

ITAT rules, Additional Depreciation on assets acquired during the year restricted under proviso to section 32(1)(ii), deductible in the subsequent year

Executive Summary

This tax alert summarises the recent ruling of Delhi Income Tax Appellate Tribunal (ITAT) in the Cosmo Films Ltd¹ (Taxpayer) on an issue: whether, additional depreciation pursuant to section 32(1)(iia) of the Income Tax Act (ITA) on new assets acquired during the previous financial year and put to use for less than 180 days, in respect of which, depreciation was claimed at 50% of the qualifying amount; the remaining depreciation out of the qualified amount be allowed to the Taxpayer in the succeeding year?

In the financial year 2003 – 04, the Taxpayer claimed balance amount of additional depreciation on the new eligible assets put to use after 30.09.2002, the 50% of the qualifying amount whereof claimed in the financial year 2002 – 03.

The Taxpayer's claim for the balance additional depreciation was denied in the assessment and in the first appeal as well. On appeal to the ITAT, held that the claim of the Taxpayer for the balance depreciation has to be allowed.

Background

To provide incentives for fresh investment in industrial sector, pursuant to section 32(1)(iia) of the ITA; it is provided that in respect of new machinery or plant (other than

ships and aircraft) acquired and installed after the 31st March 2002, additional depreciation at the prescribed rate² shall be allowed over and above the normal depreciation which a Taxpayer is entitled to under section 32(1) of the ITA. However, pursuant to proviso to section 32(1)(ii), the depreciation is restricted to 50% of the qualifying amount in a case where the assets are acquired during the financial year and put to use for less than 180 days

Facts

The Taxpayer acquired assets in the second half of the financial year 2002 – 03 in respect of which claimed additional depreciation under section

¹ ITA No. 2508 of 2007

² @ 15% - increased to 20% w.e.f. assessment year 2006 – 07

32(1)(iia) of the ITA. As the assets were put to use for less than 180 days, he claimed only 50% of the qualifying depreciation for the said financial year and claimed balance amount of the depreciation in the subsequent year. The deduction for the balance amount was denied by the Tax Authorities in the assessment. The first appellate authority confirmed the order of the Tax Authorities. The Taxpayer preferred an appeal to the ITAT, whose decision is discussed hereunder.

Taxpayer's contentions

- The assets were acquired during the second half of the financial year 2002 – 03, hence only 50% of the additional depreciation was claimed in respect of such assets in the said year
- The second proviso to section 32(1)(ii) which restricts the allowance of depreciation to 50% of

the qualifying amount, cannot overlook the one time allowance which is a statutory right earned in the year of acquisition. Had there been any legislative intention to restrict the overall allowance to 50%, then it could have been so provided expressly in the ITA

- The statutory right provided to the Taxpayer under a particular section of the ITA cannot be ignored or taken away by another provision of the ITA
- The ITA does not prohibit the allowance of the remaining amount of the additional depreciation in respect of the assets acquired in the second half of the previous financial year

Tax Authority's contentions

- The additional depreciation on assets acquired during the financial year can be allowed fully when the assets are put to use for more than

180 days in the year of acquisition. The additional depreciation on assets used for less than 180 days remains restricted to 50% of the qualifying amount as per the second proviso to the section 32(1)(ii) of the ITA

- There cannot be any carried forward additional depreciation to be allowed in subsequent year

ITAT Ruling

- The additional allowance under section 32(1)(iia) is made available as certain percentage of actual cost of new assets acquired or installed. This provision had been directed towards encouragement of industrialization by allowing additional benefits to the setting up of new industrial undertakings or for expansion of the industrial undertaking by way of making more investment in capital goods

- Section 32(2) of the ITA provides for carry forward provision of unabsorbed depreciation
- In view of the decision of the Supreme Court in the case of Bajaj Tempo Ltd.³, the provisions related to section 32(1)(iia) have to be construed reasonably, liberally and purposively to make the provision meaningful while granting allowance
- The additional depreciation benefit was provided to give impetus to industrialization and therefore deserves to get benefit in full when there is no restriction in the statute to deny the benefit of balance of 50% in respect of the new assets acquired and used for less than 180 days
- In section 32(1)(iia), the expression used is 'shall be allowed'. Thus, the Taxpayer had earned the benefit as soon as he

had purchased the new asset in full but restricted to 50% in that particular year on account of period of usage.

- The earned incentive in the form of additional depreciation to the extent could not be availed in the year of acquisition of the assets, must be available in the subsequent year

Our Comments

The ruling would bring the much needed clarity on allowability of the additional depreciation in respect of the assets acquired during the second half of the year and therefore affected by the restriction on the deduction pursuant to proviso to the section 32(1)(ii) of the ITA

However, the prescribed Income Tax Return forms, which are required to be filed electronically, do not have appropriate field where the claim of the balance depreciation amount referred

to in this ruling can be incorporated. As a practical measure, the Taxpayer may have to claim deduction under a general head and suitably modify and present the written down value of the assets in the Income Tax Return and explain the tax position by a separate communication to the Tax Authorities

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³ 196 ITR 188

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At your Service

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