IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED : 11.01.2022

CORAM :

THE HONOURABLE MR. JUSTICE R. MAHADEVAN
and
THE HONOURABLE MR. JUSTICE MOHAMMED SHAFFIQ

Tax Case Appeal No.600 of 2010
and
MP. No.1 of 2010

The Commissioner of Income Tax,
Chennai. ...Appellant/Appellant

Versus

M/s. Pentasoft Technologies Ltd.,
25, I Main Road, United India Colony,
Chennai - 600 024.
PAN AAACP1895R
...Respondent/Respondent

Appeal preferred under Section 260A of the Income Tax Act, 1961, against the order of the Income Tax Appellate Tribunal, “B” Bench, Chennai, dated 14.03.2008 in I.TA.No.690/Mds/2007, against the order of the Commissioner of Income Tax (Appeals)-VI, Chennai-600 034, dated 30.11.2006 made in ITA No.330/2004-2005 and against the order of the Deputy Commissioner of Income Tax, Central Circle-III (4), Chennai-34 made in PAN/GIR No.AAACP1895R/34104p for the Assessment year 2001-02.

For Appellant : Mr.T.Ravikumar
Senior Standing Counsel

For Respondent : Mr.N.Muthukumar

J U D G M E N T
(Judgment of the Court was delivered by R.MAHADEVAN, J.)

This tax case appeal has been filed by the appellant/Revenue, challenging the order dated 14.03.2008 passed by the Income Tax Appellate Tribunal, 'B' Bench, Chennai, in I.T.A.No.690/Mds/2007, relating to the assessment year 2001-02.

2.By order dated 19.07.2010, this court admitted the aforesaid tax case appeal on the following substantial questions of law:

"1. Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in law in holding that the expenditure on Software Technology Park and Non-Software Technology Park, on the basis of gross Profit and not on the basis of turn over is valid in law?

2. Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in law in holding that Intellectual Property rights and Non-Compete fee are intangible assets are entitled to depreciation under Section 32(1)(ii) of the Income Tax Act 1961 is valid?"

3.Today, when the appeal is taken up for consideration, the learned counsel for the appellant/Revenue as well as respondent/assessee jointly submitted that the first question of law raised in this appeal has already been considered and decided by this Court in favour of the Assessee in the case of Commissioner of Income Tax Vs. Pentasoft Technologies Ltd. [TCA.Nos.72 & 73 of 2009, dated 22.10.2013], the relevant passage of which, is usefully extracted hereunder:

"14. As far as allocable expenditure is concerned, the Tribunal found that the Department had not questioned the accounts maintained for the two units, hence, the question of finding fault with the Commissioner's order directing the allocation of expenditure based on profit could not be found fault with.

15. We agree with the Tribunal's view in this regard. Even though the Revenue has come on appeal as against this aspect, we find that when admittedly, the Department had not questioned the correctness of the accounts mentioned separately for the STP and Non-STP units showing the allocable expenditure between the 10A Unit and non-exempt unit, and that only in respect of the few expenditure, the identification of the expenditure posed difficulty, the logical way of finding the allocable expenditure would be only on the profit earned by the respective units. Even though, learned Standing Counsel appearing for the Revenue submitted that key to find out allocable expenditure would be only on the basis of the units turnover, we do not accept this contention on the simple premise and on the admitted fact that the department had not questioned the accounts of the assessee and the only issue projected by the Revenue is that working of the allocable expenditure based on profit would result in distorted picture. The reasoning of the officer is that the expenditure in STP Unit normally should have been more than

the non-STP unit considering the nature or export related activity that the assessee had to undertake and total expenditure claimed in the non-STP unit was 97.23% against the receipts, whereas in the STP unit it worked out to 82.42%. Doubting this alone, the officer adopted a formula to be based on the turnover. The view of the officer is based on conjectures and surmises only and is not based on any materials. We reject this line of reasoning as a matter of mere opinion and mere surmises not backed up by any reason or material.

16. We may point out that the revenue does not dispute the fact that the major portion of the expenditure incurred by both the units are detectable from the accounts maintained. Only in respect of such of those issues where the expenditure could not be deducted the commissioner upheld the contention of the assessee. Revenue has not placed any material to show how this working would distort the allocable expenditure on the STP unit.

17. In these circumstances, the Tribunal had rightly uphold the order of the Commissioner of Income Tax (Appeals) on the reasons given by the Commissioner."

4.In addition, the learned counsel for the appellant / Revenue fairly submitted that the second substantial question of law raised in this appeal has already been considered and decided by this Court in favour of the Assessee in the case of Pentasoft Technologies Ltd. Vs. Deputy Commissioner of Income Tax [TCA.No.1195 of 2008, dated 29.10.2013], the relevant passage of which, is usefully extracted hereunder:

"19. The only issue is whether non compete agreement/arrangement would fall within the ambit of clause (ii) of Section 32(1) of the Act.

20. It is the case of the Revenue that this non-compete fee is in the nature of a negative right and it cannot be of a commercial right of similar nature and the expression 'similar nature' shall be relatable to patents, copy rights and trade mark licence or franchise or any other business. Therefore, it is submitted that this negative right cannot be construed either as a licence or as a commercial right to be eligible for deduction.

21. We are unable to agree with the stand taken by the Revenue for the simple reason that the agreement between the parties is a composite agreement. Under the agreement, the transferor had transferred all its rights, copy rights, trade marks in respect of the word 'pentasoft' as well as the training and development division exclusively to be exploited by the assessee. In order to strengthen those rights transfer under the said composite agreement, there was a non compete clause by virtue of which, the transferor was restrained from using the same trade mark, copyrights etc., in favour of the assessee. Therefore, the non compete clause under the agreement should be read as a supporting clause to the transferor of the copy rights and patents rather to strengthen the commercial right, which was transferred in favour of the assessee.

22. Learned counsel for the assessee contended that the non-compete is in effect an indirect licence. However, we are not inclined to agree with the said submission since non compete, at best could be a commercial right because that right is relatable to the transfer of trade mark, copy rights and patents. Therefore, the view taken by the Commissioner of Income Tax (Appeals) in this regard is acceptable."

"28. In the case of hand, we have analysed the agreement and also in the previous portion of this order elaborated upon the various terms and conditions, which bind the parties had observed that the earlier transfer of the trade mark, patents and other rights in favour of the assessee was undoubtedly the transfer of intangible assets, which in terms of section 32 (1)(ii) of the Act would be a capital asset entitled to depreciation.

29. In the light of the above, we have no hesitation in setting aside the order passed by the Income Tax Appellate Tribunal and answer the issue in favour of the assessee. In such circumstances, there is no necessity for us to consider the alternative submission made by the learned counsel for the assessee.

30. In the result, the Tax Case(Appeal) is allowed. However, there shall be no order as to costs."

5.Following the aforesaid judgments, which are squarely applicable to the facts of the present case, the substantial questions of law are answered in favour of the Assessee and against the Revenue. Accordingly, the Tax Case Appeal stands dismissed. No costs. Consequently, connected miscellaneous petition is closed.

Sd/-

Assistant Registrar

//True Copy//

Sub Assistant Registrar

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To

1.The Income Tax Appellate Tribunal,
'B' Bench Chennai,

2.The Commissioner of Income - Tax,
Chennai.

3.The Commissioner of Income Tax (Appeals)-VI,
Chennai-34.

4.The Deputy Commissioner of Income Tax,
Central Circle-III (4), Chennai-34.

+1cc to Mr.T.Ravikumar, Advocate SR. No.2616
+1cc to Mr.G.Baskar, Advocate SR. No.2423

T.C.A.No.600 of 2010

NMI (CO)
PR (18/02/2022)