

IN THE HIGH COURT OF GUJARAT AT AHMEDABAD**INCOME TAX REFERENCE No. 41 of 1994****For Approval and Signature:****HONOURABLE MR.JUSTICE D.A.MEHTA****AND****HONOURABLE MS.JUSTICE H.N.DEVANI**

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- 1 Whether Reporters of Local Papers may be allowed to see the judgment?
 - 2 To be referred to the Reporter or not?
 - 3 Whether their Lordships wish to see the fair copy of the judgment?
 - 4 Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 or any order made thereunder?
 - 5 Whether it is to be circulated to the Civil Judge?
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COMMISSIONER OF INCOME-TAX - Applicant
Versus
DAUDAYAL HOTELS PVT LTD - Respondent

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Appearance :

MR BB NAIK for the Applicant.

NOTICE SERVED for the Respondent.

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CORAM : HONOURABLE MR.JUSTICE D.A.MEHTA
and
HONOURABLE MS.JUSTICE H.N.DEVANI

Date : 31/08/2005

ORAL JUDGMENT

(Per : HONOURABLE MR.JUSTICE D.A.MEHTA)

1. Income Tax Appellate Tribunal, Ahmedabad Bench "A" has referred following question under Section 256(1) of

the Income Tax Act, 1961 (the Act) at the instance of the Commissioner of Income Tax, Baroda :-

"Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that initial depreciation allowed in A.Y. 1982-83 on new hotel building is not deductible for arriving at WDV in view of the amendments effected by Finance Act, 1983?"

2. The Assessment Year is 1985-86 and the relevant accounting period is calender year ended on 31st December, 1984. While computing depreciation allowance under Section 32 of the Act, the Assessing Officer, decreased the Written Down Value (WDV) of hotel building by deducting initial depreciation, allowed to the assessee in Assessment Year 1982-83. The assessee, being aggrieved, carried the matter in appeal before the Commissioner of Income Tax(Appeals).

3. By order dated 27/07/1988, the C.I.T. (Appeals) came to the conclusion that the WDV was wrongly reduced by deduction of initial depreciation amounting to Rs. 6,74,500/- (Rupees Six Lakhs Seventy Four Thousand Five Hundred only). It was noted by the Commissioner

(Appeals) that the Assessee- Company had commenced its business of running hotel with effect from 25/10/1981. That, though normal depreciation was allowed in the Assessment Year 1982-83, initial depreciation was not debited because of provisions of Section 32(1)(v) of the Act, which prohibited such allowance, as they stood at the relevant time. It is further noted by C.I.T. (Appeals) that WDV at the beginning of calender year 1982, being Previous Year relevant to Assessment Year 1983-84, was adopted on the basis of the normal depreciation allowed for the immediate proceeding Assessment Year namely, Assessment Year 1982-83. Thereafter, the same pattern was followed for Assessment Year 1984-85, subject to addition in the Written Down Value to the extent of actual cost of newly purchased assets. The C.I.T.(Appeals) accepted the contention of the assessee that deletion of phrase "*but any such sum shall not be deductible in determining the written down value for the purposes of Clause (ii)*" with effect from 1st April, 1984 could not be applied retrospectively. He, therefore, held that the assessment order was incorrect to the extent it reduced the WDV by a sum of Rs. 6,74,500/-, which was granted as an initial depreciation in Assessment Year 1982-83.

4. Revenue carried the matter in appeal before the Tribunal. However, the Tribunal agreed with the reasoning of C.I.T.(Appeals) by its order dated 26/07/1993 and rejected the Revenue's Appeal.

5. Mr. B.B.Naik, learned standing counsel appearing on behalf of the appellant-Revenue, has assailed the impugned order of Tribunal by inviting attention to definition of "*Written Down Value*", as appearing in Sub-section(6) of Section 43 of the Act. According to him, Clause (b) of Sub-section(6) states that Written Down Value means the actual cost to the assessee less all depreciation actually allowed under the Act, in case of assets acquired before the previous year. That, therefore, one has to read the provision as it stands. The phrase "*before the previous year*" does not lay down any limitation and hence, in case of an asset acquired at any time in the past, if depreciation has been actually allowed, the same has to be taken into consideration while computing WDV. According to him, the words "*actually allowed*" cannot mean anything else but what was actually granted as a deduction towards depreciation of the assets in the past. That in the present case, admittedly, the assessee had been granted deduction under Section 32 (1)(v) of the Act in the assessment for

Assessment Year 1982-83. Once this was the position, the Assessing Officer was required to take the said figure while computing the WDV on which depreciation could be allowed for the year under consideration. That by virtue of amendment by the Finance Act, 1983 with effect from 01/04/1984, the words "*but any such sum shall not be deductible in determining the written down value for the purposes of clause (ii)*" had been omitted and, therefore, the Assessing Officer was justified in reducing the WDV by the figure of such initial depreciation granted for the Assessment Year 1982-83.

6. Though served, there is no appearance on behalf of the Respondent-assessee. Attention of Mr. Naik was invited to the decision in the case of **I.T.C. Limited V/s. Commissioner of Income Tax (1994) 205 ITR 126 (Kolkata)** and the decision in the case of **Commissioner of Income Tax V/s. Adyar Gate Hotel Ltd. (2001) 252 ITR 129 (Madras)**. In relation to decision of Kolkata High Court in case of **I.T.C. Limited V/s. Commissioner of Income Tax (Supra)**, it was contended by Mr. Naik that the same was relatable to Assessment Year 1981-82 and the Kolkata High Court was not required to render any opinion in context of the amendment carried out by Finance Act, 1983. The said decision, according to him, therefore,

could not operate as judgment in relation to controversy involved in the present reference. In relation to the decision of Madras High Court in the case of **Commissioner of Income Tax V/s. Adyar Gate Hotel Ltd. (Supra)**, it was submitted that the said decision had omitted to deal with provisions of Section 43(6) of the Act and hence, could not be treated as an authority for the purposes of resolving the present controversy.

7. Section 32 of the Act, deals with depreciation allowance. It is provided under Sub-section(1) of the said Section that an assessee would be entitled to depreciation allowance in respect of building, machinery, plant or furniture owned by the assessee and used for the purposes of business or profession, subject to fulfillment of the statutory conditions. Under Section(1)(ii) of the Act, it is stated that depreciation shall be allowed as a deduction on the written down value at such percentage as may be prescribed. Section 32(1)(v) of the Act, which is relevant for the purpose of this case reads as under :-

"(v) in the case of any new building, the erection of which is completed after the 31st day of March, 1967, where the building is owned by an Indian company and used by such company as a hotel and such hotel is for the time being approved in this behalf by the Central Government, a sum equal to twenty-five percent of the actual cost of erection of the building to the assessee, in respect of the previous

year in which the erection of the building is completed or, if such building is first brought into use as a hotel in the immediately succeeding previous year, then in respect of that previous year; [but any such sum shall not be deductible in determining the written down value for the purposes of clause (ii);]"

8. Section 43 of the Act provides for Definitions of certain terms relevant to income from profits and gains of business or profession, and lays down that in Sections 28 to 41 and in Section 43, unless the context otherwise requires, the definitions given, of various terms, would apply. "Written down value" has been defined in the following manner in Sub-Section (6) of Section 43 of the Act :-

(6) "Written Down Value" means :-

- (a) *in the case of assets acquired in the previous year, the actual cost to the assessee;*
- (b) *in the case of assets acquired before the previous year, the actual cost to the assessee less all depreciation actually allowed to him under this Act, or under the Indian Income-tax Act, 1922 (11 of 1922), or any Act repealed by that Act, or under any executive orders issued when the Indian Income-tax Act, 1866 (2 of 1886), was in force : -*

[Provided that in determining the written down value in respect of buildings, machinery or plant for the purposes of clause(ii) of sub-section (1) of section 32 "depreciation actually allowed" shall not include depreciation allowed under sub-clauses(a),(b) and (C) of clause (vi) of sub-section (2) of section 10 of the Indian Income-tax Act, 1922 (11 of 1922), where such depreciation was not deductible in determining the written down value for the purposes of the said clause(vi).]

9. It is not in dispute that under Clause (v) of Section 32 (1) of the Act, the assessee was granted initial depreciation at the rate of 25% of the actual cost of erection of the building in Assessment Year 1982-1983. The said sum had not been taken into consideration for the purpose of determination of the written down value for the purposes of granting depreciation under Section 32(1)(ii) of the Act because of the last portion appearing in Clause (v) of Section 32(1) of the Act. This phrase, *"but any such sum shall not be deductible in determining the written down value for the purposes of clause (ii)"* has been omitted from the statute by the Finance Act, 1983 with effect from 01/04/1984 and hence, according to Revenue, it is now open to the Revenue to reduce the written down value by deducting the amount of initial depreciation already granted to the assessee. In support of its case, Revenue relies on phrase *"less all depreciation actually allowed"* as appearing in Clause (b) of Sub-section(6) of Section 43 of the Act.

10. There is a basic fallacy in the contention raised on behalf of Revenue. Though clause(v) appears in Section 32(1) of the Act which deals with depreciation, in fact, it is not depreciation as understood in the commercial circles, nor has the Legislature treated the same to be

depreciation within the meaning of the provisions of the Act.

11. The term 'depreciation', as understood in the commercial circles and those dealing with the assessment of income from business, as well as within the meaning of accountancy practice, means wear and tear of the assets used for the purposes of earning revenue on user of the assets. In other words, one cannot deduce the correct income without taking into account the wear and tear which an asset undergoes while being used for the purpose of generating receipts, which on finalisation of accounts, result in taxable profits. The concept of depreciation is that any asset, on account of normal wear and tear, is required to be replaced at a point of time in future. Therefore, to enable a business to meet with the cost of such replacement, the wear and tear is permitted to be calculated at a notional rate of percentage of the cost / Written Down Value of the assets.

12. As against this, what Section 32(1)(v) provides is deduction of an amount in the Previous Year in which erection of building is completed or, in the succeeding previous year when the building is first brought to use

as a hotel. Therefore, it is apparent that it is not an allowance in the nature of depreciation. It is not an allowance towards normal wear and tear upon the assets being put to use for the purposes of business. It is a special deduction granted in the initial year when in fact, the asset is not yet put to use, or the use has just commenced. Thus, there is no possibility of wear and tear of the assets by its use in the course of business. The allowance is primarily in the nature of incentive.

13. Once this position becomes clear and the distinction between the allowance by way of incentive and an allowance by way of depreciation is borne in mind, requirement provided in clause (b) of Sub-section(6) of Section 43 of the Act cannot be said to have been fulfilled. What the provision requires is reduction of the figure of WDV by all depreciation actually allowed. Once the allowance does not bear the characteristic of depreciation, it cannot be stated that it would form part of all depreciation actually allowed so as to be deductible while computing the WDV.

14. There is one more reason. The scheme of the Act is clear from a conjoint reading of Sections 4 and 5 of the

Act, which provide for Charge of Income tax and Scope of Total Income respectively. The provisions stipulate that while computing the taxable profits of the year, the Assessing Officer is required to take into consideration all receipts falling within the previous year and all legitimate expenses coupled with statutory deductions, allowances and exemptions that fall within the previous year. Therefore, at the beginning of the previous year, the WDV which is computed at the end of the immediate proceeding previous year, becomes the starting point for the purposes of computing depreciation allowable in the year in question and any allowance which has not gone into computation of WDV in any of the earlier years cannot be brought into the zone of consideration while computing the taxable income of the year under consideration. In other words, for the purposes of assessment of income which can be brought to tax for Assessment Year 1985-86, the assessing authority is permitted to take into consideration the income received, arising or accruing during the calender year 1984 with corresponding expenses, deductions, allowances and exemptions as available for calender year 1984. The written down value, for this purpose could only be the figure which was arrived at the end of calender year 1983. There is no provision under the Act by which the

said figure can be disturbed so as to incorporate the allowance relatable to Assessment Year 1982-83.

15. Once the aforesaid basic scheme of the Act is borne in mind, it becomes clear that the approach of the Revenue in including the allowance granted in Assessment Year 1982-83 cannot be brought into computation of WDV for the year under consideration which is effectively year number three from the point of time the building was completed or first brought into use. The aforesaid Legislative intent becomes clear from the language employed in Sub-section (6) of Section 43 of the Act whereunder clause (a) stipulates a case of an asset / assets acquired in the previous year, and clause (b) stipulates the case of assets acquired before the previous year. Therefore, fulcrum of assessment is primarily the charge which is fastened on all income received, arising or accruing during the previous year relevant to an Assessment Year.

16. Decision of Kolkata High Court in the case of I.T.C. Limited (supra) lends support to the view adopted by this Court, namely, that initial depreciation allowable under Section 32(1)(v) of the Act is in the nature of incentive for the new construction or new installments and cannot

be equated with the cost of replacement which is allowed as deduction in lieu of depreciation in respect of certain assets. Therefore, the contention on behalf of Revenue that the said decision is prior to amendment by Finance Act, 1983, does not make any difference as the basic distinction between two allowances remains.

17. Similarly, decision of the Madras High Court in the case of **Commissioner of Income Tax V/s. Adyar Gate Hotel Ltd.** (*supra*) also is on the lines of view expressed hereinbefore. It is stated at page 132 of the reports that:

"the depreciation to be allowed in that assessment year is to be allowed with reference to the written down value as at the commencement of the year, which figure had been calculated by excluding the initial depreciation as that was the mode in which the written down value was required to be determined prior to April 1, 1984."

18. The Legislative intent is thus clear taking into consideration the scheme of the Act as laid down hereinbefore. However, even if the view canvassed by the Revenue can be stated to be a possible view one may usefully refer to decision of the Apex Court as stated in the case of **Mysore Minerals Ltd. v. Commissioner of Income Tax.** (1999) 239 ITR 775 at page 778 : -

"Section 32 of the Income-tax Act confers a

benefit on the assessee. The provision should be so interpreted and the words used therein should be assigned such meaning as would enable the assessee securing the benefit intended to be given by the Legislature to the assessee. It is also well-settled that where there are two possible interpretations of a taxing provision the one which is favourable to the assessee should be preferred."

19. Thus the position in law is clear. Initial depreciation granted under Section 32(1)(v) of the Act during the Assessment Year 1982-83 cannot be deducted for the purposes of computing Written Down Value within the meaning of Section 43(6)(b) of the Act for the purpose of Assessment Year 1985-86 i.e, year under consideration. The Tribunal was therefore, right in law in holding that initial depreciation allowed in Assessment Year 1982-83 on new hotel building is not deductible for arriving at WDV in view of the amendment effected by Finance Act, 1983. The question is accordingly answered in the affirmative i.e, in favour of the assessee and against the Revenue.

20. Reference stands disposed of accordingly. There shall be no order as to costs.

(D.A.MEHTA, J.)

(H.N.DEVANI, J.)

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