

**IN THE INCOME TAX APPELLATE TRIBUNAL  
'C' BENCH, BENGALURU**

**BEFORE SHRI B.R. BASKARAN, ACCOUNTANT MEMBER  
and  
SHRI PAVAN KUMAR GADALE, JUDICIAL MEMBER**

ITA Nos.2214 to 2216/Bang/2018  
(Assessment years: 2009-10 to 2011-12)

M/s.Incap Manufacturing Service Pvt. Ltd.  
Sufiya Elite, 3<sup>rd</sup> floor,  
No.18, Cunningham Road,  
Bengaluru-560052. ... Appellant  
*PAN:AABCI 6651 H*

Vs.

Deputy Commissioner of Income-tax,  
Circle 3(1)(1),  
Bengaluru. ... Respondent

Appellant by : Shri Chavali Narayana, CA.  
Respondent by : Dr. P.V.Pradeep Kumar, Addl.CIT.

Date of hearing: 28/03/2019  
Date of pronouncement: 30/04/2019

**O R D E R**

**Per PAVAN KUMAR GADALE, JM :**

These are appeals filed by the assessee against different orders of the CIT(A) passed u/ss. 143(3) and 250 of the Income-tax Act,1961 ['the Act' for short]. Since issues are common in all these appeals, they were heard together and consolidated order is passed.

2. For the sake of convenience, we shall take up the appeal in ITA No.2214/Bang/2018. The assessee raised the following grounds of appeal:

**“Ground No. 1: General Ground:**

1. The order of the learned CIT(A) is based on incorrect interpretation of law and facts and therefore is erroneous and bad in law.

**Ground No. 2: Disallowance of depreciation on Customer Relationship Rights (Non-compete fee)**

The learned CIT(A) has erred in law and facts, in upholding the disallowance of depreciation on customer relationship rights of INR 12,654,563, which is in the nature of Goodwill and is therefore eligible for depreciation under Section 32(1)(ii) of the Act.

3. The learned CIT(A) has failed to appreciate the fact that the Assessing Officer ("AO") himself characterized the customer relationship rights to be in the nature of goodwill and thus erred in not following the directions of the Hon'ble Tribunal.
4. The learned CIT(A) has erred in law and facts, in disregarding the directions of the Hon'ble Tribunal that allowability of depreciation on customer relationship rights is to be examined by considering the same as in the nature of Goodwill in line with the findings of the AO in the assessment order dated 7 December 2011.
5. The learned CIT(A) has erred in law in not appreciating that if customer relationship rights can otherwise be treated as Goodwill, the same would be entitled to depreciation in light of the decision of Hon'ble Supreme Court in **CIT v Smifs Securities Ltd. (348 ITR 302)**.
6. The learned CIT(A) has erred in disregarding the various submissions of the Appellant that depreciation on customer relationship rights to be allowed by treating the same to be in the nature of Goodwill under the Act.

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The Appellant craves leave to add, alter, vary, omit, substitute or amend any of the aforesaid grounds of appeal, at any time before, or at the time of hearing of the appeal, so as to enable the Hon'ble Tribunal to decide the appeals in accordance with the law.“

3. Brief facts of the case are that the assessee is a subsidiary of Incap OYJ (Incap Finland) and is engaged in the business of manufacturing of electrical equipment, sub-systems, inverter power products and power electronic products and filed the Return of income for the assessment year 2009-10 on 30/09/2009 declaring net loss of Rs.119,738,203/-. The case was selected for scrutiny and notices u/ss 143(2) and 142(1) of the Act were issued. The AO completed the assessment u/s 143(3) of the Act by order dated 07/12/2011 assessing the loss of Rs.107,083,640/-. In the assessment, the AO disallowed depreciation claim of Rs.1,26,54,563/- on customary relationship rights and held that depreciation on goodwill is not allowable.

4. On appeal, the CIT(A) accepted the action of the AO and dismissed the assessee's appeal. On further appeal to the Tribunal, and further the assessee has raised additional ground of appeal with respect to depreciation of Rs.47,93,063/- on goodwill and it was raised for the first time before the ITAT and same was admitted. The Tribunal rejected the contention of

the assessee for claim of depreciation on the Customary Relationship Rights and directed the AO to adjudicate the same in the light of the judgment of the Hon'ble Supreme Court in the case of *CIT vs. Smifs Securities Ltd.* (348 ITR 302) as the depreciation on goodwill is a legal issue and directed the AO to follow the decision in the case of *Smifs Securities Ltd* (supra) and remanded the matter to the file of the AO for deciding the issue.

5. Whereas the assessee has filed Misc. Petition (MP) against the order of ITAT in respect of certain errors and omissions and the Tribunal passed the order on 18/04/2017 allowing the MP and further directed the AO, on the issue of depreciation of goodwill, to consider the decision of Hon'ble Supreme Court in the case of *Smifs Securities Ltd.*, (supra). Subsequently, the AO, based on the directions of the Tribunal, has passed the consequential order. The AO found that the assessee has disclosed customary relation rights as intangible asset and claimed depreciation of Rs.1,26,54,563/-. When the case was posted, the learned AR of the assessee appeared from time to time and submitted that details and mentioned that the depreciation should be allowed on goodwill based on Hon'ble Supreme Court's decision in the case of *Smifs Securities Ltd.*, (Supra) and similarly on customary relationship rights.

Whereas the AO relied on the decision of the Tribunal in the case of *M/s.Sanyo BPL Pvt. Ltd., vs. Deputy Commissioner of Income-tax* (75 taxmann.com 253)(Bang.-Trib) where it was decided that customer distribution networks does not result in intangible asset and the AO referred to the relevant portion of the decision in the order. In the assessment proceedings, the AO dealt on two issues, first claim of depreciation on goodwill relying on the Apex Court decision in the case of *Smifs Securities Ltd.*, (supra) as per the directions of the Tribunal and the AO has worked out depreciation on goodwill Rs.47,93,063/- But in respect of the customary relationship Rights treated intangible assets by the assessee. The AO is of the opinion that the Tribunal has rejected the assessee's claim by the order dated 18/04/2017. Therefore, sustained the disallowance made by the AO in the original assessment u/s 143(3) of the Act dated 07/12/2011 and finally the AO passed the order u/s 254 of the Act dated 22/12/2017 assessing loss of Rs.11,18,76,703/-.

6. Aggrieved by the order, the assessee has filed an appeal with the CIT(A). The CIT(A), dealt on the facts of the case and the findings of the AO and the decision of the Tribunal and finally dismissed the assessee's appeal observing at 4.7 as under:

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“4.7 Considering above the grounds of appeal 2 and 3 of the appellant deserve to be dismissed as no such direction was given by the ITAT to the AO to examine the issue of depreciation on the ‘customer relationship rights’ as the issue had already been adjudicated by the ITAT and same has rightly been followed by the AO while giving effect to the order of ITAT.”

7. Aggrieved by the CIT(A) order, the assessee has filed appeal with the Tribunal. The learned AR submitted that the AO has not considered the directions of the Tribunal and referred to Tribunal order and filed paper book with supporting evidence of financial statements and business transfer agreements of the assessee and relied on the order of the Tribunal. The learned AR further contended that this issue was considered for the first time before the Tribunal since the matter was restored to the file of the AO, prayed for allowing the appeal.

Contra, the learned DR relied on the order of the CIT(A) and submitted that there is no specific direction. Therefore, the AO was correct in grant of depreciation on goodwill and not on Customer Relationship Rights.

8. We heard the rival submissions and perused the material on record. The sole disputed issue raised by the assessee in respect of granting of depreciation on Customer Relationship Rights which is in the nature of non-compete fee. The learned

AR's contention that the Tribunal has directed the AO by order dated 18/4/2017 in MP with directions as under:

“5. Having considered the rival submissions as well as careful perusal of the record, we find that while deciding the issue in para 6 of the impugned order, the Tribunal has duly given the reference of the judgment of Hon'ble Supreme Court in the case of CIT vs. Smsifs Securities Ltd. Therefore, while setting aside the issue to the record of the AO on the additional ground of claim of depreciation on intangibles including goodwill, it was directed that the AO decide the same as per law which includes the decision of Hon'ble Supreme Court on this point. Accordingly, we may clarify that the AO while deciding the issue shall consider the judgment of Honbe Supreme Court in the case of CIT vs. Smsifs Securities Ltd.”

9. We found that in the earlier order of the Tribunal in ITA Nos.1469 to 1471/Bang/2014 for the assessment year 2009-10 to 2011-12 dated 9/3/2016 held as under at para.6 pages 7 to 11 of the order which reads as under:

“6. We have heard the rival submissions as well as considered the relevant material on record. The transaction of purchase of contract manufacturing service division of TVS Electronics Ltd. by the assessee vide BTA dt.31.5.2007 is slump sale as the consideration was agreed and paid in lump sum without assigning any value to specific assets. Therefore as per the agreement the consideration was paid lump sum without giving any details of payment for any specific assets. The business was purchased by the assessee and it was transferred by the TVS Electronics as an on going business/division. However, in its books of accounts the assessee has valued the fixed asset and intangibles as per the valuation made by the consultants as under :

	(in Rs. Million)
Land	29.013
Building	15.286
Plant and Machinery	39.230
Other Fixed Assets	14.076
Inventory	
• Raw material	92.062
- Finished and semi-finished goods	23.368
Debtors	97.793
Loans and Advances	45.410
Total Assets	356.238
Current Liabilities and Provisions	79.571
Net Assets taken over	276.667
Advance for building	53.614
Customer Relationships	67.491
Goodwill	25.563
Total value of assets taken over (Net)	423.335

Thus it is clear that the excess amount paid by the assessee over and above the value assigned to the various assets had been assigned to two intangibles namely “customer relationship” and “goodwill”. The assessee did not claim any depreciation on the value of Rs.2.55 Crores assigned to the goodwill and therefore the same was not an issue before the authorities below. The assessee claimed depreciation in respect of the amount of Rs.6.74 Crores which was assigned to customer relationship (intangible). The assessee took a plea that this amount was paid as non-compete fees as the seller has expressed, agreed and undertook not to participate or engage in any jurisdiction as a owner or partner or as shareholder or in any capacity in the business of contract manufacturing services which was transferred to the assessee. Thus the learned Authorized Representative has referred to the Article 11 of BTA in support of his contention that the payment was made for non-compete fees. However, in the absence of any agreement between the parties for any consideration on account of non-compete fees as well as in the absence of any such value assigned to the non-compete fees in the books of accounts, we do not find any substance in the contention of the learned Authorized Representative that the said payment is made as non-compete fees. The assessee in its books of accounts has



allocated sum to the intangible being customer relationship. Therefore, though the seller has agreed not to engage in any business for a period of three years or participate or engage as owner, partner shareholder, consultant, advisor or any other capacity solicit the employees of the CMS Business however in the absence of any intention of parties to pay consideration for such restrictive covenants in the agreement the payment in question cannot be regarded as non-compete fees. Therefore, the decision of the Hon'ble jurisdictional High Court in the case of Ingersoll Rand International India Ltd. (supra) will not help the case of the assessee. As regards the nature of payment in question, as treated by the assessee in the books of accounts being customer relationship, the issue is clearly decided against the assessee by the decision of the Hon'ble Delhi High Court in the case of Sharp Business System (supra). **However, this can be looked from another angle because the Assessing Officer while denying the claim of depreciation has taken a view that the customer relationship rights are in the nature of goodwill as under :**

“The submissions made by company are considered. The assessee has relied upon section 32(1)(ii) of the Income Tax Act, stating that the wordings “any other business or commercial rights of similar nature” gives scope to many such business or commercial rights including customer relationship rights which are as per assessee almost in nature of goodwill. **Hence there is no dispute that customer relationship rights are in nature of goodwill.”**

**Therefore the claim of the assessee is required to be considered by treating the said payment as goodwill.** The learned Authorised Representative of the assessee has relied upon the judgment of Hon'ble Supreme Court in the case of CIT Vs. Smsifs Securities Ltd. 348 ITR 302 and submitted that in view of the said judgment of the Hon'ble Supreme Court, goodwill eligible for depreciation as per the Section 31(1)(ii) of the Act. Since the assessee did not claim depreciation on goodwill in the return of income and even not made any claim before the CIT (Appeals). Therefore, the issue of allowing depreciation on goodwill has not been examined by the authorities below.”

We found that the co-ordinate bench of the Tribunal based on the findings of the AO, in the above paragraph of the decision, has observed that the claim of the assessee is required to be considered by treating the said payment as goodwill. We found strength in the submissions of the learned AR on the claim of depreciation on Customer Relationship Rights supported with observations of the Co-ordinate bench and following the judicial discipline, we set aside the order of the CIT(A) and direct the AO to grant depreciation on Customer Relationship Rights treating the same as 'Goodwill' and allow the grounds of appeal of the assessee.

11. For the assessment years 2010-11 and 2011-12 similar grounds of appeal are raised. For the parity of reasons given by us while dealing with ITA No.2214/Bang/2018 for assessment year 2009-10, the grounds of appeal raised in the appeals for assessment years 2010-11 and 2011-12 in ITA Nos.2215 & 2216/Bang/2018 are allowed.

12. In the result, the assessee's appeals for assessment years 2009-10, 2010-11 and 2011-12 are allowed.

*Order pronounced in the open court on 30<sup>th</sup> April, 2019.*

*Sd/-*

**(B.R. BASKARAN)**  
**ACCOUNTANT MEMBER**

Place : Bengaluru  
Date : 30/04/2019  
*srinivasulu, sps*

*sd/-*

**(PAVAN KUMAR GADALE)**  
**JUDICIAL MEMBER**

**Copy to :**

- 1 Appellant
- 2 Respondent
- 3 CIT(A)-
- 4 CIT
- 5 DR, ITAT, Bangalore.
- 6 Guard file

By order

Assistant Registrar  
Income-tax Appellate Tribunal  
Bangalore