(2001) 05 CAL CK 0007

Calcutta High Court

Case No: Income-tax Appeal No. 439 of 2000

Commissioner of Income Tax		APPELLANT
	Vs	
Saroj Kumar Poddar		RESPONDENT

Date of Decision: May 22, 2001

Citation: (2006) 200 CTR 616 : (2005) 279 ITR 573 : (2006) 151 TAXMAN 153

Hon'ble Judges: Y.R. Meena, J; Arunabha Barua, J

Bench: Division Bench

Advocate: Nijamuddin, for the Appellant; R.K. Murarka, for the Respondent

Final Decision: Dismissed

Judgement

Y.R. Meena, J.

This appeal is directed against the order of the Income Tax Appellate Tribunal dated May 22, 2000. The main grievance raised in this appeal that the Tribunal has committed a mistake by treating Rs. 8,00,00,000 as capital receipt and not a revenue receipt.

2. The assessee filed return on August 28, 1996, declaring total income of Rs. 21,95,010, and subsequently filed a revised return disclosing taxable income of Rs. 21,96,555. During the course of assessment, the Assessing Officer noticed that the assessee has disclosed a sum of Rs. 8 crores as receivable from Gillette Company, U.S., by virtue of "non-compete agreement" dated January 18, 1996, the assessee claimed that it should be treated as capital receipt arising from the assessee''s intellectual rights and as there was no cost to that asset there cannot be any capital gain tax also. The Income Tax Officer did not accept the claim of the assessee. He treated that amount as a professional receipt. In appeal before the Commissioner of Income Tax (Appeals), the Commissioner of Income Tax (Appeals) has also confirmed the view taken by the Assessing Officer. In second appeal before the Tribunal, the Tribunal has discussed the nature of receipt in the light of various decisions and held that the receipt is in the nature of non-taxable capital receipt.

3. Heard learned Counsel for the parties. Learned Counsel for the Revenue has submitted that there was no material on record to prove that the assessee could set up any competitive business carried on by Gillette. The non-compete agreement is a colourable device and that amount should be treated as revenue receipt.

4. Learned Counsel for the assessee has submitted that the assessee had earlier collaboration with Gillette Company to set up an industrial unit in India for manufacturing and marketing shaving blades and other shaving products manufactured by Gillette in the U.S.A. The Indian company known as M/s. Indian Shaving Products Limited (hereinafter referred to as "I.S.P.") was formed, in which the assessee remained as a non-executive chairman. However, Gillette continued to remain the major and dominant shareholder of ISP.

5. He further submits that between 1982 and 1996 the assessee acquired considerable knowledge and expertise in the field of manufacture of shaving blades and other products with special reference to the manufacturing process, sources of raw materials and the marketing of the products of Gillette. Therefore, the assessee was approached by some other concerns to assist and associate with them in setting up a rival unit in India for manufacturing similar products as are produced by Gillette. The assessee also brought to the notice of the Assessing Officer that one officer Mr. Udayan Bose, chairman of a London based company called Credit Capital Finance Corporation Ltd. (hereinafter referred to as "Credit"), manufacturers of "SCHICK" brand blades approached the assessee for setting up a unit for similar production which are produced by Gillette. A confidential letter dated December 15, 1994, from "Credit" addressed to the assessee, to this effect, was also produced before the Assessing Officer. Shri Bose was confident in the expertise of the assessee in this field and also the successful experience in working with Gillette and wanted the assessee to consider a similar arrangement with Credit company.

6. Learned Counsel further submits that the assessee thought it fit on moral grounds to inform Gillette Company of the position, Gillette Company requested and prevailed upon the assessee not to assist or associate with any new company or person or entrepreneur to produce in India similar product to those made by Gillette. Gillette entered into a "non-compete agreement" with the assessee on January 18, 1996, wherein the facts considered relating to the assessee having earned considerable expertise in the manufacturing and marketing of shaving blades and other products by virtue of his position as chairman of ISP, and the fact of the assessee having been approached by a rival concern, the desire of the Gillette Company was to retain the assessee''s support in relation to its international shaving products business in India and outside India, thereafter, the agreement was entered into between the assessee and Gillette. The relevant part of the agreement-dated January 18, 1996, which has been referred by the Tribunal, reads as under :

"In consideration of the premises and Gillette making a payment of Rs. 80 (eighty) million as stated in Clause 3 below, the covenantor (i.e., the assessee) undertakes that he shall not at any time during continuance of his office as chairman of ISP or for three years thereafter engage himself whether directly or indirectly and whether as owner, substantial shareholder (at least 5 per cent.) director, manager, consultant or in any other manner in any business which undertakes or is engaged in the manufacture, marketing or distribution of razors, razor blades, shaving systems or shaving preparations."

7. Now the question does arise whether on these facts it can be said that the payment under the "non-compete agreement" is a colourable device, as the assessee has not sold any assets.

8. The facts are not in dispute that the assessee had earlier collaboration with Gillette Company and M/s. India Shaving Products Ltd., was formed and that the company has set on the units to produce Gillette blades and other shaving products, that company was formed in 1982, the assessee was non-executive chairman of that company. Though the major shareholding was of Gillette Company, but the assessee being non-executive chairman of ISP acquired the expertise, knowledge in Gillette Company products such as knowledge regarding raw material from where it is available cheap and better quality, manufacturing technique of Gillette products and its market. He had gained this experience for a number of years that is from 1982 to 1996. The assessee has also produced the letter dated December 15, 1994, from Credit Capital Finance Corporation, which manufactures "SHICK" brand blades, addressed to the assessee wherein Credit Corporation proposed for similar type of collaboration with the assessee, as the assessee had with Gillette Company. No material has been brought on record by the Assessing Officer to support that the "non-compete agreement" is a colourable device. In view of these undisputed facts we find no reason to disturb the finding of fact of the Tribunal that the agreement is not a colourable device.

9. Now this brings us to the question whether this amount, which was receivable under the agreement by the assessee from Gillette, should be treated as a revenue receipt or a professional receipt.

10. A similar type of questions has been considered by various High Courts including the Supreme Court. The Tribunal has also referred to some of the decisions on the issue wherein the courts have expressed the view that this type of receipt cannot be treated as a revenue receipt or income.

11. In Commissioner of Income Tax, Madras Vs. Best and Co., , the respondent was a company carrying on business including distribution of their explosives of Imperial Chemical Industries (Exports) Ltd., Glasgow. The Imperial Chemical Industries (Exports) Ltd., Glasgow, decided that all its agencies in India should be taken over by the Imperial Chemical Industries (India) Ltd., and gave notice to the respondent

terminating the agency from April 1, 1948. On termination of the agency some compensation has been paid which includes the compensation for undertaking of the assessee, that assessee for five years shall refrain from selling or accepting any agency for explosives competitive with those covered by the agency agreement. The question before their Lordships whether the amount of compensation for the "non-compete agreement" is a revenue receipt. Their Lordships held that receipt is a capital receipt and not taxable. At page 22 their Lordships observed as under :

"In the present case, the covenant was an independent obligation undertaken by the assessee not to compete with the new agents in the same field for a specified period. It came into operation only after the agency was terminated. It was wholly unconnected with the assessee''s agency termination. We, therefore, hold that that part of the compensation attributable to the restrictive covenant was a capital receipt and hence not assessable to tax."

12. In GILLANDERS ARBUTHNOT and CO. LTD. Vs. COMMISSIONER OF Income Tax, CALCUTTA., , the issue before this Court was that the compensation received on termination of several agencies, as consideration for termination, whether the receipt in the form of compensation should be treated as capital receipt. This court held that as the undertaking not to engage in a competitive business was not given, no part of the compensation money was received by the asses-see on condition not to carry on competitive business in explosives, consequently no part thereof was exempted from the Income Tax Act.

13. In Commissioner of Income Tax, Bombay City Vs. Bombay Burmah Trading Corpn., Bombay, , the issue before their Lordships was what should be the nature of compensation received against termination of lease of cutting and removing timber. Their Lordships held that the amount of compensation receipt is a capital receipt.

14. In Commissioner of Income Tax Vs. Saraswathi Publicities, , the issue before the Madras High Court was what should be the nature of the compensation received under the agreement to refrain from carrying on competitive business. The Madras High Court, following the decision of their Lordships of the Supreme Court in the case of Commissioner of Income Tax, Madras Vs. Best and Co., , has taken the view that the amount of compensation is a capital receipt and not liable to Income Tax.

15. In Commissioner of Income Tax, Bombay City-I Vs. Automobile Products of India Ltd., the assessee was manufacturing diesel engines in collaboration with a foreign company. Due to paucity of foreign exchange the assessee has transferred its undertaking and given up the licence for manufacture of engines to some other company. The giving up of the licence has affected the profit making structure of the assessee''s business for that he received the payment against the loss of opportunity to make profits under the collaboration agreement taken in conjunction with industrial licence. The court held that the amount received as compensation is a capital receipt.

16. In Commissioner of Income Tax Vs. Late G.D. Naidu and Others (By Lrs. G.D. Gopal and Another), , the dispute before the Madras High Court was that the compensation received by the assessee for not carrying on bus business for five years, whether the payment was "restrictive covenant" is a revenue receipt. The deceased and his son along with others were partners in five different firms carrying on business. During the year 1963-64 relevant for the assessment year 1964-65, all the old partners of the firms retired in stages so that by April 1, 1964 all the various firms were composed of entirely new groups of partners. The deceased and his son were paid varying amounts by the various firms to ward off competition from them in regard to the bus service business.

17. The firms in their assessments claimed this amount as revenue expense. The assessee (deceased and his son) claimed that the amount received from the various firms towards restrictive covenant is not taxable as it is a capital asset. The Madras High Court has taken the view that the amount of compensation is not liable to tax either as income or capital gains.

18. From the decisions referred above it is made clear that if the amount of compensation has been received not to compete in business from the person who paid the amount, the amount received cannot be taxed as income.

19. The relevant part of the agreement reads as under :

"Whereas

(A) Pursuant to a promoters agreement entered into on August 4, 1982, between the same parties as are parties hereto the said parties promoted the incorporation of Indian Shaving Products Ltd. (''ISP'') which is now a public listed company engaged, in the manufacture, marketing and distribution of shaving products. In the course of promotion and subsequent operations of ISP the covenantor, who has maintained close contacts with the international management of Gillette and has acted continuously as chairman of ISPs board of directors, has acquired extensive and valuable experience of the shaving products industry both in India and abroad.

(B) Gillette owns a majority of the issued equity capital of ISP and is desirous of retaining the support of the covenantor in the further development of ISP''s operations in and exports from India. Gillette is also desirous of retaining the covenantor''s support in relation to its international shaving products business outside India.

(C) The covenantor has received direct and indirect approaches and proposals from other manufacturers and marketers of shaving products requesting his participation, collaboration or advice in India and also abroad in relation to projects and activities which would be competitive, with the interests of Gillette and ISP and the covenantor has declined such approaches in consideration of Gillette having agreed to compensate him as stated hereinafter.

(D) The covenantor has made Gillette aware of such approaches and the position which he has taken in response to them and the parties have jointly agreed that it is appropriate for Gillette to formalise the matter and to compensate the covenantor in return for his covenants as set out hereinafter.

Now, therefore, upon mutual considerations and covenants the parties have agreed as follows :

1. In consideration of the premises and Gillette making a payment of Rs. 80 (eighty) million as stated in Clause 3 below, the covenantor undertakes that he shall not at any time during continuance of his office as chairman of ISP or for three years thereafter engage himself whether directly or indirectly and whether as owner, substantial shareholder (at least 5 per cent.), director, manager, consultant or in any other manner in any business which undertakes or is engaged in the manufacture, marketing or distribution of razors, razor blades, shaving systems or shaving preparations.

2. The undertaking contained in Clause I shall extend throughout the territory of India and in all other countries in which Gillette from time to time has subsidiary companies engaged in the manufacture or sale of shaving products.

3. The said amount of Rs. 80 (eighty) million to be paid by Gillette to the covenantor shall be paid within six months from the date hereof."

20. As per the "non-compete agreement" dated January 18, 1996, the Gillette company shall pay Rs. 80 million, as consideration, to the assessee, in case the assessee gives an undertaking that he shall not at any time during the continuance of his office, as chairman of ISP or for three years thereafter engage himself whether jointly or individually whether as owner or substantial shareholder, director, manager, consultant or in any other manner in any business with any other person in manufacturing, marketing or distribution of razors, razor blades, shaving systems or shaving preparations which are the products of Gillette. That has left no doubt that the payment was for not to compete in business with the Gillette.

21. Learned Counsel for the Revenue has submitted that there was no material to show that the assessee was in a capacity to compete or to set up a new unit for the same products on the same technology as produced by Gillette in India.

22. Learned Counsel for the assessee has drawn our attention in para. 7 at page 13 of the Tribunal''s order, wherein the Tribunal found that the asses-see has proved that the letter dated December 15, 1994, of Shri Udayan Bose before the Assessing Officer and the Commissioner of Income Tax (Appeals) which indicates that the chairman of Credit Capital Finance Corporation Ltd., has approached the assessee to set up a joint venture in India to produce the similar type of items which are being produced by Gillette.

23. Even otherwise the finding of fact of the Tribunal was that the assessee had earlier collaboration with Gillette to set up an industrial unit in India for manufacturing and marketing shaving blades and other shaving products manufactured by Gillette in U.S.A. The unit was set up in the name of company known as M/s. Indian Shaving Products Ltd., and of that company the assessee was a non-executive chairman and working in that capacity. From 1982 to 1996 the assessee acquired considerable knowledge and experience in the field of manufacture of shaving blades and other products with special reference to the manufacturing processes, sources of raw materials and the marketing of the products of Gillette. By that background the assessee has a capacity to set up a new unit for the products, with association of any other company such as Credit Corporation and can come in competition in the market to compete with the Gillette Company in the market. The amount has been paid to the assessee not to compete or come in competition with Gillette or not to assist any other company to compete with Gillette in Indian market.

24. That left no doubt that the payment of the amount under the agreement dated December 15, 1996, has been paid to the assessee by Gillette Company to refrain from engaging himself whether directly or indirectly in any business which undertakes or is engaged in the manufacture or marketing or distribution of razor blades, shaving systems or shaving preparations. That amount cannot be taxed as revenue receipt, especially when no material has been brought on record by the Assessing Officer to justify that the agreement dated December 15,1996, is a colourable device.

25. In the aforesaid facts we find no infirmity in the order of the Tribunal.

26. The appeal stands dismissed.