IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI E BENCH, MUMBAI

[Coram: Shri Pramod Kumar AM and Shri Vijay Pal Rao JM]

ITA No. 3900/Mum/2010
Assessment year: 2006-07

Assistant Commissioner of Income Tax
Circle 18(4), Mumbai ***……Appellant***

Vs.

Savita N Mandhana ***……Respondent***
12A, Lotus Court, 5th floor
Dr Annie Besant Road, Worli
Mumbai 400 018 [PAN AFEPM7717B]

ITA No. 3878/Mum/2010
Assessment year: 2006-07

Savita N Mandhana ***……Appellant***
12A, Lotus Court, 5th floor
Dr Annie Besant Road, Worli
Mumbai 400 018 [PAN AFEPM7717B]

Vs.

Assistant Commissioner of Income Tax ***……Respondent***
Circle 18(4), Mumbai

Appearances:
Rajan Vora, a/w **Miral Sangharajka**, *for the appellant*
G P Trivedi, *for the respondent*

Order reserved on : July 14, 2011
Order pronounced on : October 7 , 2011

O R D E R

Per Pramod Kumar:

1. These cross appeals call into question correctness of the same order dated 26th February 2010 passed by the CIT(A) in the matter of assessment under section 143(3) of the Income Tax Act. 1961, for the assessment year 2006-07, involve interconnected issues and were heard together. As a matter of convenience, therefore, both of these appeals are being disposed of by way of

this consolidated order.

2. To adjudicate on these appeals, only a few material facts need to be taken note of. The assessee before us was a shareholder in Mandhana Exports Pvt Ltd – a closely held company owned and managed by Mandhana family for a number of years. In the year 1996, the assessee company entered into a joint venture arrangement with Bornemann and Bick GmbH, Germany, under which 50% of the 50% of Equity shares were allotted to this German company and the name of the company was changed to Mandhana Boremann Industries Pvt Ltd ('Mandhana Boremann', in short) . As this German company was acquired by a Dutch company by the name of Paxar BV, the shareholdings in Mandhana Boremann were transferred to Paxar BV. In the relevant previous year, Paxar BV acquired all the shares held by Mandhana family for a consideration of Rs 570 per share which worked out to Rs 45.60 crores for the shares held by Mandhana family. All the shareholders in Mandhana family entered into an agreement with Paxar BV for the purpose of this transfer of shares, and one of the clauses in the agreement also provided that the transferor shall not carry on, or be interested in, any business which competes with the business of Mandhana Boremann. On these facts, the Assessing Officer held that a part of the sale consideration of Rs 570, a part of the consideration is attributable to the non compete consideration which is liable to be taxed in the hands of the assessee under section 28(va) of the Act. The Assessing Officer computed the value of shares, by break up method, at Rs 365. Accordingly, the balance amount of Rs 205 per share was treated as towards non compete fee and brought to tax as business income under section 28(va) in the hands of the assessee. Aggrieved, assessee carried the matter in appeal before the CIT(A) but without complete success. Learned CIT(A) upheld the action of the AO in principle, but held that only Rs 41 per share can be attributed to non compete fees. The CIT(A) further held that decision of a coordinate bench in the case of Hami Aspi Balsara Vs ACIT (30 DTR 576) does not help the assessee as there is specific mention of the non compete obligations in the share sale agreement, and, therefore, a part of the sale consideration is to be attributed to the non

compete obligations. None of the parties is satisfied. While the Assessing Officer is aggrieved of the partial relief given by the CIT(A), the assessee still maintains that no part of the consideration can be attributed to the non compete fees.

3. We have heard the rival contentions, perused the material on record and duly considered factual matrix of the case as also the applicable legal position.

4. We find that, even in the case of Hami Aspi Balsara (supra) there was a specific non compete obligation and yet the coordinate bench was of the view that no part of the sale consideration of shares could be attributed to be taxed in the hands of the assessee as business income under section 28(va)– as is clearly discernable from the following observations made by the coordinate bench:

> ***The A.O has determined the book value of shares and has treated the difference between the sale price of shares and its book value as consideration towards non-compete fees. Admittedly, in the share purchase agreement no consideration was assigned towards non-compete fees and the parties had entered into the share purchase agreement after mutually settling the price of shares. The A.O. has primarily relied on Article 11.1 of the share purchase agreement to infer that assessee had paid amount towards non-compete fees. Article 11.1 reads as under:-***
>
> ***"In consideration of the Purchase price received by the Sellers under this Agreement, the sufficiency of which is hereby acknowledged, the Sellers agree that for a period of 5 years from Completion, the Sellers shall not be engaged in any of the Restricted Business in India."***
>
> ***This clause clearly shows that in the purchase price of shares, consideration towards Restraint Clause was embedded. But the same was not specifically mentioned in the Share Purchase Agreement, As rightly pointed by the ld. Counsel for the assessee, non-compete fees***

could be payable primarily with respect to manufacturing company viz. Balasara Home Products. As regards other two IPR companies viz. Balasara Hygiene Products and Besta Cosmetics, since value of IPR was not reflected in the balance sheet, which constituted major part of the share price, the same had to be determined before arriving at the true book value of share of these two companies. The A.O. has computed approximately 80% of the consideration towards non-compete fees which, in any case, is not in conformity with the settled principles of valuation of shares. Therefore, we are of the opinion that the basis adopted for assigning consideration towards non-compete fees was not correct. Now the question would be how to assign the consideration towards non-compete fees. We really do not need to enter this area particularly because the difference, between the sale price of share and the true book value of the share, if allocated towards non-compete fees, was to be computed u/s.55(2)(a). This would be clear from subsequent discussions. Admittedly, assessee on her own was not carrying on business and it was the company in which she was share holder was carrying on the business. Section 55 2(a) reads as under:-

"Section 55(2)(a)

" (a) in relation to a capital asset, being goodwill of a business [or a trade mark or brand name associated with a business] [or a right to manufacture, produce or process any article or thing] [or right to carry on any business], tenancy rights, stage carriage permits or look hours, -"

Thus, it is evident that where capital asset is in the nature of right to carry on business, then the same will come within the ambit of capital gain tax.

Section 28 (va) reads as under:-

Section 28 (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

(b) Not sharing any know-how, patent, copy right, 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, which is chargeable under the head "Capital gains",

Thus, section 28 (va) would be attracted where the assessee was carrying on business and not where assessee only had right to carry on business in the form of capital asset. Further as per Circular No. 763 dated 18/2/1998 by Finance Act, 1997 the amendments were made in section 55(2)(a) of the Act to bring extinguishment of right to manufacture, produce or process any article or thing or right to carry on any business within the ambit of capital gain tax. Similarly Circular No.8 of 2002 dated 27/8/2002 explaining the provisions of Finance Act, 2002 by which clause (va) was inserted in section 28 of the Act, clarifies that receipts for transfer of rights to manufacture, produce or process any article or thing or right to carry on any business, which are chargeable to tax under the head capital gain would not be taxable as profits and gains of business. Thus, the difference between the sale consideration and true value of shares was chargeable as capital gains. ……..

5. Respectfully following the esteemed views of the coordinate bench, with which we are in respectful agreement, we hold that the amounts held to be attributable to non compete obligations are taxable as capital gains and not as business income. To this extent, we hold that the order of the CIT(A) is indeed vitiated in law, and, to that extent, that grievance of the assessee must be upheld. There is no dispute that the assessee has already included entire consideration for sale of shares, including what could be attributed to non compete obligations, as capital gains. In this view of the matter, the exercise of bifurcation between consideration attributable to sale of shares and for non compete obligations is rendered academic and infructuous. We may also add that it is not even in dispute that the assessee before us was not actively

engaged in the business and so far as the assessee actively engaged in the business is concerned, it has been stated at the bar that income attributable to non compete obligations has been offered to tax as business income, but then, given the uncontroverted position that the assessee was not actively engaged in business, it is not really necessary to examine that aspect of the matter any further. The stand of the assessee, in treating entire consideration received on sale of shares as taxable under the head 'capital gains' must therefore be upheld.

6. For the detailed reasons set out above, and respectfully following the coordinate bench in Homi Apsi Balsara's case (supra), we hold that the entire consideration has been rightly offered to tax under the head capital gains. The partial relief granted by the CIT(A), by reducing the quantum of amount attributable to non compete obligations, is thus rendered academic and infructuous. The grievance and the stand of the assessee, on the other hand, is upheld.

7. In the result, while appeal of the assessee is allowed in the terms indicated above, appeal of the revenue is dismissed as infructuous. Pronounced in the open court today on 7th day of October, 2011.

Sd/-	**sd/-**
(Vijay Pal Rao)	**(Pramod Kumar)**
Judicial Member	Accountant Member

*Mumbai; **7th** day of **October, 2011**.*
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1. *The appellant,*
2. *The respondent*
3. *Commissioner , Mumbai*
4. *Departmental Representative, E bench, Mumbai*
5. *Guard File*

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By Order etc.

Assistant Registrar
Income Tax Appellate Tribunal
Mumbai benches, Mumbai