

Claim of depreciation mandatory while computing deduction under section 80-IA

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In brief

In a recent decision¹, the Supreme Court of India (SC) held that depreciation is mandatorily required to be reduced while computing eligible profits for deduction under section 80-IA of the Income-tax Act, 1961 (Act).

Furthermore, the SC held that section 80-IA of the Act is a code by itself and any device adopted to reduce or inflate the profits of eligible business has to be rejected.

In detail

Facts

- The taxpayer, a Company engaged in the manufacturing of master batches and compounds, had two undertakings eligible for 100% deduction under section 80-IA of Act.
- For assessment year 1997-98, the taxpayer did not claim depreciation under the Act while computing its income. The taxpayer claimed deduction under section 80-IA of the Act based on the same profits, i.e., without claiming depreciation allowance.
- The tax officer (TO) reassessed the income of the taxpayer and computed GTI after allowing depreciation under section 32 of the Act and setting off brought forward losses. The resultant GTI being a loss, no deduction under section 80-IA was allowed to the taxpayer.
- On appeal, the Commissioner of Income-tax (Appeals) [CIT(A)], upheld the taxpayer's submission that the claim of depreciation was optional and directed the TO to work out the deduction under section 80-IA of the Act without taking into consideration the depreciation allowance.
- Aggrieved, the TO preferred an appeal before the Income-tax Appellate Tribunal (Tribunal), which reversed the order of the CIT(A).

Issue before the Supreme Court

Whether while computing the eligible income of an undertaking for the purposes of claim of deduction under

section 80-IA of the Act, depreciation has to be mandatorily allowed even though the taxpayer has exercised the option not to claim depreciation under section 32 of the Act while computing its income under the head profits and gains of business or profession (PGBP).

Taxpayer's contention

- Section 80-IA of the Act provided that where the GTI includes profit and gains from an eligible undertaking/ business there shall be allowed a deduction from "such profit and gains" at certain prescribed percentages.
- Thus, while computing the profit or gain of the eligible undertaking in accordance with section 30 to 43D of the Act, which includes section 32 of the Act, the taxpayer has the option

¹ Civil Appeal no. 238 of 2012

whether or not to claim depreciation under section 32 of the Act in light of the decision of the SC in the case of Mahendra Mills.²

- Furthermore, sub-sections (9) and (10) of section 80-IA of the Act, which provide for specific eventualities wherein the eligible profit and gains could be adjusted, did not deal with section 32 of the Act.

Revenue's contention

The explanation, which provides that depreciation shall be mandatorily allowed whether or not the same was claimed by a taxpayer, was declaratory in nature and therefore was to be applied retrospectively³. Hence, the taxpayer could not optionally claim depreciation.

Supreme Court Ruling

The SC rejected the arguments of the Taxpayer. The SC discussed the judgement of the Bombay HC and upheld the following findings made by the Bombay HC:

- The judgment of the SC in the

case Mahendra Mills, wherein it was held that whether to claim the depreciation or not is the option available with assessee and it cannot be thrust upon the assessee, is not applicable in the present case as

- i the judgment was rendered in the context of computation of income by the virtue of Chapter IV not in the context of Chapter VI-A of the Act; and
 - ii the said decision cannot be read to mean that by disclaiming current depreciation, enhanced deduction can be claimed under any other provision of the Act.
- Chapter VI-A of the Act (which contains section 80-IA) is a complete code by itself⁴ and section 80-IA is a special deduction, which is linked to profits unlike investment linked incentives.
 - Section 80-IA contains both substantive and procedural

provisions for computation of the special deduction. The deduction under section 80-IA of the Act has to be computed after all deductions allowable under sections 30 to 43D of the Act and any device adopted to reduce or inflate the profits of the eligible business has to be rejected⁵.

- The Taxpayer by not claiming current depreciation seeks to inflate the profit-linked incentives provided under section 80-IA of the Act which is not permissible as per the law laid down by the SC in the case of Liberty India⁵.

The takeaways

Depreciation is mandatorily required to be reduced while computing deduction under section 80 IA of the Act.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact your local PwC advisor

² CIT v. Mahendra Mills [2000] 243 ITR 56 (SC)

³ CIT, Bombay v. M/s Gwalior Rayon Silk Manufacturing Co. Limited [1992] 3 SSC 326 [SC]; Commissioner of Income Tax v. Alps Theatre AIR 1967 SC 1437 [SC];

Commissioner of Income-tax-I, Ahmedabad v. Gold Coin Health Foods Private Limited [2008] 9 SCC 622 [SC]

⁴ Liberty India v. Commissioner of Income Tax [2009] 317 ITR 218 [SC]; CIT v. Williamson Financial Services & Ors.

[2008] 297 ITR 17 [SC]; CIT, Dibrugarh v. Doom Dooma India Limited [2009] 310 ITR 392 [SC]

⁵ Liberty India v. Commissioner of Income-tax [2009] 317 ITR 218 [SC]

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