

IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATE: 31.03.2021

CORAM:

THE HON'BLE MR. JUSTICE M.DURAI SWAMY  
AND  
THE HON'BLE MRS.JUSTICE T.V.THAMILSELVI

T.C.A.No.288 of 2013

The Commissioner of Income Tax - IV  
121, N.H. Road, Chennai - 600 034. ... Appellant

Vs.

M.Ranjan Rao ... Respondent

Appeal preferred under Section 260A of the Income Tax Act, 1961, against the order of the Income Tax Appellate Tribunal, Madras, "B" Bench, dated 31.10.2012 in I.T.A.No.1582/Mds/2012 for the assessment year 2002-03.

against order of the Commissioner of Income Tax(Appeals), Chennai -34, dated 23/05/2012 made in ITA.No.93/11-12 Assessment year 2002-03

as against order of the Commissioner of Income Tax(Appeals)-VI, Chennai -34, dated 31/03/2008 made in ITA.No.136/07-08 in Assessment year 2002-03.

For Appellant : Mr.M.Swaminathan,  
Senior Standing Counsel  
assisted by  
Ms.V.Pushpa,  
Standing Counsel

For Respondent : Mr.M.Kaushik  
for Mr.S.Sridhar

JUDGMENT

(Judgment was delivered by M.DURAI SWAMY, J.)

Challenging the order passed in I.T.A.No.1582/Mds/2012 in respect of the assessment year 2002-03 on the file of the Income Tax Appellate Tribunal, Chennai, "B" Bench, the Revenue has filed the above appeal.

2.The above appeal was admitted on the following substantial questions of law:

"1)Whether on the facts and in the circumstances of the case, the Appellate Tribunal was right in

allowing compensation received for refraining from carrying on competitive business was a capital receipt and not taxable during the assessment year 2002-03?

2) Whether on the facts and in the circumstances of the case, the Appellate Tribunal was right in dismissing the Department Appeal observing that the Finance Act, 2002 brought to tax the capital receipts under Section 28 (va) with effect from 01.04.2003?

3) Whether on the facts and in the circumstances of the case, the Appellate Tribunal was right in following the decision of the Apex Court in the case of M/s. Guffic Chem reported in 332 ITR 602 which is not applicable to the facts of the present case, as a nomenclature of the receipt itself is disputed as to whether it was a non-compete fees?"

3. When the appeal is taken up for hearing, Mr. M. Swaminathan, learned senior standing counsel appearing for the appellant - Revenue fairly submitted that the questions of law involved in the present appeal is covered by the decision of the Division Bench of this Court in 385 ITR 326 (Madras) [*Commissioner of Income Tax, Chennai Vs. TTK Healthcare Ltd.*] wherein the Hon'ble Division Bench held against the Revenue and in favour of the assessee, as follows:

"...

6. The question, therefore, that requires to be answered is whether this receipt of money by the assessee is liable to be treated as a capital receipt or revenue receipt. It is not in doubt that, for the relevant assessment year, if the income is to be treated as capital receipt, it cannot suffer the incidence of taxation, whereas, if it were to be treated as a revenue receipt, the order of assessment as affirmed by the CIT(A) has to be upheld.

7. It will be appropriate to notice as to how this very question has been answered by the Supreme Court in *Oberoil Hotel (P) Ltd vs. CIT* [1999] 236 ITR 903/103 Taxman 236 Paragraphs 3 to 7 of the judgment read as under:

"3. The question whether the receipt is capital or revenue is to be determined by drawing the conclusion of law ultimately from the facts of the particular case and it is not possible to lay down any single test as infallible or any single criterion as decisive. This Court in the case of *Karam Chand Thapar & Bros. P. Ltd. v. Commissioner of Income Tax* (Central, Calcutta: [1971] 80 ITR 167 (SC) discussed and held that in *Commissioner of Income Tax v. Chari and Chari Ltd* : [1965] 57 ITR

400 (SC), it was held that ordinarily compensation for loss of an office or agency is regarded as capital receipt, but this rule is subject to an exception that payment received even for termination of agency agreement would be revenue and not capital in the case where the agency was one of many which the assessee held and its termination did not impair the profit making structure of the assessee, but was within the framework of the business, it being a necessary incident of the business that existing agencies may be terminated and fresh agencies may be taken. Thereafter the Court held that it was difficult to lay down a precise principle of universal application but various workable rules have been evolved for guidance.

4. Applying the aforesaid test laid down by this Court in the present case, in our view the Tribunal was right in arriving at a conclusion that it was a capital receipt. Reason is that as provided in Article XVIII of the First Agreement assessee was having an option or right or lien, if owner desired to transfer the hotel or lease or part of the hotel to any other person, the same was required to be offered first to the assessee (operator) or its nominee. This right to exercise its option was given up by a Supplementary Agreement which was executed in September, 1975 between the Receiver and assessee. It was agreed that Receiver would be at liberty to sell or otherwise dispose of the said property at such price and on such terms as he may deem fit and was not under any obligation requiring the purchaser thereof to enter into any agreement with the operator (assessee) for the purpose of operating and managing the hotel or otherwise and in its return, agreed consideration was as stated above in Clause X. On the basis of the said agreement the assessee has received the amount in question. The amount was received because the assessee had given up its right to purchase and or to operate the property. Further it is loss of source of income to the assessee and that right is determined for consideration. Obviously therefore, it is a capital receipt and not a revenue receipt.

5. Learned Counsel for the Revenue relied upon the decision in the case of *Commissioner of Income Tax v. Rai Bahadur Jairam Valji and Ors.* : [1959] 35 ITR 148 (SC) and submitted that assessee had the business of running the hotels in various countries and the amount which is received by him is for the

"Whether a payment of compensation or termination of an agency is a capital or revenue receipt, it would have to be considered whether the agency was in the nature of capital asset in the hands of the assessee, or whether it was only part of his stock-in-trade."

"Whether a particular receipt is capital or income from business, has frequently engaged the attention of the courts. It may be broadly stated that what is received for loss of capital is a capital receipt; what is received as profit in a trading transaction is taxable income. But the difficulty arises in ascertaining whether what is received in a given case is compensation for loss of a source of income, or profit in a trading transaction."

"These cases illustrate the principle that compensation for injury to trading operations, arising from breach of contract or in consequence of exercise of sovereign rights, is revenue. These cases must, however, be distinguished from another class of cases where compensation is paid as a solatium for loss of office. Such compensation may be regarded as capital or revenue; it would be regarded as capital, if it is for loss of an asset of enduring value to the assessee, but not where payment is received in settlement of loss in a trading transaction."

"Where on a consideration of the circumstances, payment is made to compensate a person for

cancellation of a contract which does not affect the trading structure of his business, nor deprive him of what in substance is his source of income, termination of the contract being a normal incident of the business, and such cancellation leave him free to carry on his trade (freed from the contract terminated) the receipt is revenue : Where by the cancellation of an agency the trading structure of the assessee is impaired, or such cancellation results in loss of what may be regarded as the source of the assessee's income, the payment made to compensate for cancellation of the agency agreement is normally a capital receipt."

7. The aforesaid principle is relied upon in the case of *Karam Chand Thapar and Bros's case* (supra). Considering the aforesaid principles laid down as per Article XVIII of the Principal Agreement, the amount received by the assessee is for the consideration for giving up his right to purchase and or to operate the property or for getting it on lease before it is transferred or let out to other persons. It is not for settlement of rights under trading contract, but the injury is inflicted on the capital asset of the assessee and giving up the contractual right on the basis of Principal Agreement has resulted in loss of source of assessee's income."

8. Thus, starting from *CIT Vs. Rai Bahadur Jairam Valji's*, [1959] 35 ITR 148 (SC) case, *Kettlewell Bullen & Co Ltd Vs. CIT* [1964] 53 ITR 261 (SC) case, *Karam Chand Thapar & Bros (P.) Ltd. Vs. CIT* [1971] 80 ITR 167 (SC) case, the underlying principle spelt-out was to ascertain from the facts and circumstances of the case as to whether the injury is inflicted on the capital asset of the assessee resulting in loss of a source of assessee's income or not. The Supreme Court in *Gillanders Arbuthnot & Co. Ltd vs. CIT* [1964] 53 ITR 283 has brought out a dichotomy between receipt of compensation by an assessee for loss of agency and receipt of compensation attributable to the negative/restrictive covenant. If the compensation is received for the loss of agency, it is to be treated as a revenue receipt whereas, if the compensation is attributable to a negative/ restrictive covenant, then, it would amount to a capital receipt. The Supreme Court in *Guffic Chem (P.) Ltd. Vs. CIT* [2011] 332 ITR 602/198 Taxman 78/10 taxmann.com 105 examined this very question and in its paragraph 7 held that compensation received for refraining from carrying on competitive

business was a capital receipt and that payment received as non-competitive fee under a negative contract was always treated as a capital receipt till the assessment year 2003-2004, i.e. till the introduction of Section 28 (va) by way of an amendment to the Act with effect from 01.04.2003."

4.Mr.M.Kaushik, learned counsel appearing for the respondent - assessee submitted that in view of the judgment of the Hon'ble Division Bench of this Court made in 385 ITR 326 (Madras) [Commissioner of Income Tax, Chennai Vs. TTK Healthcare Ltd.], cited supra, the appeal may be dismissed.

5.In view of the submission made by the learned counsel on either side, since the substantial questions of law that are raised in the present appeal are covered by the decision of the Hon'ble Division Bench of this Court 385 ITR 326 (Madras) [Commissioner of Income Tax, Chennai Vs. TTK Healthcare Ltd.], cited supra, we decide the substantial questions of law raised in the present appeal against the Revenue and in favour of the assessee. The appeal is liable to be dismissed. Accordingly, the Tax Case Appeal is dismissed. No costs.

Sd/-

Assistant Registrar(CS VII)

//True Copy//

Sub Assistant Registrar

To

- 1.The Income Tax Appellate Tribunal, Chennai, "B" Bench.
- 2.The Commissioner of Income Tax(Appeals), Chennai -34.
- 3.The Commissioner of Income Tax(Appeals)-VI, Chennai -34.

+1cc to Mr.M.Swaminathan, Advocate SR.NO..21064

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