

Depreciation allowable on Goodwill

Kerala High Court in the case of B. Raveendran Pillai (supra) and the Delhi High Court in the case of Hindustan Coco Cola Beverages (P.) Ltd. (supra) have held that assessee is entitled to depreciation on the value of goodwill. The Kerala High Court has held that 'goodwill is not specifically mentioned in section 32(1)(ii). Depreciation is allowable not only on tangible assets covered by clause (i) of section 32(1) but on the intangible assets specifically enumerated in clause (ii) and such of the other business or commercial rights similar to the items specifically covered therein. Similarly the Delhi High Court has upheld that 'payment on account of goodwill is similar to assets like patents, copyrights, trademarks, licences referred to in the definition of the block of assets in the senses that the function of all these assets is to restrict their misuse and to earn maximum profits in the business. The function of goodwill acquired by the assessee also is the same in view of the fact that it maximizes the profits of the company. Since the function of intangibles defined in the Act and the intangible acquired by the assessee is the same, the assets are similar. Therefore, the assessee's goodwill being a valuable commercial asset similar to other intangibles specified in the definition of block of assets is eligible to depreciation'. The instant case is squarely covered by the aforementioned judgments of the Delhi High Court and Kerala High Court. Therefore, the assessee was entitled for the depreciation on goodwill.

IN THE ITAT CHENNAI BENCH 'D'

Metrex Technologies Ltd.

v.

Assistant Commissioner of Income-tax

IT Appeal No. 286 (Mds.) of 2011

[Assessment Year 2005-06]

JUNE 28, 2012

ORDER

Vikas Awasthy, Judicial Member – The appeal has been filed by the assessee against the order dated 11.11.2010 passed by the CIT(A)-III, Chennai.

2. The brief facts of the case are that the assessee/appellant is engaged in the manufacture, supply, installation and integration of security, fire and building automation systems. The appellant filed return of income for the assessment year 2005-06 admitting Nil income on 30.10.2005. The return of the assessee was processed under section 143(1) on 30.03.2007. Subsequently, the case of the assessee was selected for scrutiny and notice under section 143(2) of the Income Tax Act, 1961 (hereinafter referred to as "the Act") was issued to the assessee. The Assessing Officer vide assessment order dated 20.11.2007 determined the total income of the appellant as Rs. 4,31,30,470/- after making additions in respect of interest on fixed deposits, disallowance of club membership, goodwill, leave encashment and deduction under section 80IB. Aggrieved against the assessment order, the assessee filed an appeal

before CIT(A) impugning the additions made by the Assessing Officer. The CIT(A) vide order dated 11.11.2010 partly allowed the appeal of the assessee. Still aggrieved against the order of the CIT(A), the assessee has come in second appeal before the Tribunal impugning the order dated 11.11.2010 primarily on the following grounds:-

- (i) Disallowance of depreciation on goodwill;
- (ii) Not allowing provision for leave encashment to the tune of Rs. 2,18,735/-; and
- (iii) Apportionment of expenses.

3. Mr. Devanathan, counsel appearing on behalf of the assessee submitted that the assessee is entitled for depreciation on the goodwill. The Assessing Officer as well as the CIT(A) has erred in not allowing depreciation on goodwill when the assessee had incurred cost on acquiring the same and this fact has not been disputed by the Assessing Officer. In order to support this contention, he relied on the judgement of the Hon'ble Kerala High Court in the case of *B. Raveendran Pillai v. CIT* [2011] 332 ITR 531/[2010] 194 Taxman 477 and Division Bench judgement of the Hon'ble Delhi High Court in the case of *CIT v. Hindustan Coco Cola Beverages (P.) Ltd.* [2011] 331 ITR 192/198 Taxman 104/9 taxmann.com 104. He submitted that this issue was decided against the assessee in the assessee's own case relevant to the assessment year 2003-04 and 2004-05 by the Tribunal in ITA Nos.456 & 1963/Mds/2007 vide order dated 4.2.2009. However, the aforesaid judgements of the Hon'ble Kerala High Court and Delhi High Court are subsequent to the order of the Tribunal. Therefore, the judgements of the High Courts will prevail over the order of the Tribunal.

4. With regard to leave encashment, the counsel for the assessee submitted that the authorities below have erred in not allowing provision for leave encashment to the tune of Rs. 2,18,735/- . To support his contentions, he relied on the judgement of the Hon'ble Calcutta High Court in the case of *Exide Industries Ltd. v. UOI* [2007] 292 ITR 470/164 Taxman 9 as well as the order of the Tribunal in the case of *Asstt. CIT v. Siemens Building Tech (P.) Ltd.* in [IT Appeal No.57 (Mds) of 2011, dated 27.06.2011.

5. The third issue in appeal relates to apportionment of expenses. The counsel for the assessee submitted that the CIT(A) in appeal relevant to the assessment year 2003-04 vide order dated 7.12.2006 has decided the similar issue in favour of the assessee. The CIT(A) held that the turnover method for the allocation of indirect expenses is required to be adopted in the case of the assessee for computing profits of each unit. The Assessing Officer had distributed the profit of the appellant in the ratio of turnover of various branches and the Pondy unit. The said method adopted by the Assessing Officer is neither supported by evidence nor reasonable. The view of the CIT(A) was upheld by the Tribunal in appeal in assessee's own case in ITA Nos. 456 & 1963/Mds/2007 vide order dated 4.2.2009 which was affirmed by the Hon'ble Madras High Court vide judgement dated 25.08.2009.

6. On the other hand, Mr. K.E.B. Rengarajan, DR supported the order of the CIT(A) and submitted that the order passed by the CIT(A) is well reasoned and detailed order and prays for dismissal of the appeal of the assessee.

7. We have heard the submissions made by the respective parties and have gone through the judgements relied on by the counsel for the assessee. A perusal of the order dated 4.2.2009, passed by the co-ordinate Bench of the Tribunal in ITA Nos.456 & 1963/Mds/2007 in

assessee's own case relevant to the assessment years 2003-04 & 2004-05 respectively, shows that the claim of the assessee with regard to depreciation on goodwill was rejected. However, subsequent judgements of the Hon'ble Kerala High Court in the case of *B. Raveendran Pillai (supra)* and the Hon'ble Delhi High Court in the case of *Hindustan Coco Cola beverages P. Ltd., (supra)* have held that assessee is entitled to depreciation on the value of goodwill. The Hon'ble Division Bench of the Kerala High Court has held that "goodwill is not specifically mentioned in section 32(1)(ii) of the Income Tax Act. Depreciation is allowable not only on tangible assets covered by clause (i) of section 32(1) but on the intangible assets specifically enumerated in clause (ii) and such of the other business or commercial rights similar to the items specifically covered therein." Similarly, the Division Bench of the Hon'ble Delhi High Court has upheld that "payment on account of goodwill is similar to assets like patents, copyrights, trademarks, licences referred to in the definition of the block of assets in the senses that the function of all these assets is to restrict their misuse and to earn maximum profits in the business. The function of goodwill acquired by the assessee also is the same in view of the fact that it maximizes the profits of the company. Since the function of intangibles defined in the Act and the intangible acquired by the assessee is the same, the assets are similar. Therefore, the assessee's goodwill being a valuable commercial asset similar to other intangibles specified in the definition of block assets, is eligible to depreciation."

8. We are of the considered opinion that the case of the assessee is squarely covered by the aforementioned judgements of the Hon'ble Delhi High Court and Hon'ble Kerala High Court. Respectfully following the judgements, we hold that the assessee is entitled for the depreciation on goodwill and accordingly we reverse the decision of the CIT(A) on this issue and allow this ground raised by the assessee.

9. With regard to second issue i.e. provision for leave encashment, we find that the issue has already been decided in favour of the assessee in assessee's own case for the assessment year 2002-03 by the co-ordinate Bench of the Tribunal in ITA No.57/Mds/2011 vide order dated 27.06.201, wherein it has held as under:-

"6. In the cross objection filed by the assessee, the only ground raised by the assessee is that the CIT(A) has erred in not deleting the disallowance made by the assessing authority in respect of provision of Rs. 93,815/- made for leave encashment as per existing statutory requirement as held by Calcutta High Court in the case of *Exide Industries Ltd. v. UOI & Ors* (292 ITR 470). On merit, this issue is covered in favour of the assessee by virtue of the decision of the Hon'ble Supreme Court in the case of *Bharat Earth Movers v. CIT* (245 ITR 428). In law, the issue is again in favour of the assessee by virtue of the decision of the Hon'ble Calcutta High Court in the case of *Exide Industries Ltd. v. UOI & Ors.* (292 ITR 470) wherein the Hon'ble Court has struck down sec.43B(f) which stated that leave encashment could be allowed only on actual payment. In these circumstances, we direct the assessing authority to give deduction for the provision of Rs. 93,815/- made by the assessee towards leave encashment. The assessee is successful in its cross objection."

10. Respectfully following the same, we allow the ground of appeal of the assessee for the year under consideration as well.

11. The third issue, i.e. apportionment of expenses has already been decided in favour of the assessee by the co-ordinate Bench of the Tribunal in assessee's own case which has been further reaffirmed by the Hon'ble Madras High Court in Tax Appeal Nos.788 & 789 of 2009

relevant to the assessment years 2003-04 & 2004-05, wherein the Hon'ble High Court has held as under:-

“3.The Tribunal, while examining the said issue, has found out that the approach of the Assessing Officer was arbitrary and presumptive, as it has been rightly held by the CIT(A) that there was no material evidence for the assessing authority to adopt the said method. The Tribunal has also rightly held that even according to the CIT(A), the proportionate allocation made by the assessee company was not sound, which cannot be accepted and therefore, the method adopted by the CIT(A) (viz.,) the one which is usually recognized in the matter of allocation of expenditure and the said method adopted by the CIT(A) was sound and acceptable in law.”

The co-ordinate Bench of the Tribunal on the issue in its order dated 4.2.2009 in ITA No.611 & 1832/Mds/2007 has observed as under:-

“The CIT(A) also has observed that the proportionate allocation made by the assessee-company is not sound and correct, and it cannot be accepted. The CIT(A), therefore, adopted one of the methods of apportionments usual recognized in the matters of allocation of expenditure, that is, on the basis of unit-wise turnover and directed to apportion concerned common expenditures. In the absence of any evidence brought on record by the Assessing Officer, the method adopted by the CIT(A) is sustainable in law. Once the method adopted by the CIT(A) is found to be accepted in law, the quantum modification arising out of the direction of the CIT(A) is only a consequence of a lawful direction. We have no reason to interfere in such lawful consequences. Therefore, we find that the ground raised by the Revenue on this point of allocation of expenditure is not meritorious. The appeals filed by the Revenue are liable to be dismissed.”

The D.R. was unable to produce any judgement or any other document contrary to the submissions made by the counsel for the assessee on the issue of apportionment of expenses as well. We, therefore, respectfully following the aforesaid judgement of the jurisdictional High Court, allow this ground of the assessee.

12. In view of the above, we set aside the impugned order passed by the CIT(A) and allow the appeal of the assessee.