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IN THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD "B" BENCH, HYDERABAD

BEFORE SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER AND SHRI SAKTIJIT DEY, JUDICIAL MEMBER

ITA No.435 /Hyd/2010,
1222/Hyd/2011& 1789/Hyd/11
Assessment years 2006-07 to 2008-09

M/s SKS Micro Finance Limited, Begumpet, Hyderabad. **PAN:AAICS2940J**	Vs	DCIT, Cir-3(2), Hyderabad.
{Appellant)		(Respondent)

Appellant by : Sri K.C. Devdas
Respondent by: Smt. Amisha S. Gupt

Date of hearing : 22-4-2013
Date of Pronouncement : 21-6-2013

ORDER

PER SAKTIJIT DEY, JUDICIAL MEMBER.

These three appeals filed by the same assessee are directed against separate orders of CIT (A)-IV, Hyderabad pertaining to the asstt. Years 2006-07, 2007-08 and 2008-09. Since common issues are involved in all these appeals, these are taken up together and disposed of by this combined order for the sake of convenience. First let us deal with ITA No.435/Hyd/10-Asst. year 2006-07. The assessee has filed the appeal on the following grounds:-

1.**The order of the learned Commissioner of Income Tax (Appeals)-IV, Hyderabad, in holding that the appellant is not entitled to depreciation claimed at Rs.99,25,284/- is unsustainable in law.**

2. The learned Commissioner of Income Tax (Appeals)-IV, Hyderabad, failed to note that "right to access the members of the society was an Intangible asset" falling within the meaning of the definition contained intangible

asset as laid down in section 32(1) (ii) of the Income Tax Act, 1961 and therefore the Appellant was entitled to claim the depreciation at Rs.99,25,284/-.

3.The learned Commissioner of Income Tax (Appeals)-IV, Hyderabad, failed to note that there could not be any disallowance under section 14A of the Income Tax Act, 1961 as the entire investments in mutual funds were not made from borrowed funds but from the proceeds of fresh issue of equity shares and therefore erred in directing the Assessing Officer to work out the disallowance under section 14A of the Income Tax Act in terms of Rule 80 of the Income Tax Rules, 1962.

4.Without prejudice to the aforesaid ground, the learned Commissioner of Income Tax (Appeals)-IV, Hyderabad, failed to note that exempted dividend income from mutual funds was Rs.1,31,616/- while the disallowance of expenditure was at Rs.2,15,OOO/- which was much more than the exempted dividend Income and therefore ought to have deleted the disallowance of Rs.2,15,OOO/-

5.Any other ground or grounds that may be urged at the time of hearing."

2. Ground No. 1 and 2 relates to disallowance of depreciation of an amount of Rs.99,25,284/-.

3. Briefly the facts relating to the issue in dispute are, the assessee, a private limited company is engaged in the business of Micro Financial Lending Services to women in rural areas through small joint liability groups and direct micro loans. For the impugned assessment year the assessee filed its return of income on 15-11-2006 declaring income of Rs.12,79,373/-. Initially the return was processed u/s 143(1) of the Act. Subsequently, assessee's case was selected for scrutiny assessment. During the scrutiny assessment proceeding while examining the assessee's statement of accounts the Assessing Officer noticed that the assessee had claimed depreciation at 25% in respect of intangible asset amounting to Rs.99,25,284 by mentioning that during the financial year relevant to the assessment year under dispute the assessee had incurred client creation cost of Rs.3,97,01,135 and written off 25% of that intangible asset amounting to Rs.99,25,284/- to the P & L A/c. In response to further

query made by the Assessing Officer, the assessee submitted that the assessee acquired over one lakh clients at a cost of Rs.3.97 crores @Rs.350 per customer. It was further submitted that these were trained, motivated, credit checked and risk filtered and are a source of assured economic benefits over the next five years and in that process, the assessee capitalised the cost in the books and amortised the cost over a period of five years. It was submitted that the assessee has the capacity to control the future benefits from the customer which arises from legal rights enforceable in a court o f law. It was submitted that the customers once acquired would have business relationship with the assessee company between three to five years and the association was reasonably secured and assured and the cost was also measured reliably as those have been separately identified and paid for. It was therefore contended that the consideration paid to Swayam Krishi Sangam (SKS)towards transfer of customers was for an intangible asset eligible for depreciation.

4. The Assessing Officer noted that as per appendix to Rule-5 of the IT Rules any assessee would be eligible for depreciation @ 25% in respect of intangible assets of know-how, patents, copy of rights, trade marks, licenses, franchises or any other business or commercial rights of similar nature. The Assessing Officer was of the view that the intangible asset claimed to have been acquired by the assessee does not come under any of the identified assets appearing in the depreciation schedule. The Assessing Officer was also of the view that since the assessee had acquired part of the already existing business of SKS the said asset had not been created during the course of business of the assessee, hence cannot be considered to be a business or commercial rights of similar nature. The Assessing Officer observed that the amount of Rs.3,97 crores paid by the assessee for acquisition of clients who were already enrolled with SKS and participating in their finance business. The Assessing Officer further noted that subscribers were already having a participation in the finance business of SKS and had got finance assistance from that concern and were in

the process of repayment of the financial facility already availed. Assessing Officer felt that the fruits of the business were being enjoyed by SKS. Whereas, the assessee had only acquired the clientele available on the rolls of SKS by making a lumpsum payment. The Assessing Officer therefore concluded that, the same could not be compared with the intangible assets mentioned in Rule 5 of the schedule as it was not amounting to an asset in the assessee's business and could not have been said to be used in its business. Further the clientele acquired by the assessee did not have similar characteristics as that of know-how, patent etc., identified as intangible assets by the statute.

5. The Assessing Officer referred to the definition of 'plant' in section 43(3) of the Act which includes all other things except livestock, furniture and fittings and buildings. Furniture and fittings are kept under a separate head under rule 5. Thus, the only item left is livestock. The Assessing Officer was of the view that the assessee cannot be said to have purchased the clients of another concern by paying specific consideration. He observed that even if the assessee had obtained a specific number of clients by making lumpsum payment and taken them to into its business hold, it could only mean that the assessee had acquired future business rights with them, excluding the transferor concerned from the picture as they had foregone the rights of having business relationship with the existing business customers. The Assessing Officer opined that the assessee made the lumpsum payment in lieu of foregoing of future business relationship by the transferor company, hence the expenditure incurred by the assessee is of capital nature. However, the Assessing Officer was of the view that by such lumpsum payment the assessee did not bring any durable asset into existence. He observed that for claiming depreciation ownership and user are the prerequisites whereas members taken over from SKS are living beings who can default in payment at any time and therefore even though the assessee had the right of legal action, it could not be said to be the

owner of such clients. The Assessing Officer also opined that mere collections of instalments in respect of the finances already made by the SKS cannot be said as amounting to user for the purpose of its business. The Assessing Officer finally concluded that as no intangible asset has come into the possession of the assessee no depreciation can be allowed. Accordingly, the Assessing Officer disallowed the depreciation claimed of Rs.99,25,284/-.

6. Being aggrieved of the assessment order passed, the assessee filed an appeal before the CIT (A). During the course of hearing before the CIT (A), it was contended by the assessee that it had entered into understanding with Swayam Krishi Sangham Society (SKSS), an NGO engaged in microfinance and acquired the entire business of micro finance of SKS through a business transfer agreement. The acquisition was made as a slump sale. While arriving the value of the business besides physical and actual assets, a value for creating a customer base of more than 1,10,000 borrowers, related brand recall value, trust and faith on the business concept, including the usage and adoption of SKSS logo and brand, which the source of income to the business that was being acquired was also arrived at Rs.3,97,00,000 included in the total consideration of Rs.5.127 crores. It was submitted that the acquisition made by the assessee is not about the borrowers, but about the copy right and trade mark in the usage of the micro finance lending and the commercial rights to use a methodology to effect near 100% recovery through groups, group recognition tests, training methodology to group members, recruitment method, criteria for selection and motivation and monitoring fund etc. It was submitted that the consideration and payment towards consideration does not include only customer transfer cost but also for the entire business transfer and further support for smooth transition also. It was contended that SKSS sold the business on slump sale basis, hence though the value has been allotted to the customer transfer for the identification purposes, it is incorrect to isolate the customer transfer separately

and deny the available benefits under the IT Act, 1961. It was submitted that client transfer cost and the customer's acquisition cost and the customer creation cost are one and the same as referred in various document s while the original intention through MOU was for client's transfer. It was further contended that the definition of intangible asset u/s 32 of the Act is an inclusive definition and hence for any other asset to fall within the purview of depreciable asset, it should partake the character of "any other business or commercial right of similar nature". It was submitted that depreciation on other intangible assets is available on fulfilment of the following conditions:-

i) The asset acquired should be an intangible asset as per section 32 of the Act.

ii) The intangible asset should be in the nature of business or commercial rights of similar nature.

iii) `The intangible asset should be owned by the assessee.

iv) The intangible asset is acquired on or after 1st April, 1998 and

v) The intangible asset is used for the purpose of business or profession.

7. It was submitted that the business of micro finance institution depends on borrowers and the lenders spent most of their time in identifying them, training them for undertaking business ventures, bringing credit discipline through groups and do a detailed check of monitoring of 'borrowers and undertake the risk profile of the clients before funding. It was submitted that in assessee's case such scrutiny of borrowers was carried out by SKSS which had also lent monies to such borrowers and the borrowers were repaying the amounts regularly. These borrowers with proven track records have high value for any lender. SKSS had also created a financial service delivery mechanism and due to the efforts of SKS, NPA as a percentage of advances stood at 1.54% in the year 2005-06 which was later reduced to 0.12%. It was therefore contended that the right to access the customers of the society is an intangible asset which is used for the purpose of business of the assessee. Referring to the decision in the

case of Ravindra Kumar Jain vs. CIT (263 ITR 368), Upendra M. Dalal (89 ITD 629), Techno Shares and Stocks Limited vs. (101 TTJ 349), it was submitted that even the membership card of stock exchange though not specified u/s 32(1) (ii) is held to be a right to carry on business or profession and therefore would be eligible for depreciation as intangible asset. It was submitted that the term "business or commercial rights" has not been defined in the Act, hence is to be assigned the meaning as has been assigned to the same in various judicial precedents. It was submitted that the right acquired by the assessee being essential to do the business is necessarily a business or commercial rights. In support of such contention, the assessee relied on the decision of Hon'ble Bombay High Court in case of I.L. and FS Investment Manager's Ltd. ITO (298 ITR 32), Income-tax Appellate Tribunal, Mumbai Bench decision in Skyline Caterers Pvt. Ltd. Vs. ITO (20 SOT 260) and Income-tax Appellate Tribunal Chennai Bench in case of ITO vs. Medico Technologies India td. (2009-TIOL-203. The assessee also contended that the term 'similar nature' has also not been defined under the Act, hence as per the ratio laid down in the judicial precedents, the right to access the customers of the Society which facilitates the business of the assessee and allows the assessee to market its products to them is essentially a business or commercial right of similar nature as mentioned in section 32 of the Act. The assessee referring to the decision of Hon'ble Supreme Court in case of State of UP vs. Renusagar Power Plant (70 Company case 127) submitted that the word "own" is a generic term embracing within itself several gradation of titles dependent upon the circumstances and it does not necessarily mean ownership in fee simple. It means "to possess, to have or hold as property". It was submitted that the assessee owns/possess the right to access the customers of the society thus satisfying the condition of acquisition in respect of an intangible asset on or after 1-4-1998 and the said asaset has been used in the business/profession of the assessee. It was further contended that to fall under the definition of intangible asset as mentioned in Rule-5 it is not necessary that the asset has to be

created during the course of business. It was submitted that such intangible asset could either be created or acquired from outside for a consideration. It was submitted that depreciation on goodwill was held as allowable as it was covered under the scope of "any other business or commercial right of similar nature". In support of such contention, the assessee relied upon the decision in the case of Hindustan Coca Cola Beverages Pvt. Ltd vs. DCIT (ITA No.1884/Del/06 and in case of Piaggio Vehicle Pvt. Ltd. Vs. DCIT (2009-TIOL-626). The assessee referred to the decision of Income-tax Appellate Tribunal Mumbai Bench in the case of Kotak Forex Brokerage Limited wherein the Tribunal held that the business or commercial rights are rights obtained for effectively carrying on business or commerce and therefore any right obtained for carrying business effectively and profitably has to fall within the meaning of intangible asset.

8. The CIT (A) after considering the submissions of the assessee and referring to section 32(1) (ii) of the Act observed that depreciation is intended to a limited category of intangible asset. The CIT (A) was of the view that the customer base acquired by the assessee cannot be termed as know-how, patent, copy right or trade mark or franchise. It also cannot be considered a licence or business or commercial right of similar nature as it does not relate to any intellectual property whereas section 32(1)(ii) contemplate depreciation in respect of those license or right which relate to intellectual property. In this context, the CIT (A) relied upon a decision of Hon'ble Bombay High Court in case of CIT vs. Techno Shares and Stocks Limited and others (225 CTR 337) wherein the Hon'ble High Court held that the expression licence is a very wide term and it would embrace within its sweep not only the permission to use immovable property for lawful purposes but also permission to carry on any trade business, profession etc., including the right to acquire the intellectual property rights. It was held that construing the expression "license" in section 32(1)(ii) widely so as to apply to all

types of licenses relating to intangible assets would defeat the object of the Act because depreciation u/s 32 is intended to a limited category of intangible asset. It was held that section 32(1)(ii) contemplates business or commercial right relating to intellectual property and not to all categories of business or commercial right. The CIT (A) applying the aforesaid ratio of Hon'ble Bombay High Court was of the view that right to control and use the customer base is not relating to any intellectual property but, it relates to clients developed and trained by SKS and is based on the expenditure incurred in creation of such clients. Therefore, the right to earn income from the same cannot be considered as right relating to any intellectual property. Accordingly, the CIT (A) sustained the disallowance of depreciation made by the Assessing Officer.

9. The learned authorised representative of the assessee reiterating the stand taken before the lower authorities submitted that the assessee had entered into memorandum of understanding with SKS as per which the entire business of SKS was transferred to the assessee as a slump sale which also included the client base created by SKS. In this context, the learned authorised representative of the assessee referred to the MOU at page-15 of the paper book. It was submitted that as per the terms of the MOU, the assessee paid Rs.3,97,00,000/- towards one time reimbursement customer transfer cost to SKS. The learned authorised representative of the assessee referring to the notes on accounts from the audit report at page-30 of paper book and specifically referring to note 2.2 submitted that the amount of Rs.3,97,01,135 being client's acquisition cost was part of total consideration for transfer of the business. It was submitted that as per section 32(1)(ii) of the Act, the client acquisition cost paid by the assessee is a license in the nature of business or commercial rights. In this context the learned authorised representative of the assessee referred to the definition of business as provided u/s 2(13) of the Act. The learned authorised representative of the assessee submitted that by paying the aforesaid amount the assessee has

acquired the right over more than 1 lakh clients hence, it has to be considered as a right acquired the purpose of business of the assessee. The right acquired for being a commercial right, the assessee is entitled for depreciation. In support of his contention, the learned authorised representative of the assessee relied upon the following decisions:-

i) Areva T & D India Ltd. Vs. DCIT (345 ITR 421) (Del)
ii) The AP Paper Mills Ltd. Vs. ACIT (2010) 128 TTJ (Hyd) 596
iii) CIT vs. Hindustan Coca Colas Beverages Pvt. Ltd (331 ITR 192) (Del)
iv) Skyline Caterers P. Ltd. Vs. ITO (306 ITR (AT) 369)
v) CIT vs. SMIFS Securities Ltd. (348 ITR 302) (SC)
vi) M/s India Capital Markets Pvt. Ltd. Vs. DCIT (56 SOT 32)

The learned departmental representative, on the other hand, supporting the order of the CIT (A) submitted that the assessee has only acquired the right over the SKS and not over all the customers. It was submitted that even assuming that the assessee has acquired right over the clients still then it cannot be said to be an intangible right as defined u/s 32(1)(ii) of the Act read with rule-5 of the schedule in the Appendix of IT Rules. Therefore, depreciation cannot be allowed to the assessee.

10. We have heard rival submissions of the parties and perused the material on record. We have also carefully applied our mind to the decisions cited before us. As would be evident from the orders of the revenue authorities, assessee 's claim of depreciation was disallowed by holding that the acquisition of client base of SKS society is neither an intangible asset nor a business or commercial right of similar nature. Before venturing into deciding the issue, it is necessary at this stage to look at the actual nature of transaction between the assessee and SKS society. As per the terms of MOU (page-15 of the paper book) SKS Society transferred all the assets and properties

including the existing loans and the receivables in relation to the Micro Finance Activity carried out by it till 31st August, 2005 together with the software/hardware/furniture and fixtures and other movable properties. The consideration for portfolio transfer as mentioned in clause-1 of the MOU reads as under:-

> **"Parties agree that the assets, properties loans, software, hardware, furniture and fixtures more particularly set out in Annexure A comprises the Portfolio.**
>
> **The Portfolio has been valued by the Statutory Auditor of SKS Society and based on such valuation, the Parties agree to the following consideration payable for the Portfolio transfer to SKS Company.**
>
> **One time reimbursement of customer transfer costs Rs. 39.70 Million for having identified, motivated, trained, credit checked and risk-filtered, approximately 113,270 customers on August 31, 2005, or at the cost of Rs 350.50 per customer, since all of these customers are generating net positive revenue for SKS at present.**
>
> **(b) One time reimbursement of an amount of Rs. 8.25 million towards cost of internal controls systems, computer software and related procedure based recovery systems etc.**
>
> **(c) Towards corporate services including strategic planning, all technical matters of group formation, addressing recovery issues, identification of new markets, market surveys, change in the method and procedures of financial services, introduction of new products, impact assessment, avenues for negotiation of new loans from prospective funders, generation additional revenues through grants, fees etc, training of key human resources, establishing/upgrading the MIS and ongoing accounting, quality control and internal audit systems.**
>
> **(d) Rs. 3.32 MilIion towards furniture, computers and fixtures.**
>
> **In consideration of the SKS Company agreeing to pay the above amounts, SKS Society agrees to transfer the Portfolio to SKS Company. It is hereby agreed and acknowledged between the Parties that the transfer of the loans would require the consent of the lenders, Parties agree to cooperate with each other to ensure that the approvals from the lenders are duly obtained,…."**

11. Clause-3 of the MOU even provided for transfer of employees of SKS Society. Therefore, reading of the MOU as a whole gives an impression that the entire business of SKS Society was transferred to the assessee company as a going concern by way of slump sale. This also included the acquisition of rights over more than 110000 existing clients of SKS Society. This fact has also not been disputed by the Assessing Officer or CIT (A). The Assessing Officer even has accepted

it as a capital asset. However, both the Assessing Officer as well as CIT (A) have disallowed the claim of depreciation solely on the ground that the right acquired over the clients of SKS Society is not an intangible asset u/s 32(1)(ii) of the Act. At this stage it would be appropriate to look into the provision contained u/s 32(1)(ii) of the Act.

"**32(1) In respect of depreciation of –**

(i).....

(ii) Know-how, patents, copyrights, trade marks, licences, franchises or any other business or commercial rights of similar nature, being intangible assets acquired on or after the 1st day of April, 1998,

owned, wholly or partly, by the assessee and used for the purposes of the

business or profession, the following deductions shall be allowed ......"

A reading of the aforesaid provision makes it clear that depreciation would be allowable on intangible assets being know-how, patents, copy-rights, trade marks, licenses, franchises or any other business or commercial rights of similar nature if the following conditions are fulfilled.

i) Such asset is acquired after 1-4-1998.

ii) The asset is owned wholly or partly by the assessee

iii) Such asset is used for the purpose of business or profession of the assessee

So far as the aforesaid conditions are concerned, it appears from facts on record that the assessee has acquired the asset after 1-4-1998. The assets are owned wholly by the assessee and it is also used for the purpose of business or profession of the assessee. Therefore, the only requirement for allowability of depreciation is whether the cost paid for acquisition of clients can be considered as an intangible asset as per the definition u/s 32(1)(ii) of the Act. It is not disputed that the assessee has acquired the entire business and commercial asset of

SKS on payment of lumpsum consideration which included the cost of acquisition of the existing customer base of SKS Society. It is also a fact that, the customer base acquired by the assessee has provided an impetus to the business of the assessee as the customers acquired are with proven track record since they have already been trained, motivated, credit checked and risk filtered. They are source of assured economic benefit to the assessee and certainly are tools of the trade which facilitates the assessee to carry on the business smoothly and effectively. Therefore, by acquiring the customer base the assessee has acquired business and commercial rights of similar nature. The CIT(A) has rejected assessee' claim of intangible asset on the conclusion that it does not come within the terms of know-how, patent, copyright, trademark, licence or business and intangible asset referred to in Sec.32(1)(ii) will apply to these limited category of intangible assets and not to a wider category of intangible assets. The Hon'ble Delhi High Court in case of Areva T & D India Ltd. Vs. DCIT (supra) while interpreting the term "business or commercial rights of similar nature" by applying the principle of ejusdem generis held as under :

> **"In the present case, applying the principle of ejusdem generis, which provides that where there are general words following particular and specific words, the meaning of the latter words shall be confined to things of the same kind, as specified for interpreting the expression "business or commercial rights of similar nature" specified in section 32(1)(ii) of the Act. It is seen that such rights need not answer the description of "know-how, patents, trade marks, licences or franchises" but must be of similar nature as the specified assets. On a 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 the aforesaid intangible assets are not of the same kind and are clearly distinct from one another. The fact that after the specified intangible assets the words "business or commercial rights of similar nature" have been additionally used, clearly demonstrates that the Legislature did not intend to provide for depreciation only in respect of specified intangible assets but also to other categories of intangible assets, which were neither feasible nor possible to exhaustively**

enumerate. In the circumstances, the nature of "business or commercial rights" cannot be restricted to only the aforesaid six categories of assets, viz., know-how, patents, trade marks, copyrights, licences or franchises. The nature of "business or commercial rights" can be of the same genus in which all the aforesaid six assets fall. All the above fall in the genus of intangible assets that form part of the tool of trade of an assessee facilitating smooth carrying on of the business. In the circumstances, it is observed that in the case of the assessee, intangible assets, viz., business claims; business information; business records; contracts; employees; and know-how, are all assets, which are invaluable and result in carrying on the transmission and distribution business by the assessee, which was hitherto being carried out by the transferor, without any interruption. The aforesaid intangible assets are, therefore, comparable to a licence to carry out the existing transmission and distribution business of the transferor. In the absence of the aforesaid intangible assets, the assessee would have had to commence business from scratch and go through the gestation period whereas by acquiring the aforesaid business rights along with the tangible assets, the assessee got an up and running business. This view is fortified by the ratio of the decision of the Supreme Court in Techno Shares and Stocks Ltd. [2010] 327 ITR 323 (SC) wherein it was held that intangible assets owned by the assessee and used for the business purpose which enables the assessee to access the market and has an economic and money value is a "licence" or "akin to a licence" which is one of the items falling in section 32(1) (ii) of the Act.

In view of the above discussion, we are of the view that the specified intangible assets acquired under slump sale agreement were in the nature of "business or commercial rights of similar nature" specified in section 32(1)(ii) of the Act and were accordingly eligible for depreciation under that section."

12. The Hon'ble Supreme Court in case of CIT vs. Smifs Securities Limited (supra) while considering whether goodwill would fall under the expression "any other business or commercial right of similar nature" held that the principle of ejusdem generis would strictly apply while interpreting the expression "any other business or commercial right of similar nature" and by applying the said principle goodwill is held to be an intangible asset. In case of Hindustan Coca

Cola Beverages Pvt. Ltd. (supra) the Hon'ble Delhi High Court upholding the view of the Income-tax Appellate Tribunal, Delhi Bench in treating goodwill as an intangible asset held that the meaning of business or commercial rights of similar nature if understood in the backdrop of section 32(1)(ii) of the Act would mean commercial rights or such rights which are obtained for effectively carrying on business and commerce and commerce as is understood is a wider term which encompasses in its fold many of facet . The Hon'ble High Court held that any right which is obtained for carrying on the business with effectiveness is likely to fall or come within the sweep of meaning of intangible asset. The Income-tax Appellate Tribunal Mumbai Bench in case of Skyline Caterers P. Ltd. Vs. ITO [306 ITR (AT) 369] has held that any other business or commercial rights of similar nature include such rights which can be used as a tool to carry on the business. The Income-tax Appellate Tribunal Hyderabad Bench in case of AP Paper Mills Ltd. Vs. ACIT (128 TTJ 596) while allowing depreciation on goodwill holding it to be an intangible asset observed that it is a business of commercial rights of similar nature to the rights mentioned in section 32 of the IT Act. The Income-tax Appellate Tribunal Mumbai Bench in case of M/s India Capital Markets P. Ltd. Vs. DCIT (ITA No.2948/Mum/2010 dated 12-12-2012 while considering a similar nature of acquisition of clientele held that acquisition of such clientele would come within the expression "any other business or commercial rights of similar nature" as the rights over the clients is used as a tool to carry on the business by the assessee and as such depreciation is allowable on such intangible asset.

13. It will be pertinent to mention here that the CIT (A) while coming to his conclusion that the clients creation cost paid by the assessee is not an intangible asset has relied upon the decision of Hon'ble Bombay High Court in case of CIT vs. Techno Shares and Stocks Ltd. And Others (225 CTR 337) wherein the Hon'ble Bombay High Court while considering the issue of transfer of membership

card of Bombay Stock Exchange has held that it does not constitute an intangible asset. However, this decision of the Hon'ble High Court has been reversed by the Hon'ble Supreme Court in Techno Shares and Stocks Ltd. Vs. CIT (327 ITR 323).

14. The learned departmental representative has relied upon a decision of Hon'ble Delhi High Court in case of Sharp Business Systems vs. CIT (ITA No.492/Del/2012 dated 5-11-2012) wherein the Hon'ble Delhi High Court has held that depreciation cannot be allowed on non compete fee as it does not come within the meaning of intangible asset as provided u/s 32(1)(ii) of the Act. However, a reading of the aforesaid judgment would make it clear that the Hon'ble Delhi High court came to such a conclusion as it held that an agreement on non compete fee is purely personal. The Hon'ble High Court further held that the words similar or commercial rights have to necessarily result in an intangible asset against the entire world which can be asserted as such to qualify for depreciation u/s 32(1) (ii) of the Act. However, the facts in the present case are different. The MOU between the assessee and SKS Society cannot be said to be purely personal. On the other hand, the acquisition of rights over the assets of SKS Society including the customer base is an intangible asset against the entire World as held by the Hon'ble Delhi High Court. Therefore, the facts of the case considered in the light of the ratio laid down by various judicial precedents referred to hereinabove, in our view, the client acquisition cost paid by the assessee is towards acquiring an intangible asset and therefore eligible for depreciation u/s 32(1)(ii) of the Act. In aforesaid view of the matter, we direct the Assessing Officer to allow the assessee's claim of depreciation. Hence, the grounds raised by the assessee are allowed.

15. The next issue as raised in ground Nos. 3 and 4 is with regard to disallowance of proportionate expenditure u/s 14A of the Act on earning of exempted income. During the assessment proceedings, the Assessing Officer noticed from the computation statement that

the assessee has received dividend from mutual fund amounting to Rs.1,13,616/- which is claimed as exempt u/s 10(35) of the Act. The disallowed amount of Rs.2,15,000/- treating it to be the expenditure incurred for earning the exempted income u/s 14A of the Act by observing that assessee has not furnished any details. The assessee challenged the disallowance before the first appellate authority.

16. On appeal, the CIT (A) also confirmed the disallowance.

17. The contention of the learned authorised representative of the assessee before us is twofold. Firstly, the assessee has not utilised any interest bearing fund for investing in the mutual fund. Hence, there can be no disallowance of expenditure. The second contention of the learned authorised representative of the assessee is that before making any disallowance u/s 14A of the Act, there must be a finding that the assessee has in fact incurred expenditure for earning the exempted income. In support of such contention, the learned authorised representative of the assessee relied on the decision of Hon'ble Bombay High Court in case of Godrej and Boyce Mfg. Co. Ltd. Vs. DCIT (328 ITR 81).

18. The learned DR , on the other hand, supported the order of the CIT (A).

19. We have heard rival submissions of the parties and perused the material on record. It is not in dispute that the assessee has earned dividend from mutual fund amounting to Rs.1,13,616 which is not taxable. The Assessing Officer has disallowed an amount of Rs,2,15,000 towards expenditure incurred for earning the exempted income u/s 14A of the Act with the observation that the assessee has failed to furnish any details. The CIT (A) has also confirmed such disallowance by observing that there was an increase in the borrowed funds during the year and though the term loans were to be utilised for the earmarked purposes however had the assessee not invested

in mutual fund the assessee 's borrowings could have been reduced to that extent. The CIT (A) by applying the ratio of decision of Hon'ble Kerala High Court in case of VI Baby & Co (254 ITR 248) held that interest to the extent on the amount of investment made on mutual fund cannot be considered as incurred for the purpose of business and has to be treated as earning exempted income. He therefore directed the Assessing Officer to work out the disallowance u/s 14A as per the terms of Rule 8D of the IT Rules.

20. Section 14A(1) of the Act provides that no deduction shall be allowed in respect of the expenditure incurred by the assessee in relation to the income which does not form part of the total income under the Act. Therefore, the expenditure incurred for earning the exempted income is subjected to disallowance. The Hon'ble Bombay High Court in case of Godrej Boyce Mfg. Co. Ltd vs. DCIT(supra) had held that the Assessing Officer should determine as to whether the assessee has incurred any expenditure (direct or indirect) in relation to dividend income/income from mutual fund which does not form part of the total income. The Hon'ble High Court further held while making that determination the Assessing Officer should provide a reasonable opportunity to the assessee for producing its accounts or relevant material having a bearing on the facts and the circumstances of the case. In the case of the assessee, the Assessing Officer has not afforded adequate opportunity to the assessee and has not given any finding whether the assessee has incurred direct or indirect expenditure for earning dividend income from mutual fund. The CIT (A) has also not given any conclusive finding in this regard. Further, the direction of the CIT (A) to determine the disallowance by applying Rule 8D is also not correct as the Hon'ble Bombay High Court in case of Godrej Boyce Mfg. Co. Ltd (supra) has held that provisions of Rule 8D is not applicable for the asst year 2006-07. In aforesaid view of the matter, we remit this issue to the file of the Assessing Officer who shall consider the issue afresh after giving a reasonable opportunity of being heard to the assessee.

21. In the result, this appeal is partly allowed.

ITA No.1222/Hyd/2010

22. The only issue in this appeal is with regard to disallowance of claim of depreciation of Rs.73,43,963/-. This issue is similar to the issue raised in ground No.1 and 2 of ITA No.435/Hyd/10. In view of our decision taken in ITA No.435/Hyd/120 while deciding the same, we direct the Assessing Officer to allow assessee's claim of depreciation.

23. In the result, this appeal is allowed.

ITA No.1789/Hyd/11

24. In ground Nos. 2 and 3, the assessee has raised the issue of disallowance of depreciation of an amount of Rs.55,82,972/-. In view of our decision taken on similar issue in ITA No.435/Hyd/2010 (supra), we allow the ground raised by the assessee and direct the Assessing Officer to allow the assessee's claim of depreciation.

25. In ground No.4 with its sub-grounds, the assessee has challenged disallowance of interest of Rs.14,72,524 on loan to Managing Director and disallowance of notional interest at the rate of 9% amounting to Rs.23,03,480 on account of advancing loans to employees welfare trust.

26. Briefly the facts are, during the assessment proceedings, the Assessing Officer noticed that the assessee has given an interest free loan of Rs.1,63,61,380/- to its Managing Director (MD in short)on 27-3-2007. The assessee explained before the Assessing Officer that the MD has utilised the loan to buy shares in the assessee company. It was further submitted that the MD had considered the interest of Rs.

29,79,860 as a perquisite u/s 17(2) of the Act in his individual return. The Assessing Officer however did not accept the contention of the assessee and disallowed interest of Rs. 14,72,524/-. It was further noticed by the Assessing Officer that the assessee has advanced interest free loan of Rs.2,55,94,223/- to SKS employees Trust during the year. In response to the query made by the Assessing Officer it was submitted that the trust has been created exclusively for the benefit of the employees of the company and to provide financial assistance to the employees for purchasing equity shares of the company under employee share purchase scheme. It was submitted that as the loan has been advanced for the benefit of the employees it should be regarded as solely and exclusively for the purpose of business and no disallowance of interest payment should be made. The Assessing Officer however did not accept the submissions of the assessee and disallowed an amount of 23,03,418.

27. The CIT (A) after considering the submissions of the assessee sustained the addition by observing that the shares to be acquired by the MD or the employees were to be their personal properties. He further observed that the assessee has not been able to establish that but for the acquisition of share by the MD or the employees the assessee could have been put to some financial disadvantage. He further observed that the assessee has also not established that the loan was given to the MD or the employees to promote the business of the assessee company itself. Accordingly, the CIT (A) held that proportionate interest has to be disallowed as funds of the company were diverted for non business purposes by providing interest free loans.

28. We have heard rival submissions of the parties and perused the material on record. It is the contention of the assessee that the interest free loans were advanced due to commercial expediency and for the purpose of business. It is the further contention of the assessee that no borrowed fund was utilised for advancing loan to the

MD or the employee's welfare trust. From the assessment order or the order of the CIT (A), we do not find any clear cut finding whether the assessee has utilised borrowed funds for giving loan to the MD or employees welfare trust. In case of SSPDL Ltd. Vs. DCIT (24 ITR (Trib) 290 co-ordinate bench of this Tribunal held that unless interest payment is directly related to the diverted funds, it cannot be said that interest incurred by the assessee was for non business purpose. Since this fact has not been properly verified, we remit this issue to the file of the Assessing Officer who shall decide the same after a reasonable opportunity of being heard to the assessee.

29. In ground No.5, the assessee has challenged the disallowance of de-recognition of interest on NPA amounting to Rs. 9,63,944/-.

30. During the assessment proceedings, the Assessing Officer noticed that the assessee has offered the interest income on loan net of interest de-recognised of Rs.9,63,944/-. In the notes to accounts, the assessee has mentioned that the income on NPA is recognised only when realised and any interest accruing on such asset is de-recognised totally by reversing the interest income already recognised. It was submitted before the Assessing Officer that the prudential norms and the directions of the RBI on NBFCs laid down that income from NBFCs may not be recognised merely on the basis of accruals. The assessee also relied upon the Board's Circular No. 491 dated 30-6-87. The Assessing Officer did not accept the contention of the assessee as the assessee is following mercantile system of accounting. Hence interest having been credited to the Profit & Loss a/c, the interest in respect of NBPCs could not been reversed. The Assessing Officer further observed that RBI guidelines cannot over-ride the provisions of the IT Act nor it can create any liability beyond the provisions of the Act. Accordingly, the amount of Rs.9,63,944/- wad added back to the income of the assessee . The CIT (A) also sustained the addition by observing that the assessee having already recognised the income cannot de-recognise it again.

31. We have heard rival submissions of the parties and perused the material on record. It is not disputed that the interest amount of 9,63,944/- relate to interest on NPAs and has been taken on accrual basis. It is nobody's case that the assessee has actually received the interest income. The prudential norms of RBI or NBFCs have laid down that income from NPAs may not be recognised on accrual basis. The Hon'ble Supreme Court in case of Southern Technologies Ltd. Vs. JCIT (320 ITR 577) held that income recognition with regard to NPAs should be as per section 45Q of the RBI Act. Following the aforesaid decision of Hon'ble Supreme Court, the Hon'ble Delhi High Court in case of CIT vs. Vasisth Chay Vyapar Ltd., and another (330 ITR 440) held that where even the principal amount itself had become doubtful of recovery it cannot be said that interest thereupon had accrued. The Hon'ble Delhi High Court further held that having regard to the provisions of section 45Q of the RBI and prudential norms issued by the RBI in exercise of its statutory powers where interest was not received on non performing asset and the possibility of recovery was almost nil it could not be treated to have been accrued in favour of the assessee. Therefore, considered in the light of the ratio laid down as above it cannot be said that interest of an amount of Rs.9,63,944/- has accrued to the assessee. In aforesaid view of the matter, we direct the Assessing Officer to delete the amount of Rs.9,63,944. Hence, this ground of the assessee is therefore allowed.

32. Ground No. 6 with its sub-grounds relate to the disallowance of interest amounting to Rs.2,26,850/- u/s 14A towards earning of exempted income. While considering similar in assessee's appeal in ITA No. 435/Hyd/10, we have remitted the issue back to the file of the Assessing Officer for determining whether any expenditure is relatable to earning of the exempted income after affording a reasonable opportunity of being heard to the assesseex. This ground is allowed for statistical purposes.

33. In ground No.7, the assessee has challenged the levy of interest u/s 234B of the Act.

34. We have heard rival submissions of the parties and perused the material on record. Levy of interest is consequential in nature and it would ultimately depend upon final computation of tax to be made by the Assessing Officer. Hence, at this stage, this issue is not required to be adjudicated upon.

35. In the result, ITA Nos. 435/Hyd/10 and 1789/Hyd/11 are partly allowed while ITA No. 1222/Hyd/2010 is allowed.

Order was pronounced in the open Court on 21 -06-2013.

Sd/-	Sd/-
(CHANDRA POOJARI)	(SAKTIJIT DEY)
ACCOUNTANT MEMBER	JUDICIAL MEMBER

Dated: the 21st June, 2013.

Copy forwarded to:

1. C/o M/s Sekhar & Co./ CAs, 133/RP Road, Secunderabad.
2. Addl.CIT, Range-3, Hyderabad.
3. CIT (A)-IV, Hyderabad.
4. CIT concerned, Hyderabad.
5. The DR, ITAT, Hyderabad

Jmr*