

आयकर अपीलीय अधिकरण 'सी' न्यायपीठ चेन्नई में।
IN THE INCOME TAX APPELLATE TRIBUNAL
"C" BENCH, CHENNAI

माननीय श्री महावीर सिंह, उपाध्यक्ष एवं
माननीय श्री मनोज कुमार अग्रवाल, लेखक सदस्य के समक्ष।
BEFORE HON'BLE SHRI MAHAVIR SINGH, VICE PRESIDENT AND
HON'BLE SHRI MANOJ KUMAR AGGARWAL, AM

आयकर अपील सं./ITA No. 2247/Chny/2016
(निर्धारण वर्ष / Assessment Year: 2000-01)

Late Shri. T.T. Vasu Rep. By L/R. Shri Arun Vasu, #6, Cathedral Road, Chennai – 600 086.	बनाम/ Vs.	ACIT Company Circle –III (2), Chennai- 600 034.
स्थायी लेखा सं./जी आइ आर सं./PAN/GIR No. AAHPV-2508-D		
(पीलार्थी/ Appellant)	:	(प्रत्यर्थी / Respondent)

अपीलार्थी की ओर से/ Appellant by	:	Shri Philip George (Advocate) – Ld. AR
प्रत्यर्थी की ओर से/ Respondent by	:	Ms. R. Halen Ruby Jesintha (Addl. CIT) –Ld. DR

सुनवाई की तारीख/ Date of Hearing	:	16-02-2022
घोषणा की तारीख / Date of Pronouncement	:	21-03-2022

आदेश / ORDER

Manoj Kumar Aggarwal (Accountant Member)

1. Aforesaid appeal by assessee for Assessment Year (AY) 2000-01 arises out of the order of learned Commissioner of Income Tax (Appeals)-11, Chennai [CIT(A)] dated 22-04-2016 in the matter of assessment framed by Ld. Assessing Officer [AO] u/s. 143(3) r.w.s. 147 of the Act on 14-02-2005. Though the assessee has raised multiple

grounds of appeal, however, the grounds urged before us are ground Nos.3 & 4. The ground No.3 read as under: -

3. non-Compete fees

3.1. The Commissioner of Income Tax (Appeals) erred in holding that Non-Compete Fee has to be assessed as revenue receipt and thereby upholding the action of the Assistant Commissioner of Income Tax in bringing to tax the non-compete fees received amounting to Rs.1,15,00,000/-.

3.2. The Commissioner of Income Tax (Appeals) ought to have appreciated that during the relevant period, the Non-Compete Fee was totally exempt.

3.3. The Commissioner of Income Tax (Appeals) erred in holding that the Non-Compete Fee received was only a compensation for loss of business profit in the next three years and it was only a colorable device to avoid Capital Gains Tax, merely on suspicion and surmises.

3.4. The Commissioner of Income Tax (Appeals) grossly erred in holding that valuation of other divisions are pegged up while structuring the transaction in such a way that those non-foreign exchange divisions are transferred to some non-extant shareholder as well, merely due to non-availability of valuation report of foreign exchange division.

3.5. The Commissioner of Income Tax (Appeals) ought to have deleted the addition made as the receipt was a capital receipt not liable to tax.

This is second round of appeal, since the appeal was restored back to the file of Ld. CIT(A) by Tribunal vide ITA No.1114/Mds/2006 order dated 17/10/2007 with a direction to Ld. CIT(A) to pass speaking order and decide the issue afresh on merits.

2. In ground No.4, the assessee is aggrieved by confirmation of addition of Rs.96,595/- as deemed dividend u/s 2(22)(e). The Ld. AR submitted that this addition was made on protective basis whereas substantive addition was made in the case of Shri Arun Vasu. In case of Shri Arun Vasu, the matter has already been settled under *Direct Tax Vivad Se Vishwas Scheme* and Form No.5 has been issued by the department in favor of Shri Arun Vasu. The copy of Form No.5 has been placed on record. Therefore, we direct Ld. AO to verify the same and if found correct, delete the protective addition as made in the hands of the assessee. This ground stand allowed for statistical purposes.

3. With respect to ground No.3, Ld. AR submitted that non-compete fees was brought to tax only by way of amendment to Sec.28(va) w.e.f. 01/04/2003 and therefore, the receipts would be capital receipts not chargeable to tax. The Ld. AR relied on the decision of Hon'ble Supreme Court in the case of **Guffic Chem (P) Ltd V/s CIT (332 ITR 602)** wherein it was held that prior to 01.04.2003, payment received as non-competition fee under a negative covenant was a capital receipt, not taxable under the Act. The Ld. DR, on the other hand, defended the orders of lower authorities and submitted that the non-complete fees as received by the assessee was for loss of profits for 3 years and therefore, the same has rightly been held to be revenue receipt.

4. Having heard rival submissions and after due consideration of material on record, our adjudication would be as under.

Proceedings before lower authorities

5.1 The material facts as noted in the impugned order are that the assessee along with Shri Arun Vasu and Shri P. Varadan was the promoter of an entity i.e., M/s T.T.Travels (P.) Ltd. (TTTL). This entity carried on the business of foreign exchange, cargo services and tours etc. M/s TTTL entered into an agreement with another entity i.e., M/s TATA Finance Amex Ltd. (TFAL) for transfer of foreign exchange division at agreed consideration of Rs.352.72 Lacs which was exclusive of non-complete fees. Pursuant to transfer agreement, the three promoters entered into non-compete agreement with M/s TTTL as well as with M/s TFAL under which they were paid certain amount. The assessee received amount of Rs.69 Lacs from M/s TFAL and another Rs.46 Lacs from M/s TTTL and the taxability of the same form the subject matter of dispute before us. As per the terms of the agreement,

the promoters agreed not to carry on the business of foreign exchange for three years. The transfer agreement was executed through share transfer agreement dated 25.12.1999. On the same day, three non-complete agreements were entered into by the three promoters with M/s TTTL. As per the terms, the three promoters were paid non-compete fees to stop them from carrying on fresh business in foreign exchange. The assessee was paid Rs.46 Lacs under this agreement. Three similar non-complete agreements were entered into by the promoters with M/s TFAL. The assessee was paid Rs.69 Lacs under this agreement. Both these amounts were claimed to be exempt on the ground that it was capital receipt.

5.2 During the course of assessment proceedings, It was stated that the assessee was restrained from doing foreign exchange business for a period of 36 months from the date of agreement. However, Ld. AO opined that the fees were nothing but compensation for loss of business profits for the next three years and thus, the same would be taxable as business income. The same would also be taxable u/s 10(3) also since the receipts were casual and non-recurring in nature. Reliance was placed on the decision of Hon'ble Supreme Court in the case of **Ramkumar Agarwal & Bros. (63 ITR 622)** as well as the decision of Hon'ble High Court of Madras in **Mineral Mining Co. Pvt. Ltd. (194 ITR 258)** wherein similar issue was held in department's favor. The Ld. AO also noted that such receipts were brought to tax by introduction of Sec.28(va) w.e.f. 01.04.2003. Therefore, the amount was held to be taxable income and added to the income of the assessee. In the alternative, if the amount was not taxable as revenue receipt, then it should be treated as part of sale consideration for the purpose of capital

gains as these agreements appear to be colorable device to reduce the tax liability on capital gains due to the sale of the above company.

5.3 Pursuant to the set-aside directions of Tribunal, the matter was re-adjudicated by Ld. CIT(A) in impugned order dated 22.04.2016. The assessee distinguished both the case laws as relied upon by Ld. AO and submitted that the assessee was restrained from carrying on the business of foreign exchange whereas there was no such restriction in the cited case laws. The assessee relied upon the decision of Hon'ble Supreme Court in the case of **CIT V/s Guffic Chem. P. Ltd. V/s CIT (332 ITR 602)** wherein it was held that such receipts were capital receipts. Reliance was also placed on the decision of Hon'ble High Court of Madras in **CIT V/s T.I.& M Sales Ltd. (259 ITR 116)** wherein similar payment were held to be compensation for impairment of the profit-making apparatus of the assessee and for the sterilization of the very source of income. Similar was stated to the decision of Hon'ble Court in **CIT V/s Ambadi Enterprises Ltd. (267 ITR 702)**. The assessee thus submitted that the amount were capital receipts and not taxable. The provisions of Sec. 28(va) were incorporated w.e.f. 01.04.2003 and therefore, the same would not be applicable to earlier years. The provision of Sec. 10(3) would also not be applicable since the receipts were pursuant to the written agreements and could not be termed as casual or non-recurring in nature.

5.4 However, Ld. CIT(A) opined that the way in which the transaction was structured would reveal assessee's intention to circumvent the tax laws. The same would be clearly evident from the fact that the assessee received non-compete fees from the old company as well as from the acquirer company with a view to reduce the overall tax liability by

reducing the sale considerations. When the corporate veil is pierced, it is in fact paid by the same set of acquirers to same set of shareholders. Further, TFAL being top player need not pay non-complete fees to small promoters to ward-off competition. Even if they have to be paid, they could have been paid to the erstwhile company which in turn could have passed it on to them. Had that been done, the sale consideration would have been more. The forex division was not highly personalized business which involves complex interplay between the parties involved. Therefore, the amount was nothing but a compensation for the three years' profits which is on revenue front. The ratio of decision of Hon'ble Apex Court in **Gillanders Arbuthnot & Co. Ltd. V/s CIT (53 ITR 283)** would apply which held that where trading structure was not disturbed then the compensation would be revenue receipt. Since the assessee was refrained from carrying on the foreign exchange division for 3 years, the fees were revenue in nature and hence, taxable in his hand. Had the fees been embedded in the share price according to the share transfer agreement, the entire consideration would be chargeable to capital gains. This would further be fortified by the facts that the assessee did not produce the basis for valuation of company's share and the non-compete fees along with a valuation report. Therefore, the transaction was held to be colorable device to avoid capital gains. Accordingly, the addition was confirmed. Aggrieved, the assessee is in further appeal before us.

Our findings and Adjudication

6. Upon careful consideration of factual matrix, it could be gathered that forex division of M/s TTTL was acquired by M/s TFAL vide Share Transfer Agreement dated 25.12.1999 for certain consideration. As per

the recitals of the agreement, the three promoters of M/s TTTL had developed foreign exchange division into a full-fledged money changing business with a branch network throughout the county and the same, presently, enjoys a high reputation in the field. The promoter agreed to sell their own holding of 85.5% as well as 14.5% holding of other shareholders to M/s TFAL against aggregate consideration of Rs.352.75 Lacs. On the same day, M/s TFAL entered into non-compete agreement with the assessee promoter wherein the assessee has assured M/s TFAL not to start a fresh business or take over and / or in any manner whatsoever participate in an existing business in the field of foreign exchange and / or money changing for a period of 36 months. Against such assurance, the assessee was to be paid a sum of Rs.69 Lacs. Thus, this agreement, in essence, put negative covenant on the assessee not to compete in similar line of business for a period of 36 months. Another similar agreement has been executed between M/s TTTL with the assessee wherein similar assurance has flown from assessee to M/s TTTL against consideration of Rs.46 Lacs. Upon perusal of both these agreements, it could be seen that these are in the nature of non-compete agreement debarring the promoters not to compete in similar line of business for a period of 36 months. Under these agreements, the assessee was put to negative covenant not to carry on the competing business for a period of 36 months and therefore, it was case wherethe profit-making apparatus of the assessee got extinguished. In such a case, the decision of Hon'ble Supreme Court in the case of **Guffic Chem (P) Ltd V/s CIT (332 ITR 602)** would become applicable wherein Hon'ble Apex Court observed that the position in law is clear and well-settled. There is a dichotomy between the receipt of

compensation by an assessee for the loss of agency and receipt of compensation attributable to the negative/restrictive covenant. The compensation received for the loss of agency is a revenue receipt whereas the compensation attributable to a negative/restrictive covenant is a capital receipt. It was further held that the payment received as non-competition fee under a negative covenant was always treated as a capital receipt till the assessment year 2003-04. It was w.e.f. 01.04.2003 that the said capital receipts have been made taxable u/s 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 Act. It became taxable only with effect from 01.04.2003. It is well-settled proposition that a liability cannot be created retrospectively. In the instant case, compensation received under non-competition agreement became taxable as a capital receipt by specific legislative mandate vide section 28(va) and that too with effect from 01.04.2003. Hence, the said section 28(va) is amendatory and not clarificatory. Finally, the receipts were held to be capital receipt not chargeable to tax. This case law has been rendered after considering the decision of **Gillanders Arbuthnot & Co. Ltd. V/s CIT (53 ITR 283)** which has been relied upon by Ld. CIT(A) while adjudicating the appeal of the assessee. The Hon'ble Court has already distinguished this case law in this judgement. We find that similar is the decision of Hon'ble High Court of Madras in **CIT V/s T.I. & M Sales Ltd. (259 ITR 116)** wherein similar payment were held to be compensation for impairment of the profit-making apparatus of the assessee and for the sterilization of the very source of income and therefore, the receipts were held to be capital receipts not chargeable to

tax. Similar is the decision of Hon'ble Court in **CIT V/s Ambadi Enterprises Ltd. (267 ITR 702)** as well as in **CIT V/s Spencers & Co. Ltd. (359 ITR 612)**.

7. The revenue has relied on the decision of Hon'ble High Court of Madras in **Indo Tech Electric Co. V/s DCIT (196 Taxman 514)**. Upon study of this case law, we find the same to be factually distinguishable. In that case, a partnership firm consisting of a father and son was taken over by a limited company. The partners of the firm were the new directors of the company. The Company paid certain sum to the firm on account of transfer of technical know-how and compensation for pending orders and expected orders under negotiation i.e., not to compete and indulge in the business. These receipts were claimed to be exempt from tax. However, Hon'ble Court noted that the consideration was paid to the assessee firm and not to the partners. There was no competition as alleged between the firm and new private limited company and there was also no contract between the partners of the assessee firm and new private limited company. Therefore, the receipts were held to be taxable. Clearly, the factual matrix is different from the factual matrix of the present case before us.

8. Lastly, the allegations of Ld. CIT(A) that the transaction was structured to circumvent the tax laws are bereft of any concrete material on record. The payments for transfer of business as well as non-compete fees are well evidenced by duly executed agreements and the terms of the agreements have been acted upon by all the parties. The allegation that the same set of acquirer has made payment to same set of promoters is also ill-founded in view of the fact that the promoters was having share of 85.5% in the transferred entity whereas the remaining

shares were held by other shareholders. The observation that there was no need to pay such a separate compensation would stand negated by the argument that it was none of revenue's business to sit on arm chair of the businessmen and to guide as to how the transactions were to be executed unless facts showing mala-fide intentions to evade the taxes were brought in record. No such fact based findings have been rendered in the impugned order and the observations are nothing but mere allegations. Therefore, these cannot be upheld.

9. In view of the foregoing, the impugned addition stand deleted since the same are capital receipts not chargeable to tax. The Ld. AO is directed to recompute the assessee's income.

10. The appeal stands partly allowed in terms of our above order.

Order pronounced on 21st March, 2022.

Sd/-
(MAHAVIR SINGH)
उपाध्यक्ष / VICE PRESIDENT

Sd/-
(MANOJ KUMAR AGGARWAL)
लेखासदस्य / ACCOUNTANT MEMBER

चेन्नई/ Chennai; दिनांक/ Dated : 21-03-2022
JPV

आदेशकीप्रतिलिपिअग्रेषित/Copy of the Order forwarded to :

1. अपीलार्थी/Appellant
2. प्रत्यर्थी/Respondent
3. आयकरआयुक्त (अपील)/CIT(A)
4. आयकरआयुक्त/CIT
5. विभागीयप्रतिनिधि/DR
6. गार्डफाईल/GF