

IN THE HIGH COURT OF KARNATAKA, BENGALURU

DATED THIS THE 21ST DAY OF AUGUST 2018

PRESENT

THE HON'BLE Dr.JUSTICE VINEET KOTHARI

AND

THE HON'BLE Mrs.JUSTICE S.SUJATHA

I.T.A.No.862 OF 2017

BETWEEN:

1. Pr. COMMISSIONER OF INCOME TAX
(EXEMPTIONS), MISSION ROAD,
BENGALURU.
2. INCOME TAX OFFICER (EXEMPTIONS)
WARD-3, BANGALORE.

...APPELLANTS

(BY MR. SANMATHI.E.I, ADVOCATE)

AND:

SHUSHRUTHA EDUCATIONAL TRUST
GURUKRUPA, 12TH MAIN,
NO.2366/27, 'A' BLOCK,
RAJAJINAGAR,
BENGALURU-560 010.
PAN:AAETS7079K

...RESPONDENT

(BY MR. A.SHANKAR AND MR. M.LAVA, ADVOCATES)

THIS I.T.A IS FILED UNDER SECTION 260-A OF
INCOME TAX ACT 1961, ARISING OUT OF ORDER

DATED 23.6.2017 PASSED IN I.T.A.No.852/BANG/2016, FOR THE ASSESSMENT YEAR 2011-2012 VIDE ANNEXURE-A PRAYING THIS HON'BLE COURT TO: DECIDE THE FOREGOING QUESTION OF LAW AND/OR SUCH OTHER QUESTIONS OF LAW AS MAY BE FORMULATED BY THE HON'BLE COURT AS DEEMED FIT AND SET ASIDE THE APPELLATE ORDER DATED: 23.06.2017 PASSED BY THE INCOME TAX APPELLATE TRIBUNAL, 'A' BENCH, BANGALORE AS SOUGHT FOR, IN THE RESPONDENT-ASSESSEE'S CASE, IN APPEAL PROCEEDINGS NO. ITA.NO.852/BANG/2016 FOR ASSESSMENT YEAR 2011-2012, AND GRANT SUCH OTHER RELIEF AS DEEMED FIT, IN THE INTEREST OF JUSTICE.

THIS I.T.A. COMING ON FOR ADMISSION THIS DAY, **Dr. VINEET KOTHARI J.** MADE THE FOLLOWING:-

ORDER

Mr. Sanmathi.E.I., Advocate for Appellants- **Revenue**

The learned counsel for the appellants submits that the questions raised in the present appeal is covered by the decisions of this Court.

2. The proposed substantial questions of law in the memo of appeal of Revenue are quoted herein below for ready reference:-

“1. Whether on the facts and in the circumstances of the case and in law,

the Tribunal is right in not appreciating the fact that the normal computation of income under respective heads as envisaged under Sections 15 to 59 are not applicable to the computation of income in respect of charitable trust/institution for the purpose of claiming exemption under Sections 11, 12 and 13 and, therefore, the provisions relating to set-off of loss from one source against the income from another source, set-off of loss from one head against income from another head and carry forward and set-off of loss against the income of subsequent years as envisages under Sections 70 to 79 are also not applicable to the charitable trusts/institutions?

2. Whether on the facts and in the circumstances of the case and in law, the Tribunal is right in setting aside disallowance of accumulation/set apart of income under Section

11(1)(a) without appreciating the fact that the issue of application of income more than the income computed does not arise, except in a case where the assessee has incurred huge amount of capital expenditure sourced out of borrowed or corpus donations or 15% of income set apart over a period of time and even otherwise expenditure incurred out of the above sources cannot be termed as application of funds out of the income earned in a particular assessment year inasmuch as loan borrowed does not fall under the category of income earned by the assessee?

3. Whether on the facts and in the circumstances of the case, the Tribunal were justified in law in allowing assessee's claim for depreciation on new assets put into use during the accounting year relevant to this asst. year, even though the entire cost of these assets

have been claimed by the assessee as an application of income for charitable activities and has failed to take cognizance of the fact that allowing of total cost of the asset as an applicable of income and allowing of depreciation on the value of such assets in the same year results in double deduction and is not admissible in the absence of clear statutory indication?”

3. The learned counsel for the Revenue submits that he does not press question No.2. He further submitted that question No.1 is covered by a decision of this Court in the case of **‘Commissioner of Income Tax-III, Pune v. Rajasthan & Gujarati Charitable Foundation Poona’ [2018] 89 taxmann.com 127 [SC]** with regard to allowability and Depreciation in the hands of Religious and Charitable Trust held as under:

“5. Learned Counsel at the Bar submitted that so far as the issue regarding claim of Depreciation under Section 32 of the Act is concerned, the controversy is no longer *res integra*, having been settled by the Hon’ble Supreme Court in the case of **‘Commissioner of Income Tax-III, Pune v. Rajasthan & Gujarati Charitable Foundation Poona’ [2018] 89 taxmann.com 127 [SC]**, by which the Hon’ble Supreme Court has affirmed the view taken by the Bombay High Court in **‘Commissioner of Income Tax v. Institute of Banking Personnel Selection (IBPS)’ [2003] 131 Taxman 386 [Bom.]**. The relevant portion of the said Judgment of Bombay High Court as quoted by the Hon’ble Supreme Court and affirmed is quoted below for ready reference.

“In the said judgment, [Bombay High Court] the contention of the Department

predicated on double benefit was turned down in the following manner:

3. As stated above, the first question which requires consideration by this court is : *whether depreciation was allowable on the assets, the cost of which has been fully allowed as application of income under section 11 in the past years? In the case of CIT v. Munisuvrat Jain 1994 Tax Law Reporter, 1084 the facts were as follows. The assessee was a Charitable Trust. It was registered as a Public Charitable Trust. It was also registered with the Commissioner, Pune. **The assessee derived income from the temple property which was a Trust property.** During the course*

*of assessment proceedings for assessment years 1977-78, 1978-79 and 1979-80, **the assessee claimed depreciation on the value of the building at the rate of 2.5 per cent** and they also claimed depreciation on furniture at the rate of 5 per cent. The question which arose before the court for determination was: whether depreciation could be denied to the assessee, as expenditure on acquisition of the assets had been treated as application of income in the year of acquisition? It was held by the Bombay High Court that section 11 of the Income Tax Act makes provision in respect of computation of income of the Trust from the property held for charitable or religious*

purposes and it also provides for application and accumulation of income. On the other hand, section 28 of the Income Tax Act deals with chargeability of income from profits and gains of business and section 29 provides that income from profits and gains of business shall be computed in accordance with section 30 to section 43C, That, section 32(1) of the Act provides for depreciation in respect of building, plant and machinery owned by the assessee and used for the business purposes. It further provides for deduction subject to section 34. In that matter also, a similar argument, as in the present case, was advanced on behalf of the revenue, namely, that depreciation can be allowed

10/27

as deduction only under section 32 of the Income Tax Act and not under general principles. The court rejected this argument. It was held that normal depreciation can be considered as a legitimate deduction in computing the real income of the assessee on general principles or under section 11(1)(a) of the Income Tax Act. The court rejected the argument on behalf of the revenue that section 32 of the Income Tax Act was the only section granting benefit of deduction on account of depreciation. It was held that income of a Charitable Trust derived from building, plant and machinery and furniture was liable to be computed in normal commercial manner although the Trust may not be carrying on any business and

the assets in respect whereof depreciation is claimed may not be business assets. In all such cases, section 32 of the Income Tax Act providing for depreciation for computation of income derived from business or profession is not applicable. However, the income of the Trust is required to be computed under section 11 on commercial principles after providing for allowance for normal depreciation and deduction thereof from gross income of the Trust. In view of the aforestated Judgment of the Bombay High Court, we answer question No. 1 in the affirmative i.e., in favour of the assessee and against the department.

4. Question No. 2 herein is identical to the question

12/27

*which was raised before the Bombay High Court in the case of Director of Income Tax (Exemption) v. Framjee Cawasjee Institute (1993) 109 CTR 463 (Bom). In that case, the facts were as follows: 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 Officer 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 Assistant Appellate 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.** This view of the Tribunal has been confirmed by, the Bombay High Court in the above judgment. Hence, Question No. 2 is covered by the

14/27

decision of the Bombay High Court in the above judgment. Consequently, Question No. 2 is answered in the affirmative i.e., in favour of the assessee and against, the department.

*After hearing learned counsel for the parties, **we are of the opinion that the aforesaid view taken by the Bombay High Court correctly states the principles of law and there is no need to interfere with the same.***

6. Since the issue regarding claim of Depreciation in the hands of the Charitable Trust is no longer res integra, We are of the opinion that no substantial question of law now arises in the present Appeals filed by the Revenue.”

4. The third suggested question is also covered by another decision of this Court in the case of **Commissioner of Income Tax (Exemptions) and**

another .vs. Ohio University Christ College

rendered on **17.07.2018** in **ITA.No.312/2016** and

ITA No.313/2016, in which this Court held as

under:

“16. In so far as the second question proposed by the Revenue, quoted above is concerned also, we find that the Tribunal’s findings in this regard do not give rise to any substantial question of law. The said findings are quoted below for ready reference :

*“5.1 In the course of assessment proceedings, the Assessing Officer observed that the assessee had claimed application of income on account of **expenditure of earlier years, which has been brought forward and set off in the year under consideration.** The Assessing Officer disallowed the same on the ground that there is no express provision in the Act permitting the adjustment of*

earlier years brought forward expenses as application of income in the current year. According to the Assessing Officer, the application of income for charitable purposes must be during the relevant previous year. Since the income of the trust is exempt from tax, the question of deficit does not arise and also the trust is required to utilize 85% of the income of the previous year for charitable purposes during the year. In this view of the matter and for the above reasons, the Assessing Officer disallowed the assessee's claim of expenditure of earlier years being brought forward and set off during the year.

5.2 On appeal, the learned CIT (Appeals) allowed the amortization of the expenditure as claimed by the assessee and

*deleted the disallowance made by the Assessing Officer by placing reliance on the decision of the **Hon'ble Karnataka High Court in the case of CIT Vs. Society of the Sisters of St. Anne reported in 146 ITR 28 (1984) and CBDT Circular No.5-F(LXX)-6 of 1968.***

5.3.1 We have heard the rival contentions of both the learned Departmental Representatives for Revenue and the learned Authorised Representative for the assessee and perused and carefully considered the material on record, including the judicial pronouncements cited. The facts of the issue before us is that the **assessee had incurred certain preliminary expenditure in the year of setting up of the trust. The same is amortised by the**

assessee trust over a period of 5 years from the year of incurring of expenditure. The fact of amortization was not disputed by the Assessing Officer in the assessment proceedings for Assessment Year 2007-08 where the entire amount was added back claiming 1/5th of the expenditure. The un-amortized expenditure has been brought forward and set off as application of income in subsequent years, including the assessment years 2008-09 and 2009-10 which are under consideration.

5.3.2 We find that the issue before us is directly related to the issue decided by the Hon'ble Karnataka High Court in the case of Sisters of St. Anne (supra) cited by the assessee. In the said case, the Hon'ble Karnataka High Court

19/27

*at paras 8 to 10 thereof has held
as under : -*

Xxxxxxx

5.3.3 Further, the CBDT Circular No.5-P (LXX)-6 of 1968 cited by the assessee makes it clear that income should be understood in its commercial sense : in the case of trusts also and therefore the commercial principle enunciated by the Hon'ble Karnataka High Court in the above referred case of Sisters of St. Anne (supra) applies to trusts as well. In view of the factual and legal matrix of this issue in the case on hand as discussed above, we concur with the decision of the learned CIT (Appeals) in cancelling the disallowance made by the Assessing Officer and in allowing the amortization of expenses. Consequently, Ground No.B (1 to

20/27

6) of the Revenue's appeal for Assessment Year 2008-09 and Ground No.C for Assessment Year 2009-10 are dismissed.”

17. In our opinion, the matter is squarely covered by a decision of the cognate Bench of this Court in the case of **CIT vs. Society of the Sisters of St. Anne (1984) 16 Taxman 400 (Kar.) and (1984) 146 ITR 28**, wherein the cognate Bench of this Court held that even the depreciation not involving any cash outflow is also in the character of expenditure and therefore such depreciation is nothing but decrease in the value of property through wear and tear, deterioration or obsolescence and the allowance made for that purpose in the books of accounts were deemed to be the application of funds for the purpose of Sec. 11 of the Act. The relevant portion of the said judgment is also quoted below for ready reference:

“11. Mr. Srinivasan, however, urged that there are

enough indications in Section 11 to exclude the mercantile system of accounting. The learned counsel relied upon sections 11(1)(a) and 11(4) in support of his contention. We do not think that there is anything in these sub-sections to support the contention of Mr. Srinivasan. Explanation to section 11(1)(a) on the contrary takes note of the income not received in a particular year. It lends support to the contention of the assessee that accounting need not only be on cash basis. Section 11(4) is not intended to explain how the accounts of the business undertaking should be maintained. It is intended only to bring to tax the excess income computed under the provisions of the Act in respect of business undertaking.

12. The depreciation if it is not allowed as necessary deduction for computing the income from the charitable institutions, then there is no way to preserve the corpus of the trust for deriving the income. The Board also appears to have understood the 'income' under section 11(1) in its commercial sense. The relevant portion of the Circular No.5XX-6 of 1968, dated 19-6-1968 (See Taxmann's Direct Taxes Circulars, Vol. 1, 1980 edn. P.85) reads:

"Where the trust derives income from house property, interest on securities, capital gains, or other sources, the word 'income' should be understood in its commercial sense, i.e., book income, after adding back any appropriations or applications thereof towards the purposes of

the trust or otherwise, and also after adding back any debits made for capital expenditure incurred for the purposes of the trust or otherwise. It should be noted, in this connection, that the amounts so added back will become chargeable to tax under section 11(3) to the extent that they represent outgoings for purposes other than those of the trust. The amounts spent or applied for the purposes of the trust from out of the income, computed in the aforesaid manner, should not be less than 75 per cent of the latter, if the trust is to get the full benefit of the exemption under section 11(1).”

13. In CIT v. Trustee of H.E.H. The Nizam’s Supplemental Religious Endowment Trust (1981) 127 ITR 378, the Andhra Pradesh High Court has accepted the

accounts maintained in respect of the trust in conformity with the principles of accountancy for the purposes of determining the income derived from the property held in trust.”

18. In view of the aforesaid findings of the learned Tribunal, allowing any expenditure of the earlier year which has been brought forward and set off in the year under consideration, is a justified finding of fact based on the correct interpretation of law and the judgment relied upon by it rendered by the cognate Bench. Therefore, the same does not call for interference. A similar view was also taken by the Division Bench of Bombay High Court in **Commissioner of Income-tax v. Institute of Banking (2003) 264 ITR 110**, wherein the Division Bench of Bombay High Court held that the income derived from the trust property has also got to be computed on commercial principles and if commercial principles are applied, then adjustment of

expenses incurred by the trust for charitable and religious purposes in the earlier years against the income earned by the trust in the subsequent year will have to be regarded as application of income of the trust for charitable and religious purposes in the subsequent year. The relevant portion of the said judgment of Bombay High Court is also quoted below for ready reference :

“Normal depreciation can be considered as a legitimate deduction in computing the real income of the assessee on general principles or under section 11(1)(a) of the Income-tax Act, 1961. Income of a charitable trust derived from building, plant and machinery and furniture is liable to be computed in a normal commercial manner although the trust may not be carrying on any business and the assets in respect whereof depreciation is claimed may not be business assets. In all such cases, section

32 of the Act providing for depreciation, for computation of income derived from business or profession is not applicable. However, the income of the trust is required to be computed under section 11 on commercial principles after providing for allowance for normal depreciation and deduction thereof from the gross income of the trust.

Income derived from the trust property has also got to be computed on commercial principles and if commercial principles are applied, then adjustment of expenses incurred by the trust for charitable and religious purposes in the earlier years against the income earned by the trust in the subsequent year will have to be regarded as application of income of the trust for charitable and religious

27/27

purposes in the subsequent year in which adjustment had been made having regard to the benevolent provisions contained in section 11 of the Act and such adjustment will have to be excluded from the income of the trust under section 11(1)(a)."

5. Since all the proposed questions are covered by the aforesaid two decisions of this Court, we do not think that any substantial questions of law arises for our further consideration in the present appeal filed by the Revenue and therefore, the present appeal is **dismissed**. No costs.

**Sd/-
JUDGE**

**Sd/-
JUDGE**