

Notes on the 10th K.R.Ramamani National Taxation Moot problem

1. Markiv (European company) paid assessee (and others) to not-compete with it ie a non-compete agreement basically so as to prevent assessee and others from producing drugs Markiv had IP on. Money came to assessee of say, Rs.X, amount from Markiv in FY 04-05.
2. EU Commission subsequently looked into the non-compete and held non-compete agreement is invalid. It levied a fine asking assessee to disgorge the Rs.X amount paid in full.
3. Assessee claimed this Rs.X amount that it paid back in its IT Return of AY 14-15 (FY 13-14)
4. Short point is assessee claimed the amount in this year FY 13-14 and whether it was paid directly to EU or via markiv (and) whether it was a provision merely claimed on accrual (and) whether it was actual payment in the financial year is not relevant; it was per directions of the EU commission proceedings and assessee claimed it in the IT return and so as far as the fact pattern is concerned it is an allowable expenditure of the assessee according to it this year (FY 13-14).
5. Dept disagreed only on the basis of it being a payment which attracts Explanation to s.37 .
6. Assessee said explanation 1 to s.37 is not attracted as it is not illegal in Indian law whichever way you look at it. In the alternate, Assessee also asked it to be allowed as a business loss u/s 28 (as this amount it offered to income earlier year when it was received and now assessee has effectively incurred a loss of the same amount in the course of running its business)
7. The Department said the fine amount was in the nature of a penalty. It has tried to highlight the nuance that in this instant case the fine so happens to be exactly the amount assessee received i.e., it was just asked to pay back as fine what it received and hence is not a mere "take-back" as per assessee claim but a penalty in quantum equivalent to what assessee received. And as it is a penalty for an offence/infracton of law with the non-compete having both Indian and European parties, Explanation 1 to s.37 is attracted. Further as it is a penalty, it cannot be claimed even as business loss u/s 28 and so alternate plea shouldn't hold.
8. ITAT agrees with assessee that explanation 1 to s.37 isnt attracted as it is not an offence/infracton under Indian law. On the alternate please, ITAT agrees with Dept that it appears not to be disgorgement *simplicitor* but allows the alternate claim of assessee u./S 28 as business loss having offered it in earlier year.
9. Dept is on appeal before HC.