IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 18.11.2015

CORAM:

THE HONOURABLE MR.JUSTICE **M.JAICHANDREN**
and
THE HONOURABLE MRS.JUSTICE **S.VIMALA**

Tax Case (Appeal) No.2529 of 2006

Commissioner of Income Tax,
Central III,
Chennai. .. Appellant

Vs.

Ram Kumar Giri .. Respondent

PRAYER: Tax Case Appeal filed under Section 260A of the Income Tax Act, 1961 as against the order dated 12.05.2006 made in I.T.A.No.1661/Mds/2004 on the file of the Income Tax Appellate Tribunal, Madras 'D' Bench for the assessment year 2000-2001.

For Appellant :Mr.T.R.Senthil Kumar

For Respondent :Mr.Sandeep Bagmar
for Mr.V.S.Jayakumar

J U D G M E N T

(Judgment of the Court was delivered by S.Vimala, J.)

This Appeal has been preferred by the Revenue, under Section 260(A) of the Income Tax Act, 1961, (hereinafter referred to as "the Act"), challenging the order passed by the Income Tax Appellate Tribunal, in I.T.A.No.1661/Mds/04, dated 12.05.2006.

Brief facts:

2. The Assessee is the Managing Director of Chennai Bottling Company Ltd., which was engaged in bottling and marketing of various beverages, for which, the concentrate was purchased from Coca-Cola Company of U.S.A. The bottling was done under an Agreement, dated 15.08.1994, between Chennai Bottling Company Ltd. and Coca-Cola Company, U.S.A. On 27.04.1999, Hindustan Coca-Cola Bottling South West Pvt. Ltd. entered into an agreement to purchase the entire business of the said Chennai Bottling Company, for Rs.29.86 Crores. There was an Agreement with the Assessee, even prior to the agreement with the Company, to pay him a sum of Rs.57.84 Crores, over the period 1999 to 2002, for "non compete, non disclosure, non sharing of know how, as per the restrictive covenants specified in the Agreement".

2.1. The Assessee claimed that the amount of Rs.57.84 Crores is a capital receipt, by way of compensation, for not carrying out any competitive business or non disclosure to third parties, regarding the know how gained by him. The Assessee had also claimed that the interest on the escrow account should be brought to tax only on receipt basis and not on accrual basis. The Assessing Officer had held that the amount of Rs.57.84 Crores, as well as the interest on the escrow account should be taxed on accrual basis and brought the entire amount to tax during the year 2000-2001.

3. The Assessing Officer had held that Section 28(va) of the Act should be treated as explanatory or clarificatory in nature. Hence, the provisions of the section would also be applicable, for the earlier years, as well.

4. The Assessee had filed an appeal before the Commissioner of Income Tax (CIT), who had decided the issues in favour of the Assessee and had allowed the appeal.

5. The Revenue took up the matter in Appeal to the Income Tax Appellate Tribunal. The Tribunal had held that Section 28(va) of the Act would be applicable only prospectively and the transaction is not a colourable device to minimise the tax liability, as held by the Commissioner of Income Tax.

6. Aggrieved by the order of the Income Tax Appellate Tribunal, the Revenue has filed this appeal, which has been admitted on the following substantial questions of law:-

> 1. Whether in the facts and circumstances of the case, the Tribunal was right in treating the amount of Rs.57.85 crores received by the assessee under an agreement for non

disclosure and non sharing of know how, as a capital receipt?

2. Whether the provisions of Section 28(1)(va) are to be treated as clarificatory in nature and read as having retrospective operation?

3. Whether the fees received for non disclosure and non sharing of know how is to be taxed as income from closure of agency, since it was linked with the closure of the franchisee business of the company of which the assessee was the managing director?

4. Whether in the absence of Section 28(1)(va) during the relevant assessment year, the receipt for non disclosure and non sharing of know how should automatically be treated as a capital receipt, or should it be treated as income from other sources?.

7. The main contention of the learned counsel for the appellant is that the amount of Rs.57.84 Crores, received by the Assessee, should not have been treated as non compete fee/capital receipt. The further contention is that, in any event, the sum of Rs.57.84 Crores is taxable, under Section 28(va) of the Act, under the head of Income from other sources, if not as income from business. It is strenuously contended that, in every case, where ingenuity is expended to avoid payment of tax, it is the duty of the Court to get behind the smoke screen and discover the true state of affairs.

8. Per contra, the learned counsel for the Assessee would submit that there is a distinction between receipt of compensation by an Assessee, for the loss of agency and receipt of compensation attributable to the restrictive / negative covenant and that in the case of the former, it is a revenue receipt, whereas, in the case of the later, it is a capital receipt; inasmuch as the contract is only in respect of a restrictive covenant, it is only a capital receipt and of which, the Assessee is entitled to exemption from tax liability.

8.1. Yet another contention is that the payment received as non compete fee has been treated only as capital receipt, till the assessment year 2003-04, and only vide Finance Act 2002, the said capital receipt has been made as taxable, under Section 28(va) of the Act, with effect from 01.04.2003, and that Section 28(va) of the Act is amendatory and not clarificatory in nature. In support of the said contention, the decision, reported in ***(2011) 332 ITR 602 (Guffic Chem (P) Ltd., vs. Commissioner of Income Tax)*** is relied upon, wherein, it has been held as follows:

> *"7. Two questions arose for determination, namely, whether the amounts received by the appellant for loss of agency was in normal course of business and therefore, whether they constituted revenue receipt? The second question which arose before this Court was whether the*

amount received by the assessee (compensation) on the condition not to carry on a competitive business was in the nature of capital receipt? It was held that the compensation received by the assessee for loss of agency was a revenue receipt whereas compensation received for refraining from carrying on competitive business was a capital receipt. This dichotomy has not been appreciated by the High Court in its impugned judgment. The High Court has misinterpreted the judgment of this Court in Gillanders' case (supra). In the present case, the Department has not impugned the genuineness of the transaction. In the present case, we are of the view that the High Court has erred in interfering with the concurrent findings of fact recorded by the CIT(A) and the Tribunal. One more aspect needs to be highlighted. Payment received as non-competition fee under a negative covenant was always treated as a capital receipt till the assessment year 2003-04. It is only vide Finance Act*, 2002 with effect from 1.4.2003 that the said capital receipt is now made taxable [See:* Section 28(va)]. The Finance Act*, 2002 itself indicates that during the relevant assessment year compensation received by the assessee under non- competition agreement was a capital receipt, not taxable under the 1961 Act. It became taxable only with effect from 1.4.2003. It is well settled that a liability cannot be created retrospectively. In the present case, compensation received under Non-Competition Agreement became taxable as a capital receipt and not as a revenue receipt by specific legislative mandate vide* Section 28(va) *and that too with effect from 1.4.2003. Hence, the said* Section 28(va) *is amendatory and not clarificatory. ....".*

9. We find that the above decision squarely applies to the facts of the case. In the case on hand, the Assessment year is 2000-01. As held in the decision cited supra, the capital receipt is taxable only from 01.04.2003. Therefore, the order passed by the Income Tax Appellate Tribunal does not suffer from any infirmity and therefore, it is liable to be confirmed.

10. In the result, this Tax Case (Appeal) stands dismissed and the order, dated 12.05.2006, passed in I.T.A.No.1661/Mds/2004 by the Income Tax Appellate Tribunal, Madras 'D' Bench, is confirmed.

Index: Yes / No (M.J.J.) (S.V.,J.)
Internet: Yes / No 18.11.2015
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To

1. The Income Tax Appellate Tribunal,
   Madras 'D' Bench.
2. The Commissioner of Income Tax,
   Central III, Chennai.

M.JAICHANDREN, J.
and
S.VIMALA, J.

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