T.S. Manocha vs Dy. Cit on 17 August, 2005

Equivalent citations: [2006]98ITD242(ASR), [2006]5SOT277(ASR)

ORDER

Bhavnesh Saini, J.M. This appeal by the assessee is directed against the order of the Commissioner (Appeals), Jammu, headquarters at Amritsar dated 11-12-2001 for the assessment year 1999-2000 on the following grounds :

> "1. That the learned Commissioner (Appeals), has erred in law and on facts of the case in rejecting the appeal of the assessee.
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> 2. That the learned Commissioner (Appeals) has erred in law and on facts of the case in confirming the addition of Rs. 1,00,00,000.
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> 3. That the provisions of section 28(ii)(a) are not applicable.
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> 4. That the said amount was received as non-compete fee directly from Hindustan Coca Cola and the learned Commissioner (Appeals) has erred in rejecting the claim of the assessee that the said amount is not taxable, without there being any material on record.
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> 5. That the assessment was a protective assessment and the learned Assessing Officer is of the opinion that the same is assessable in the hands of Jammu Bottling Company Private Limited, a Company in which the assessee is a Director, and the matter is before the Hon'ble Tribunal.
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> 6. That the addition of rupees one crore is, therefore, illegal, unjustified and its confirmation by the learned Commissioner (Appeals), was therefore not justified. It is prayed that the addition of Rs. 1 crore is deleted.
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> 6A. That proper opportunity to plead the case was not allowed."

2. This appeal was earlier dismissed in default on two occasions but was restored to its original number vide different orders in the M.As.

3. We have heard the learned representatives of both the parties and gone through the observations of the authorities below.

4. The facts on the issue involved in appeal are that the assessee filed return of income on total income of Rs. 80,612. It was processed under section 143(1). Later on, it was selected for scrutiny. The assessing officer observed that the assessee had received a sum of Rs. 1 crore as non-compete fee from Hindustan Coca Cola Private Limited in terms of agreement dated 25-2-1999, The assessee

is stated to be the Managing Director of M/s. Jammu Bottling Co. (P) Ltd., Jammu. Salary received from this company had been declared in the return of income. Interest is also declared. As regards receipt of Rs. 1 crore statement was annexed with the return in which it was mentioned that the assessee has received a sum of Rs. I crore as non-compete fee from Hindustan Coca Cola Private Limited in terms of agreement dated 25-2-1999 as the same is exempt from tax in view of the decisions of the Hon'ble Supreme Court in CIT v. Best & Co. (P) Ltd. (1966) 60 ITR 11, the Madras High Court in CIT v. Saraswathi Publicities (1981) 132 ITR 207 and Calcutta High Court in CIT v. Dunlop Rubber Co. (I) Ltd. (1977) 107 ITR 182. The assessee filed a copy of the agreement before the assessing officer. In reply before the assessing officer it was stated that the said company was franchise of M/s. Hindustan Coca Cola (P) Ltd. The business of the company along with its rights and goodwill was sold to M/s. Hindustan Coca Cola (P) Ltd. One of the conditions for the sale was that the Directors of Jammu Bottling Co. will not indulge in any business which is in any way in competition with the business of Hindustan Coca Cola (P) Ltd. An agreement to this effect was made between the assessee and M/s. Hindustan Coca Cola on 25-2-1999. The assessee had received a sum of Rs. 1 crore under the agreement dated 25-2-1999. This amount was deposited in the bank account of the assessee. The assessing officer noted the feature of the agreement dated 25-2-1999 between the assessee and M/s. Hindustan Coca Cola Bottling North West (P) Ltd. dated 25-2-1999 in the assessment order along with the brief feature of agreement being purchase of goodwill dated 6-8-1998 between the Hindustan Coca Cola Bottling North West (P) Ltd. and M/s. Jammu Bottling Company (P) Ltd. and business purchase agreement dated 7-12-1998 between M/s. Jammu Bottling Co. (P) Ltd. and M/s. Hindustan Coca Cola (P) Ltd. and observed the purpose of agreement dated 25-2-1999. The assessing officer briefly observed that if two agreements dated 6-8-1998 and 7-12-1998 are read together, it becomes clear that there was nothing more either by way of assets, value of all the rights and goodwill to be sold by M/s. Jammu Bottling Co. According to the assessing officer since there was nothing further to be sold no further agreement was required to be made either by M/s. Jammu Bottling Co. or by its Directors. The assessing officer further observed that the payment of non-compete fee made to oblige the Directors of the Company. The assessing officer also observed that business goodwill will include the market reputation, trading style and distribution know-how etc. The assessing officer further observed that the goodwill was purchased prior to the purchase of the business. The assessing officer further observed that further information and know-how of the business of M/s. Jammu Bottling Co. was already covered by the earlier agreements. Moreover, the said assets cannot be sold twice. The assessing officer further observed that the circumstances indicate that whatsoever was paid by the purchaser company, i.e., M/s. Hindustan Coca Cola was simply the purchase price. He has further observed that the Directors were getting salary from this company. The terms and conditions relating to their service were modified when this company sold the whole business to the purchaser. Whatever compensation or other payments were-received by its directors are to be taxed under section 28(ii)(a) of the Income Tax Act which provides that 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. The statement of the assessee was also recorded. The assessing officer also observed that three directors have obtained different amounts and no satisfactory explanation is filed as to why there was difference in the amounts received by the three directors.

5. The assessing officer in view of the facts recorded in the assessment order held that the compensation received by the assessee under the agreement dated 25-2-1999 was certainly not a non-compete fee. This was essential part of cost price paid by M/s. Hindustan Coca Cola for purchase of the business and other rights from M/s. Jammu Bottling Co. As a matter of fact, this amount was payable from M/s. Hindustan Coca Cola (P) Ltd. to M/s. Jammu Bottling Co. and it was shared by three directors holding the shares. The assessing officer further observed that the intention in adopting this method was to reduce the tax liability in the hands of the directors. This course or method did not cost anything extra to the M/s. Hindustan Coca Cola (P) Ltd. and he further observed that it could be said that to this extent there was a collusion between the seller, i.e., M/s. Jammu Bottling Co., its Directors and the purchaser company, namely M/s. Hindustan Coca Cola. The assessing officer did not rely upon the decision of the Hon'ble Supreme Court in the matter of Best & Co. (P) Ltd.'s case (supra) and the decision of the Madras High Court in the matter of Saraswathi Publicities case (supra).

6. The assessing officer observed that M/s. Jammu Bottling Co. (P) Ltd. has sold its business as a whole alongwith all the assets as a going concern vide agreements dated 6-8-1998 and 7-12-1998. The assessment for the assessment year 1999-2000 in the case of M/s. Jammu Bottling Co. was completed vide order dated 24-3-2000. The argument that company had received Rs. 10 crores against sale of goodwill was not accepted and Rs. 10 crores was treated as a sale proceeds of other assets and business. The argument that the company was not liable to capital gain on this transaction was also not accepted. The assessing officer further observed that later on while examining the case of the present assessee, Shri. T.S. Manocha, for the assessment year 1999-2000, it was noticed that a sum of Rs. 3.8 crores was received by three Directors which was shown as a non-compete fee. Request was made to the Commissioner (Appeals) to enhance long-term capital gain by Rs. 3.8 crores because the amount of Rs. 2.8 crores was nothing but the sale proceeds of the assets of the company. The Commissioner (Appeals) further observed that the appeal of the company M/s. Jammu Bottling Co. was decided by the Commissioner (Appeals) vide order dated 9-1-2001 in which the Commissioner (Appeals) observed that the amount of Rs. 3.8 crores received by the Directors was not a part of sale consideration for the transfer of the business assets as it was paid to the Directors individually for accepting the non-compete fee agreement. The assessing officer further observed that the department has filed appeal before the ITAT, Amritsar Bench against the order of the Commissioner (Appeals) dated 9-1-2001 in the case of the company and the appeal is pending.

7. The assessing officer in view of the above facts concluded that the nature of receipt of Rs. 1 crore is not altered by showing it to be a non-compete fee in the agreement dated 25-2-1999. The assessing officer further held that the compensation received by the assessee due to the reasons that M/s. Jammu Bottling Co. sold its whole business and the terms and conditions enjoyed by Shri T.S. Manocha as a Director of the company were modified. Various contracts which were available to the company were terminated and the business was sold. Therefore, Rs. 1 crore received by the assessee is held to be taxable under the head Profits and gains of the business or profession' under section 28(ii)(a) of the Income Tax Act. The assessing officer clarified that in case the appeal filed by the department before the ITAT in the case of M/s. Jammu Bottling Co. is allowed then Rs. 3.8 crores received by the three Directors will be treated as part of the sale proceeds than amount of Rs. 1 crore

will not be taxed in the hands of the assessee in his individual assessment. The assessing officer accordingly made the addition of Rs. 1 crore in the hands of the assessee.

8. The addition was challenged before the Commissioner (Appeals) and the submissions made before the assessing officer were reiterated. It was briefly submitted that the findings of the assessing officer itself are doubtful about the taxability of the amount either in the hands of the company or the assessee. It was further submitted that M/s. Jammu Bottling Co. had a bottling plant for filling aerated water in the brand name of Coca Cola, Fanta, Gold Spot, Limca, Thumps Up etc., which was originally set up in 1975 and additions were made and the capacity was increased from time to time. In the year 1998-99 as per policy of M/s. Hindustan Coca Cola (P) Ltd. for most of the bottling plants were purchased by M/s. Hindustan Coca Cola including the plant of the company where the assessee was a working Director. The said plants were sold as a going concern excluding goodwill for Rs. 10 crores and independent agreement was executed by M/s. Hindustan Coca Cola (P) Ltd. with the assessee for payment of non-compete fee. It was further submitted that no addition was made in the hands of the company and even the Commissioner (Appeals) refused to enhance the assessment and it was held that the assessee and the remaining Directors held independent contract with M/s. Hindustan Coca Cola (P) Ltd. It was submitted that the Commissioner (Appeals) held that said amount has been paid to the Directors individually to avoid competition. Therefore, same decision should be applied in case of assessee (individual). It was submitted that the onus to prove that payment is not real its on the party who claimed it to be so. In this case, the assessing officer makes a claim that payment is not real but it failed to prove the same. The working Director of the company entered into separate agreement with M/s. Hindustan Coca Cola (P) Ltd. with regard to the non-disclosure of confidential information as also desist from taking up the competitive business. This agreement has been executed at arms length. The Coca Cola Company is known multi-national company and they have taken over 25 plants in India. In all these takeovers non-compete fee has been paid to the working Directors to safeguard the company's interest. Therefore, it was a genuine agreement. It was further submitted that one of the conditions for sale was that the Directors of the said company will not indulge in any business, which is in any way in competition with the business of M/s. Hindustan Coca Cola. It was further submitted that with regard to the pace of industrialization, technology transfers have become quite common. It is in this background that the protection of technical know-how etc. assumes a lot of importance for the survival of the Organisation. Therefore, secracy with respect to the same has to be maintained. It is for the reason that when a relationship breaks and there is likelihood of a competition with the original business through exploitation of the knowledge, experience and expertise of the directors or some other persons with business, non-compete agreements are entered into. Such agreements are in the form of restrictive covenants where a lump sum payment is paid in lieu of the non-competition in the said business. It was, therefore, submitted that the said amount of compensation is a capital receipt in the hands of the assessee and it is not taxable. It was further submitted that the competitions are ready to lure top executing of other company's having substantial know-how of the trade and the market as in the case of the assessee. Considering the competition the assessee could give M/s. Hindustan Coca Cola Pvt. Ltd,, if they had joined their rivals, as the assessee had long knowledge of soft drinks business in the State of Jammu & Kashmir, M/s. Hindustan Coca Cola (P) Ltd. deemed it fit and prudent to offer the monetary benefit in lieu of their covenant that they will not take up or give their knowledge of soft drinks business to any other

person or persons for a specific period. It was further submitted that as per terms and conditions of the business purchase agreement all the employees of M/s. Jammu Bottling Co. were taken even by the buyer except the working directors. No offer was made to these directors for their continuing in the unit by the new management. It was, therefore, very necessary for the buyer that some monetary benefit was given to them so that their experience of over 25 years in this line of business, their knowledge of the trade, their relationship with the dealers and agents, are not taken advantage by the rival group by giving them employment or otherwise. The payment of non-compete fee is, therefore, on account of business consideration to the assessee and the company has no role to play. This is an independent agreement between the assessees and the said company, M/s. Hindustan Coca Cola (P) Ltd.

9. The Commissioner (Appeals) considering the facts available on record did not agree with the submissions of the assessee and was of the view that after the execution of the agreements dated 6-8-1998 and 7-12-1998 by M/s. Jammu Bottling Co. with the purchaser, there was nothing left with the company or its directors to be sold to M/s. Hindustan Coca Cola (P) Ltd. The Commissioner (Appeals) accordingly confirmed the findings of the assessing officer and dismissed the appeal of the assessee.

10. The assessee is in appeal before us on the grounds mentioned above. The learned counsel for the assessee reiterated the submissions made before the authorities below. He has submitted that non-compete fee was received by the assessee against independent agreement. The assessee has restricted himself from doing similar business or profession for a stipulated period with restrictive conditions. Therefore, it was capital receipt in nature. He has further argued that section 28(ii)(a) of the Income Tax Act is not applicable. The learned counsel for the assessee further argued that the findings of the authorities below are against the law and facts of the case as explained above. He has further submitted that M/s. Hindustan Coca Cola (P) Ltd., has entered into an agreement with the company for sale of goodwill and purchase of the business. It was in the business interest to get the agreement also executed by the assessee in favour of M/s. Hindustan Coca Cola (P) Ltd. It was not a sale of any item of M/s. Jammu Bottling Co. He has further argued that the assessing officer has not made out a case of collusive agreement. He has further argued that the Commissioner (Appeals) in the case of M/s. Jammu Bottling Co. decided the issue in favour of the company which was confirmed by the I.T.A.T., Chandigarh Bench. The learned counsel for the assessee relied upon the decision referred to before the Commissioner (Appeals) and also filed list of cateena of authorities in support of the submissions, which we will discuss later on in this order. The learned counsel for the assessee in his written submissions explained the purpose of entering into the agreement between the assessee and M/s. Hindustan Coca Cola (P) Ltd. The learned counsel for the assessee further submitted that since the agreement dated 25-2-1999 was independent agreement having restrictive clauses against the assessee, therefore, in case this agreement would not have been executed then the directors of the company, having independent entity shall have indulged into the competition with regard to the rival group and as such M/s. Hindustan Coca Cola (P) Ltd. entered into this agreement with the restrictive clauses and as such the same is capital in nature.

11. On the other hand, the learned D.R. relied upon the findings of the authorities below and submitted that no formula for bottling cold drinks or experience have been supplied to the assessee

by the Coca Cola, therefore, this agreement is a part of sale consideration of the business of M/s. Jammu Bottling Co. has been correctly treated to be revenue receipt by the assessing officer, The learned D.R. further submitted that the authorities below are justified in making the addition in the hands of the assessee. The learned D.R. submitted that the appeal of the assessee may be dismissed.

12. We have considered the rival submissions, material available on record as pointed out by the parties in reference to the facts of the case.

13. Before considering the submissions of the parties, it would be relevant to discuss certain decisions relied upon by the learned counsel for the assessee before the authorities below as well as before us.

> (1) The decision of the Hon'ble Supreme Court in the case of CIT v. Best & Co. (P) Ltd. (1966) 60 ITR 11. In this case, the assessee is a Privatc Limited Company carrying on a business of agency in innumerable lines. One of such agencies was from the Imperial Chemical Industries (Exports) Ltd., Glasgow (Principal) for distribution and marketing in certain territories in South India of its ammunition, blasting explosives and accessories. The said agency came into existence in 1900. The terms of the agency were not reduced to writing. The rates of commission were paid on terms agreed upon from time to time. The agency was terminable at will, but, because of their mutual confidence, it continued without break till the year 1947, when the principal gave notice to the agency company (assessee) terminating its agency. The agency was ultimately terminated on 31-3-1948 and Principal paid certain amount on the basis of income earned by the Imperial Chemical Industries (India) Ltd., which took over the business from that date. Pursuant to the agreement, the principal paid commission to the assessee for various period, i.e., 31-3-1949 to 31-3-1951. During the same year, it was brought to tax and the assessment had become final but in respect of other two assessment years, namely, 1951-52 and 1952-53, the agency company objected to the inclusion of the said amounts in its taxable income on the ground that the said amounts represented only compensation received for termination of the agency business and also as consideration for the restrictive covenant not to do business in the same line for a prescribed period. The Income Tax Officer and the Appellate Assistant Commissioner held that the termination of the said agency did not alter the structure of the respondent's business and that they represented only the remuneration paid voluntarily by the principal to the agent in the appreciation of its past services. On further appeals by the agency company, the I.T.A.T. held, as the three annual instalments were based on future sales in the same territory as before, they were of the same nature as the normal commission receipts of the respondent. On that ground, the appeals were dismissed. Question was referred to the Hon'ble Madras High Court for opinion which the Division Bench of the High Court having regard to the circumstances of the case, came to the conclusion that by the termination of the agency the assessee lost an earning asset and the compensation paid for the destruction of such an asset was a capital receipt and, therefore, not liable to tax. The matter came up before the Hon'ble Supreme

> Court. The letter dated 11-3-1947 is reproduced in the judgment, issued by the principal to the agency in which one of the conditions for paying the compensation on the basis outlined above was that to give them a formal undertaking to refrain from selling or accepting any agency for explosives or other commodities competitive with those covered by the agency agreement now being terminated. The Hon'ble Supreme Court considering the facts and the material on record, held :
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> "(i) that the compensation agreed to be paid was not only in lieu of the loss of the agency but also for the respondent accepting a restrictive covenant for a specified period;
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> (ii) that the restrictive covenant was an independent obligation which came into operation only when the agency was terminated and that part of the compensation which was attributable to the restrictive covenant was a capital receipt and hence not taxable."

In this case since the compensation paid was severable, therefore, since part of it was connected with restrictive covenant, therefore treated as capital receipt and was apportioned accordingly.

(2) The decision of the Hon'ble Madras High Court in the matter of CIT v. Saraswathi Publicities (1981) 132 ITR 207 in which it was held :

> "The assessee had secured the rights for distribution and exhibition of advertisement films, with a right to enter into agreement with other persons for distribution and exhibition. The assessee entered into an agreement with B which had similar agreements with various firms for the purpose of seeing that the business of each other did not suffer by competition in certain States. The agreements were extended and modified. Under the agreement of 16-5-1965, the assessee agreed not to represent or otherwise do business in film shorts and any sort of advertisement on the cinema screen for Hindustan Lever Ltd. or Lintas Ltd. in the agreed area. The assessee had agreed also to Blaze "taking over and handling" the said business from 1-4-1966, and further agreed to refrain from carrying on the business with Hindustan Lever Ltd. or handle any film advertising business till the end of 1975. In consideration of these terms, Blaze agreed to pay the assessee a sum of Rs. 1,50,000. The assessee's claim that this amount was a capital receipt not liable to tax was negatived by the Income Tax Officer but upheld by the Appellate Assistant Commissioner and the Tribunal. On a reference :
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> Held, that as the receipt was referable to the restrictive covenant, it was a capital receipt not liable to income-tax."

(3) The order of the I.T.A.T., Mumbai Bench in the matter of ITO v. Anilkumar Rudra (1999) 71 ITD 96 in which the facts were that the assessee retired on superannuation and the employer entered into an agreement with him 10 months after the date of superannuation whereby the assessee was to

receive an amount of Rs. I lakh in return for a covenant not to accept employment with any other employer. It was held;

> "The amount was received as purely in lieu of a restrictive covenant which put fetters on the freedom of the assessee to engage in employment of his choice. The right surrendered by the assessee was only a personal right and not a proprietary right. The extinguishment of every type of right does not give rise to a capital gain. In the case of the assessee, the surrender of the right which was of a personal nature consequent to a restrictive covenant, did not involve the receipt of any income of the nature of capital gain and so the amount received by virtue of the covenant could not be regarded as even a casual receipt liable to tax.
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> Further, all receipts are not of an income nature liable to tax under the Act. While income' is of a very wide scope, the age-old distinction between a capital receipt and a receipt of an income nature cannot be ignored. When an amount is received by virtue of a restrictive covenant or in lieu of the loss of a potential source of income, it has to be regarded only as a capital receipt.
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> Hence, the Commissioner was right in deleting addition by holding the payment was in nature of capital, thus, not assessable in the hands of the assessee,"

(4) The order of the I.T.A.T., Calcutta 'E' Bench in the matter of Saroj Kumar Poddar v. Jt. CIT (2001) 77 ITD 326 in which it was held :

> "The agreement imposed a restraining duty on the assessee and did not expect any positive activity towards rendering of any services by the assessee to Gillette. There was no other clause in the agreement which might lead to a converse decision. Therefore, the payment under consideration was merely for the assessee undertaking the restraining obligations. The provisions of the non-compcte agreement were clear enough to convince any one about the real intention of the parties. Neither any where did the agreement spell out any positive services to be rendered by the assessee in favour of the Gillette or even ISP, nor was there anything on record to show that after execution of the said agreement, the assessee started performing such services. On the other hand, the facts of the case were clear enough that the position of the assessee with reference to ISP and Gillette remained the same; even after execution of the non-executive chairman of ISP not taking part in the day-to-day activities of the said company, which fact had been acknowledged by the assessing officer himself.
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> There was no room to suspect that in the guise of a restraining clause what Gillette wanted from the assessee was actual performance of any service of professional nature. Thus, the provisions towards receipt of the amount from Gillette being a part of the non-compete agreement and non-compete agreement merely providing certain restrictions on the assessee in the line of non-undertaking any competitive enterprise hampering with the interests of Gillette, the receipt must be considered to be directly

related to the said restrictive activities and could not be stretched to be pertaining to any other duties of the nature of active performances. Hence, the question of treating the receipt amount as professional income of the assessee could not arise at all. A receipt of this nature constitutes capital receipt in his hands."

(5) The order of the ITAT, Mumbai Bench 'B' in the matter of Asstt. CIT v. Prakash G. Heblkar (2002) 83 ITD 495 in which it was held :

"What was under consideration was a restrictive covenant which pertained to the future. The payment involved had a contingency attached to it, i.e., the restraint agreed to between the assessee and his former employer. The assessee was to refrain from soliciting and/or engaging his former employer's employees, as stipulated by the covenant, for a period of three years. As such, there was no infirmity in the impugned order of the Commissioner (Appeals) holding that the amount received by the assessee was a capital receipt and, hence, not taxable."

(6) M.R. Muchhala v. Fourth Income Tax Officer (1996) 56 TTJ (Mum) 504 :

"Income-Capital or revenue receipt-Assessee while selling its business as a going concern, also agreeing not to carry on any other business competing with that of the purchaser for a period of three years for a consideration of Rs. 2,00,000, and receiving a sum of Rs. 10,000 out of it-Amount having been received by the assessee on account of restrictive covenant is a capital receipt and not taxable Gillanders Arbuthnot & Co. Ltd v. CIT (1964) 53 ITR 283 (SC), CIT v. Best & Co. (P) Ltd. (1966) 60 ITR 11 (SC) and CIT v. Saraswati Publicities (1981) 132 ITR 207 (Mad) followed. (Para 18) Conclusion Assessee while selling its business as a going concern, also agreeing not to carry on any other business competing with that of the purchaser for a period of three years for a consideration of Rs. 2,00,000, and receiving a sum of Rs. 10,000 out of it; the amount having been received by the assessee on account of restrictive covenant, is a capital receipt and not taxable."

(7) CIT v. G.D. Naidu (1987) 165 ITR 63 (Mad) :

"Held, that so far as the cash compensation paid by the new partners referable to the assets and goodwill of the firm was concerned, the cash took the place of the assets of the partnership and the compensation paid for restrictive covenant not to carry on similar business for a period of five years was in the nature of a separate transaction unconnected with the business of the assets of the partnership. The Tribunal was right in its view that the total compensation paid by the firms to the old partners was for (a) the share in the assets, (b) the share of the goodwill, and (c) for the restrictive covenant and that the part of the amount referable to the acquisition of the share in the assets and the share of the goodwill would be on capital account as it was in the nature of an initial outgoing and the payment towards the restrictive covenant was on revenue account and it would not amount to an acquisition of an advantage of an

> enduring nature. The Tribunal was also right in its view that the amount received by the recipients was not liable to tax either as income or capital gain."

(8) Chelpark Company Ltd. v. CIT (1991) 191 ITR 249 (Mad) :

> "Held, that though, under the agreement, the benefit of the restrictive covenant was for a period of five years, from the terms of the dissolution deed as well as from the facts stated in the Tribunal's order that the partnership which was a potential competitor to the assessee had vanished and that the ex-managing director had also left India, it was clear that the assessee paid the amount to the partnership in order to ward off damaging competition from a potential competitor, resulting in the acquisition by the assessee of a right as well as protection to carry on its business activities as a whole for so long as the assessee carried on such business. Consequently, the payment by the assessee was in the nature of a capital expenditure and not revenue expenditure."

14. On consideration of the facts of the case and the case laws referred to above, we find that the assessing officer considering all the three agreements was of the view that the compensation received by the assessee through agreement dated 25-2-1999 not a non-compete fee which was essentially a part of the cost price paid by M/s. Hindustan Coca Cola (P) Ltd. for the purchase of business and other rights of M/s. Jammu Bottling Co. The assessing officer was also of the view that it should be added in the hands of the company M/s. Jammu Bottling Co. as it was a part of the sale consideration of the business by the said company. The assessing officer was also of the view that the amount paid by way of non-compete fee was, in fact, the sale consideration and was paid in the guise of this method to accommodate profits of the company. The assessing officer also tried to move before the Commissioner (Appeals) in the case of M/s. Jammu Bottling Co. to prove that the aforesaid amount has, in fact, belong to the company. The assessing officer, however, observed that the Commissioner (Appeals) vide order dated 9-1-2001 did not make addition of the amount of Rs. 1 crore, i.e., the amount received by the directors in the hands of the assessee-company. The findings of the Commissioner (Appeals) were confirmed by the ITAT, Chandigarh Bench vide order dated 16-7-2004, Therefore, the whole case of the assessing officer is demolished. The facts above clearly show that the view of the assessing officer was erroneous and as such it was not accepted in the case of M/s. Jammu Bottling Co. The Commissioner (Appeals) vide order dated 9-1-2001 in the case of M/s. Jammu Bottling Co. observed while allowing the appeal of the assessee that :

> "There was a possibility that after receiving the sale consideration for the business, the Directors could have started their own business as they had sufficient knowledge and experience in this line. Such an action on the part of the directors would have given a tough competition to the new company. It was to avoid this competition with the directors that the buyer company had entered a separate agreement with the directors. It may be mentioned here that the company and the directors arc scparate entities. Any agreement entered into with the company is not binding on the directors individually. Therefore, a separate agreement was signed for a price and the price was paid to the Directors to stop them from entering into any competition. In

view of this position, I hold that the amount of Rs. 3.8 crores was not a part of the sale consideration for the transfer of the business assets. It was paid to the directors individually and as such not liable to be included in the sale consideration."

15. The revenue department challenged the order of the Commissioner (Appeals) before the ITAT, Amritsar Bench in ITA No. 111 (ASR)/2001 in which ground No. 5 is taken to challenge the above findings of the Commissioner (Appeals). However, at the time of hearing of the appeal, this ground was not agitated before the Tribunal. The matter was decided by the In the ITAT, Chandigarh Bench and it was held that the amount of Rs. 3.8 crores, referred to in the ground was paid to the Directors of the Company and not to the Company. This ground of appeal of the revenue was rejected by the Appellate Tribunal. The findings of the assessing officer are thus to that extent set aside. The learned counsel for the assessee argued that the taxability of the amount was doubtful because of the contradictory finding of the assessing officer. We find force in the submissions of the learned counsel for the assessee. The assessing officer held that in case non-compete fee is not taxable as part of the sale consideration in the case of M/s. Jammu Bottling Co. then the same will be added in the hands of the present assessee. The findings of the assessing officer are not approved by the Commissioner (Appeals) as well as Appellate Tribunal and it was held that this cannot be part of the sale consideration of the assets of M/s. Jammu Bottling Co. and, therefore, the amount could not be included in the hands of the Company. The assessing officer as well as the Commissioner (Appeals) held that since there was agreement executed for the sale for goodwill and on going concern between M/s. Jammu Bottling Co. and M/s. Hindustan Coca Cola (P) Ltd., therefore, nothing is left to be sold. The whole basis of rejecting explanation of assessee therefore stands disapproved. The findings of the assessing officer are not relevant on those facts. Ultimately the Appellate Tribunal in the case of M/s. Jammu Bottling Co. taken a contrary view and did not approve the addition. Therefore, the genuineness of agreement between the parties could not have been disputed at this stage.

16. The agreement between the assessee and M/s. Hindustan Coca Cola (P) Ltd. dated 25-2-1999 provides that compensation to be paid by the above company to the assessee in a sum of Rs. 1 crore. Prior to it M/s. Hindustan Coca Cola (P) Ltd. entered into the agreement with M/s. Jammu Bottling Co. (P) Ltd. on dated 6-8-1998 for purchase of goodwill and executed agreement dated 7-12-1998 for purchase of business. The amounts are settled in that way. It is provided that the employees of the seller employed in the acquired business undertaking whose names have been given in Schedule 1.1 and who shall be given fresh employment in the services of the buyer on terms no less favourable than their existing terms and conditions of service pursuant to the agreement at the closing. Similarly, it is provided that the company shall deliver to the buyer approved undated non-compete agreements with Shri Harjit Singh Sahni, Shri Jitpal Singh Sahni and Shri T.S. Manocha (assessee) Directors of the seller to be effective and dated as of the closing date. It is also provided that the company shall get the duly dated non-competition agreement in favour of the buyer from the above directors including the assessee to be effective from the closing company. It is so provided in the business purchase agreements, copies of which are filed on pages 27 to 30 of the paper book and, therefore, execution of this agreement clearly provides that M/s. Jammu Bottling Co. not only sold its on going concern as well as goodwill of the company, was also under obligation to get the non-compete agreement to be delivered in favour of the buyer duly executed by its directors including the assessee. These clauses would show that the buyer not only wanted to purchase the

business and goodwill of M/s. Jammu Bottling Co. but also wanted that its working directors should also refrain from doing the competitive business with intention that the Directors should not disclose the business secrets to the other rival company. The assessee explained such competition between Pepsi and Coca Cola before the Commissioner (Appeals) but no findings have been given by the Commissioner (Appeals). In case the agreement could not have been executed between the assessee and the buyer M/s. Hindustan Coca Cola (P) Ltd., then the very purpose of sale of goodwill and purchase of on going concern agreements dated 6-8-1998 and 7-12-1998 would have been frustrated. M/s. Jammu Bottling Co. and its Directors including the assessee are having independent and distinct legal character. M/s. Jammu Bottling Co. cannot bind its Directors to execute the non-competition agreement in favour of the buyer without their consent to refrain themselves from doing the same business in competition with M/s. Hindustan Coca Cola (P) Ltd. Since the rights of the Directors cannot be curtailed by M/s. Hindustan Coca Cola (P) Ltd., therefore, they have their own right either to agree or not to agree with the terms of the buyer. The Commissioner (Appeals) in the case of M/s. Jammu Bottling Co. held that "There was a possibility that after receiving the sale consideration for the business, directors could have started their own business as they have sufficient knowledge and experience in this line. Such action on the part of the directors could have given a tough competition to the new company. The Commissioner (Appeals) further held that it was to avoid this competition with the directors that the buyer company had entered into an agreement with the director". This finding has been confirmed by the Appellate Tribunal in the case of M/s. Jammu Bottling Co. These findings would clearly prove that the agreement entered between the assessee and M/s. Hindustan Coca Cola (P) Ltd. were independent agreement and have nothing to do so with the sale of on going concern of M/s. Jammu Bottling Co. The learned counsel for the assessee in his submissions explained that the scope of agreement dated 25-2-1999 in which in clause (c) it is provided that "For purposes of this agreement, know-how shall mean all information (including that comprised in or derived from manuals, instructions, catalogues, booklets, data disks, tapes, source codes, formula cards and flow charts) relating to the acquired business undertaking and the services provided or products manufactured by the acquired business undertaking, know-how includes, without limitation, the knowledge of evolving, developing and systematically organising the marketing and distribution network for beverages". It is also provided in clause (d) that "At any time after the closing date, covenator shall not do anything which might prejudice carrying on the acquirer business undertaking". The learned counsel for the assessee further explained that the assessee is one of the promoters of the company M/s. Jammu Bottling Co. since 1975 and is actively engaged in the running of the business which is of Coca Cola Company of U.S.A. He has further submitted that Coca Cola delivers the special concentrate to be used in their strict control to maintain its integrity and security. Some of the know-how/standard supplied to this company are in the knowledge of the Managing Director and Joint Managing Director of the company. Some of the standards for taking business have been explained. It was, therefore, explained that on account of working experience of the assessee for this company for about 24 years, the assessee had developed a great knowledge about the marketing of this product as per the policies from U.S.A. company. It is, therefore, explained that due to his vast experience, M/s. Hindustan Coca Cola (P) Ltd. entered into an agreement with the assessee dated 25-2-1999 by which the assessee agreed that for five years from the date of closing not to disclose to any person for any purpose or use any know-how in any business or venture either directly or indirectly through any person, firm or company in the area of State of Jammu & Kashmir for above consideration. The

restrictive covenant in this agreement clearly shows that the assessee independently agreed and restricted himself from doing same business or profession to be carried out as well as not disclosing the know-how and business secret etc. to any rival competitor. The statement of the assessee was recorded by the assessing officer, copy of which is filed at page 74 of the paper book, in which also the assessee has explained that he has signed the agreements dated 6-8-1998 and 7-12-1998 of M/s. Jammu Bottling Co. as a witness. The assessee explained in his statement that he was not personally bound by the agreements dated 6-8-1998 and 7-12-1998. We find that the assessee was justified in explaining these facts before the assessing officer. As is held above, the assessee and the company are legal distinct entities and as such assessee was not bound by the terms of agreement of the company. These clearly proved that M/s. Hindustan Coca Cola (P) Ltd. entered into instant agreement with the assessee with idea that since the assessee is one of the working directors of M/s. Jammu Bottling Co., therefore, he may be refrained from doing same business or profession and not to disclose the know-how and other secret of the business to rival competitors so that the very purpose of purchase of business and goodwill of M/s. Jammu Bottling Co. could not be frustrated. The assessee himself entered into an agreement and agreed independently to non-compete agreement and restricted himself from doing the same business directly or indirectly and also from entering in the competitive business. It was, therefore, a personal restriction on the movement of the assessee from entering into the competitive business or to disclose any business secret to any third person.

17. The same matter in issue came for consideration before the Third Member of I.T.A.T., Delhi Bench in the matter of Shivraj Gupta v. Asstt. CIT (IT Appeal No. 4898 (Delhi) of 1998) in which point for reference was "Whether, on the facts and in the circumstances of the case, the amount of Rs. 6.6 crores received by the assessee from SWC is on account of handing over management and control of CDBI (which were earlier under the management and control of the assessee) to SWC as terminal benefit and is taxable under section 28(ii) of the Income Tax Act or same is exempt as capital receipt being non-competition fee by executing deed of covenant". The Third Member considered the facts of the case decided the point in favour of the assessee. His findings in para 34 are reproduced as under :

> "34. Now comes the second deed. SWC group realised the importance of assessee who had been in the same business of liquor and beer for more than 35 years and acquired expertise knowledge and specialisation in the same. They evaluated the worth of assessee and agreed to pay Rs. 6.6 crores if assessee undertakes not to come in the business in any manner for a period of ten years. Learned A.M. rightly observed that it was the perception of a businessman and none else but concerned businessman can be the best judge. Business expediency sometimes requires harsh decisions to be taken and this was one of such decision that SWC group realised that in case assessee is allowed to remain free to carry on the business in manufacturing and trading in IMFI and beer, it may cause threat to their company particularly CDBI and that too when assessee was having another concern M/s. Maltings Ltd. which was running in the same field. Assessee was at liberty to obtain licence in the same line. Keeping all these facts SWC group rightly took a decision to restrain the assessee from coming in their way in that line of business for a period of ten years and agreed

> to part with that amount of Rs. 6.6 crores. To argue that this amount was quite big and not in consonance with the amount of salary and other remuneration being received by the assessee from CDBI and other concerns is no criteria to take it as exorbitant amount being paid as it is perception of SWC group. Whatever they thought fit they did and Income Tax Authorities have no business to challenge their perception unless they bring on record anything to show that SWC group and assessee were in collusion to defraud them. No such evidence or material came on record to show that there had been any collusion in between assessee and SWC group. All these facts completely go in favour of the assessee and law also is towards the side of the assessee. The above deal was completely a restrictive covenant executed by the assessee for a consideration and that consideration is to be treated as capital receipt as laid down by the Apex Court and other High Courts as well as by different Benches of the Tribunal."

18. The learned Third Member considering the above was of the view that the assessee got this amount of Rs. 6.6 crores under restrictive covenant and that was a capital receipt not taxable and there was no colourable device adopted by the assessee in getting this amount and the case is not hit by the ratio of the decision of the Hon'ble Supreme Court in the case of McDowell & Co. Ltd. v. CTO (1985) 154 ITR 148 .

19. The I.T.A.T. Delhi Bench 'D' in the case of P.L. Lamba (HUF) v. Asstt. CIT (2005) 90 TTJ (Delhi) 388 considering various decisions of the different Benches of the Appellate Tribunal on the same matter in issue and considering the Board's Circular held that the receipt under non-competition agreement is capital receipt not chargeable to tax.

20. The I.T.A.T. Delhi Bench 'A' in the matter of Sunil Lamba v. Dy. CIT (2004) 83 TTJ (Delhi) 174 held :

> "The assessee was engaged in the marketing and distribution of ice-cream and other related products. Under an agreement, he assigned his rights of marketing to BBL with the conditions that he will not engage himself directly or indirectly in such activities for a period of 10 years not only in relation to the products of the affiliated concerns but of any other concern. A sum of Rs. 1 crore was received in consideration thereof. Such amount was, therefore, received under a restrictive covenant of not engaging himself directly or indirectly in the activities carried on by it. The amount being not taxable, it cannot be said that the order passed by the assessing officer was erroneous insofar as prejudicial to the interest of the revenue. Thus even on merits, the CIT was not justified in assuming jurisdiction under section 263. The order under section 263 is, therefore, quashed."

21. The assessing officer held that section 28(ii)(a) of the Income Tax Act is applicable in this case and treated that the compensation received by the assessee was on the termination of his services. However, we find that this section is not applicable to the case of the assessee as there was no employer-employee relationship between the assessee and M/s. Hindustan Coca Cola (P) Ltd. No

amount is paid to the assessee for terminating the terms and conditions of services even as per explanation of assessee all the employees of M/s. Jammu Bottling Co. were taken over by buyer except for working Directors.

22. We may refer to section 28(va) of the Income Tax Act which provides that the following income shall be chargeable to income-tax under the head "Profits and gains of business and profession", "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

(b) not sharing any know-how, patent, copyright, trademark, 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 ....."
>
> This section is inserted in the Income Tax Act by the Finance Act, 2002. At the most the assessing officer could have relied upon the aforesaid section for the purpose of taxing non-compete amounts in the hands of the assessee. However, the present appeal pertains to the assessment year 1999-2000 and aforesaid section is inserted in the Act with effect from 1-4-2003 and as such even this provision would not be applicable to the case of the assessee. Anyway the aforesaid provision in the Act would show that prior to insertion of this provision in Act, the non-compete fee received by the assessee on account of restrictive covenant was not taxable under the Income Tax Act. The assessing officer was, therefore, not justified in relying upon the provisions of section 28(ii)(a) of the Income Tax Act against the assessee in this case.

23. The above facts in this case clearly show that the assessee has restricted himself from doing business or profession of above nature because of the experience as explained above in the business of M/s. Jammu Bottling Co., therefore, it was independent restrictive covenant for a specific period. The assessee in lieu of restrictive covenant was paid a sum of Rs. 1 crore and as such the compensation which was attributable to the restrictive covenant was a capital receipt and hence was not taxable. The compensation in the case of the assessee is very specific from his independent agreement. The very object of the agreement was to avoid competition in all matters between the assessee and M/s. Hindustan Coca Cola (buyers). Therefore, the assessee lost earning assets for specified period. The decision of the Hon'ble Supreme Court in the case of Best & Co. (P) Ltd (supra) is, therefore, directly applicable to the above case alongwith other decisions referred to above in this order.

24. We may remind that the Hon'ble Supreme Court in the matter of CIT v. Durga Prasad More (1971) 82 ITR 540 held that :

> "though an apparent statement must be considered real until it was shown that there were reasons to believe that the apparent was not the real, in a case where a party

> relied on self-serving in documents, it was for that party to establish the truth of those recitals : the taxing authorities were entitled to look into the surrounding circumstances to find out the reality of such recitals;"

25. In the present case, the authorities below took the view that the amount of Rs. 1 crore was part of the sale proceeds of on going concern M/s. Jammu Bottling Co. In that garb it was observed that because of execution of the agreement for sale of business concern and goodwill, M/s. Jammu Bottling Co. had nothing to sale further. The authorities below, therefore, were of the view that the amounts should be taxed in the hands of M/s. Jammu Bottling Co. However, the findings of the authorities below were not approved by the Commissioner (Appeals) and the Appellate Tribunal in the case of M/s. Jammu Bottling Co. The authorities below as such even on giving adverse finding against the assessee could not find out other meaning of the agreement against the assessee.

26. Considering the above discussion and following rule of consistency, we are of the view that the authorities below have failed to prove that it was a case of collusive transaction. The receipt in the hands of the assessee is treated as capital receipt and as such the findings of the authorities below are set-aside, addition is deleted.

27. As a result, the appeal of the assessee is accordingly allowed.