

**IN THE INCOME TAX APPELLATE TRIBUNAL  
MUMBAI BENCH "I" MUMBAI**

**BEFORE SHRI SAKTIJIT DEY (JUDICIAL MEMBER) AND  
SHRI N.K. PRADHAN (ACCOUNTANT MEMBER)**

**ITA No. 3170/MUM/2016  
Assessment Year: 2006-07**

**&**

**ITA No. 3171/MUM/2016  
Assessment Year: 2007-08**

The Asst. Commissioner of  
Income Tax 15(2)(1) Room  
No. 357, 3<sup>rd</sup> floor, Aayakar  
Bhavan, Maharshi Karve  
Road, Mumbai-400020.

**PAN No. AACCK5409J**

**Appellant**

Vs. M/s Krystal Colloids Pvt. Ltd.  
119, Purusharth Bldg., Nawroji  
Hill Road, No. 2, Dongri,  
Mumbai, 400009.

**Respondent**

Revenue by : Mr. Anoop Hiwase, DR  
Assessee by : Mr. Anuj Kisnadwala, AR

Date of Hearing : 07/05/2018  
Date of pronouncement: 31/07/2018

**ORDER**

**PER N.K. PRADHAN, AM**

The captioned appeals filed by the Revenue are directed against the order of the Commissioner of Income Tax (Appeals)-12, Mumbai [in short 'CIT(A)'] and arise out of the assessment completed u/s 143(3) r.w.s.147 of the Income Tax Act 1961 (the 'Act'). As common issues are involved, we are proceeding to dispose them off through a consolidated order for the sake of convenience. Facts being identical, we begin with the assessment year (AY) 2006-07.

2. The ground of appeal reads as under:

On the facts and circumstances of the case in law, the Ld. CIT(A) erred in deleting the disallowance of depreciation on intangible assets and other assets amounting to Rs.36,75,000/- acquired by the assessee from proprietary concern pursuant to conversion u/s 47 (xiv) of the Act even when the proprietary concern was not possession of any intangible assets which could fit into basic definition of intangible assets as per the Income Tax Act, 1961.

3. In a nutshell, the facts are that the assessee had claimed depreciation of Rs.36,75,000/- [@ 10% on Written Down Value (WDV) of intangible assets of Rs.3,67,50,000/-] as per Schedule-4 of fixed assets to Form 3CD. In response to a query raised by the AO during the course of assessment proceedings, the assessee submitted that the business of the proprietor Mr. Nayan Mevani was acquired by way of a transfer by the assessee and the conversion was carried out under the provisions of section 47(xiv) of the Act. It was also stated before the AO that the conversion was carried out by bringing all the assets and liabilities of the proprietary firm at their respective fair value including intangible assets and the valuation of the assets was carried out by a government approved valuer. The intangible assets comprised of the following :

1.	Technical Knowhow	Rs. 2,75,00,000/-
2.	Trademarks & Trade Name	Rs. 67,50,000/-
3.	Goodwill	Rs. 25,00,000/-
	<b>Total</b>	<b>Rs. 3,67,50,000/-</b>

It was also submitted before the AO that in the course of corporatization, the assessee acquired all the assets (including intangible assets) and liabilities from Mr. Nayan Mevani, proprietor of Krystal Colloids vide 'Agreement for Assignment of Business' dated 24.03.2005 and had discharged the consideration for the transfer by issue of equity shares. The assessee thus submitted before the AO that it has rightly claimed depreciation @ 10% on WDV of intangible assets.

However, the AO was not convinced with the above explanation of the assessee for the reason that the assessee himself is the owner in the instant case and there is no transfer involving sister concerns as the management and owners remain the same. The AO noted that the assessee-company is claiming depreciation on intangible assets acquired on conversion from proprietary concern to corporate entity on 31.03.2005. The proprietary-firm, just before conversion, carried out valuation of its fixed assets on account of which intangible assets of Rs.3,67,50,000/- were added to the fixed assets, on the basis of registered valuer's valuation report. The AO further observed from details filed in respect of creation of intangible assets and its valuation that the proprietary-firm was infact not in possession of any intangible assets which had allegedly been transferred to the assessee-company on conversion. The AO noted that as per the valuer's report, on revaluation, the proprietary-firm was in possession of technical knowhow worth Rs.275.00 lakhs and trademarks at Rs.67.50 lakhs.

The AO, referring to Accounting Standard (AS)-26 observed that there were three parameters which should exist to meet the definition

of an intangible assets namely identifiability, control over resource and expectation of future economic benefits flowing to the enterprise. The AO found from the details filed by the assessee that it had tried to project the technique and expertise in its manufacturing process as an intangible assets owned by it, which is not acceptable as per AS-26 as well as within the meaning of intangible asset in the Act.

The AO also found that the assessee is not eligible for depreciation on intangible assets as per the 5<sup>th</sup> proviso to section 32(1) which provides that the aggregate deduction in respect of depreciation allowable to the predecessor and successor in the case of succession referred to in clause (xiii) of section 47 shall not exceed in any previous year the deduction calculated at the prescribed rate as if succession had not taken place. The proprietary concern has added the intangible assets in its fixed assets on the basis of the registered valuer's report just before conversion. The intangible assets added on revaluation, were self-generated assets in the hands of the proprietary-firm and its actual costs to the proprietary concern was Nil. Thus the AO held that the assessee-company as well as the proprietary-firm were not entitled to claim any depreciation on the intangible asset, the same being internally generated assets and having no actual cost.

Finally, the AO also held that the assessee is not entitled to depreciation claim on intangible asset in view of provisions of Explanation-3 to section 43(1), which has been created as a safeguard to protect the interest of revenue against corporatization schemes, which

are devoid of economic or commercial justification and can be regarded as pure tax planning scheme.

The AO thus held that in assessee's case, the proprietary concern has been converted into corporate concern having two shareholders i.e. the assessee and his wife. The assessee is having 99% of shareholding and the remaining 1% shareholding is with his wife. Thus, for all practical purposes, the control and management of business has remained with the same person as before conversion. No new shareholder has been added to augment the share capital base of the company or professional/technical competence.

By holding that the sole aim of conversion appears to claim extra depreciation on intangible assets acquired during the course of running of proprietorship-firm, the AO disallowed the claim of depreciation of Rs.36,75,000/- made by the assessee.

4. Aggrieved by the order of the AO, the assessee filed an appeal before the Ld. CIT(A). We find that the Ld. CIT(A) has followed the appellate order passed by her predecessor in respect of AYs 2008-09 and 2009-10 and allowed the appeal, thus holding that (i) the action of the AO in disallowing the benefit of depreciation on intangible assets to the assessee cannot be upheld, if such disallowance was to be made, it should have been done in AY 2005-06, itself, (ii) the 5<sup>th</sup> proviso to section 32 is only applicable in the year of succession and it cannot be applied to the succeeding year, in this case the succession was carried out on 31.03.2005 and the appeal pertains to AY 2008-09.

5. Before us, the Ld. DR submits that the proprietary concern was not in possession of any intangible asset which could fit into the basic definition of intangible assets as per the Act, therefore, the Ld. CIT(A) erred in deleting the disallowance of depreciation on intangible assets and other assets amounting to Rs.36,75,000/- acquired by the assessee from the proprietary concern pursuant to conversion u/s 47(xiv) of the Act. Thus the Ld. DR supports the order passed by the AO.

6. *Per contra*, the Ld. counsel of the assessee reiterates statement of facts filed before the Ld. CIT(A) stating that erstwhile, the business of the assessee was carried out by a proprietary concern by the trade name of Krystal Colloids, headed by Mr. Nayan Mepani. With a view to organize its business as a corporate entity for the purpose of better image, for getting economies of scale, setting up of new factory, raising of debt and equity resources etc., it was decided to convert the business from a proprietary concern to a corporate entity. Accordingly, the business was assigned to a private limited company (the assessee) being the successor. The assessee purchased/acquired the entire business and had accordingly issued shares to the proprietor for a like amount in compliance with the provisions of section 47(xiv) of the Act. The proprietary concern had transferred all the assets and liabilities to the assessee at the book values of the respective assets and liabilities. For the purpose of transfer and conversion, the proprietary concern had revalued certain assets to bring them to their fair values, on the basis of a detailed valuation report from the government approved valuer. Thereafter, the proprietary concern had transferred these assets to the assessee and the assessee acquired the business, including the assets at

the revalued amounts. The assessee had claimed depreciation u/s 32 on the cost paid by it in accordance with the provisions of law and as per judicial decisions. The intangible assets acquired included trademarks, technical knowhow and goodwill.

The Ld. counsel submits that the AO failed to acknowledge that the actual cost of assets cannot be challenged once the asset forms part of the block of assets because once the asset becomes part of the block of assets, the individual asset loses its independent identity. It is stated that the depreciation on intangible assets was allowed to the assessee in AY 2005-06 i.e. the year of acquisition during scrutiny assessment.

7. We have heard the rival submissions and perused the relevant materials on record. The reasons for our decision are given below.

In the instant case, the AO has allowed the depreciation on intangible assets in AY 2005-06. There is no dispute that the year of acquisition of the intangible assets was financial year 2004-05, relevant to the assessment year 2005-06.

Now we turn to the concepts of 'block of assets'. The same has been defined by section 2(11) to mean a group of assets falling within a class of assets, comprising-

- a. tangible assets, being buildings, machinery, plant or furniture;
- b. intangible assets, being knowhow, patents, copyrights, trademarks, licenses, franchises or any other business or commercial rights of similar nature,

in respect of which the same percentage of depreciation is prescribed. A “block of assets” includes assets of all units of the assessee having same rate of depreciation and not assets of only one unit.

Once an asset is part of the block of assets and depreciation is granted on that block, it cannot be denied in its subsequent year on the ground that one of the assets is not used by the assessee in some of years. The concept “user” of assets has to apply upon block as a whole instead of an individual asset. In this context, we place reliance on the decision in *Unitex Products Ltd. v. ITO* [2008] 22 SOT 430 (Mum.), *CIT v. Bharat Aluminum Co. Ltd.* (2010) 187 Taxman 111 (Delhi), *CIT v. Oswal Agro Mills Ltd.* (2011) 197 Taxman 25 (Delhi), *Swati Synthetics Ltd. v. ITO* (2010) 38 SOT 208 (Mum).

7.1 The Hon’ble Bombay High Court in the case of *CIT v. Western Outdoor Interactive Pvt. Ltd.* (2012) 349 ITR 309 (Bom) has held that whether a benefit of deduction is available for a particular number of years on satisfaction of certain conditions and under the provisions of the Act, then without withdrawing or setting aside the relief granted for the first AY in which claim was made and accepted, the AO cannot withdraw the relief for subsequent assessment years. This ratio was laid down in the context of section 80A of the Act. Subsequently, similar issue was upheld in *CIT v. Arts & Crafts Exports* (2012) 246 CTR 463 (Bom).

The Hon’ble Delhi High Court in the case of *CIT v. Tata Communication Internet Services Ltd.* (2012) 204 Taxman 606 (Del) has held that bar as provided u/s 80IA(3) is to be considered only for the



first year of a claim for deduction u/s 80IA and not in the subsequent years. In that case, the AO had raised the issue of splitting up or reconstruction of already existing business in the subsequent year, when in the first year of claim this issue was not disturbed.

Again, the Hon'ble Bombay High Court in *CIT v. Paul Brothers* (1995) 216 ITR 548 (Bom), *Direct Information (P) Ltd. v. ITO* (2011) 203 Taxman 70 (Bom) has held that once a benefit of deduction was extended in respect of a provision for a particular number of years then unless the benefit is withdrawn for the first year, it cannot be withdrawn subsequent years, particularly, when there is no change in the facts.

In view of the ratio laid down in the above decisions, the above issue could be raised in the AY 2005-06 when the assets entered into the block. Once the assets became part of a block of assets in AY 2005-06, and depreciation is granted on that block, the issue cannot be agitated in the AYs 2006-07 and 2007-08.

In view of the above reasons, we uphold the order of the Ld. CIT(A).

8. In the result, the appeals are dismissed.

**Order pronounced in the open Court on 31/07/2018.**

Sd/-  
(SAKTIJIT DEY)  
JUDICIAL MEMBER

Sd/-  
(N.K. PRADHAN)  
ACCOUNTANT MEMBER

Mumbai;

Dated: 31/07/2018

*Rahul Sharma, Sr. P.S.*

**Copy of the Order forwarded to :**

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

//True Copy//

BY ORDER,

(Dy./Asstt. Registrar)  
**ITAT, Mumbai**