

THE HON'BLE SRI JUSTICE RAMESH RANGANATHAN
And
THE HON'BLE SRI JUSTICE M.SATYANARAYANA MURTHY

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I.T.T.A.No.164 of 2015

ORDER: (per Hon'ble Sri Justice Ramesh Ranganathan)

This appeal, under Section 260-A of the Income Tax Act, 1961 (for brevity, 'the Act'), is preferred by the Revenue aggrieved by the order passed by the ITAT, Hyderabad Bench in I.T.A.No.1228/Hyd/2005 dated 08.06.2012 for the assessment year 2002-03.

The respondent-claimant claimed deduction of Rs.3.25 Crores paid by them, to M/s Kannumuri Holdings Private Limited (for brevity, 'KHPL'), as consideration for their not competing with the assessee in setting up new power projects in the State of Andhra Pradesh for a period of three years commencing from 28.12.2001. The payment made, pursuant to the said agreement, was claimed as revenue expenditure and debited to the profit and loss account. The assessing authority held that merely because an agreement was entered into with one person, not to set up a power plant in Andhra Pradesh, did not disable others from establishing power project; several power projects were coming up in the State of Andhra Pradesh; in such a situation there was no basis for the assessee to pay any substantial amount to one person; keeping one person away from the project would not enable the assessee to stop competition in their business;

Sri K.Raghu Ramakrishna Raju was setting up a project in Tamilnadu and was associated with an existing power project in Andhra Pradesh established by M/s R.K.Energies Private Limited; and that expenditure incurred by the assessee was capital expenditure in nature, without bringing about any depreciable asset into existence. He, therefore, disallowed the expenditure treating it as capital expenditure. He did not also allow any depreciation thereon.

In appeal the Commissioner of Income Tax (Appeals), by his order dated 30.09.2005, held that there was no dispute about the genuineness of the payment or the identity of the payee; the only dispute was whether the said non-competition fee paid by the assessee was revenue expenditure or capital expenditure; the facts relevant to decide the issue were: the assessee was initially promoted by three companies including M/s KHPL and associates, represented by

Sri K.Raghu Ramakrishna Raju; because of certain disputes, among the Directors, it was decided that Sri K.Raghu Ramakrishna Raju would exit from the company and set up his own power project; Sri K.Raghu Ramakrishna Raju was already setting up a power project in Tamilnadu under the banner of his group company M/s R.K.Energies Limited; in the said background the assessee felt that, if Sri K.Raghu Ramakrishna Raju competed with their business, it would lead to serious repercussions affecting their profitability; in order to stall the immediate potential threat, the assessee entered into an agreement to keep Sri K.Raghu Ramakrishna Raju away from all his contacts with the suppliers, funding agencies and other business associates of the assessee, and also to stop him from creating any legal problems; and the non-competition agreement was only for a limited period of three years to ward off competition in the territory of Andhra Pradesh.

The Commissioner held that payment was made by the assessee to a rival company to ward off competition in business; by making this payment, the assessee had not derived any advantage of an enduring nature to hold the expenditure as capital in nature; the agreement was only for a limited period of three years; the main object was to stall the immediate potential threat on the parting away of the other Director by keeping him away from all his contacts with the suppliers, funding agencies and other business associates, and

also to stop him from creating any legal problems for the assessee; payment was made in order to enable the assessee to derive more profits in the business without any hindrance from the parting Director; payment was made for the purpose of running the business, and not for the purpose of acquiring the business; the expenditure incurred did not relate to the acquisition of an asset or a right of permanent character or an advantage of enduring nature; such expenditure could not, therefore, be held to be capital expenditure; and, since payment was made wholly and exclusively for the purposes of the business, the same had to be allowed as revenue expenditure in terms of provisions of Section 37 (1) of the Act. The Commissioner held that non-competition fee of Rs.3.25 Crores paid by the assessee was allowable as revenue expenditure of the business of the assessee. Aggrieved thereby the Revenue carried the matter in appeal to the ITAT. In the order under appeal, the Tribunal relied on the judgment of the **Supreme Court in CIT v. Coal Shipments Private Limited**^[1] and the Delhi High Court in **CIT v. Eicher Limited**^[2].

The extracted portion of the order of the Supreme Court in **Coal Shipments Private Limited**¹, in the order of the Tribunal, reads thus:-

“.....The case which has been set up on behalf of the Revenue is that, as the object of making the payments in question was to eliminate competition of a rival exporter, the benefit which ensured to the respondent was of an enduring nature and, as such, the payment should be treated as capital expenditure. We find ourselves unable to accede to this contention because we find that the arrangement between the respondent and M/s H.V.Lowe & Co.Ltd., not for any fixed term but could be terminated at any time at the volition of any of the parties. Although an enduring benefit need not be of an everlasting character, it should not, at the same time, be so transitory and ephemeral that it can be terminated at any time at the volition of any of the parties. Any other view would have the effect of rendering the word enduring to be meaningless. No cogent ground or valid reason has been given to us in support of the contention that,

even though the benefit from the arrangement to the respondent may not be of a permanent or enduring nature, the payments made in pursuance of that arrangement would still be capital expenditure.....”.

In **Eicher Limited**² the Delhi High Court, after referring to several judgments, including the judgment of the Supreme Court in **Coal Shipments Private Limited**¹, held that the assessee could not be said to have acquired any capital asset by making payment of a non-competing fee; it merely eliminated competition in its business for a while; from the record it was not clear how long the restrictive covenant was to last, but it was neither permanent nor ephemeral; in that sense, the advantage was not of an enduring nature; and, on a cumulative appreciation of the facts, it must be held that the CIT (A) and the Tribunal did not err in concluding that payment of non-compete fee by the assessee was a business expenditure, and not a capital expenditure.

The Tribunal held that the assessee did not acquire any capital asset by making payment of the non-competition fee; it merely eliminated competition for a while, for which it had paid the amount; and, on a cumulative appreciation of the facts, they were of the opinion that the Commissioner of Income Tax (Appeals) was justified in allowing the appeal. The order of the Commissioner was confirmed, and the appeal of the Revenue was dismissed.

Sri J.V.Prasad, learned Senior Standing Counsel for the Income Tax Department, would draw attention of this Court to the findings recorded by the assessing authority in support of his submission that a non-competition fee could not be treated as a revenue expenditure, and no deduction could be claimed of such expenditure in the profit and loss account of the assessee.

The non-competition agreement entered into by the assessee

with M/s KHPL was to prevent K.Raghu Ramakrishna Raju from establishing a power plant in Andhra Pradesh for a period of three years. As has been held by the Commissioner of Income Tax (Appeals), the fact that the amount was paid, and a non-competition agreement was entered into, is not in dispute. The law declared by the aforesaid judgment of the Supreme Court, and the Delhi High Court, is that it is only if the non-competition agreement is of a permanent or an enduring nature can it be said to be a capital expenditure. The agreement, in the present case, prevented Sri K.Raghu Ramakrishna Raju from establishing a power plant only for a period of three years from the date of the agreement. The restrictive covenant was neither permanent nor was the advantage derived by the assessee therefrom of an enduring nature. The Tribunal was, therefore, justified in holding that the assessee did not acquire any capital asset by making payment of a non-competition fee; and it merely eliminated competition in its business for a while.

The Tribunal is the final Court of fact. As an appeal, under Section 260-A of the Act, can be entertained only on a substantial question of law, this Court would not re-appreciate the findings recorded either by the Tribunal or the Commissioner of Income Tax (Appeals). Save findings based on no evidence, or a perverse finding, no interference is called for in proceedings under Section 260-A of the Act. Neither the order of the Tribunal, nor that of the Commissioner of Income Tax (Appeals), suffer from any such patent error necessitating interference in appeal under Section 260-A of the Act.

The appeal fails and is, accordingly, dismissed. Miscellaneous petitions pending, if any, shall also stand dismissed. There shall be no order as to costs.

RAMESH RANGANATHAN, J

03rd November, 2015.
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[\[1\]](#) 82 ITR 902
[\[2\]](#) 302 ITR 249