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IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH 'D' MUMBAI

BEFORE SHRI B.R.MITTAL, JUDICIAL MEMBER
SHRI T.R.SOOD, ACCOUNTANT MEMBER

I.T.A.NO.3857/Mum/2009 – A.Y 2006-07

The Asst. Commissioner of I.T. 4(2), Mumbai.	Vs.	Shri Devang N. Kamdar, 9, Ram Vatika Prarthana Samaj Road, Vile Parle (E), Mumbai 400 057. **PAN: AAFPK 0778 A**
(Appellant)		(Respondent)
Appellant by	:	Shri C.G.K.Nair.
Respondent by	:	Shri Vijay Mehta.

Date of Hearing: 15-3-2012.

Date of Pronouncement: 22-03-2012.

O R D E R

Per T.R.SOOD, AM:

In this appeal, revenue has raised the following grounds:

1."on the facts and in the circumstances of the case and in law, the Ld. CIT(A) erred in treating the agreement between the assessee and Sharekhan as on principal to principal basis in spite of the fact that the assessee was only a sub broker of Sharekhan and hence was only an agent of Sharekhan.
2. "On the facts and in the circumstances of the case and in law, the Ld. CIT(A) erred in treating the amount of Rs. 1,11,00,000/- received by the assessee as capital receipts and allow exemption u/s. 54EC in spite of the fact that the receipts of Rs. 1,11,00,000/- were revenue in nature."
3. "On the facts and in the circumstances of the case and in law, the Ld. CIT(A) erred in not applying sec the revenue receipts of Rs.1,1 1,00,000/- by the assessee as an agent of Sharekhan."

2. After hearing both the parties, we find that during the assessment proceedings AO noticed that assessee has declared long term capital gains of Rs.1,11,00,000/-. This receipt was on account of

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goodwill sold to Sharekhan. It was further noticed that assessee was carrying on some broking business with Sharekhan from 1997 and had about 1800 clients. This business was transferred to Sharekhan w.e.f. 30-1-2006 and for the transfer of goodwill at Rs.1.11 crores was paid by Sharekhan. Further since the cost of goodwill was nil and assessee had purchased the capital bonds, assessee claimed deduction u/s.54EC. The AO Perused the sub-broking agreement and noted that vide clause 8(e) assessee could not execute any transaction for sale and purchase of securities for the initial period of three years except through the transferor i.e. Sharekhan. On the basis of this and some other clauses, AO concluded that assessee's argument that assessee has sold the goodwill could not be accepted because of the following reasons.

> (i) The assessee, it may be borne in mind, was the sub broker of ShareKhan for past 8 years and that too under a contract. This agreement has superseded the agreement dt.24.1O.1997 between Sharekhan and the assessee. Thus there has been termination of a agreement.
>
> (ii) During the year, the Stock Exchange changed the rules of the Share trading. No Sub-brokers allowed to issue the bills. The stock exchange, during this year, revived the institution of remisier under its rule, byelaws and regulations. A remisier is a person who is engaged by a member primarily to solicit business in securities on a commission basis. The rules no.216 to 235 of the Rules, byelaws, regulations of the exchange provide for appointment and regulation of remisiers. The remisiers appointed by the members are required to registered with the Exchange. A remisier is /expected to solicit the business for the member and get commission thereon. He is not supposed to issue contract notes, confirmation memos or bills to the clients in his own name.

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He observed that since there were changes in the regulations and assessee no more could act as a sub broker, therefore, assessee could not have continued his business and accordingly there was no question of transfer of goodwill. Accordingly, he taxed the sum of Rs.1.11 crores u/s.28(ii)© by treating the same as termination of agency.

3. Before the CIT(A) it was mainly submitted that assessee was acting on principal to principal basis with Sharekhan because assessee was working on behalf of his clients for purchase and sale of shares and securities. Reference was made to the Indian Contract Act for the definition of Agency and it was pointed out that for holding an agency a person must be appointed by another person as a agent to represent the principal with the third parties. Since by becoming the sub broker assessee was not representing Sharekhan to the third parties because assessee could not bind the principal which was not permissible under the agreement of sub-brokership. The Ld. CIT(A) agreed with these submissions and decided the issue in favour of the assessee vide para 4.3 which is as under:

> :4.3. I have gone through the order of the A.O. and submission of the appellant. The appellant was a sub-broker of Sharekhan and the relationship between Sharekhan and appellant was on principal to principal basis and the termination of the agreement between Sharekhan and the appellant was termination of agreement of two principals. The relationship between a broker and sub-broker is not that of a principal or agent but the relationship is that of two principles. The sub-broker does not work on behalf of the broker but he solicits business from the clients and in turn provides business to the broker and the brokerage is shared between the sub-broker and the broker. The sub-broker is responsible for his own action and the

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> appellant has correctly pointed out he cannot bind Sharekhan for his actions. The action of the A.O. to treat the appellant as agent of Sharekhan is found to be not correct. As the amount of Rs.1,11,00,000/- was paid as compensation by the Sharekhan for trading infrastructure of business of the appellant, and the amount was received by the appellant as an agent but, the provision of section 28 (2)(e) s not a applicable. The A.O. is directed to treat the amount of Rs.1,11,00,000/- as capital receipt and assess income under the head "Income from Capital Gain" and allow exemption u/s.54EC after verifying that the appellant has fulfilled the conditions provided in section S4EC. Ground 4 is allowed."

4. Before us, Ld. DR strongly supported the order of the AO and submitted that in fact during the year there was a change in the regulations and it was no more possible for the assessee to act as a sub broker. The assessee could have acted only as a remisier which is expected to solicit the business for members and get commission from them. Therefore, there was no question of selling such clients and receive the receipt of the goodwill.

5. On the other hand, Ld. Counsel of the assessee reiterated the submissions made before the first appellate authority and then invited our attention to the provisions of sec.28(ii)©. He argued that for invoking this provision, the main requirement is that a person who is in receipt of some payment should have held an agency in India, but assessee never had any agency. In this regard he referred to the agreement entered into with M/s. Sharekhan Ltd. on 24-10-1997, copy of which is placed at pages 4 to 11 of the paper book. He referred to clause-2 and pointed out that the assessee was entitled to conduct his business on behalf of his clients as a sub broker, which basically means

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conducting of business from principal to principal basis and it cannot be called an agency agreement. As per clause=18 both the parties had the right to terminate this agreement at will. He also referred to the agreement for sale of goodwill, copy of which is available at pages 12 to 23 of the paper book and invited our attention to recitation clauses © and (e), which clearly state that assessee was running his business under the name and style of 'Dev Investments' and had agreed to sell tangible as well as intangible assets for a consideration of Rs.1.17 crores [consisting Rs.6,00,000/- for tangibles and Rs.1.11 crores for intangible assets]. He argued that AO has un-necessarily laid emphasis on the change of regulations by which assessee could no more act as a sub broker but only as a remisier. In fact, by change of regulation, the only change which was made was that from the effective date of change the sub brokers were restricted not to issue contracts in their names and contracts were to be issued by the main brokers and payments were also to be made and received by the main brokers and sub brokers were designated as the remisiers and they were still entitled to the brokerage in respect of the business conducted by such sub brokers on behalf of their clients. Therefore, by change of regulation the business has not changed. The assessee has simply sold his assets including the tangible assets and charged a sum of Rs.1.17 crores for transferring the net worth of 1800 clients and, therefore, it

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was simply a case of sale of tangible assets along with the intangible assets and it cannot be termed as termination of the agency.

6. We have considered the rival submissions carefully and find force in the submissions of the Ld. Counsel of the assessee. Section 28(ii© reads as under:

> **28.**(*ii*) any compensation or other payment due to or received by -
> (*c*) any person, by whatever name called, holding an agency in India for any part of the activities relating to the business of any other person, at or in connection with the termination of the agency or the modification of the terms and conditions relating thereto ;

A plain reading of the above provision clearly shows that any compensation or any other payment which is received by a person by whatever name called for holding an agency or in connection with the termination of such agency, the main ingredient of the provision is that such payment should be made by a principal to an agent. Whether the assessee was an agent or not can be deciphered from the sub-broking agreement entered into by the assessee on 24th October, 1997. Clause 2 of the agreement reads as under:

> "2) The sub-broker may conduct business on behalf of his client with the member broker as may be mutually agreed upon and subject to such conditions as may be agreed to mutually between the member broker and the sub-broker. Such agreement shall not contravene any provisions of this agreement and said rules and regulation."

The above clearly shows that the assessee who was described as a sub broker was to conduct the business on behalf of his clients. The sub broker mainly places order for purchase or sale of shares and securities with the main broker. The main broker would charge a brokerage to

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the sub broker and the sub broker is free to charge any amount of commission subject to maximum prescribed under the SEBI Regulations by adding on his margin. Therefore, this arrangement cannot be termed as arrangement of an agency. The assessee cannot bind principal by his act and he would remain bound to his clients by his actions. Binding of the principal is main ingredient for constitution an agency which is not there in the agreement of sub brokership is clear from the above clause (2). Clause 18 of the agreement reads as under:

> "18) Either party shall be entitled to terminate this agreement at will and without giving any reasons to the other party notice in writing of not Less than six months a their respective addresses mentioned above. The above shall also be intimated to stock exchange and SEBI"

The above clearly shows that both parties had right to terminate the sub-brokership agreement at will by giving a six months notice.

7. It is further noticed that assessee had transferred not only his intangible assets but also tangible assets which becomes clear from clauses © and (e) of the agreement which read as under:

> "© The transferor carries n the business of sub-broking from said Office Premises in the name and style of 'Day Investments" (hereinafter referred to as 'the said Undertaking'). In the' course of its/his, the Transferor has developed a network of over 1,800 (One Thousand Eight Hundred) clients including, Inter alia, corporates, high networth individuals etc."
>
> (e) Pursuant to the discussions which have taken place between the parties hereto, the Transferor' has agreed to sell, assign and transfer to the Transferee, and the Transferee has agreed to purchase and acquire from the Transferor, certain tangible and Intangible assets of the said Undertaking more particularly listed out andscrlbedTn the SCHEDULE hereunder written, at the consideration and on 'the other

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> terms and conditions mutually agreed upon. The aforesaid assets which are more particularly listed out, and, described in para A of the SCHDULE are hereinafter collectively referred to as "the said Tangible Assets" and the aforesaid assets which are more particularly listed out and described in para B of the SCHEDUIT.E are hereinafter collectively referred to as "the said Intangible Assets". The said tangible Asses the said Intangible Assets are hereinafter collectively referred to as "the said Assets". It is hereby expressly provided that the said Tangible Assets do not include the said Office Premises".

Clause (e) makes it clear that assessee has sold assets as per Schedule and the Schedule shows that assessee had agreed to sell furniture and fixtures, computer and printers, office equipment etc. along with the intangible assets consisting of net worth of 1800 clients and trained men power as well as research report and credit risk assessment procedures etc. The assessee had agreed to sell furniture, computer etc., i.e. intangible assets which included net worth of 1800 clients, research reports, well trained employees, credit risk assessments etc. Thus it is clear that assessee has sold the whole of the business and, therefore, the compensation received on sale of such business cannot be called compensation for termination of the agency. The net worth of 1800 clients along with trained men power and research report etc., would definitely constitute an intangible assets which have been sold by the assessee.

8. We further find that AO has decided this issue against the assessee on the basis of his main observation which is at para 5.4 which reads as under:

> "5.4 As already discussed above, the assessee was the exclusive sub broker of Sharekhan and an agreement to this effect was signed between the Sharekhan and Dev Investment whose proprietor was Shri.

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Devang Kamdar. On january,2006, the SEBI vide its circular__no.9(SEBI/MRD/MIRSD/DPS-1/CIR-31/2004) dated 26th .\ugust,2004 has prescribed a model format for broker, sub broker and clients. The requirement relating to tripartite agreement was to come into effect 01.12.2004 and was extended up toJan,2005 ride SEBI circular no.41 dt.24.ll.2004 and further extended vide Circular No..44 dt.29.12.2004 . From the above scheme, the assessee could not carry on the business of share broker for Sharekhan and thus his agreement with Sharekhan dated 24-10-1997 terminated. The assessee had no other option but to link himself with some other member broker and re negotiate the terms and conditions for further conduct of the business in the same line, while on the other hand Sharekhan saw this an opportunity for development and expansion of its business as narrated earlier [in Sharekhan's own words]. Share Khan was parting with money to keep his flock together in the competitive environment. Thererore, Sharekhan with a view to compensate the assessee and use his services , compensated him with Rs.1 .11 Cr and also took Mr.Devang Kamdar, the assessee into its fold as its salaried employee along with 10 other personnel. In these circumstances, the said amount is a compensation for cessation of an agency agreement dated 24.10.1997. The Income Tax Act in its definition of profits & gains of business /profession has included such compensation as one chargeable under the head "profits & gains of business/profession".

We find that when a person was allowed to act as sub broker, he was initially allowed to issue even a contract note to his clients. Moreover, such sub broker could receive payments from clients and make payments to clients from his accounts. This position was changed vide Circular No.9 (SEBI/MRD/MIRSD/DPS-1/CIR-31/2004) dated 26th August, 2004 as noted by the AO. But by this change assessee could still act as a remisier and the only restriction is that now he cannot issue the contract note for any transaction which has to be issued by the main broker. Even the payments were to be received and made by the main broker. However, assessee still remained entitled to his commission which was to be shared by the main broker with such remisier. Therefore, the assessee even after the change of regulation

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could have still acted and could have shared the commission with the main broker i.e. Sharekhan or he could have changed his broker or even he could have himself become a member of the stock exchange because he had a large client basis. Simply because assessee preferred to sell his business along with tangible assets would not mean that the agreement would become that of an agency. It still remained an agreement between a principal to principal. Therefore, in our opinion, it is a clear case of sale of assets and the Ld. CIT(A) has correctly decided the issue and accordingly we confirm his order.

9. In the result, revenue's appeal is dismissed.

Order pronounced in the open Court on this day of 22/3/2012.

Sd/-	Sd/-
(B.R.MITTAL)	**(T.R.SOOD)**
Judicial Member	**Accountant Member**

Mumbai: 22/3/2012.
P/-*