

Executive Summary

- Income Tax Act, 1961, (Act) lays down diverse provisions on depreciation and/or amortisation for tax purposes as deduction to an assessee/ a company in the course of its business with the intention for promoting economic growth within the Country. It is important to ensure that these provisions are properly utilised as per the existing tax laws to avoid any major revenue loss. The objective of this study was to focus on whether the systems and procedures are sufficient and in place to ensure compliance with the provisions of the Act/Rules and instructions issued by Central Board Direct Taxes (CBDT) in this regard. The study also seeks assurance that adequate internal control mechanism exists within the Income Tax Department (ITD) for monitoring the allowance of depreciation in general and under special circumstances viz., amalgamation, demerger, reconstruction etc.
- We audited assessments completed during the period FY 10 to FY 13 and all cases of scrutiny assessments, appeal and rectification cases etc, within the selected units. We covered all circles/wards taken up for regular audit during the period from July to September 2013. We checked 87,023 records of the assessees. This report contains 725 cases of deficiencies in the implementation of provisions of the Act with tax effect of ₹ 2,464.06 crore.
- Rates of depreciation on different assets/ block of assets as provided in the Act differ from those prescribed under the Companies Act 1956 for the same assets. We found that depreciation as per the Act was higher in 6,267 cases and lower in 5,926 cases by a difference aggregating ₹ 57,665.41 crore and ₹ 11,754.80 crore respectively. We suggested harmonising these rates as assessees and ITD make additional efforts in computation of taxable income. The intended purpose for allowing depreciation in the Act has also not been evaluated (*paragraph 2.2*). Due to non-existence of proportionate allowance of depreciation depending upon the use of assets, assessees have claimed unintended benefits. We observed that 986 assessees made additions of various assets worth ₹ 1,41,725.45 crore in the month of March and claimed depreciation of ₹ 15,617.86 crore instead of allowable depreciation of ₹ 2,602.61 crore on *pro rata* basis for the month of March only, the assets being purchased in the month of March itself (*paragraph 2.3*). Besides this, there are inconsistencies in allowance of depreciation on assets owned by Charitable / Religious Trusts and Association of Persons (*paragraph 2.4*).

- A number of mistakes were noticed in compliance with the provisions of the Act dealing with allowance of depreciation and amortisation and the relevant circulars/instructions issued by CBDT/ Judicial decisions delivered by the Apex court and jurisdictional High Courts.
 - 20 assessees claimed and were allowed depreciation on assets which were not owned by them at all and resulted in under assessment of income to that extent involving tax effect of ₹ 92.79 crore (*paragraph 3.2*).
 - Assessing Officers (AOs) allowed depreciation to 35 assessees on assets which were not used in the business which resulted in under assessment of income to that extent involving tax effect of ₹ 43.96 crore (*paragraph 3.3*).
 - We noticed mistakes in determination of actual cost or written down value of assets in 29 cases, which resulted in excess allowance of depreciation involving tax effect of ₹ 85.47 crore (*paragraph 3.4*).
 - In 18 cases while calculating depreciation, AOs did not deduct capital investment subsidies received from the cost of the assets which resulted in under assessment of income to that extent involving tax effect of ₹ 35.65 crore (*paragraph 3.6*).
 - 44 assessees committed mistakes in adoption of correct figure of depreciation in computation of income involving tax effect of ₹ 212.97 crore (*paragraph 3.8*).
 - In 142 cases, AOs allowed depreciation at the rates which were higher than the rates provided in Appendix I to Income Tax Rules 1962. The mistake resulted in excess allowance of depreciation involving tax effect of ₹ 107.85 crore (*paragraph 3.9*).
 - In carrying forward/setting off of depreciation which resulted in under assessment of income to that extent, we found that in 87 cases, tax effect was ₹ 694.65 crore (*paragraph 3.11*).
 - 26 assessees irregularly claimed and was allowed capital expenditure as revenue expenditure which resulted in under assessment of income to that extent involving tax effect of ₹ 344.97 crore (*paragraph 3.13*).
- The Act also provides for additional depreciation to assessees and here also we found mistakes in assessments done by AOs. We found that AOs committed mistakes in grant of additional depreciation in 99 cases resulting in under assessment of income to that extent involving tax effect of ₹ 656.19 crore (*paragraph 3.19*). In case of 13 assessees, AOs did not allow additional depreciation during tax holiday which resulted in over assessment of income to that extent involving tax effect of ₹ 3.33 crore (*paragraph 3.20*).

- Regarding allowance of amortisation to assessees, we found that in case of 12 assessees, AOs irregularly allowed amortisation expenses under section 35D which resulted in under assessment of income to that extent involving tax effect of ₹ 6.70 crore (paragraph 4.2). We also found that four assessees irregularly claimed and were allowed expenses towards amortisation under section 35DDA which resulted in under assessment of income to that extent involving revenue impact of ₹ 5.38 crore (paragraph 4.3).
- We have also highlighted the control issues of the ITD relating to allowance of depreciation and amortisation (paragraphs 5.2 to 5.4).
- The allowance of depreciation and amortisation under the Act is intended to promote economic growth within the country but in absence of any monitoring mechanism within ITD, the purpose remained to be achieved. Besides, AOs committed mistakes in applying provisions relating to depreciation and amortisation correctly which resulted in under assessments. CBDT needs to improve the quality of assessments and explore the possibility of capacity building for AOs for reducing the incidence of mistakes.