



* IN THE HIGH COURT OF DELHI AT NEW DELHI

+ ITA No. 728 of 2009

% Decided on : July 29, 2009

Commissioner of Income-Tax-II
New Delhi

. . . Petitioner

through :

Mr. Sanjeev Sabharwal with
Mr. Mohan Prasad Gupta,
Advocates

VERSUS

Mandalay Investment Pvt. Ltd.

. . . Respondent

through :

Mr. K. Sampath with
Mr. S. Krishnan, Advocates

CORAM :-

THE HON'BLE MR. JUSTICE A.K. SIKRI

THE HON'BLE MR. JUSTICE VALMIKI J. MEHTA

1. Whether Reporters of Local newspapers may be allowed to see the Judgment?
2. To be referred to the Reporter or not?
3. Whether the Judgment should be reported in the Digest?

A.K. SIKRI, J. (ORAL)

1. Admit.

2. The following question of law arises for consideration :-

"Whether the amount of Rs.26 lacs received by the Assessee without impairment of the Capital Structure or mode of profession is a capital receipt?"

3. Thus the only question of law raised in this appeal relates to addition

of Rs 26 lacs received by the assessee. In the return filed by the



as income of the assessee. In appeal, order of the Assessing was reversed and the contention of the assessee that the aforesaid receipt was a Capital Receipt was accepted. The Revenue filed appeal thereagainst on this aspect, which has been dismissed by the Tribunal vide its impugned judgment dated 31.7.2008 affirming the view taken by the CIT (Appeal).

4. In order to appreciate as to whether the receipt in question is a Capital Receipt or Revenue Receipt, we may first state the nature of transaction under which the aforesaid amount was received by the assessee.
5. The assessee had entered into some arrangement with one Mr. Ronnie Screwvala. In fact, Mr. I.C. Malhotra, Director of the assessee company, had developed a retailing communication project for conducting research into retailing and marketing various consumer products via TV programmes. These consumer products were to be exhibited and demonstrated on television in an attempt to woo the customers through product information. A marketing and distribution network had to be developed, which was to be viewed through the cable operator to the household of all TV viewers. A network of warehouses was also to be set up in different cities to stock the products and dispatch the orders by VPP. As per this concept developed by the assessee the cable operators were to be



conceived this project and researched on it and thereafter prepared a feasibility report. In the transaction entered into between the assessee through Mr. Malhotra, its Director, and Mr. Ronnie Screwvala, the assessee agreed to sell this retailing communication project as well as the feasibility report to Mr. Screwvala and in consideration thereof he received the aforesaid sum of Rs.26 lacs. After the transfer of its rights in the aforesaid project in favour of Mr. Screwvala against the aforesaid consideration, the assessee also agreed for non-duplication of the said work. What it meant was that the assessee was thereafter not allowed to use or exploit the aforesaid concept or the project, which meant that the exclusivity contract was entered into between the parties as per which Mr. Screwvala, after buying the rights in the said project, had exclusive right to make use of and exploit that project.

6. This amount was received over and above the professional charges of Rs.26 lacs and Rs.5 lacs for direct expenses. Thus, after development of the aforesaid project, the assessee had received a sum of Rs.26 lacs. There is no dispute that the amount received as professional charges was shown as income and tax was paid thereupon. It is the additional sum of Rs.26 lacs which was received in giving up the rights by the assessee in the said project which has become the subject matter of dispute, viz. whether it is Capital or Revenue Receipt.



agreement, this amount of Rs.26 lacs was paid for ex contract over and above the professional charges of Rs.26 lacs and Rs.5 lacs for direct expenses, it is to be treated as a Capital Receipt. In arriving at this conclusion, the Tribunal has also observed that with the transfer of rights, the assessee is restricted from using or divulging any part of the retailing communication project and this restriction is for lifetime as per letter dated 23.9.1994 from Mr. Ronnie Screwvala to the assessee company, which was placed on record.

On these facts, the Tribunal was of the view that the case is squarely covered by the judgment of the Apex Court in the case of *CIT v. Best & Co. Pvt. Ltd.*, 60 ITR 11 (1966).

8. Mr. Sanjeev Sabharwal, learned counsel for the Revenue/appellant, submits that the Supreme Court in the case of *Kettlewell Bullen And Co. Ltd. v. Commissioner of Income-Tax, Calcutta* 53 ITR 261, has spelled out the test to determine as to whether the receipt in a particular case would be Revenue or Capital Receipt. He drew our attention to the following discussion in the said judgment :-

“Cases which have lately arisen before the Courts in the United Kingdom have elaborated this distinction. In *Commissioner of Inland Revenue v. Fleming and Co.* [33 T.C. 57], the Court, of Session held, following *Kelsall Parsons and Cos'* case [21 T.C. 608, 620], that compensation paid the assessee who carried on business as manufacturers' agent and general merchants and had acted as the sole agents since 1903 for certain products of the manufacturers for termination in 1948 of the agency at the instance of the manufacturers was regarded as revenue. In the view of Lord President Cooper the cases relating to determination of agencies, broadly speaking, fall on two sides



(b) "the cancellation of a contract which does not affect recipient's trading structure nor deprive him of any endu trading asset, but leaves him free to devote his energies and organisation released by the cancellation of the contract to replacing the contract which has been lost by other like contracts",

and held that the case fell within the second class, and not the first.

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It is manifest that the principle broadly stated in the earlier cases, that compensation for loss of officer, or agency, must be regarded as a capital receipt, has not been approved in later cases. An exception has been engrafted upon that principle that where payment even if received for termination of an agency agreement, the agency is one of many which the assessee holds, and the termination of the agency does not impair the profit-making structure, but is within the framework of the assessee's business, it being a necessary incident of the business that existing agencies may be terminated and fresh agencies may be taken, the receipt is revenue and not capital.

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On an analysis of these cases which fall on two sides of the dividing line, a satisfactory measure of consistency in principle is disclosed. Where on a consideration of the circumstances, payment is made to compensate a person for cancellation of a contract which does not affect the trading structure of his business, nor deprive him of what in substance is his source of income, termination of the contract being a normal incident of the business, and such cancellation leaves him free to carry on his trade (freed from the contract terminated) the receipt is revenue : Where by the cancellation of an agency the trading structure of the assessee is impaired, or such cancellation results in loss of what may be regarded as the source of the assessee's income, the payment made to compensate for cancellation of the agency agreement is normally a capital receipt."

9. The test which is laid down in the aforesaid judgment, as is clear from the portion extracted above, is that where on a consideration of the circumstances payment is made to compensate a person for




the assessee is impaired the same would be treated as a Receipt.

10. Even when we apply the aforesaid test to the facts of the present case, as discussed in detail above, it is clear that in the concept/intellectual property developed by the assessee through its Director, entire rights have been transferred by the assessee in favour of the transferee. After this transfer, not only the assessee has no right to use the same, the arrangement even restricts the assessee from sharing the said concept with anybody else.
11. Whether a receipt is a Capital or Revenue Receipt depends on the facts of each case and no hard and fast rule can be laid down for this purpose. In the present case, for the work undertaken by the assessee, the assessee was given remuneration of Rs.26 lacs apart from Rs.5 lacs as the expenditure. This amount was shown by it as Revenue Receipt and the tax paid accordingly. It is the further sum of Rs.26 lacs, which is the bone of contention. This sum is received by the assessee as lumpsum amount for giving up his entire rights in the aforesaid concept/intellectual property developed by him and in the circumstances of this case, has to be treated as a Capital Receipt.
12. The Supreme Court in the case of *Oberoi Hotel Pvt. Ltd. v. Commissioner of Income Tax*, 236 ITR 903, reiterated the test to



transaction is taxable income. But the difficulty arises in ascertaining whether what is received in a given case is compensation for loss of a source of income, or profit in a trading transaction. Where on a consideration of the circumstances, payment is made to compensate a person for cancellation of a contract which does not affect the trading structure of his business, nor deprive him of what in substance is his source of income, termination of the contract being a normal incident of the business, and such cancellation leaves him free to carry on his trade (freed from the contract terminated) the receipt is revenue : Where by the cancellation of an agency the trading structure of the assessee is impaired, or such cancellation results in loss of what may be regarded as the source of the assessee's income, the payment made to compensate for cancellation of the agency agreement is normally a capital receipt."

13. We are of the view that the Tribunal, in these circumstances, rightly relied upon the judgment of the Apex Court in the case of *Best & Co. (supra)* and distinguished the case of *Gillanders Arbuthnot and Co. Ltd. v. CIT*, 53 ITR 283 observing that the compensation paid for agreeing to refrain from carrying on competitive business in the commodities in respect of the agency terminated or for loss of goodwill was *prima facie* of the nature of a Capital Receipt.
14. We, thus, answer the question formulated above in favour of the assessee and against the Revenue, as a result whereof this appeal is dismissed.


(A.K. SIKRI)
JUDGE


(VALMIKI J. MEHTA)