IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO.675 OF 2018

Pr. Commissioner of Income Tax – 14, Mumbai, Room No.469, Aayakar Bhavan, M.K. Road, Mumbai – 400 020 ….Appellant

V/s.

Music Broadcast Private Limited, 5th Floor, RNA Corporate Park, Opp. Western Express Highway, Kalanagar, Bandra (E), Mumbai – 400 051 ….Respondent

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Mr. Suresh Kumar for appellant.
Mr. Dharan Gandhi for respondent.

CORAM : K. R. SHRIRAM AND
FIRDOSH P. POONIWALLA, JJ.
DATED : 9th AUGUST 2023

ORAL JUDGMENT : (PER K.R. SHRIRAM, J.) :

1 Respondent (assessee) filed return of income on 30th September 2008 for Assessment Year 2008-2009 declaring total loss to the tune of Rs.78,22,75,709/-. In the assessment proceedings, the Assessing Officer disallowed various amounts which included a sum of Rs.12,60,00,000/- and a sum of Rs.19,40,00,000/- that assessee had treated as revenue expenditure. Assessee filed an appeal before the Commissioner of Income Tax (Appeals) [CIT(A)] who, by an order dated 8th February 2013, partly allowed the appeal of assessee. The CIT(A) deleted the addition to the tune of Rs.12,60,00,000/- and allowed it to be treated as revenue expenditure and as regards the amount of

Rs.19,40,00,000/- upheld the findings of the Assessing Officer that it should be treated as capital expenditure but allowed depreciation on the ground that it was an intangible asset. Both Revenue and assessee filed an appeal before the Income Tax Appellate Tribunal (ITAT). The ITAT, vide its order of 25th January 2017, dismissed the appeal filed by Revenue and also the cross objections filed by assessee.

2 Assessee was earning its income mainly from advertising through the intermittent breaks of various programs that it was relaying in its radio station by the name “Radio City”. For procuring the advertisement from various clients, assessee had engaged Star India Pvt. Ltd. (SIPL). A dispute arose between SIPL and assessee resulting in assessee terminating the agreement with SIPL. While terminating the agreement, assessee paid a sum of Rs.12,60,00,000/- as compensation for Advertisement and Agency Sales Termination Agreement (ASTA) and a sum of Rs.19,40,00,000/- for Restrictive Covenant Agreement (RCA). The amount under RCA was paid for restricting SIPL for not competing against assessee in similar business for another 2 ½ years. The Assessing Officer disallowed the compensation paid for ASTA and RCA treating the same as capital expenditure within the meaning of Section 28(va) of the Income Tax Act, 1961 (the Act). The Appellate Authority, i.e., CIA(A), reversed the findings of the Assessing Officer as regards ASTA on the basis that as per original agreement between

SIPL and assessee, assessee was earning 85% of the advertising amount and 15% was parted to SIPL for services rendered in procuring the advertisements. By terminating the agreement, the CIT(A) concluded that, assessee had not obtained any capital asset which was of enduring nature or any right which was not existing with assessee. The agency commission that assessee was paying to SIPL was an expenditure incurred for earning the advertisement income. If assessee would not have terminated the agreement, it would have been allowed to continue with the agreement but assessee had paid compensation of Rs.12,60,00,000/- to SIPL for premature termination of the agreement, that would have to be treated as revenue expenditure. The CIT(A) also relied upon judgment in the case of ***CIT V/s. Glaxo Laboratories India P. Ltd.***[1]

3 As regards the RCA, where assessee paid a sum of Rs.19,40,00,000/- as non-compete fees to SIPL, the CIT(A), relying upon a judgment of the Apex Court in ***Guffic Chem P. Ltd.***[2], held that the compensation paid would be capital in nature. The CIT(A) also held that it will be an intangible asset where assessee would be entitled to claim depreciation.

The ITAT, in its order, which is impugned in this appeal, concurred with the view expressed by the CIT(A) under both the heads.

1. 197 ITR 110
2. 332 ITR 602 (SC)

4 Mr. Suresh Kumar tendered revised substantial questions of law, which read as under :

> (1) Whether in law and on the facts of the instant case, was the Tribunal right in upholding the decision of CIT(A) in deleting the addition of Rs.12,60,00,000/- being the payment made to Star India Pvt. Ltd. for premature termination of Advertising Sale Agreement and treating the said amount as revenue expenditure instead of capital expenditure?
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> (2) Whether on the facts and circumstances of the case, was the Tribunal right in upholding the decision of CIT(A) that the amount of Rs.19,40,00,000/- being paid under RCA was in the nature of capital expenditure and intangible asset entitling assessee to claim depreciation?

Both these questions have been considered by various Courts and the Courts have held in favour of assessee.

5 As regards the proposed first question, the Apex Court in *Commissioner of Income Tax V/s. Ashok Leyland Ltd.*[3] held that a payment made for termination of contract by way of compensation would be an allowable deduction in computing the total income of assessee. The Court observed that when an expenditure is made with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, there is good reason (in the absence of special circumstances leading to the opposite conclusion) for treating such an expenditure as properly

3. (1972) 86 ITR 549 (SC)

attributable not to revenue but to capital. But as a result of termination of the services, if assessee got rid of its liability to pay the commission it was required to pay under the agreement not only during the accounting year but also for a few years more, the expenditure thus saved undoubtedly swelled the profits of the company and where the termination was on business considerations and as a matter of commercial expediency it cannot be stated that by terminating the agreement, assesee acquired any enduring benefit or any income yielding asset. By terminating the services, assessee not only saved the expense that it would have had to incur in the relevant previous year but also for few more years to come. Therefore, it will not be correct to say that by avoiding certain business expenditure, the company can be said to have acquired enduring benefits or acquired any income yielding asset.

In the case at hand also, by paying the compensation under ASTA, assessee not only saved the expense that it would have had to incur in the relevant previous year but also for few more years to come.

6 Therefore, the CIT(A) as well as the ITAT, in our view, was correct in allowing this amount of Rs.12,60,00,000/- paid on account of termination of agreement to SIPL as revenue expenditure.

7 As regards the second question, a similar question came up for consideration before the Division Bench of this Court in ***Principal***

Commissioner of Income Tax V/s. Piramal Glass Ltd.[4] The Court was considering whether the Tribunal was right in deleting the disallowance of depreciation claim on the non-compete fees paid. It was the Revenue's case that the non-compete fees paid, being an intangible asset, no depreciation under Section 32 of the Act was available. The Court negatived this submission of the Revenue and in paragraph 4 held as under :

> *4. We however notice that similar issue has been considered by the different High Courts and held in favour of the assessee. A reference can be made to the decision of the Division Bench of the Gujarat High Court in the case of Principal Commissioner of Income Tax v. Ferromatice Milacron India (P.) Limited. It was also the case where the Assessee had incurred expenditure pursuant to the non-compete agreement and claimed depreciation on such asset. While dismissing the Revenue's Appeal against the Judgment of the Tribunal, following observations were made :*
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> > *We may recall the Assessing Officer does not dispute that the expenditure was capital in nature since by making such expenditure, the assessee had acquired certain enduring benefits. He was, however, of the opinion that to claim depreciation, the assessee must satisfy the requirement of Section 32(1)(ii) of the Act, in which Explanation 3 provides that for the purpose of the said sub-section the expression "assets" would mean (as per clause (b)) intangible assets, being known-how, patents, copyrights, trade marks, licenses, franchises or any other business or commercial rights of similar nature. In the opinion of the Assessing Officer, the non-compete fee would not satisfy this discrimination. Going by his opinion, no matter what the rights acquired by the assessee through such non-compete agreement, the same would never qualify for depreciation in section 32(1)(ii) of the Act as being depreciable intangible asset. This view was plainly opposed to the well settled principles. In case of Techno Shares & Stocks Limited (supra) the Supreme Court held that payment for acquiring membership card of Bombay Stock Exchange was intangible assets on which the depreciation can be claimed. It was observed that the right of such membership included right of nomination as a license which was one of the items which would fall under Section 32(1)(ii). The right to participate in the market had an economic and money value. The expenses incurred by the assessee which satisfied the test of being a*

4. Judgment dated 11.6.2019 in IT Appeal No.556 of 2017

license or any other business or commercial right of similar nature In case of Areva T & D India Limited (supra) Division Bench of Delhi High Court had an occasion to interpret the meaning of intangible assets in context of section 32(1)(ii) of the Act. It was observed that on perusal of the meaning of the categories of specific intangible assets referred to in section 32(1)(ii) of the Act preceding the term "business or commercial rights of similar nature" it is seen that intangible assets are not of the same kind and are clearly distinct from one another. The legislature thus did not intend to provide for depreciation only in respect of the specified intangible assets but also to other categories of intangible assets which may not be possible to exhaustively enumerate. It was concluded that the assessee who had acquired commercial rights to sell products under the trade name and through the network created by the seller for sale in India were entitled to deprecation.

In the present case, Mr. Patel was erstwhile partner of the assessee. The assessee had made payments to him to ward of competence and to protect its existing business. Mr.Patel, in turn, had agreed not to solicit contract or seek business from or to a person whose business relationship is with the assessee. Mr. Patel would not solicit directly or indirectly any employee of the assessee. He would not disclose any confidential information which would include the past and current plan, operation of the existing business, trade secretes lists etc.

It can thus be seen that the rights acquired by the assessee under the said agreement not only give enduring benefit, protected the assessee's business against competence, that too from a person who had closely worked with the assessee in the same business. The expression "or any other business or commercial rights of similar nature" used in Explanation 3 to sub-section 32(1)(ii) is wide enough to include the present situation.

This was followed by another Bench of this Court in ***Principal Commissioner of Income Tax V/s. India Medtronic (P) Ltd.***[5] The Court held that the expression “or any other business or commercial rights of similar nature” used in Explanation 3 to sub-section 32(1)(ii) is wide enough to include the present situation.

5. Judgment dated 30.9.2021 in IT Appeal No.1453 of 2017

8 Therefore, by paying the amount of Rs.19,40,00,000/- as non-compete fees under the RCA, the rights acquired by assessee was not only giving it enduring benefit but also protected assessee's business against competition, that too from a person who had closely worked with assessee.

9 In our view, therefore, the Tribunal has not committed any perversity or applied incorrect principles to the given facts. We do not think that the questions as proposed raised any substantial question of law.

10 Appeal dismissed. No order as to costs.

(FIRDOSH P. POONIWALLA, J.) (K. R. SHRIRAM, J.)

Gauri Gaekwad