Bangalore subsidiary and there would be an investment agreement also between the parties for this purpose. The necessary guidelines as to how the subsidiary would be formed, various assignments of the bottling rights only to such a newly formed company and to be held and formed by Parle Group and later on the Coca Cola Company will join in after subscribing 30 per cent of the shares, are the provisions or guidelines in the master agreement itself. It was to this subsidiary company that the bottling rights were to be given in the territory of Bangalore. This subsidiary company was formed as Parle Soft Drinks Pvt. Ltd. Thus, the assessee company was formed only for carrying out bottling activities in the territory of Bangalore. There was, thus, no dispute that the assessee was entitled to receive the compensation amount on the breach of this agreement from Coca Cola Company. Thus, even though the right of first refusal was with LFFL, but it was always agreed upon by the parties that the same should be for the newly formed subsidiary at Bangalore. That Bangalore subsidiary is the assessee company only. These bottling activities were to be carried out for the Coca Cola Company in the Bangalore territory for which the assessee was formed. It was not necessary that the assessee should have installed entire plant and machinery for carrying on such business. The right of first refusal itself stated a substantial right and foundation on which the assessee could have built its bottling business. If such right would have been assigned to the assessee, it would have been the source of assessee's income and profit making apparatus. The assessee has also submitted its business plans and various modes for carrying out the bottling business to the Coca Cola Company. There is no dispute that the Coca Cola Company had breached the agreement and particularly the right of first refusal by not assigning the rights. It was on account of breach of this agreement that the compensation amount was settled between the parties. The fundamental right for starting the bottling business was taken away as a result of breach of the right of first refusal by the Coca Cola Company. That is the reason why the Coca Cola Company paid this amount to the assessee and not to LFFL.
- All the tests that were evolved by the Supreme Court in the decisions noted above, have been applied and to arrive at the correct conclusion. The view of the Tribunal is not in any way erroneous or illegal. Thus, it is not vitiated by any error of law apparent on the face of the record of perversity.

#### ***Pearle Bottlings***

- The matter has to be approached from a factual view point.
- Even in the case of *Parle Bottling Private Limited*, where the Assessing Officer has treated the receipt to be taxed as long term capital gains on protective basis and the Commissioner (Appeals) has treated the same receipt to be taxed as casual and non-recurring taxable income under section 10(3), the argument was that the assessee received this sum of Rs. 16.06 crore as compensation from the Coca Cola Company for breach of the right of first refusal agreement with regard to

bottling rights of Pune territory. The Assessing Officer, according to the assessee, solely relied upon the observations and findings in the assessment order dated 30th March, 2001 in the case of *Aqua Bisslery Limited*, wherein, the receipt was taxed under the head 'long term capital gains'. Once the factual basis was laid before the Commissioner (Appeals) and it was found that the same was identical to the case of *Parle Soft Drinks Private Limited* except for the fact that in the present case, the assessee was in the bottling business for Parle Group of Companies, there was a right of first refusal and the assessee was to carry on the business of bottling for the Coca Cola Company. A detailed business plan was submitted. However, the Coca Cola Company, without any specific reason, rejected the business plan. Thus, there was a breach of the right of first refusal and after negotiation (sic) received compensation in the above sum, which was shown as non-taxable capital receipt. The argument was identical that the Coca Cola Company had deprived the assessee of all potential right and that was to set up a bottling plant for Pune territory. There was a breach of contract giving rise to a claim for damages and same was paid on account of failure to honour the commitment. That is capital in nature. That source of income, by way of setting up of a bottling plant at Pune territory was lost forever. Hence, relying upon the judgment in the case of *Oberoii Hotel (P.) Ltd. v. CIT* [\[1999\] 103 Taxman 236/236 ITR 903 \(SC\)](#), the argument that such a receipt cannot be taxed as revenue receipt or casual income, was accepted. The Tribunal, noted the arguments of the revenue and particularly the summary of the same. Thereafter, the Tribunal dealt with the main dispute and as above.

- Therefore, a different view on facts could not have been taken.