



CBDT Notification – Rules amended to restrict depreciation rate at 40 per cent

Recently, the Central Board of Direct Taxes (CBDT) has issued a Notification¹ amending Rule 5 of the Income-tax Rules, 1962 (the Rules). The amendments are as follows:

- In case of a domestic company, which has exercised an option under Section 115BA of the Income-tax Act, 1961 (the Act), the depreciation allowance under Section 32(1)(ii) of the Act in respect of any block of assets entitled to more than 40 per cent shall be restricted to 40 per cent on the written down value of such block of assets with effect from 1 April 2016.
- New Appendix I which provides a table of depreciation rates has been amended. The Notification states that wherever higher rates (i.e. 50, 60, 80 and 100) occurs, the figure '40' shall be substituted with effect from 1 April 2017.

Background

The Finance Minister, in his Budget Speech in 2015, had announced a road map for a reduction in corporate tax rate from 30 per cent to 25 per cent over the next four years, along with phasing out of exemptions, deductions and incentives available under the Act.

In the Budget of 2016, the Finance Minister had announced amendments to the Act to implement the phase-out plan. One of the measures was to reduce the highest rate of depreciation on all assets to 40 per cent by notifying amendments to Rules with effect from 1 April 2017.

The Finance Act, 2016 has introduced Section 115BA in the Act with effect from 1 April 2017. Section 115BA of the Act states that the income tax payable in respect of the total income of a person, being a domestic company, not engaged in any business other than the business of manufacture or production of any article or thing and research in relation to, or distribution of, such article or thing manufactured or produced by it, for any previous year relevant to assessment year beginning on or after 1 April 2017, shall, at the option of such person, be computed at the rate of 25 per cent, subject to certain conditions. Further, Section 115BA of the Act states that depreciation under Section 32, other than clause (iia) of sub-section (1) of the said section, is determined in the manner as may be prescribed.

Highest depreciation rates are restricted to 40 per cent

In case of a domestic company, which has exercised option under Section 115BA of the Act (i.e. newly domestic manufacturing companies set up and registered on or after 1 March 2016, which opt for a concessional rate of 25 per cent rate of tax, instead of normal rate of 30 per cent, without any tax incentives), the depreciation allowance under Section 32(1)(ii) of the Act in respect of any block of assets entitled to more than 40 per cent shall be restricted to 40 per cent on the written down value of such block of assets with effect from 1 April 2016.

¹ Notification No. 103/2016, dated 7 November 2016

Further a plain reading of the Notification suggests that for all taxpayers, the highest rate of depreciation has been restricted to 40 per cent for all assets, which were eligible for depreciation at a rate higher than 40 per cent with effect from 1 April 2017.

The effective date of amendment

The Notification provides for different effective dates for companies that have exercised an option under Section 115BA of the Act and for other taxpayers. It states that the effective date is 1 April 2016 for new companies that have exercised an option under Section 115BA of the Act and 1 April 2017 for other taxpayers.

Our comments

This notification may have far reaching implications. A plain reading of the Notification suggests that for all taxpayers, the highest rate of depreciation has been restricted to 40 per cent for all assets, which were eligible for depreciation at a rate higher than 40 per cent.

For new companies that have exercised an option under Section 115BA of the Act, the effective date of 1 April 2016 coincides with the introduction of Section 115BA of the Act i.e. assessment year 2017-18 (i.e. financial year 2016-17). If this interpretation is accepted, the effective date of 1 April 2017 for all other taxpayers with respect to restriction on depreciation rates to 40 per cent, will apply from assessment year 2018-19 (i.e. financial year 2017-18). On the other hand, considering the interpretation of the statute, since this is a substantive change impacting computation of taxable income, it should come into effect from the first day of assessment year i.e. assessment year 2017-18 (i.e. financial year 2016-17).

The exact financial year from which these amendments shall come into effect is a matter of ambiguity. Therefore, it would be apt if CBDT issues a suitable clarification on the effective date of these amendments.



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