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Bangalore tribunal ruling clarifies trademark and goodwill of a business as two separate assets

Facts

The assessee was engaged in the manufacture and marketing of electrical appliances under the name "Sharp". The trade mark "Sharp" was registered on 7.12.1961. However, a dispute arose between Sharp Corporation ('SC') of Japan - a leading manufacturer of electric and electronic items under the brand name "Sharp" and a well recognized global brand and the assessee. The dispute was due to the use of the brand name, Sharp, which SC believed was clearly an infringement of trademark policies. Pursuant to negotiations, a settlement tripartite agreement was entered into on 20.6.1995 between the assessee, Sharp Corporation and one of the directors of the assessee.

The essence of the settlement agreement was as follows:

- The assessee acknowledged the ownership of the trade mark "Sharp" with SC of Japan. Furthermore, the assessee assigned the rights and goodwill relating to and in trademark Sharp and other trademarks similar to the trademark Sharp in favour of SC.
- In turn, SC agreed to pay INR.35 million to the assessee for the above assignment of registered trade mark.
- SC agreed to grant a non-assignable, non-transferrable, royalty free and sole license to the assessee to use the trade mark "Sharp" in respect of six items.
- A deed of assignment entered into between the parties stipulated that the assessee will not use the trademarks as part of its business or corporate name and will not commit any infringement of the trademark except under a valid license from Sharp Corporation.

The assessee adopted a position that what was transferred was trade mark and not goodwill. Given that a trade mark did not have any cost of acquisition, there could be no assessment to capital gains in accordance with the Supreme Court decision in the case of CIT Vs. B.C.Srinivasa Shetty (128 ITR 294).

The Assessing Officer ('AO') did not accept the assessee's claim and held that the amount received from SC was for transfer of the goodwill and was therefore assessable to tax as capital gains. On appeal, the Commissioner of Income-tax (CIT (A)) upheld the order of the AO. The issue was carried to the Bangalore Tribunal for consideration.

Observations/Ruling of the Tribunal

- Trade mark and goodwill are two separate assets. Capital gains arising on transfer of Goodwill are taxable with effect from 1st April, 1988 by deeming the cost of acquisition of goodwill as 'nil'. However, similar provisions for taxability of gains arising on transfer of trade mark came in to effect only

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from 1st April 2002. In the present case, the assessment related to assessment year 1996-97 and prior years and hence, gains arising on transfer of trade mark were not taxable.

- As per the agreement, the assessee had not transferred the goodwill of the business but only the trade mark.
- The assessee continues to carry on business by using the trade mark “Sharp” in respect of six items. Since the goodwill of a business cannot be sold without the business itself, it is hence logical to conclude that only the trade mark was transferred by the assessee in favour of SC. The provision enabling the cost of acquisition to be taken at Rs. Nil in respect of trade mark came into effect only from 1.4.2002 and therefore for the year under appeal; no capital gains on the sale of the trade mark can be computed.

Conclusion

This ruling is of special interest as it clarifies that goodwill of a business cannot be sold without the business itself and transfer of trademark cannot be regarded as transfer of goodwill.

Source: Associated Electronic & Electrical Industries (Bangalore) Pvt Ltd vs. Deputy Commissioner of Income Tax (Bangalore Bench)

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