

IN THE HIGH COURT OF HIMACHAL PRADESH, SHIMLA

ITA No.42 of 2007 alongwith
ITA Nos.46, 52, 53 & 57 of 2007.

Judgment reserved on:26.5.2011

Date of decision: 08.07.2011

Commissioner of Income Tax (in all cases)

....Appellants

-versus-

M/s.Kriti Resorts Pvt. Ltd. (in all cases)

....Respondents

Coram

The Hon'ble Mr. Justice Deepak Gupta, Judge.

The Hon'ble Mr. Justice Sanjay Karol, Judge.

*Whether approved for reporting?*¹ Yes

For the Appellant(s):

*Mr. Vinay Kuthiala & Mrs. Vandana Kuthiala,
Advocates.*

For the Respondents:

*Mr. Rupesh Jain, Advocate with
S/Sh. S.S. Panta & Paresh Sharma,
Advocates.*

Deepak Gupta, J.

1. These appeals are being disposed of by a common judgment since all these appeals have been admitted on the following substantial questions of law:

“1. Whether on the facts and in the circumstances of the case, the Tribunal was correct in law in holding that depreciation on vehicles is allowable as a deduction against the interest income earned, even when such income had been held by the Tribunal to be income chargeable under the head “other sources’ under section 56 of the Income Tax Act and in spite of the express provisions of Section 57 of the Act?

2. Whether the Tribunal was correct in law in holding that the unabsorbed depreciation in the case of the assessee for and up to A.Y.1996-97 could be carried forward and set off against income chargeable under any head of income in any subsequent year, on the ground that such unabsorbed

¹ *Whether the reporters of the local papers may be allowed to see the Judgment?*
yes

depreciation was not governed by the provisions of Section 32(2) as substituted by the Finance (No.2) Act, 1996 w.e.f. 1.4.1997, in spite of the judgment of the Hon'ble Supreme Court in the case of CIT v. Virmani Industries Ltd., (216 ITR 607) according to which such unabsorbed depreciation once carried forward to the A.Y. 1997-98 would be deemed to be the depreciation for A.Y. 1997-98?"

2. Briefly stated, the facts of the case are that the assessee was running a hotel at Manali till September, 1995. On the night intervening 6th/7th September, 1995 heavy floods took place in the river Beas and the hotel building was washed away in the floods. The assessee did not carry out any hotel business thereafter and advanced the surplus funds available with it to its sister concern on interest.

3. The assessee filed return for the year 1998-99 on 23.11.1998 and the interest income received by the assessee was declared to be income under the head 'profits and gains' of business and against this income the assessee claimed deduction of various expenses and depreciation on furniture and depreciation on vehicles against the income earned by way of interest. The assessee also claimed set off of unabsorbed depreciation brought forward from the assessment year 1996-97.

4. The Assessing Officer held that since the assessee had discontinued its business since 1995 the income was not income from business but income from other sources and therefore the expenses claimed and

depreciation brought forward could not be set off against the said income.

5. The Assessee filed appeals and the CIT (Appeals) vide his order for the assessment years 1998-99 to 2000-2001 held that the interest income declared by the assessee was income from profit and gains from business as the assessee had made efforts to re-start its business and therefore the unabsorbed depreciation brought forward could be set off against such income.

6. The Department filed appeals before the ITAT and the ITAT for the assessment years 1998-99 to 2002-2003 held that the interest income should be assessed under the head other sources and not profit and gains of business. It however went on to hold that as far as unabsorbed depreciation is concerned the amendment would not apply and un-amended provisions of Section 32 would continue to apply and consequently held that the un-absorbed depreciation accumulated on April, 1997 could be set off against the income of subsequent years even if the income be from other sources.

7. The Revenue has now challenged these orders and the basic questions which arise for consideration are whether the income from interest could be said to be income from business or from other sources and secondly whether the un-amended provisions of Section 32(2) would apply to benefit the assessee or it

is the amended provisions which would apply and what is the effect of the amendment.

8. Section 32(2) of the Act, as it stood before its amendment which came into effect from 1.4.1997, reads as follows:

“(2) Where, in the assessment of the assessee, full effect cannot be given to any allowance under clause (ii) of sub-section (1) in any previous year, owing to their being no profits or gains chargeable for that previous year, or owing to the profits or gains chargeable being less than the allowance, then, subject to the provisions of sub-section (2) of section 72 and sub-section (3) of section 73, the allowance or part of the allowance to which effect has not been given, as the case may be, shall be added to the amount of the allowance for depreciation for the following previous year and deemed to be part of that allowance, or if there is no such allowance for that previous year, be deemed to be the allowance for that previous year, and so on for the succeeding previous years.”

9. Vide Finance Act of 1996 sub section (2) was substituted by the following:

“(2) Where in the assessment of the assessee full effect cannot be given to any allowance under clause (ii) of sub-section (1) in any previous year owing to there being no profits or gains chargeable for that previous year or owing to the profits or gains being less than the allowance, then, the allowance or the part of allowance to which effect has not been given (hereinafter referred to as unabsorbed depreciation allowance), as the case may be,-

- (i) shall be set off against the profits and gains, if any, of any business or profession carried on by him and assessable for that assessment year;
- (ia) if the unabsorbed depreciation allowance cannot be wholly set off under clause (i), the amount not so set off shall be set off from the income under

any other head, if any, assessable for that assessment year;

(ii) if the unabsorbed depreciation allowance cannot be wholly set off under clause (i) and clause (ia), the amount of allowance not so set off shall be carried forward to the following assessment year and-

(a) it shall be set off against the profits and gains, if any, of any business or profession carried on by him and assessable for that assessment year;

(b) if the unabsorbed depreciation allowance cannot be wholly so set off, the amount of unabsorbed depreciation allowance not so set off shall be carried forward to the following assessment year not being more than eight assessment years immediately succeeding the assessment year for which the aforesaid allowance was first computed:

Provided that the business or profession for which the allowance was originally computed continued to be carried on by him in the previous year relevant for that assessment year:

Provided further that the time limit of eight assessment years specified in sub-clause (b) shall not apply in the case of a company for the assessment year beginning with the assessment year relevant to the previous year in which the said company has become a sick industrial company under sub-section (1) of section 17 of the Sick Industrial Companies (Special Provisions) Act, 1985 (1 of 1986), and ending with the assessment year relevant to the previous year in which the entire net worth of such company becomes equal to or exceeds the accumulated losses.

Explanation.- For the purposes of this clause, "net worth" shall have the meaning assigned to it in clause (ga) of sub-section (1) of section 3 of the Sick Industrial Companies (Special Provisions) Act, 1985 (1 of 1986)."

10. The Finance Minister while moving the amendment in Parliament relating to this clause stated thus:

"4. Clause 11 of the Bill seeks to amend section 32 of the Income-tax Act, 1961, relating to depreciation. During the course of discussion on

the General Budget, a number of Hon'ble members have expressed their apprehension that the proposed amendment limiting carry forward of unabsorbed depreciation to 8 years will adversely affect the growth of industry. Similar apprehensions have been raised in a large number of post-budget memoranda. I would like to allay these fears. The proposed amendment is only prospective inasmuch as the cumulative unabsorbed depreciation brought forward as on 1st April, 1997, can still be set off against taxable business profits or income under any other head for the assessment year 1997-98 and seven subsequent assessment years. Therefore, the proposed change will have effect only after 8 years and there is no cause for immediate concern about its likely impact on industry. Eight years is a period long enough for industry to adjust itself to the new dispensation and provide for depreciation accordingly. A number of Hon'ble members have brought to my notice that the proposed amendment may adversely affect sick companies. I accept the suggestions made by them. I, therefore, propose to provide that the time limit of 8 years shall not apply to sick companies, during the period the company is treated as a "sick company" under the Sick Industrial Companies (Special Provisions) Act, 1985.

5. I further propose to make a drafting amendment in clause 11 to clarify that the depreciation for the year can be set off not only against profits and gains of any business carried on by the assessee but also against income under any other head, as is the case with the set off of business losses." *(emphasis supplied)*

11. Relevant portion of the Circular issued by the CBDT reads as follows:

"23.5 Sub-section (2) of section 32, as it existed upto assessment year 1996-97, provided that the

unabsorbed depreciation of a year shall be added to the amount of the allowance for depreciation of the following previous year and deemed to be part of that allowance. Therefore, the unabsorbed depreciation allowance, if any, of the assessment year 1996-97 shall be added to the amount of the allowance for depreciation of assessment year 1997-98 and deemed to be part of the allowance for this year. In other words, the unabsorbed depreciation allowance of assessment year 1996-97 shall be added to the allowance of 1997-98 and will be deemed to be the allowance of that year. The limitation of eight years shall start from the assessment year 1997-98.”

12. The first question which arises is whether the assessee can still be said to be in business or not. No doubt the hotel of the assessee was washed away and in that respect it can be said that it has not conducted any hotel business thereafter. However, the Company does not cease to exist. The Company is a juristic entity and incorporated under the Indian Companies Act. It will have to fulfill its obligations imposed upon it by the Companies Act till it is wound up. Therefore, some staff will have to be maintained. It cannot be said that the business has come to an end. In this behalf reference may be made to the judgment of the Madras High Court in **Commissioner of Income-Tax vs. Vellore Electric Corporation Ltd., (2000) 243 ITR 529** and a judgment of the Calcutta High Court reported in **Commissioner of Income Tax vs. Karanpura Collieries Ltd. (1993) 201 ITR 498**.

13. Therefore, once the Company is in existence the assessee can seek depreciation. Reliance placed by the

Revenue on the first proviso of Section 32(2) is totally misplaced. Therefore, as far as question No.1 is concerned the same is answered in favour of the assessee and against the Revenue.

14. Coming to Question No.2, a Division Bench of the Madras High Court in **Commissioner of Income-Tax vs. Pioneer Asia Packing P. Ltd. (2009) 310 ITR 198 (Mad)** considered this point at length. It was held that as per the amended provisions of Section 32(2) of the Act, with effect from April 1, 1997, if the income from business for the assessment year is insufficient to absorb the depreciation allowance of that assessment year, the amended provision permits absorption of depreciation allowance of a business against profits and gains of any other business of the same assessment year. When the depreciation allowance of a business of the assessment year is not absorbed by any other business of the same assessment year, then the remaining unabsorbed depreciation allowance could be set off against the income under any other head, that is assessable for the same assessment year. In the event of the depreciation allowance of the year being not absorbed by any other business income or from income under any other head in the same assessment year, the remaining unabsorbed depreciation allowance shall be carried forward to the following year. Therefore, it follows that (a) unabsorbed allowance shall be set off against the profits and gains of

any business carried by a person, (b) if the unabsorbed depreciation allowance cannot be wholly set off so, it shall be allowed to be carried forward for the following eight assessment years immediately succeeding the assessment year in which it was first computed. The proviso provides that the business to which depreciation allowance is related to must be carried on in the succeeding year so as to allow such set off. The period available for absorbing the unabsorbed depreciation against the profit of the succeeding years was limited to eight years. The clarification of the Finance Minister in Parliament is also to the effect that inasmuch as the cumulated unabsorbed depreciation brought forward as on April 1, 1997, could still be set off against the taxable business profit or income under any other head for the assessment year 1997-98 and seven subsequent years.

15. Similar view was again taken by the Madras High Court in **Commissioner of Income-Tax vs. S& S Power Switchgear Ltd. (2009) 318 ITR 187 (Mad)** and the Delhi High Court has taken a same view in **Commissioner of Income Tax vs. M/s.JCL International Ltd. ITA No.1255 of 2009 decided on 1.12.2009.**

16. The speech of the Finance Minister while moving the proposed amendment clearly states that the proposed amendment was only prospective in nature and it is apparent that the entire un-absorbed depreciation brought forward as on 1st April, 1997 could be set off firstly against

the business profits and if these were not sufficient against the income obtained under any other head for the assessment year 1997-98 and subsequent assessment years. Thus, the amendment only provides that the benefit of brought forward assessment could be set off; firstly against income from profits and gains of business; secondly from income under any other head and this benefit could be taken for a period of 8 years alone.

17. The main contention of the Revenue is that since the hotel was not in existence therefore the un-absorbed depreciation became part of the depreciation for the assessment year 1998-99 and now could not be set off against the income from other sources. We are unable to accept this contention. The fact is that this was depreciation of the previous year and the Finance Minister in his speech clearly indicated that there was no substantial change and that the only difference was that now limitation of 8 years would be applicable. Therefore, we find no merit in the contention of the revenue.

18. In view of the above discussion, both the questions are answered in favour of the assessee and against the revenue. The appeals are disposed of in the aforesaid terms. No costs.

(Deepak Gupta), J.

July 8, 2011.
PV

(Sanjay Karol), J.