

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

I.T.T.A.No.458 of 2015

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

This appeal, under Section 260-A of the Income Tax Act, 1961 (for short "the Act"), is preferred against the order passed by the Commissioner of Income Tax (Appeals) dated 23.09.2008 setting aside the order passed by the Assessing Authority for the assessment year 2002-03.

The respondent herein was earlier known as "M/s.Kanumuri Holdings Pvt. Ltd. (KHPL)", and was carrying on the business of setting up and running power projects. Along with M/s.Andhra Fuels Pvt. Ltd. (AFPL), the respondent formed two companies viz., M/s.Arkay Energy Ltd. for the purpose of setting up power projects in Tamil Nadu, and M/s. RVK Energy Pvt. Ltd. for setting up power plants in Andhra Pradesh. By way of an agreement dated 28.12.2001, M/s.Andhra Fuels Pvt. Ltd. withdrew their investment from M/s.Arkay Energy Ltd. in favour of the respondent. The respondent, in turn, agreed not to set up any power project directly or indirectly in the State of Andhra Pradesh for a period of 3 years. In view of the non-competition covenant, the respondent was paid compensation of Rs.3.25 crores which was credited by them to their capital reserve account. They claimed this receipt as capital receipt, and as not liable to tax under the Act. The Assessing Authority, however, treated the said receipt as a revenue receipt and observed that it was a sham transaction and a colourable device adopted just to claim that it was a capital receipt.

In appeal the Commissioner of Income Tax (Appeals) held that payment was made to the respondent to ward off competition in business; 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 suppliers, funding agencies and other business

associates; the amount was paid also to stop him from creating any legal problems; and, therefore, the said payment was made in order to enable the other party to derive more profits in the business without any hindrance from the parting director and his group companies.

In the order under appeal before us, the Tribunal relied on its earlier order in the case of **ACIT vs. Late Dr.B.V.Raju**, and on the judgment of the Supreme Court in **Guffic Chem. P. Ltd. vs. Commissioner of Income Tax**^[1]. In **Guffic Chem. P. Ltd.**¹, the Supreme Court held that payment received as non-competition fee under a negative covenant was always treated as a capita receipt till the assessment year 2003-04; it is only vide the Finance Act, 2002, with effect from April 2003, that receipt by way of a non-compete fee was made taxable under Section 28(va) of the Act; and a liability cannot be created retrospectively.

The assessment year in question in this appeal is 2002-03, and is prior to the assessment year 2003-04. As a result, the law declared by the Supreme Court, in **Guffic Chem. P. Ltd.**¹, would apply; and the payment received by the respondent, as non-competition fee under a negative covenant, must be treated as a capital receipt. The order of the Tribunal does not, therefore, necessitate interference.

Sri J.V.Prasad, learned Senior Standing Counsel for the Income Tax Department, would, however, draw attention of this Court to the question of law framed by the Commissioner that, even if the said amount is treated as a taxable receipt and is held not chargeable to tax as revenue income in the subject assessment year, the said amount is liable to be subjected to tax as capital gains in terms of Section 28(va) of the Act read with the definition of “capital asset” under Section 2(14) of the Act, and the definition of “transfer” under Section 2(47) of the Act.

As this question was not even raised before the Tribunal, it would be wholly inappropriate for us, in proceedings under Section 260-A of the Act, to undertake the exercise of ascertaining whether the

capital receipt, of a non-competition fee, can be subjected to tax under the head “capital gains”, and whether payment of the said amount to the respondent amounts to transfer of a capital asset or not. Suffice it to observe that while no interference is called for in this regard, as it was not even raised before the Tribunal, this question is left open for examination in an appropriate case.

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

RAMESH RANGANATHAN, J

M. SATYANARAYANA MURTHY, J

Date: 16.02.2016
JSU

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