IN THE INCOME TAX APPELLATE TRIBUNAL
PUNE BENCH, 'A' PUNE

BEFORE SHRI R.S. SYAL, VICE PRESIDENT AND
SHRI S.S. VISWANETHRA RAVI, JUDICIAL MEMBER

आयकर अपील सं. / ITA No.23/PUN/2019

निर्धारण वर्ष / Assessment Year : 2015-2016

Jayant Avinash Dave Office No.801-804, 8th Floor, Amar Business Park, Sadanand Estates, Plot No.1, S.No.105, Baner Road, Pune – 411045 PAN: AAQPD6875J	Vs.	DCIT, Circle 5, Pune
Appellant		Respondent

आयकर अपील सं. / ITA No.182/PUN/2019

निर्धारण वर्ष / Assessment Year : 2015-2016

DCIT, Circle 5, Pune	Vs.	Jayant Avinash Dave 46/2/1B, Kaka Halwai Industrial Estate, Pune Satara Road, Pune – 411009 PAN: AAQPD6875J
Appellant		Respondent

Cross Objection No.11/PUN/2022
(Arising out of ITA No.182/PUN/2019

निर्धारण वर्ष / Assessment Year : 2015-2016

Jayant Avinash Dave Office No.801-804, 8th Floor, Amar Business Park, Sadanand Estates, Plot No.1, S.No.105, Baner Road, Pune – 411045 PAN: AAQPD6875J	Vs.	DCIT, Circle 5, Pune
Cross Objector		Respondent

Assessee by	Shri Mihir Naniwadekar
Revenue by	S/Shri Keyur Patel CIT-DR and Ramnath P Murkende
Date of hearing	26-10-2023
Date of pronouncement	30-10-2023

आदेश / ORDER

PER R.S. SYAL, VP :

These two cross appeals – one by the assessee and the other by the Revenue along with one Cross-objection by the assessee emanate from the order dated 19.11.2018 passed by the ld. CIT(A) in relation to the A.Y. 2015-16.

2. The first issue raised in the cross appeals is against treating the extent of sale consideration received on transfer of shares as Business income chargeable u/s 28 of the Income-tax Act, 1961 (hereinafter also called 'the Act').

3. Briefly stated, the facts of the case are that the assessee, an individual, filed his return declaring total income of Rs.69,68,33,360/-. A company, namely, Begu Diesel Start Systems Pvt. Ltd. (hereinafter called `the Indian company') was incorporated on 16.10.1996. The assessee and a Germany company started business pursuant to the Joint venture agreement dated 16.12.1996.

The assessee, along with his wife, held 51% shares in the Indian company, while the remaining 49% held by BorgWarner Ludwigsburg GmbH, Germany (hereinafter called `the foreign company'). The assessee's wife transferred her shares to the assessee, which point is not disputed. The assessee transferred the resultant total shareholding of 10,71,000 shares in the Indian company to the foreign company for a consideration of Rs.85.79 crore. After taking the benefit of cost of acquisition of these shares at Rs.3.82 crore, the assessee offered income on this score as long term capital gain. The Assessing Officer (AO) examined the terms and conditions of Share Sale and Purchase Agreement (SSPA) dated 29.01.2015 between the assessee and the foreign company and show caused as to why the consideration of Rs.85.79 crore be not treated as receipt for handing over the management and control of the Indian company and hence charged to tax as Business income as against capital gains shown. The assessee sought directions u/s 144A from the JCIT, Range-5, Pune, who also opined on the same lines as did the AO. This led the AO to finalize the assessment by treating receipts shown from sale of shares as business income u/s 28. He computed the business income at Rs.80,78,52,914/- after

reducing the cost price along with certain other expenses from the sale price of Rs.85.79 crore. The ld. CIT(A), on appreciation of various clauses of the SSPA, observed that the assessee not only transferred his shares but also the right to manage along with agreeing not to compete, non solicitation and non interference, etc. He, thus, held that the consideration for termination of bundle of management rights and non-compete was liable to be considered u/s 28(va). Relying on the decision of Mumbai Bench of Tribunal in *ACIT vs. Savita N Mandhana (ITA No.399/Mum/2010 & Ors)*, he held that some part of the sale consideration was required to be attributed to termination of management and non compete obligations. In the absence of SSPA specifying any consideration for non compete and termination of bundle of management rights, he held that 10% of the sale consideration should be treated as consideration for these. That is how, he held that Rs.8.57 crore was to be treated as 'Business income' and balance consideration towards sale of shares for computing long term capital gain. Both the sides have come up in appeal before the Tribunal on their respective stands.

4. We have heard the rival submissions and perused the relevant material on record. There is no dispute on the fact that the assessee received total consideration of Rs.85.79 crore. He claimed this sum as consideration for transfer of shares resulting into long term capital gain. On the other hand, the AO canvassed the view that the entire consideration was in the nature of 'Business income' chargeable to tax u/s 28(va). However, the ld. CIT(A) attributed 10% of the consideration to non-compete clause and termination of the management. Now, the moot question is to find out if the assessee received Rs.85.79 crore only towards transfer of shares liable to tax under the head `Capital gains' or such amount or a part thereof was attributable to termination of role in management and non compete obligation as mentioned in sections 28(ii)(a)/28(va), liable to be treated as 'Business income'. Basically, this question involves determination of two points -

i. Is entire consideration only for transfer of shares? and

ii. How is it taxable?

We will espouse these two points in seriatim.

I. IS ENTIRE CONSIDERATION ONLY FOR TRANSFER OF SHARES?

5. In order to reach any decision on this factual count, it would be apposite to have a look at SSPA dated 29.01.2015, a copy of which has been provided at page 143 onwards of paper book. The preamble of this Agreement provides that the assessee is a legal and beneficial owner of 10,71,000 Equity shares of the Indian company representing 51% of its issued capital and the foreign company is the legal and beneficial owner of the remaining 10,29,000 Equity shares. Article 6 of the SSPA provides that upon receipt of a copy of the Remittance Instruction, the Seller (assessee) shall tender his resignation from the Indian company. Article 7 is important for our purpose, which states the "Post completion covenants". Articles 7.2 is the "Confidentiality clause", which provides that the details of transactions and any other information and other material marked as confidential shall not be disclosed by the assessee to third parties for a period of two years. Article 7.3 is a continuation of the same, with the heading `Confidentiality of the Company Technical Information and Company Information". This clause provides that: `The Seller (the assessee) shall not directly or indirectly, disclose, reveal, divulge or communicate to any person or use or exploit for his own benefit or for the benefit of any Person other than the Company, the

Company Technical Information for a period of four years from the date of completion'. Article 7.4 is Non compete clause which provides that: The Seller (the assessee) shall not directly or indirectly own, manage, operate, control or assist any person or participate in the ownership, management, operation or control of any Restricted Business in India'. The term 'Restricted business' has been defined to mean "the manufacture, import, distribution or sale of Glow Plugs, heater plugs or controllers (for Glow Plugs only) for the automotive industry." Precisely, this is a business carried on by the Indian company, whose shares were transferred by the assessee to the foreign company. It is thus explicit that the assessee agreed not to compete with the business of the Indian company for a period of two years. Article 7.6 is a `Non solicitation' clause, which provides that the assessee shall not solicit the existing employees or consultants of the Indian company for a defined period. Article 7.7 is a `Non interference' clause, which prohibits the assessee from causing or inducing or encouraging any existing customer or existing qualified supplier of the Indian company. Article 7.8 is a `Non disparaging' clause.

6. An overview of the above clauses of the SSPA clearly transpires that the assessee received a sum of Rs.85.79 crore not only for the transfer of shares but also for agreeing to the negative covenants of non compete, non disclosure, non solicitation etc. for a definite period. It is further corroborated from Article 3 of the SSPA, which states that the Purchaser (the foreign company) shall, *in accordance with the terms of this Agreement,* pay to the Seller (the assessee), a purchase price of Rs.801.027077 per Sale Share aggregating to Rs.85,79,00,000 as consideration'. This indicates that albeit total consideration of Rs.85.79 crore has been given in the form of Rs.801.027077 per share, but it is, in fact, both towards the purchase of shares and post completion negative covenants accepted by the assessee. It becomes more glaring when we note that these negative covenants are integral part of the SSPA have binding force on the assessee in the same way as is the obligation to transfer the shares to the foreign company. It is not a case of the AO inferring the existence of some negative covenants. Rather, such negative covenants actually exist in the SSPA. The consideration of Rs.85.79 crore is subject to the acceptance of such negative covenants. As the SSPA puts obligations towards the negative covenants, which were

also accepted by the assessee, it is simple and plain that the consideration of Rs.85.79 crore is towards sale of shares and also accepting the negative covenants.

7. Our view gets further fortified by the `Indemnification by the Seller' clause contained in Article 12 of the SSPA, which provides that: `The Seller shall….indemnify, defend and hold BWLG, the Purchaser and their respective directors and employees … against any and all Losses directly and actually incurred or suffered by the Purchaser Indemnified Person or the Company … arising from…. (ii) any breach of the covenants or obligations in Articles 7.2 (Confidentiality of this Transaction), 7.3 (Confidentiality of the Company Technical Information and Company Information), 7.4 (Non-compete), 7.6 (Non-solicitation) and 7.7 (Non-Interference) of this Agreement by the Seller….'. Further, Clause (b) of Article 12.6 provides that the maximum aggregate liability of the Seller to indemnify the Purchaser, *inter alia*, towards Articles 7.2 (Confidentiality of this Transaction), 7.3 (Confidentiality of Company Technical Information and Company Information, 7.6 (Non-Solicitation) and 7.7 (Non-Interference) of this Agreement, shall be limited to Rs. 150 million; and for any Indemnification

Claim arising out of or in connection with any covenant and obligation of the Seller in Articles 7.4 (Non-compete) of this Agreement shall be limited to an amount equal to the amount specified in Article 12.6(b) (iii) that is Rs.150 million plus Indian Rupees One Hundred Million (INR 100,000,000). It thus crystallizes that the liability of the assessee to indemnify the Purchaser for violation of the negative covenants contained in Article 7 of the SSPA can extend up to a maximum of Rs.40.00 crore (Rs. 150 million + Rs. 150 million + Rs.100 million). No person will undertake the liability to indemnify the foreign company for a sum up to Rs.40.00 crore for violation of the negative covenants without receiving any consideration there against in the first instance. Had the consideration of Rs.85.79 crore been exclusively towards sale of shares, there was no question of the assessee accepting the obligation of indemnifying the buyer up to a sum of Rs.40.00 crore for the violation of the negative covenants. It is thus graphically glaring that even though there is no separate mention of the consideration for the negative covenants, but they, forming an essential and integral part of the SSPA, do carry value, which is embedded in total consideration. It is the substance rather

than the form of the SSPA, which should be looked into. It is ergo held that the consideration of Rs. 85.79 crore was not only for transfer of shares but also for accepting the negative covenants. We, therefore, jettison the contention advanced on behalf of the assessee that the entire consideration was towards transfer of shares.

II. HOW IS IT TAXABLE?

8. The assessee claimed taxability of the entire profit under the head `Capital gains' by treating it as profit arising from the transfer of shares. The AO held the entire profit as arising from transfer of business including negative covenants chargeable to tax u/s 28. The ld. CIT(A) held that 10% of the consideration was chargeable u/s 28 towards termination of role in management and non compete obligation leaving the remaining amount towards transfer of shares chargeable as capital gain. For this proposition, he drew strength from the order of the Mumbai Bench of Tribunal in *ACIT vs. Savita N Mandhana (ITA No.399/Mum/2010 & Ors)* holding that: `it has been stated at the Bar that income attributable to non-compete obligations has been offered to tax as business income.'

9. It is axiomatic that if there is one price given for more than one thing (transfer of shares and negative covenants) and there are

separate provisions enshrined in the Act dealing with their taxation independently (as will be discussed *infra*), then income from transfer of one of these (shares) needs to be computed by considering price paid for such item alone (share) and not the consolidated price. It is for the *raison d'etre* that income from the other (negative covenants) requires separate determination, governed by the independent provisions, with reference to the price paid for these.

10. The Department has made out a case that the entire consideration for the transfer of shares and also accepting negative covenants is business income alone. The ld. DR supported the view point of the AO of taxing the entire amount as business income u/s 28 by relying on the judgment of Hon'ble Punjab & Haryana High Court in *Sumeet Taneja vs. CIT (2013) 261 CTR 494 (P&H)*. It was contended that the facts of that case were identical to those of the case under consideration inasmuch as the assessee therein transferred his full shareholding along with agreeing to not compete and the Hon'ble Court held the entire amount chargeable as business income u/s 28(va) and not separately towards transfer of shares chargeable under the head 'Capital gains'. Per contra, the

case of the assessee is that the entire amount was received towards transfer of shares alone. The ld. AR relied on the judgment of Hon'ble Bombay High Court in *Premier Automobile Ltd. vs. ITO & Anr. (2003) 264 ITR 193 (Bom)* to contend that when the business is transferred, chargeability arises in terms of section 50B. It is no doubt true that both the Hon'ble High Courts have held as has been argued.

11. The AO/ld. CIT(A) have fully/partly taken shelter of section 28(ii)(a)/(va) to canvass their respective points of view. It thus becomes essential to mull over the prescription of the relevant parts of the section, as under: -

> "28. The following income shall be chargeable to income-tax under the head `Profits and gains of business or profession'-
>
> ……
>
> (ii) any compensation or other payment due to or received by,—
>
> (a) any person, by whatever name called, managing the whole or substantially the whole of the affairs of an Indian company, at or in connection with the termination of his management or the modification of the terms and conditions relating thereto;
>
> ……..
>
> (va) any sum, whether received or receivable, in cash or kind, under an agreement for—
>
> (a) not carrying out any activity in relation to any business or profession; or
>
> (b) not sharing any know-how, patent, copyright, trade-mark, licence, franchise or any other business or commercial right of similar nature or information or technique likely to assist in the manufacture or processing of goods or provision for services:

Provided that sub-clause (a) shall not apply to—

(i) any sum, whether received or receivable, in cash or kind, on account of transfer of the right to manufacture, produce or process any article or thing or right to carry on any business or profession, which is chargeable under the head "Capital gains";

(ii) any sum received as compensation, from the multilateral fund of the Montreal Protocol on Substances that Deplete the Ozone layer under the United Nations Environment Programme, in accordance with the terms of agreement entered into with the Government of India.

Explanation.—For the purposes of this clause,—

(i) "agreement" includes any arrangement or understanding or action in concert,—

(A) whether or not such arrangement, understanding or action is formal or in writing; or

(B) whether or not such arrangement, understanding or action is intended to be enforceable by legal proceedings;"

12. The AO invoked both clause (ii)(a) and (va) of section 28 in a combined manner to hold that the amount is chargeable as business income. The ld. CIT(A) assigned 10% value of the total consideration to non-compete clause and termination of management, which are subject matter of sub-clause (a) of clause (va) and sub-clause (a) of clause (ii) of section 28.

13. Clause(ii)(a) of section 28 deals with compensation received by a person, managing the affairs of an Indian company, for termination of management or the modification of the terms and conditions of managing the whole or substantially the whole of the

affairs of an Indian company. In order to be covered under this provision, firstly, the recipient of the compensation should have the management rights, which are later on terminated or modified. Lawful prior holding of managing rights is *sine qua non* for the attractability of this provision. The assessee in the instant case was only the Managing director of the Indian company and *per se* did not hold any management rights thereof. It is thus overt that section 28(ii)(a) is not applicable to the facts of the case. The sequitur is that the ld. CIT(A) was not justified in holding that the assessee received 10%, *inter alia*, for termination of management rights.

14. Now we turn to section 28(va), which embodies two elements, viz., (a) not carrying out any activity in relation to any business or profession; and (b) not sharing any know-how, patent, copyright, trade-mark, licence, franchise or any other business or commercial right of similar nature or information or technique likely to assist in the manufacture or processing of goods or provision for services. The first thing which is accentuated from this provision is that it brings within the ambit of `Business income', any sum paid for `not doing' the specified things. Unlike, the usual business income, which is earned on `doing' something, say, sale of goods or

rendering of services etc., this provision taxes as business income a consideration for `not doing' the specified things. But for their inclusion in this provision, any sum received for such `not doings', being a capital receipt, was not chargeable to tax.

15. When we examine all the relevant clauses of Article 7 of the SSPA, they symbolize only `not doings', that is, negative covenants. Articles 7.2.and 7.3 contain Confidentiality clause (prohibiting the assessee from sharing the Technical Information etc); Articles 7.4 and 7.5 are non-compete clauses (prohibiting the assessee from starting similar business); Article 7.6 is non-solicitation clause (prohibiting the assessee from soliciting existing employees and consultants); Article 7.7 is Non-Interference clause (prohibiting the assessee from inducing the existing customers and suppliers); and Article 7.8 is Non disparaging (prohibiting the assessee from defaming the buyer or his business). This shows that the obligations undertaken by the assessee, having huge financial consequences for their violation in the form of indemnity, are all negative covenants. Any compensation received for the negative covenants will fall for taxation under section 28(va), if the obligations are of the nature covered under sub-clauses (a) and (b) of this provision. Sub-clause

(a) of section 28(va) taxes any sum received by the assessee for `not carrying out any activity in relation to any business'. Non-compete clauses contained in Articles 7.4 and 7.5 are directly covered within the purview of this provision. Similarly, Non-solicitation, Non-interference and Non-disparaging clauses contained in Articles 7.6, 7.7 and 7.8 are also extension of `not carrying out any activity in relation to the business'. Sub-clause (b) of section 28(va) taxes any sum received by the assessee for `not sharing any know-how, patent, copyright, trade-mark, licence, franchise or any other business or commercial right of similar nature or information or technique likely to assist in the manufacture or processing of goods or provision for services. Articles 7.2 and 7.3 are for not sharing Company Technical Information, which gets covered within the term `know-how' given in the provision. Thus all the negative covenants contained in Article 7 of the SSPA are the items covered under sub-clauses (a) or (b) of section 28(va).

16. The ld. CIT(A) included only non-compete clause within the purview of sub-clause (a) of section 28(va) and left out the remaining negative covenants given under Article 7, which also fall under either of the two sub-clauses of section 28(va). In our view,

the ld. CIT(A) was not justified in not considering the sum received towards the remaining negative covenants within the overall scope of section 28(va). To this extent, the impugned order is modified.

17. The view point of the ld. DR that the full consideration should be attributed to section 28(va), in our considered opinion, again does not merit acceptance. We have noted above that the SSPA is a consolidated agreement not only for accepting the negative covenants but also for the transfer of shares. Actual transfer of shares by the assessee to the foreign company is not denied. When the consideration in the agreement is a consolidated figure, the part relatable to transfer of shares cannot be covered u/s 28(va) by treating it also towards negative covenants, when in fact the assessee did transfer his shares also. In that scenario, the part of consideration relatable to transfer of shares needs to be considered for taxation under the head `Capital gains'.

18. The decision in *Sumeet Taneja (supra)*, relied by the ld. DR, does not support his case. The assessee in that case was holding 100% shares of the business which were transferred along with agreeing to non-compete. Cent percent transfer of shares led to the transfer of business. It was in that backdrop of the facts that the

Hon'ble High Court held that the assessee transferred its business as a whole. Right now, we are concerned with the facts wherein the assessee had only 51% shares in the Indian company. By transferring these shares, it cannot be said that the assessee transferred the business.

19. The ld. AR contended that section 28(va) can be triggered only when the assessee receives a well-defined consideration for the non compete clause. Since in this case the assessee transferred shares and did not receive any separate consideration for the negative covenants, no amount could be brought to tax under section 28(va). We are unable to accord our imprimatur for the obvious reason that this provision simply provides that any sum received or receivable under an agreement for the negative covenants is chargeable to tax as business income. The term 'agreement' has been defined quite widely in Explanation to section 28(va) to include any arrangement or understanding or action in concert, whether or not such arrangement, understanding or action is formal or in writing; or whether or not such arrangement, understanding or action is intended to be enforceable by legal proceedings. The sum and substance of section 28(va) is that when

an assessee accepts a negative covenant under an agreement, the *quid pro quo* for that should be taxed as business income u/s 28(va). No further stipulation has been set up in the provision that the agreement providing for the negative covenants should be exclusively for this purpose *de hors* the transfer of any shares.

20. To bolster his submission that no part of the consideration should be attributed to anything other than the shares, the ld. AR relied on the judgment of Hon'ble Supreme Court in *Vodafone International Holdings B.V. vs. Union of India (2012) 341 ITR 1 (SC)*. That was a case in which Hutchison International, Hong Kong set up its 100% subsidiary, CGP Investments in Cayman Islands. CGP Investments purchased shares of an Indian company, namely, Hutchison Essar Ltd. Vodafone International, Netherlands entered into an agreement in Australia with Hutchison International, Hong Kong for purchase of shares of CGP Investments. The AO held that since Vodafone International, Netherlands purchased Indian business of Hutchison Essar Ltd. with the purchase of 100% shareholding of CGP, it resulted in income chargeable to tax in India in the hands of Hutchison, Hong Kong and hence Vodafone ought to have deducted tax at source. The Hon’ble Bombay High

Court upheld the view point of the AO. However, the Hon'ble Supreme Court reversed it by holding that it was case of purchase of shares of a Non-resident, namely, CGP Investments by a Non-resident, namely, Vodafone International, Netherlands from another Non-resident, namely, Hutchison International, Hong Kong under an agreement which was entered outside India and hence no capital gains chargeable to tax in India arose in the hands of Hutchison International, Hong Kong. To neutralize the *ratio* of the judgment of Hon'ble Supreme Court in *Vodafone International,* the legislature stepped in and carried out certain statutory amendments, including altering the definition of 'capital asset' u/s 2(14), the definition of 'transfer' u/s 2(47) and insertion of Explanations (4), (5), (6) and (7) to section 9(1)(i). When we examine the factual matrix under consideration in the hue of the judgment in *Vodafone International*, it becomes overt that the facts of both the cases are poles apart. In that case, the question was whether the shares of the foreign company, deriving value from assets situated in India, would constitute 'capital asset' in India so as to magnetize the chargeability in the hands of the non-resident transferor? In other words, the issue was taxability vs. non-taxability of profits in India.

In the oppugnation, the case under consideration does not involve any doubt about the taxability of the profits in India. In fact, the assessee itself offered the profit as chargeable to tax under the head 'Capital gains'. The dispute is only about the head under which such profits should be charged to tax, that is, whether 'Capital gains' or 'Business income.' Apart from the distinction in the factual panorama of the two cases, the decision in *Vodafone International (supra)* has been statutorily negated through the amendments discussed *supra*.

21. The crux is that so long as the agreement talks of some specified negative covenants, the consideration - whether shown inclusively or exclusively, will be hit by the mandate of section 28(va). The contention of the ld. AR, being, sans merit is repelled.

22. The reliance of the ld. AR on *Premier Automobile Ltd.(supra)* again does not lend any strength. That was a case dealing with the assessment year 1995-96 relating to *slump sale* of the business as a going concern. The Hon'ble High Court remanded the matter to the AO to compute the quantum of capital gains under ss. 45 to 50. Right now, we are examining a case in which the business of Indian company continued with the company itself. There was no transfer

of business in slump sale. The assessee, being a shareholder, simply transferred his holding of 51% of the shares in the Indian company to the foreign company. Be that as it may, the position of law has underwent change by insertion of section 50B w.e.f. 01.04.2000 containing special provision for capital gains in case of slump sale. This section provides that any profit or gain arising out of slump sale shall be chargeable as capital gains arising from the transfer of long term capital asset. As the assessee has not transferred any business with all its assets and liabilities, the provisions of section 50B do not get not attracted.

23. The legal position which thus follows from the above discussion is that on the transfer of business as a whole in a slump sale, the provisions of section 50B are attracted and the income is computed accordingly. On the other hand, if some non-depreciable capital assets are transferred separately (not in a slump sale), then capital gain is computed in accordance with the normal provisions of Chapter IV-E. If along with transfer of some capital assets, not resulting in transfer of business as a whole, the assessee undertakes some negative covenants, then consideration for the transfer of shares should be considered for computation of capital gain and for

the negative covenants as chargeable under section 28(va) of the Act. If however, the capital asset under transfer is any right to manufacture, produce or process any article or thing or right to carry on any business, income is computed under the head `Capital gains' by taking cost of acquisition of such right to manufacture etc. or right to carry on business u/s 55(2)(a) at Nil, unless the assessee or the previous owner paid some purchase price for acquiring such rights. In case the assessee transfers such right to manufacture etc. and also simultaneously accepts the negative covenant of non-compete, total consideration received is considered for computing capital gain u/s 45 without taking any recourse to the provisions of section 28(va) of the Act. This position is enshrined as the proviso to section 28(va). If however, an assessee accepts the negative covenant of non-compete along with the transfer of any capital asset such as shares, other than right to manufacture etc., entire consideration cannot be devoted to the transfer of shares for computing capital gain u/s 45. Recourse will have to be taken to the provisions of section 28(va) of the Act insofar as consideration for the negative covenant is concerned. The without prejudice contention of the ld. AR, invoking proviso to section 28(va), for

buttressing his argument that no separate income should be determined as business income and the entire consideration, even relating to negative covenants, should be considered under the head `capital gains', therefore, does not hold water. Proviso to section 28(va) gets attracted only when the right to manufacture etc. or carry on business is transferred along with the assessee agreeing for non-compete [not the other negative covenants as mentioned in sub-clause (b) to section 28(va)]. In that case, no part of the total consideration on account of non-compete is separately charged to tax as business income under section 28(va), if the total consideration is chargeable under section 45. The proviso rather gives a clear clue that in all other cases where right to manufacture etc. or to carry on business is not transferred and there is a non-compete clause in the agreement, then the portion of the total consideration relatable to non-compete should be segregated and charged to tax as business income.

24. Reverting to the facts, it is seen that the assessee never claimed that Rs.85.79 crore was for transfer of any right to manufacture, produce or process any article or thing or right to carry on any business. In fact, the assessee did not have any such right. He had

only 51% shareholding in the Indian company, which he transferred.

25. We, therefore, hold that the total consideration of Rs.85.79 crore needs to be segregated towards the transfer of shares and negative covenants. The part relatable to transfer of shares will be considered for computing tax under the head `Capital gains'; and the part relating to the negative covenants covered under sub-clauses (a) and (b) of section 28(va) will be taxed as `Business income'.

26. Now we embark upon the exercise of finding out the part of total sale consideration as relatable to transfer of shares and the part towards negative covenants. In his without prejudice argument, the ld. AR contended that the agreed sale price of each share as per the SSPA was Rs.801.027. While referring to the letter dated 29.01.2015 of the foreign company addressed to Citi Bank NA, the ld. AR submitted that the price per share as per valuation guidelines was determined at Rs.774 per share. He argued that the differential amount of Rs.2.79 crore at the rate of Rs.26.027 per share [Rs.801.027 minus Rs.774] may be attributed to the negative covenants chargeable to tax u/s 28(va), as against the ld. CIT(A)

assigning the value of Rs.8.57 crore. This was strongly countered by the ld. DR. Referring to the Joint venture agreement dated 16.12.1996, the ld. DR submitted that Para 14 deals with "Restriction on transfer of shares". While referring to para 14.5, he submitted that the sale of shares was required to be made on the basis of the Net Asset Value method. Drawing our attention towards the Valuation report submitted on behalf of the assessee, the ld. DR showed that the Valuer did not compute value of shares under the Net Asset Value method as was agreed under the JV Agreement. We find that para 14.5 of the JVA deals with the situation in which a shareholder agrees to purchase the shares of the company from another shareholder. This para states that: "In the event the Shareholders agree to purchase the shares but do not agree to the price at which the same are offered for sale, then the sale shall take place at the *net sale value* of the shares to be determined by ….'. Obviously, this para is referring to the situation of transfer of shares between the shareholders post the JV agreement, as is instantly prevailing. The Valuer did not value the shares under the Net asset value method, leave aside the determination of the value under this method. The AO treated full sale consideration of

Rs.85.79 crore as attributable to the transfer of business, leaving no scope for finding out separate consideration towards the transfer of shares for the computation of capital gains. The ld. CIT(A) also did not go deep into the part of the consideration relatable to transfer of shares. He simply applied the magic wand and held that 10% of the consideration was towards non-compete and termination of role of the assessee in management. No reason or rationale has been given for the *ad hoc* figure of 10%. Under these circumstances, we are satisfied that the exercise of attributing sale consideration to the shares and the negative covenants is required to be done afresh by the AO. We order accordingly and direct him to segregate the consideration relatable to sale of shares and then accordingly compute the capital gains on transfer of such shares; and the remaining amount towards negative covenants should be taxed as business income u/s 28(va) of the Act. Needless to say, the assessee will be provided a reasonable opportunity of hearing.

27. The next issue taken up by the assessee in his appeal is against confirmation of disallowance of Rs.16,86,377/- made by the AO u/s 14A of the Act. Succinctly, the factual matrix of this ground is that the assessee claimed exempt income of Rs.42,80,861/-, which

included dividend from shares, dividend from mutual funds, income from PPF and income from tax free bonds. The assessee had not made any *suo motu* disallowance u/s 14A. On being called upon as to why no disallowance was offered, the assessee submitted a general reply about his having own capital more than the amount invested in securities yielding exempt income. The AO, on appreciation of entire material, made disallowance of Rs.16,86,377/- u/s 14A read with rule 8D(2)(iii) at 0.5% of average value of investments. This disallowance was echoed in the first appeal.

28. Having heard the rival contentions and perused the material on record, it is seen that the AO made the disallowance only towards rule 8D(2)(iii), which is 0.5% of the average value of investments. It is further borne out from para 30 of the assessment order that the average value of investments was computed by the AO considering only those securities which yielded exempt income and not all the investments. Considering the fact that the assessee had own capital more than the amount invested in securities yielding exempt income, the AO did not make any disallowance towards interest. In our opinion, no exception can be taken to the disallowance made

and sustained u/s 14A. We, therefore, dismiss this ground of appeal.

29. The ld. AR submitted that the other grounds taken up in the assessee's appeal are either general or consequential, not requiring any separate adjudication.

30. The only other ground which survives in the appeal of the Revenue is against the deletion of addition of Rs.92,159/- made by the AO towards deemed rent on vacant property. The assessee was having a proprietorship concern by the name and style of M/s Aarushi Developers, which was engaged in the business of properties. The AO observed that the built up area of 550 sq.ft., which was part of stock in trade, was vacant throughout the year. He computed the deemed rent of such area at Rs.93,559/-. The ld. CIT(A) deleted the addition by relying on the order dated 12.09.2018 passed by the Pune Bench of Tribunal in *M/s Cosmopolis Construction vs. ITO* (ITA Nos.230 & 231/PUN/2018). Aggrieved thereby, the Revenue has come up in appeal before the Tribunal.

31. Having heard the rival contentions and perused the material on record, it is found as an admitted position that the vacant property,

in respect of which deemed rent was calculated by the AO, was stock in trade of the assessee. The Pune Bench of Tribunal in *M/s Cosmopolis Construction vs. ITO (supra)* has held that no income from house property can result in respect of unsold flats held by the builder as stock in trade at the year-end. Insertion of sub-clause (5) to section 23 by the Finance Act, 2017 w.e.f. 01.04.2018, requiring determination of the ALV in respect of building and land appurtenant thereto which is held as stock in trade, is prospective and cannot apply to the assessment year 2015-16 under consideration. We, therefore, uphold the impugned order on this score.

32. The ld. AR submitted that the Cross Objection was only in support of the impugned order.

33. In the result, the cross appeals are partly allowed for statistical purposes and the CO is dismissed as infructuous.

Order pronounced in the Open Court on 30th October, 2023.

Sd/-	Sd/-
(S.S. VISWANETHRA RAVI)	**(R.S.SYAL)**
JUDICIAL MEMBER	**VICE PRESIDENT**

पुणे Pune; दिनांक Dated : 30th October, 2023
GCVSR

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order is forwarded to:

1. अपीलार्थी / The Appellant;
2. प्रत्यर्थी / The Respondent
3. The CIT(A)-4, Pune
4. The Pr.CIT-3, Pune
   DR, ITAT, 'A' Bench, Pune
5. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

// True Copy //

Senior Private Secretary
आयकर अपीलीय अधिकरण ,पुणे / ITAT, Pune

		Date	
1.	Draft dictated on	26.10.2023	Sr.PS
2.	Draft placed before author	30.10.2023	Sr.PS
3.	Draft proposed & placed before the second member		JM
4.	Draft discussed/approved by Second Member.		JM
5.	Approved Draft comes to the Sr.PS/PS		Sr.PS
6.	Kept for pronouncement on		Sr.PS
7.	Date of uploading order		Sr.PS
8.	File sent to the Bench Clerk		Sr.PS
9.	Date on which file goes to the Head Clerk		
10.	Date on which file goes to the A.R.		
11.	Date of dispatch of Order.		

*