



Subsidy in the form of concession of entertainment tax to new multiplex complexes is capital in nature – Supreme Court

Background

Recently, the Supreme Court in the case of Chaphalkar Brothers¹ (the taxpayer) held that subsidy in the form of the concession of entertainment tax to new multiplex complexes is capital in nature. The Supreme Court observed that the receipt of subsidy is capital or revenue will have to be determined by having regard to the purpose for which the subsidy is given.

Facts of the case

- As a result of the onslaught of cable television and advancement in the field of Information Technology, the average occupancy in cinema theatres has fallen considerably and hardly any new theatres have been started in the recent past. The public at large these days prefer to see movies at home. Keeping in view this scenario, a concept of the complete family entertainment centre, i.e. 'Multiplex Theatre Complex' has emerged. These multiplex theatre complexes offer various entertainment facilities for the entire family under a single roof. However, these complexes are highly capital intensive, their gestation period is also quite long, and therefore, need government's support and incentive in entertainment duty.
- With a view to commemorate the birth centenary of Chitrapati late Shri V. Shantaram, the government decided to grant concession in entertainment duty to multiplex theatre complexes to promote construction of new cinema houses in the State with effect from 17 August 2001. The concession was to support

the on-going activities of the multiplex and not for its construction. Since the concession was given in the form of a charge on the gross value of the ticket and contributed towards the day-to-day running expenditure, the Assessment Officer (AO) held that it was in the nature of a revenue receipt. The CIT(A) upheld the order of the AO.

- The Tribunal held that the scheme does not provide any assistance for reimbursement of day to day revenue expenditure but the concession was meant to build-up and to promote new multiplex cinema halls which are nothing, but for the construction purpose hence reimbursement is to cover up the capital expenditure.
- The High Court held that since the object of subsidy was to promote construction of multiplex theatre complexes, the receipt of subsidy would be on capital account.

Supreme Court's decision

- In the case of Sahney Steel², the Supreme Court held that the idea of the subsidy scheme was to provide a helping hand for five years in order to enable the industry to be viable and competent. The Supreme Court held that since funds were made available to the taxpayer to assist it in carrying on its trade and business, there can be little doubt that the object 'of various assistances under the subsidy scheme was to enable the taxpayer to run the business more profitably'.

¹ CIT v. Chaphalkar Brothers (Civil Appeal Nos. 6513-6514 of 2012, dated 7 December 2017) – Taxsutra.com

² Sahney Steel & Press Works Ltd. v. CIT [1997] 228 ITR 253 (SC)

- The test of whether the receipt of subsidy is capital or revenue will have to be determined by having regard to the purpose for which the subsidy is given. If it is given by way of assistance to the taxpayer in carrying on of his trade or business, it has to be treated as a trading receipt. The source of the fund is quite immaterial.
- The Supreme Court also referred the decision of Ponni Sugars³ wherein the Supreme Court held that the character of the receipt in the hands of the taxpayer has to be determined with respect to the purpose for which the subsidy is given. The point of time at which the subsidy is paid is not relevant. The source and the form of subsidy are immaterial. If the object of the subsidy scheme was to enable the taxpayer to run the business more profitably, then the receipt is on revenue account. On the other hand, if the object of the assistance under the subsidy scheme was to enable the taxpayer to set up a new unit or to expand the existing unit then the receipt of the subsidy was on capital account. Therefore, it is the object for which the subsidy/assistance is given which determines the nature of the incentive subsidy.
- Applying the aforesaid purpose test contained in both Sahney Steel as well as Ponni Sugar, the Supreme Court was of the view that the object, as stated in the statement of objects and reasons, of the amendment ordinance was that since the average occupancy in cinema theatres has fallen considerably and hardly any new theatres have been started in the recent past, the concept of a complete family entertainment centre, more popularly known as multiplex theatre complex, has emerged. These complexes offer various entertainment facilities for the entire family as a whole. It was observed that these complexes are highly capital intensive and their gestation period is quite long and therefore, they need government support in the form of incentives qua entertainment duty.
- The object of the grant of the subsidy was in order that persons come forward to construct multiplex theatre complexes, the idea being that exemption from entertainment duty for a period of three years and partial remission for a period of two years should go towards helping the industry to set up such highly capital intensive entertainment centres.
- It is difficult to accept the tax department's argument that it is only the immediate object and not the larger object which must be kept in mind

in that the subsidy scheme kicks in only post construction that is when cinema tickets are actually sold. The Supreme Court hasten to add that the object of the scheme carried out in a particular manner is irrelevant, as has been held in both Ponni Sugar and Sahney Steel.

- The taxpayer relied on the decision of Jammu and Kashmir High Court⁴ wherein also concessions were given in order to achieve the twin object i.e. acceleration of industrial development and generation of employment. It has been held that the finding of the Jammu and Kashmir High Court on the facts of the incentive subsidy contained in that case is absolutely correct. In that, once the object of the subsidy was to industrialise the State and to generate employment in the State, the fact that the subsidy took a particular form and the fact that it was granted only after commencement of production would make no difference.
- Accordingly, the subsidy is capital in nature.

Our comments

The issue whether subsidy received from the government is capital or revenue in nature has been a matter of debate before the Courts.

In the instant case, the Supreme Court reaffirmed that the 'purpose test' is the essential test that is to be adopted in determining the character of a subsidy, and the outward form in which the subsidy is granted is not determinative of the issue. The Supreme Court while upholding some of the earlier decisions observed that the fact that the subsidy was not meant for repaying the loan taken for construction of multiplexes cannot be ground to hold that subsidy receipt was on revenue account. If the object of the scheme were to promote cinema houses by constructing multiplex theatres, then irrespective of the fact that the multiplexes have been constructed out of own funds or borrowed funds, the receipt of subsidy would be on the capital account.

It is important to note that the Finance Act, 2015 amended the definition of 'income'⁵ to provide that a subsidy or grant, etc. from the government in any form is to be treated as taxable income unless it is reduced from the cost of the capital asset as per the provisions of the Act⁶.

³ CIT V. Ponni Sugars and Chemicals Limited [2008] 306 ITR 392 (SC)

⁴ Shri Balaji Alloys v. CIT [2011] 333 ITR 335 (J&K)

⁵ Finance Act, 2015 introduced Section 2(24)(xviii) of the Act with effect from AY 2016-17

⁶ As per Explanation 10 to clause (1) of Section 43 of the Act

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