Controversies

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Whether depreciation can also be claimed by a Charitable Trust when the investment in fixed asset is also claimed as deduction treating the same as application of income?

Issue:

MGD Charitable Trust a Public Charitable Trust registered u/s. 12 AA of the Income Tax Act 1961 as a Charitable Trust. For the A.Y. 2014-15 the assessee trust has claimed depreciation on certain assets acquired earlier & claimed as application of money. The Assessing Officer has disallowed the claim of depreciation calculated as per statutory provision on the ground that since income of the assessee was exempt from tax u/s 11 to 13, the deduction would amount to double benefit.

Proposition:

It is proposed that the income of the Charitable Trust being exempt, the assessee trust is only claiming that amount of depreciation should be reduced from the income for determining the percentage of funds which have to be applied for the purpose of the trust.

View against the proposition:

The Hon. Supreme Court in the case of Escorts Ltd. V/s. UOI & others reported in 199 ITR 43, has held as under:

"Where a capital asset used for scientific research related to the business of the assessee is also ipso facto an asset used for the purpose of the business, it is impossible to conceive of the Legislature having envisaged a double deduction in respect of the same expenditure, one by way of depreciation under section 32 of the Income Tax Act, 1961, and the other by way of allowance under section 35(1)(iv) of a part of the capital expenditure on scientific research, even though the two heads of deduction do not completely overlap and there is some difference in the rationale of the two deductions. Under the provisions of the Act as they stood prior to the 1980 Amendment, the assessee could not have claimed continued grant of depreciation after the expiry of the period of five years before the 1968 Amendment and after the expiry of the first year after the 1968 Amendment during which period the entire cost of the capital asset has been allowed to be set off completely by way of allowance u/s. 35(1)(iv) against the business profits of those five years or the one previous year as the case may be.

There is a fundamental, though unwritten, axiom that no Legislature could have at all intended a double deduction in regard to the same business outgoing and if it is intended, it will be clearly expressed. In other words, in the absence of clear statutory indication to the contrary, the statute should not be read so as to permit an assessee two deductions both u/s. 10(2)(vi) and section 10(2)(xiv) of the 1922 Act or both u/s. 32(1)(ii) and section 35(1)(iv) of the 1961 Act. The use of the words "in respect of the same previous year" in clause (d) of the proviso to section 10(2)(xiv) of the 1922 Act and section 35(2)(iv) of the 1961 Act is to indicate that there is a basic scheme, unspoken but clearly underlying the Acts, that the two allowances cannot be and are not intended to be granted in respect of the same asset or expenditure. These provisions mandate that the assessee should, in a case where the assessee qualifies for both the allowances, be granted the special allowance for scientific research and not the routine annual one for depreciation.

View in favour of the proposition:

The Hon. Bombay High Court in the case of CIT v. Institute of Banking (2003) 264 ITR 110 (Bom.) has held as under:

"The tribunal was right in law in directing the Assessing Officer to allow depreciation on the assets, the cost of which had been fully allowed as application of income under section 11 in the past years.

Income of the Trust is required to be computed under section 11 on commercial principle after providing for allowance for normal depreciation and deduction thereof from the gross income of the Trust."

Also the Hon. Bombay High Court in the case of DIT Exemption v. Framjee Cawasjee Institute (1993) 109 CTR 463 (Bom.) has held that the assessee was the trust. It derived its income from depreciable assets. The assessee took into account depreciation on those assets in computing the income of the trust. The Income-tax Officers held that depreciation could not be taken into account because; full capital expenditure had been allowed in the year of acquisition of the assets. The assessee went in appeal before the appellant assistant commissioner. The appeal was rejected. The tribunal, however, took the view that when the income tax officer stated that full expenditure had been allowed in the year of acquisition of the assets, what he really meant was that the amount spent on acquiring those assets had been treated as "application of income" of the trust in the year in which the income was spent in acquiring those assets. This did not mean that in computing income from those assets in subsequent years, depreciation in respect of those assets cannot be taken into account.

In the case of CIT v. Society of the sisters of St. Anne (1984) 146 ITR 28 the Karnataka High Court has held that if depreciation is not allowed as a necessary deduction for computing the income of a charitable institution, then there can be no way to preserve the corpus of the trust for deriving the income. Therefore, the amount of depreciation debited to the accounts of a charitable institution is to be deducted to arrive at the income available for application to charitable and religious purposes.

This has been followed in Recent Tribunal's judgment of Chennai Tribunal which confirms with the same principle. In Shri Rengalatchumi Education Trust v. ITO (OSD) Exemptions (2012) 137 ITD 318 (Chennai)

It was Held For the purpose of determining the income of trust eligible for exemption u/s. 11, income should be construed strictly in commercial sense (i.e. normal accounting principles), without reference to the heads of income specified in section 14. The income to be considered is the book income and not the total income as defined in section 2(45). The concept of commercial income necessarily envisages deduction of depreciation on the assets of the trust. This position is as confirmed by the CBDT vide its circular No. 5-P (LXX-6), dated 19/05/1968. Normal accounting principles clearly provide for deducting depreciation to arrive at income. Income so arrived at (after deducting depreciation) is to be applied for charitable purpose. Capital expense is applicable of income so determined. Hence, there is no double deduction or double claimed of the same amount as application.

Thus, depreciation is to be deducted to arrive at income and it is not application of income.

Summation:

The Punjab & Haryana High Court distinguishing the Supreme Court judgment in the case of Escorts Ltd. u/s. UOI 199 ITR 43(SC) has held in the different case as under:

In CIT v/s Market Committee Pipli 330 ITR 16 and also in CIT v/s Tiny Tots Education Society 330 ITR 21.

In the present case, the assessee is not claiming double deduction on account of depreciation as has been suggested by learned counsel for the Revenue. The income of the assessee being exempt. The assesse is only claiming that depreciation should be reduced from the income for determining the percentage of funds which have to be applied for the purpose of the trust. There is no double deduction claimed by the assessee as canvassed by the Revenue. The judgment of the Hon'ble Supreme Court in Escorts Ltd. (1993) 199 ITR 43 is distinguishable for the above reasons. It cannot be held that double benefit is given in allowing claim for depreciation for computing income for purposes of section 11. The questions proposed have, thus, to be answered against the Revenue and in favour of the assessee.

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