# Partners can get depreciation benefits against income

## Partners of firms can consider claiming depreciation on assets—in their personal name and used for the firm's business—against the remuneration and interest income from their firms.

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**Case Laws for Reference**

*CIT v. Excel Industries Ltd. (2013) 358 ITR 395 (SC) : 2013 TaxPub(DT) 2414 (SC), Radhasoami Satsang v. CIT (1992) 193 ITR 321 (SC) : 1992 TaxPub(DT) 0858 (SC), CIT v. Ramniklal Kothari (1969) 74 ITR 57 (SC) : 1969 TaxPub(DT) 0354 (SC).*

A partner in a partnership firm earns income from two sources—by way of remuneration from the firm and from his share of profits in the firm. While the profit share is exempt under the provisions of the Income Tax Act (the Act), the remuneration earned is taxable for the partner. In many of the cases, it is observed that partners have motor cars registered in their personal names but are used for their business purposes. In such cases, I have observed many tax payers claim the depreciation benefit for the car against the taxable remuneration income earned.

In one of the cases that came before the Special Bench of the Ahmedabad Tribunal, the taxpayer had income by way of profits from a firm in which he was a partner, capital gains, interest, dividends and from house property. The tax payer had claimed the depreciation benefit on his car against the remuneration income, after deducting $1/10^{th}$ of the depreciation towards usage of the car for personal purposes. However, the tax officer disallowed the claim for depreciation on the grounds that the expenditure so incurred in not necessarily for earning the business income from the partnership firm.

At the first level of appeal, the appellate authority observed that 76% of the tax-payers professional income is by way of share of profit and the balance by way of remuneration and interest income from the firm. In pursuance to the relevant provisions of the Act, the authority ruled that as expenses incurred in relation to income not chargeable to tax are not allowed to be claimed (section 14A); only 24% of the depreciation benefit is allowable against the remuneration and interest income earned from the firm. Thus the balance 76% of the expense was disallowed.

Not happy with the said order, the tax-payer placed an appeal before the Special Bench. The tax-payer argued that under the Indian Partnership Act, the partnership firm and partners are not distinct and therefore the business carried on by firm can be construed as business carried on by partners too. By virtue of this, any expenditure incurred by the partners for the business should be allowed to be deducted from their business income. The tax-payer also argued that the profit share from the firm does not qualify as 'income not chargeable to tax' since the same has already suffered tax in the hands of the firm. By virtue of the Section 10(2A) of the Act, as the tax on profits has already been paid, the same is tax-exempt in the hands of the partners. In view of the same, the provisions of Section 14A of the Act are not applicable in this case. The tax-payer relied on a number of judgements in support of the above claim.

The tax department's representative argued that the motor car has not been used by the tax payer for the purpose of his business, but for the purpose of business of the firm, thus the expenditure could not be allowed to be claimed by the tax-payer. It was further provided that while under the Indian Partnership Act, the firm and its partners are synonymous, under the Act, the law is quite clear where both the firm and partners are two separate entities liable to tax. Both the firm and the partners are taxed on their separate incomes without any double taxation.

The Tribunal, while relying on the arguments of both sides, held that although a firm is nothing but the collective name of the partners under the Partnership Act, as far as the Income Tax Act is concerned, it is an entity distinct and separate from its partners. ***So, while the remuneration and interest earned by partners from the firm is taxable in the hands of the partners, the same is allowed as an expense for the firm from its profits.*** Once the firm pays taxes on its profits, any share distributed thereon to partners is exempt in their hands. Thus, it is quite clear that the amount taxed in the hands of the firm is not taxed again in the hands of the partners. Therefore, in view of specific provisions available under the Act, the Tribunal did not accept the tax-payers claim that the profit share is not excluded from his total income because the firm has already paid tax on it.

The Tribunal also held that Section 10(2A) of the Act speaks about exclusion from total income, it refers to the income of the person under consideration. In the said case, as profits from firm is exempt from tax, the same is obviously excluded from the tax-payers income. Consequently, provisions of Section 14A would be applicable for disallowance of the depreciation benefit to the extent of 76%.

However, the Tribunal also held that section 14A only deals with expenditure incurred in relation to income and not statutory allowances admissible to tax-payers under the Act. Depreciation charged under the Act is an allowance granted and does not qualify as expenditure for the said purpose.

To conclude, The above ruling thus interprets the provisions of the Act to provide that partners of firms can consider claiming depreciation on assets (in their personal name and used for the firm's business) against the remuneration and interest income from their firms. Any other expenditure to be claimed, namely travelling, conveyance, books, printing and stationery, etc, will need to be proportionately apportioned between the exempt profit share and taxable remuneration.

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