(2012) 02 KAR CK 0021

In the Karnataka High Court

Case No : ITA No. 628 and 629 of 2004

CIT APPELLANT

Vs

Micronic Devices RESPONDENT

Date of Decision : 23-02-2012

Acts Referred:

Citation : (2012) 02 KAR CK 0021

Hon'ble Judges : Ravi Malimath, J;N. Kumar, J

Bench : Division Bench

Advocate : M.V. Seshachala, for the Appellant; S. Parthasarathi, P. Dinesh and K. Mallaha Rao, for the Respondent

Final Decision : Dismissed

Judgement

N. Kumar, J.—This two appeals arise of a common order of the Tribunal preferred by the revenue. Therefore, they are taken up for consideration together and disposed of by this common order. The assessee was carrying on the business of agency and development of software. It was a partnership firm. In respect of assessment ears 1995-96, the assessee filed return of income declaring income of Rs. 94,112 on 31-10-1995. Intimation u/s 143(1)(a) of the Act came to be issued. Thereafter, scrutiny assessment came to be completed u/s 143(3) of the Act by an order dated 30-9-1996. Thereafter, the assessing officer found that income liable to tax had escaped assessment. Therefore, he prescribed to reopen assessment u/s 147 of the Act. Notice u/s 148 was issued. The assessee filed a reply stating that income already filed may be treated as a response to the notice u/s 148 of the Act. In the course of reassessment proceedings, the assessing officer held that Rs. 2.97 crores paid to the assessee firm by the company had not been reflected in its accounts and the entire arrangement was fictitious and a colourable devise to avoid tax. Therefore, entire amount of Rs. 2.97 crores was brought to tax by an order dated 28-3-2002. The assessee preferred an appeal to the Appellate Commissioner. He contended that the said amount of Rs. 2.97 crores was paid to conduct agency business which was only a goodwill. The said contention was rejected by the Appellate Commissioner. He held that the entire transaction was a colorable device to describe the consideration of Rs. 2.97 crores as payment for non-competition and transfer of right to conduct agency business and to claim the same as capital receipt, not chargeable to capital gains. Therefore, he directed the assessing officer to tax Rs. 2.97 crores as long term capital gains on the sale of goodwill, inasmuch as, the cost of acquisition of the same has to be taken as ''nil'' as per section 55(2)(a) of the Act. Consequently, the finding of the assessing officer that the entire amount should be treated as revenue receipt was set-aside. Challenging the said order, the assessee preferred an appeal to the Tribunal. The revenue also preferred an appeal to the Tribunal challenging the said finding that the entire consideration should be treated as capital receipt. The Tribunal held that the entire reopening of assessment was at the instance of audit object and therefore, the assumption of jurisdiction for reopening of assessment was held to be invalid. Further, it was held that the balance sheet reflecting the sum of Rs. 2.97 crores and the retirement deed was before the assessing officer when the original assessment came to be passed and therefore it amounts to change of opinion. Further, it was held that the said company took over the entire business with all its assets and liabilities including goodwill. The sum of Rs. 2.97 crores was paid in composite manner for non-competition fee, goodwill and other assets. Having regard to the circumstances and the facts of the case, it was held that 75% of the above sum should be treated as non-compete fee and the rest towards goodwill and other assets. Against the said order, the assessee has not preferred any appeal. It is only the revenue which has challenged the said order.

2. The learned counsel for the revenue assailing the impugned order contended that the finding of the Tribunal for reopening assessment was passed on an audit objection and it amounts to change of opinion and accordingly is not valid in law, is erroneous. It is not based on audit objection. The assessing officer has independently applied his mind and because the said amount had escaped assessment, he has passed the order u/s 147, which is valid and legal. Therefore, the said finding requires to be set-aside. He further contended that there was no jurisdiction for the Tribunal to apportion 75% of the said amount as non-compete fee and consequently not liable to tax and for directing only 25% to be taxed as goodwill. Therefore, he submits that the impugned order requires interference. Per-contra, learned counsel for the assessee supported the impugned order. In the light of the aforesaid facts and the rival contentions, the substantial questions of law that arise for our consideration in these appeals are as under:

1. Whether the Tribunal was justified in holding that the reopening of assessment was based on audit objection and it constitute change of opinion and therefore, section 147 of the Act is not attracted?

2. Whether the Tribunal was justified in holding that the sum of Rs. 2.97 crores is paid in composite manner for non-compete fee, goodwill and other assets and

apportioning 75% of the said sum as non-competing fee and the rest towards goodwill and other assets?

Point No. 1

The facts are not in dispute. The assessee firm received Rs. 2.97 crores from the company which was one of the partners in the firm for transferring the agency business. Clause (5) of the Deed of Retirement provides that the parties hereto agree that the continuing partners shall not carry on the agency business and compete with Advance Micronic Devices (P) Ltd., in the line of business for a period of five years. Therefore, the deed of retirement contains a non-competing clause. In the entire retirement deed, there is no mention about transfer of goodwill. At any rate, there is no indication in the retirement deed how this amount of Rs. 2.97 crores is arrived at, in other words, what are its components. In the schedule to the balance sheet, this amount of Rs. 2.97 crores is shown as business asset. In the original order passed u/s 143(3) of the Act, the assessing officer treated this as amount received towards non-competing fee and did not levy any tax. It is after audit objection, this amount has come to light. As is clear from the order of the assessing officer, he looked into the accounts of the firm for the assessment years 1995-96. As the said amount was not shown as revenue receipt in the hands of the firm, said income escaped assessment. He has also noted that the company which paid Rs. 2.97 crores has claimed it as revenue expense and claimed adjustment in five equal instalments. Therefore, it is not a case where proceedings u/s 147 was initiated on the basis of audit objection. May be the audit objection made the assessing officer to open his eyes. Therefore, he has independently looked into the material and on being convinced that the said amount had escaped assessment, he has initiated the proceedings. It was contended that it is a case of two opinions and on that ground, reopening of assessment is not permissible. If it is a case of two opinions, certainly reopening on that ground is not permissible.

The reading of entire order u/s 143(3) of the Act do not disclose the application of mind by the assessing officer. He formed no opinion earlier and therefore, the question of changing his opinion, which was formed earlier do not arise. Therefore, the Tribunal was not justified in holding that the order of reassessment is bad on the ground that the basis for said order is audit objection and that the assessing officer has formed two opinions. On the contrary, it is a case of over-sight, inadvertence or mistake committed by the assessing officer and therefore, reassessment u/s 147 is permissible as held by this Court in the case of Commissioner of Income Tax and Another Vs. Rinku Chakraborthy, Accordingly, we set-aside the said finding recorded by the Tribunal and answer to first substantial question of law in favour of the revenue and against the assessee.

Point No. 2

The aforesaid facts set out above clearly demonstrates the firm/assessee had 15 contracts with Foreign companies and the firm derives income by way of commission and other changes from the said companies. In the reconstitution of the firm entered on 4-4-1994, the company was allowed to take this agency business exclusively and the company agreed to pay Rs. 2.97 crores on the condition that the firm should not carry on similar business for a period of five years. The material on record also disclosure after such transfer all the foreign companies gave agency to the company and the assessee/firm is but of the said business. Therefore, it is clear that on execution of deed of retirement, the company took over this agency business and the firm stopped doing agency business. Further, the material on record shows before said transfer, roughly Rs. 6.00 crores of the income was received by the firm as commission from the said agency business. Keeping that in mind, they were paid Rs. 2.97 crores as consideration for their non-carrying the business for a period of five years from the date of retirement. It is under these circumstances, the total consideration was paid by the company to the firm for taking over the entire agency business at Rs. 2.97 crores. The Tribunal was of the view 25% of the said consideration represents goodwill and other assets and 75% should be taken as non-computing fee. The need to apportion arose because the assessee had not given any particulars and the said amount was paid in composite manner towards non-competing fee, goodwill and other assets. Having regard to the nature of the business and that the foreign sellers are involved, we are of the view that, it is not a goodwill, it is denial of right to carry on the business, which should have a major share. Treating 75% as non-competing fee in the facts and circumstances of these cases appears to be just. Therefore, the same does not call for interference. Accordingly, second substantial question of law is answered in favour of the assessee and against the revenue.

No merit. Appeals are dismissed.

