

Levy of MAT on receipts which are either tax exempt or not 'income' at all



Levy of Minimum Alternate Tax ('MAT') on tax-free receipts under the Income-tax Act, 1961 ('the Act') is turning out to be a highly debatable topic in present times. To illustrate, a taxpayer can earn a receipt on account of capital gains which are specifically exempt under Section 47 of the Act or could have income arising out of receipts purely on capital account which are not 'income' itself under the Act. Such taxpayer would claim such receipt as tax free under the normal provisions of the Act. However, for the purposes of the MAT provisions, such (tax-free) receipts would form part of its 'book profits' and become subject to MAT. It is often probed as to whether or not it should exclude the tax-free income from book profits for MAT purposes and there is no clear mechanism or legal basis provided for such proposition. Towards this, there have been several judicial precedents wherein the positions adopted by the taxpayers have been put to test. Interestingly, there have been decisions on both sides. Read on to know more.....



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In the case-laws favouring taxpayers, the Hon'ble Authorities have upheld that MAT can be levied only on 'working results' of the taxpayers and that the tax-free receipts / earnings of taxpayer must be excluded from book profits for the purposes of levy of MAT. Accordingly, the book profits of a taxpayer require and merit exclusion of tax-free items for MAT purposes. On the other side, it has also been

upheld that MAT provisions need to be applied strictly as provided in law and there is no scope to tamper the profits shown in taxpayer's P&L Account. Resultantly, book profits has to be derived from the taxpayer's books of accounts and MAT should be applied thereon after making only the adjustments provided in Section 115JB (Explanation 1) of the Act.

DCIT vs. Sicpa India Pvt. Ltd. (Kolkata ITAT)

In the aforesaid series of case-laws, in a recent case before the Hon'ble Kolkata ITAT, the Revenue's appeal was that the assessee, *Sicpa India Private Limited*¹, availed Excise Duty exemption of ₹2,14,60,052/- in respect of its new unit situated in the notified area of Sikkim. In the taxpayer's accounts the said incentive was shown as revenue grant from the Government which was clubbed and included under 'Other Income'. The assessee excluded excise duty exemption in its computation of tax under normal provisions and also for computation of book profit u/s. 115JB of the Act, which was not allowed by the Assessing Officer.

In its appeal before the Hon'ble CIT(A), the assessee submitted that the subsidy in question was a capital receipt not chargeable to tax as the subsidy was given for the purpose of enabling coming into existence new industries and not to enable carrying on of existing industries. It is also argued that while computing book profits u/s. 115JB of the Act, the excise subsidy should be excluded though it is credited in the Profit and Loss Account. The CIT(A) agreed with the submissions of the assessee and held that central excise exemption received by the assessee was not in nature of income and therefore ought to be excluded from book profits for the purposes of Section 115JB of the Act. In arriving at said decision, the Hon'ble CIT(A) relied on the case-law of *Ponni Sugar & Chemicals Ltd*² to determine its nature as capital receipt. In respect of the position of reducing capital receipts from book profits for MAT computation, the CIT(A) inferred from the following case-laws:

- Hon'ble Supreme Court decision in the case of *Padmaraje R. Kadambande vs. CIP*³;
- Hon'ble Supreme Court decision in the case of *Indo Rama Synthetics*⁴;

The Hon'ble ITAT confirmed the CIT(A) conclusion that subsidies being a capital receipt is not in nature of income under normal tax provisions and/or under MAT provisions and have to be excluded from book profits under Section 115JB of the Act.

and construed that the intention of MAT provisions is to bring out/tax real (working) profits of companies.

It was also upheld that any capital receipt which is not 'income' itself under the Act must not be brought into MAT computation. The CIT(A) placed reliance on the following case-laws for the above:

- Hon'ble Supreme Court decision in case of *Apollo Tyres*⁵;
- Hon'ble Jaipur Bench of the ITAT in case of *ACIT vs. Shree Cement Ltd.*

In the revenue's appeal before the Hon'ble ITAT, the ITAT agreed with CIT(A)'s conclusions that the subsidy in question is capital receipt and not subject to tax. On the point of exclusion of such receipt from book profits, the ITAT drew inference from the decision of Hon'ble Kolkata Bench of the ITAT in the case of *Binani Industries Ltd.*⁷ wherein after due consideration to several judicial precedents favouring the assessee, it was concluded that a capital receipt has to be excluded from book profits for MAT purposes. In view thereof, the Hon'ble ITAT confirmed the CIT(A) conclusion that subsidies being a capital receipt is not in nature of income under normal tax provisions and/or under MAT provisions and have to be excluded from book profits under Section 115 JB of the Act.

JSW Steel Ltd. vs. ACIT (Mumbai ITAT)

In another recent judgement of the Hon'ble Mumbai ITAT, the facts examined were that, the assessee, *JSW Steel Ltd*⁸, had availed term loans from various Indian and foreign financial institutions and banks for setting up integrated steel plants. Thereafter, the assessee had incurred huge losses and entered into a financial restructuring package under which a part of the principal and interest amounts were waived.

¹ DCIT Circle-8 v. Sicpa India Pvt Ltd [ITA No 933/Kol/2012]

² (2008) 306 ITR 392 (SC)

³ (1992) 195 ITR 877 (SC)

⁴ (2011) 330 ITR 363 (SC)

⁵ (2002) 255 ITR 273 (SC)

⁶ 2012 TIOL 02 ITAT Jaipur

⁷ 178 TTJ 658 (Kol)

⁸ JSW Steel Ltd v. ACIT [ITA No 923/Bang/2009 and ITA No 930/Bang/2009]

Accordingly, the assessee credited the entire sum so waived off to its P&L Account as an exceptional item with specific note in 'Notes to Account' that the exceptional item represents waiver of dues. Resultantly, the book profits as per its Profit and Loss account included the aforesaid item of ₹314.14 crore, however the said amount was reduced from profits in the tax computation both in normal tax computation and also from book profits while computation of MAT.

In assessment proceedings, the assessee contended that waiver of principal amount of borrowing is a capital receipt, thus the same is not taxable u/s. 41(1) of the Act (as it was not claimed as allowance or deduction in the earlier years). As regards the levy of MAT on such item, the assessee by way of a note in the computation gave a *caveat* that the amount of ₹314.14 crore represents capital receipt and the same is not includible in book profits under Section 115JB of the Act. The Assessing Officer, however, did not agree to reduce the aforesaid waiver of dues from book profits under MAT. On appeal, the Hon'ble CIT(A) rejected the assessee's contentions.

On further appeal before the Hon'ble ITAT, the assessee contended that the waiver of loan is a 'capital receipt' since it was taken for purchase of capital assets and hence does not fall in the definition of 'income' under the Act. Once a particular receipt is not recognised as income at all under the charging provisions of Section 4 & 5 of the Act, it cannot be taxed under any provisions of the Act, including Section 115JB of the Act. The assessee inferred Accounting Standards 5 and 9 and contended that the aforesaid cannot be considered as revenue and also in view of the Hon'ble Supreme Court decision in the case of *Indo Rama Synthetics*⁹, emphasised

The relevant provisions of the Act reveal that sub-Section (1) to Section 115JB of the Act has a non-obstante clause which overrules anything in contrary to it in the Act. Sub-Section (2) to Section 115JB of the Act provides that for the purpose of computation of Book Profit, every Company shall be required to prepare its Profit and Loss Account for the relevant previous year in accordance with the Schedule III of the Companies Act, 2013.

that object of MAT is to bring out 'real profits' of the taxpayer. The Department contended that the assessee itself credited the waiver amount to the P&L Account, then neither the Revenue nor the assessee can tinker with such P&L Account for MAT. It also relied upon Hon'ble Supreme Court decision in *Apollo Tyres Ltd vs. CIT*¹⁰ and contended that notes appended to P&L Account cannot be read into and ultimately the results shown by the assessee are to be considered.

In view of the above, the Hon'ble ITAT upheld that as per Section 41(1) of the Act, waiver of remission of liability cannot be regarded as 'income' under the Act. It also observed that the purpose behind MAT provisions has been to take care of the phenomenon of zero tax companies which continued to show profits and distribute dividends and yet pay no taxes. The object of enacting MAT provisions was never to fasten any liability in respect of something which is not an 'income' at all. It also relied on decisions of Spl. Bench in case of *Sutlej Cotton Mills Ltd vs. ACIT*¹¹ and Cochin Bench of ITAT in case of *ACIT vs. Nilgiri Tea Estate Ltd*¹² wherein it was upheld that an item of income which does not come within the purview of the Income tax cannot be subjected to tax under any other provision of the Act.

The ITAT further referred the Accounting Standards and observed that there are two types of compulsions while preparing annual accounts, one is accounting compulsions and second is disclosure compulsions. A mere disclosure of an extraordinary item in the Profit and Loss Account does not mean that said item represents the working result of the Company. The ITAT upheld that in view of clause (ii) of Explanation 1 of Section 115JB of the Act, it requires exclusion from book profit all that income which are exempt and are not in nature of income, if any such amount is credited to Profit & Loss Account. On the same logic, it would be inconceivable that capital surplus arising due to waiver of loan be excluded from book profits for MAT computation. Thus, it concurred with the assessee.

The above-mentioned case-laws clearly seem to examine a few fundamental questions – (i) that once a particular receipt does not have characteristics of being an 'income' under the Act, could tax in the form of MAT be levied on the same (due to taxpayer's obligation under Accounting Standards to include such receipts in its Profit and Loss Account)

⁹ (2011) 330 ITR 363 (SC)

¹⁰ 255 ITR 273

¹¹ 45 ITD 22 (Cal) (SB)

¹² (2014) 65 SOT 14

through a mechanical application of provisions; and (ii) whether in the derivation of 'Book Profits' for MAT purposes, one can adjust it to derive real and operational profits/results.

The relevant provisions of the Act reveal that sub-Section (1) to Section 115JB of the Act has a *non-obstante* clause which overrules anything in contrary to it in the Act. Sub-Section (2) to Section 115JB of the Act provides that for the purpose of computation of Book Profit, every Company shall be required to prepare its Profit and Loss Account for the relevant previous year in accordance with the Schedule III of the Companies Act, 2013. Further, Explanation 1 to Section 115JB of the Act provides for certain specific inclusions or exclusions for computation of Book Profit. Thus, the net profit in the Profit and Loss Account has to be computed in accordance with the Companies Act, 2013 and then adjusted with the inclusions or exclusions provided in Explanation 1 to Section 115JB of the Act, to compute the MAT payable by the taxpayers. Thus, the scope and application of the underlying provisions appear to be mechanical and there is no clear window provided to the taxpayers for making any kind of adjustments to its book profits and derive the real or working profits. In view thereof, the proposition upheld in the above-mentioned case-laws is certainly landmark.

B&B Infotech vs. ITO (Bangalore ITAT)

Interestingly, there have been judicial precedents wherein the Hon'ble Authorities have upheld different tax positions adopted by the taxpayers on this account. In the case of *B&B Infotech*¹³ before the Hon'ble Bangalore Bench of ITAT, the assessee had credited the remission of bank loan to the Profit and Loss Account, but, on the ground that such remission was a capital receipt, a note to that effect was inserted in Notes to Accounts. For computation of Book Profit, this amount was reduced by the assessee from the net profit as per Profit and Loss Account. The Tax Authorities did not accept this claim and held this amount could not be reduced from the net profit for the purpose of computing MAT. The Hon'ble ITAT held that once the accounts are prepared in accordance with the Companies Act, 1956, adjustment could not be made to the Book Profit by making a disclosure in the Notes to Account. Crediting the amount of remission of bank

The Hon'ble ITAT held that once the accounts are prepared in accordance with the Companies Act, 1956, adjustment could not be made to the Book Profit by making a disclosure in the Notes to Account. Crediting the amount of remission of bank loan, it was held, was in accordance with Schedule VI to the Companies Act, 1956.

loan, it was held, was in accordance with Schedule VI to the Companies Act, 1956 and therefore, the amount so credited could not be reduced from the net profit and MAT was payable thereon. In the above-mentioned decision of JSW Steel Ltd., the decision of Bangalore Bench of ITAT in case of *B&B Infotech* has been distinguished. Thus, divergent views of the Hon'ble Authorities are emerging on a very similar position adopted by different taxpayers. There are other case-laws such as *Duke Offshore Ltd. vs. DCIT*¹⁴, *CIT vs. Veekaylal Investment Co. (P) Ltd.*¹⁵ which are held against the assessee on similar position(s).

Shivalik Ventures P. Ltd. vs. DCIT (Mumbai ITAT)

There is another decision of the Hon'ble Mumbai ITAT involving similar facts in case of *Shivalik Ventures P. Ltd. vs. DCIT*¹⁶. Here, the assessee had transferred certain assets (being development rights to a piece of land) to its wholly owned subsidiary. The assessee did not include gains arising from such transfer in the Book Profits computed for the purpose of paying MAT and such fact was disclosed in the Notes to Accounts. The tax authorities were of the view that the provisions of Section 115JB of the Act did not provide any specific exclusion of such gains, and it could not be reduced from the Book Profits. The Hon'ble ITAT however, pronounced its judgement in favour of the assessee, on the basis that the underlying receipt is not 'income' as per Section 2(24) of the Act and further that the taxpayer has disclosed in its Notes to Accounts which merit its exclusion from book profits.

In this series of judgements, there are few other decisions such as in the case of *DCIT vs. Binani Industries Ltd*¹⁷, wherein the Hon'ble Kolkata Bench of ITAT upheld that a receipt on forfeiture of share

¹³ *B&B Infotech vs. ITO*: [2015] 155 ITD 1040 (Bang-Trib.)

¹⁴ [2011] 45 SOT 399 (Mumbai)

¹⁵ [2001] 249 ITR 597

¹⁶ [2015] 43 ITR(T) 187 (Mumbai-Trib.)

¹⁷ ITA No.144/Kol/2013 dated 15 February 2016

warrants is a capital receipt and has to be excluded from book profits even if credited to the Profit and Loss Account. Following the same decision, the Kolkata ITAT has recently upheld in the case of *McNally Bharat Engineering Co. Ltd.*¹⁸, to exclude retention money from book profits for the purposes of MAT calculation u/s. 115JB in case of assessee (engaged in executing turnkey contracts) for AY 2006-07.

Another important decision has been of the Hon'ble ITAT Lucknow in the case of *L. H. Sugar Factory Ltd.*¹⁹. In this case, the assessee was in receipt of income from sale of carbon credits. It was held

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by the ITAT that income from sale of carbon credits was in the nature of capital receipt and placing its reliance on judgement of Hon'ble Jaipur Bench of ITAT in the case *Shree Cement Ltd.*²⁰, the ITAT held that capital receipts has to be excluded from Book Profits for computing MAT.

In light of the above, it emerges that due to the manner of application of MAT provisions, there could be a widespread levy of MAT on capital items and/or receipts which are not 'income' *per se* under the Act. It could be due to an underlying accounting obligation of the taxpayer and a mechanical application of tax (MAT) provisions thereon and could result in hardship to the assessee. Also, this position remain subject to interpretation(s) and it remain litigative, contentious and highly debatable. Thus, the legislators must bring in the much needed clarity on this subject to bring in consistency in the tax positions adopted by the taxpayers and also for settling the disputes and controversy in a much wider interest. ■

¹⁸ ITA No 100/Kol/2011, ITA No 532/Kol/2012, ITA No 217/Kol/2012, ITA No 533/Kol/2012, ITA no 218/Kol/2012

¹⁹ ITA No. 417/LKW/2013

²⁰ M/s Shree Cement Limited vs. The Addl. CIT: ITA/503/JP/2012



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