

IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 25.08.2015

CORAM

THE HONOURABLE MR.JUSTICE V.RAMASUBRAMANIAN
AND
THE HONOURABLE MR.JUSTICE T.MATHIVANAN

Tax Case (Appeal) No.933 of 2005

M/s Dharmapuri Paper Mills Pvt.Ltd.,
140, Luz Church Road
Mylapore
Chennai 600 004

.. Appellant

-vs-

The Joint Commissioner of Income Tax
Special Range
Salem

.. Respondent

Memorandum of Grounds of Tax Case Appeal under Section 260A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal, Chennai 'A' Bench dated 21.7.2005 made in I.T.A.No.1612/Mds/2000 for the assessment year 1997-98.

For Appellant	:	Mr.R.Vijayaraghavan for Mr.P.J.Rishikesh
For Respondent	:	Mr.J.Narayanasamy

JUDGMENT

(Judgment of the Court was delivered by V.RAMASUBRAMANIAN, J.)

This appeal by the assessee under Section 260A of the Income Tax Act, 1961, was admitted on the following substantial questions of law:-

“(1) Whether on the facts and circumstances of the case, the Tribunal is right in law in holding that books profit is not to be reduced by the excess provisions of

depreciation credited in the profit and loss account?

(2) Whether on the facts and circumstances of the case, the Tribunal is right in law in holding that excess provision for depreciation provided for in earlier years and credited to profit and loss account consequent to the change in the method of depreciation, would not qualify for adjustment under clause (i) of Explanation to Section 115JA and should not be reduced to arrive at book profit for the purpose of Section 115JA?

(3) Whether the Tribunal is justified in holding that since the appellant has already got some benefits, the same has to be surrendered?"

2. Heard Mr.R.Vijayaraghavan, learned counsel for the appellant/assessee and Mr.J.Narayanasamy, learned standing counsel for the department.

3. With respect to the assessment year 1997-98, the assessee filed a return of income on 28.11.97 admitting a loss. The return was processed under Section 143(1) on 30.3.98.

4. However, on the ground that the assessee had written back depreciation wrongly in their profit and loss account and that therefore the income chargeable to tax had escaped assessment, a notice under Section 148 was issued, to assess the escaped income under Section 115JA of the Act.

5. By an order passed on 24.2.2000, the assessing officer held that the book profit was the net profit as shown in the profit and loss account prepared

under sub-section (2) of Section 115JA and that it was deliberately inflated to bring back depreciation written back in the earlier years. Therefore, the assessing officer treated 30 per cent of the book profit so calculated as the income of the assessee under Section 115JA.

6. An appeal filed by the assessee was partly allowed by the Commissioner of Income Tax (Appeals) by an order dated 20.7.2000. On the issue relating to the applicability of Section 115JA, the Commissioner decided the matter in favour of the assessee.

7. The Revenue filed an appeal before the Income Tax Appellate Tribunal in I.T.A.No.1612 of 2000. The Tribunal reversed the decision of the appellate Commissioner on the basis of the decision of the Punjab and Haryana High Court in **Sterling Steels & Wires Ltd., v. Deputy Commissioner of Income Tax, (2004) 271 ITR 260 (P&H)**. Therefore, the assessee is before us.

8. As contended by the learned counsel for the assessee, Chapter XII-B was inserted by the Finance Act, 1987 with effect from 1.4.1988. Section 115JA was inserted by the Finance Act, 1996 with effect from 1.4.1997. The question that actually arises for consideration is as to whether the reserves created or the provisions made by an assessee in a previous year which has no relevance to the assessment year commencing on or after the first day of April, 1997 could be reduced or not. It is not necessary to extract Section 115JA in entirety. It will be sufficient to extract the Explanation under sub-section (2) of Section 115JA,

which reads as follows:-

*“Explanation.--*For the purposes of this section, “book profit” means the net profit as shown in the profit and loss account for the relevant previous year prepared under sub-section (2), as increased by--

- (a) the amount of income-tax paid or payable, and the provision therefor; or
- (b) the amounts carried to any reserves by whatever name called; or
- (c) the amount or amounts set aside to provisions made for meeting liabilities, other than ascertained liabilities; or
- (d) the amount by way of provision for losses of subsidiary companies; or
- (e) the amount or amounts of dividends paid or proposed; or
- (f) the amount or amounts of expenditure relatable to any income to which any of the provisions of Chapter III applies;
- (g) the amount or amounts set aside as provision for diminution in the value of any asset,

if any amount referred to in clauses (a) to (g) is debited to the profit and loss account, and as reduced by,--

- (i) the amount withdrawn from any reserves or provisions if any such amount is credited to the profit and loss account:

Provided that, where this section is applicable to an assessee in any previous year (including the relevant previous year), the amount withdrawn from reserves created or provisions made in a previous year relevant to the assessment year

commencing on or after the 1st day of April, 1997 but ending before the 1st day of April, 2001 shall not be reduced from the book profit unless the book profit of such year has been increased by those reserves or provisions (out of which the said amount was withdrawn) under this Explanation; or
(ii) the amount of income to which any of the provisions of Chapter III applies, if any such amount is credited to the profit and loss account; or
(iii) the amount of loss brought forward or unabsorbed depreciation, whichever is less as per books of account.
....”

9. Before we actually get into the scope of the Explanation under sub-section (2) of Section 115JA, it may be relevant to take note of the object behind the introduction of Chapter XII-B. The object behind the introduction of Chapter XII-B was indicated by the Supreme Court in **Dynamic Orthopedics P.Ltd. v. Commissioner of Income Tax, (2010) 321 ITR 300**, on the following lines:-

“7. In our view, with respect, the judgment of this court in Malayala Manorama Co.Ltd., v. CIT reported in (2008) 300 ITR 251 needs reconsideration for the following reasons: Chapter XII-B of the Act containing “Special provisions relating to certain companies” was introduced in the Income Tax Act, 1961, by the Finance Act, 1987, with effect from April 1, 1988. In fact, Section 115J replaced section 80VVA of the Act. Section 115J (as it stood at the relevant time), inter alia, provided that where the total income of a

company, as computed under the Act in respect of any accounting year, was less than thirty percent of its book profit, as defined in the Explanation, the total income of the company, chargeable to tax, shall be deemed to be an amount equal to thirty per cent of such book profit. The whole purpose of section 115J of the Act, therefore, was to take care of the phenomenon of prosperous "zero tax" companies not paying taxes though they continued to earn profits and declare dividends. Therefore, a minimum alternate tax was sought to be imposed on "zero tax" companies. Section 115J of the Act imposes tax on a deemed income. Section 115J of the Act is a special provision relating only to certain companies. The said section does not make any distinction between public and private limited companies. In our view, section 115J of the Act legislatively only incorporates the provisions of Parts II and III of Schedule VI to the 1956 Act. Such incorporation is by a deeming fiction. Hence, we need to read section 115J(1A) of the Act in the strict sense. If we so read, it is clear that, by legislative incorporation, only Parts II and III of Schedule VI to the 1956 Act have been incorporated legislatively into section 115J of the Act. Therefore, the question of applicability of Parts II and III of Schedule VI to the 1956 Act does not arise. If a company is a MAT company, then be it a private limited company or a public limited company, for the purposes of section 115J of the Act, the assessee-company has to prepare its profit and loss account, in accordance with Parts II and III of Schedule VI to the 1956 Act alone. If, with respect, the judgment of this

court in Malayala Manorama Co.Ltd. (2008) 300 ITR 251 is to be accepted, then the very purpose of enacting section 115J of the Act would stand defeated, particularly when the said section does not make any distinction between public and private limited companies. It needs to be reiterated that, once a company falls within the ambit of it being a MAT company, section 115J of the Act applies and, under that section, such an assessee-company was required to prepare its profit and loss account only in terms of Parts II and III of Schedule VI to the 1956 Act. The reason being that rates of depreciation in rule 5 of the Income Tax Rules, 1962, are different from the rates specified in Schedule XIV to the 1956 Act. In fact, by the Companies (Amendment) Act, 1988, the linkage between the two has been expressly de-linked. Hence, what is incorporated in section 115J is only Schedule VI and not section 205 or section 350 or section 355. This was the view of the Kerala High Court in the case of CIT v. Malayala Manorama Co.Ltd., reported in (2002) 253 ITR 378, which has been wrongly reversed by this court in the case of Malayala Manorama Co.Ltd. v. CIT reported in (2008) 300 ITR 251."

10. Therefore, the very object of introduction of Chapter XII-B was to make very prosperous companies that managed to be "zero tax" companies by a clever process of accounting, pay tax. But what happened was that Chapter XII-B had to evolve over a period of about 14 years. It is stated that Section 115J was inserted with effect from 1.4.1988, with reference to the

assessment year 1988-89 and it continued to be in force till the assessment year 1990-91. Thereafter, Section 115JA was inserted in relation to the assessment year 1997-98 and the same was in force upto the assessment year 2000-2001. Thereafter, Section 115JB was inserted with effect from the assessment year 2001-2002. But the object behind each of these provisions was to ensure that by adopting different methods of preparing profit and loss account, the companies do not keep the income tax department at bay even while making profits.

11. Keeping the above in mind, let us now come back to Section 115JA. Under sub-section (1) of Section 115JA, if the total income of an assessee which is a company in respect of any previous year relevant to the assessment year commencing on or after the first day of April, 1997 but before the first day of April, 2001 is less than 30 per cent of its book profit, the total income of such assessee chargeable to tax for the relevant previous year shall be deemed to be an amount equal to 30 per cent of such book profit. Sub-section (2) of Section 115JA made it obligatory for every company to prepare its profit and loss account for the relevant previous year in accordance with the provisions of Parts II and III of Schedule VI to the Companies Act, 1956. But in the second proviso to sub-section (2), the legislature also took note of the fact that it is possible for a company to adopt the method and rates of calculation of depreciation differently and hence an Explanation was inserted to sub-section (2).

12. The question as to whether the assessing officer was entitled to recompute the book profit for the purpose of Section 115J of the Act after

allowing depreciation as per Schedule XIV to the Companies Act, 1956 and not as per the rates specified in rule 5 of the Income Tax Rules, 1962, came up for consideration before the Supreme Court in **Malayala Manorama Co.Ltd., v. Commissioner of Income Tax, (2008) 300 ITR 251**. But the correctness of the view expressed in Malayala Manorama by a two-member Bench of the Supreme Court was doubted by another two-member Bench in **Dynamic Orthopedics P.Ltd. v. Commissioner of Income Tax, (2010) 321 ITR 300 (SC)** and hence a reference has been made to a larger Bench. We are not concerned in this case with the reference so made, as the same relates to the method of computation as stipulated in the Companies Act, 1956 and the one that is prescribed by the Income Tax Rules.

13. What happened in the case of the appellant/assessee is that they had made a provision for depreciation in relation to certain assessment years which did not happen to be the relevant previous year for the assessment year commencing on or after the first day of April, 1997. But after the insertion of Section 115JA, the assessee switched over from the written down value method of depreciation to the straight-line method of depreciation. The assessee did it in terms of the provisions of Section 205(2)(b) of the Companies Act, 1956. This created a surplus in the provision for depreciation to the extent of Rs.130.97 lakhs. For the purpose of income tax, the appellant/assessee showed a loss of Rs.10,81,859/-. However, after taking the surplus in the provision for depreciation that accrued on account of a change in the method of depreciation, the profit and loss account of the assessee showed a profit of Rs.1,20,15,429/-.

14. The assessing officer as well as the Tribunal held that in terms of the proviso under Explanation (i) under sub-section (2) of Section 115JA, the assessee is not entitled to reduce the surplus amount from the book profit. For rejecting the claim of the assessee, the Tribunal relied upon the decision of the Punjab and Haryana High Court in **Sterling Steels & Wires Ltd., v. Deputy Commissioner of Income Tax, (2004) 271 ITR 260**. But as rightly contended by the learned counsel for the assessee, the Punjab and Haryana High Court, though concerned in that case with the scope of the proviso to Explanation (i) to Section 115J, was dealing in that case with a factual scenario that was completely different. The Punjab and Haryana High Court had noted in that case that the assessee had created reserves in the previous year relevant to the assessment year 1990-91, which had commenced after 1st April, 1988. The Punjab and Haryana High Court specifically noted that this was an undisputed fact. As we have pointed out earlier, Section 115J was introduced with effect from 1.4.1988 and Explanation (i) to Section 115J which is similar to Explanation (i) to Section 115JA (with which we are concerned in this case) also contained the same expression, namely, previous year relevant to the assessment year. This factual distinction was lost sight of by the Tribunal. If this had been taken into account, the Tribunal would have actually found that the decision in Sterling Steels could be taken advantage of by the assessee in this case. Therefore the question that arises is as to whether the proviso to Explanation (i) would get attracted in this case at all or not.

15. We have already extracted the Explanation under sub-section (2) of

Section 115JA in entirety. In simple terms, the Explanation under sub-section (2) can be understood as follows:-

- (i) An assessee which happens to be a company, is entitled to increase the net profit as shown in the profit and loss account, for the purpose of arriving at the book profit by adding whatever is mentioned in clauses (a) to (g) of the Explanation.
- (ii) Similarly, an assessee is entitled to have the net profit reduced by certain items mentioned in clauses (i) to (ix).

16. According to Mr.J.Narayanasamy, learned standing counsel for the department, the increases and the reductions stipulated in the Explanation should go together. It is contended by the learned standing counsel that unless the net profit of an assessee being a company as shown in the profit and loss account for the relevant previous year is increased by the amounts indicated in the Explanation (a) to (g), the assessee may not be entitled to the reduction under (i) to (ix). In support of the said contention, the learned standing counsel relies upon the decision of the Supreme Court in **Indo Rama Synthetics (I) Ltd. v. Commissioner of Income Tax, (2011) 330 ITR 363.**

17. It is seen from the decision of the Supreme Court in Indo Rama Synthetics that the Supreme Court was concerned in the said case primarily with the question as to whether the amount transferred from the revaluation reserve and set off against the amount of depreciation debited to profit and loss account could be excluded in terms of Explanation (i) to Section 115JB(2) read with the

proviso thereto or not. Though the decision of the Supreme Court arose out of Section 115JB, the principles laid down in the said decision, if were applicable to the case on hand, would apply in principle to the cases arising under Section 115JA also. This is for the reason that the scope and ambit of Sections 115J, 115JA and 115JB are one and the same, except the fact that they had their applications with effect from different assessment years.

18. In paragraphs 13 to 17 of the said decision, the Supreme Court indicated the steps to be followed in arriving at the book profit by an assessee being a company. In simple terms, the Supreme Court stated that the first step towards arriving at the book profit is to increase the net profit shown in the profit and loss account for the relevant previous year prepared under Section 115JB(2) by the amounts specified in clauses (a) to (f), if such amounts had been debited to the profit and loss account. The second step was to reduce the amount so arrived at, by the amounts specified in clauses (i) to (vii) under the Explanation to Section 115JB. Paragraphs 15 to 17 of the decision of the Supreme Court in *Indo Rama Synthetics* read as follows:-

“15. The first step for arriving at the “book profit” is that the net profit as shown in the P&L a/c for the relevant previous year prepared under s.115JB(2) has to be increased by the amount(s) in cls.(a) to (f) if such amount(s) is debited to the P&L a/c. Clause (b) refers to amount(s) carried to any reserves by whatever name called. As stated above, such increase needs to be made only if any amount referred to in cls.(a) to (f) is debited to P&L a/c.

16. The second step for arriving at the "book profit" is that the net profit as shown in the P&L a/c for the relevant previous year prepared under s.115JB(2) and as increased by any amount, as stated above, has to be reduced by the amount(s) in cls.(i) to (vii).

17. For the purposes of deciding this case it may be noted that we are concerned with cl.(i) which inter alia refers to an amount(s) withdrawn from any reserves if any such amount(s) is credited to P&L a/c. During the relevant assessment year, cl.(i) had an exception to such exclusion. That exception was in the form of a proviso which inter alia stated that the exclusion in cl.(i) to the Explanation will not apply "to the amount(s) withdrawn from reserves created in a previous year relevant to the assessment year 1997-98 or any subsequent assessment year unless the book profit of such year stood increased by those reserves (out of which the said amount(s) stood withdrawn)."

19. While we have no quarrel with the method of computation of the book profit as enunciated by the Supreme Court under Section 115JB and while we also have no difficulty in applying the same yardstick to the method of computation stipulated in Section 115JA, we think that the decision of the Supreme Court in Indo Rama Synthetics cannot go beyond that point. The reason is that in the case on hand, we are concerned about a provision made or reserve created by the assessee in a previous year which is not relevant to the assessment year commencing from first day of April, 1997. This is an issue which

was not addressed in Indo Rama Synthetics. In Indo Rama Synthetics, the Supreme Court was concerned with the creation of a reserve during the assessment year 2000-2001. But in this case, the provision was made long prior to the year that could be taken as the previous year relevant to the assessment year commencing from the first day of April, 1997.

20. The proviso under clause (i) of the Explanation makes it clear that in case where Section 115JA is applicable to an assessee in any previous year, the amount withdrawn from the reserves created or provisions made "***in a previous year relevant to the assessment year commencing on or after the first day of April, 1997***", shall not be reduced from the book profit unless the book profit of such year has been increased by those reserves or provisions out of which the said amount was withdrawn under the Explanation. It is not the case of the assessing officer that the provisions made by the assessee in this case were relatable to a previous year relevant to the assessment year commencing on or after the first day of April, 1997.

21. Pointing out the object behind Section 115JA, it was contended by Mr.J.Narayanasamy, learned standing counsel that by a jugglery of the accounting methods, the assessee cannot always make it a "zero tax" company even while making profits or at least showing profits to certain stakeholders. We appreciate the concern. But the law relating to income tax being what it is, we do not think that the Court is entitled to go in for a purposive interpretation when the plain language of the taxing statute is clear. Explanation (i) is very clear in its

purport. The assessee may fall within the ambit of the mischief sought to be undone by Section 115JA. But so long as the express language is in its favour, the mischief or no mischief cannot be cured. Therefore, the substantial questions of law are answered in favour of the assessee. In fine, the Tax Case (Appeal) is allowed. Consequently, T.C.M.P.No.675 of 2005 is closed. No costs.

Index : yes

(V.R.S.J.,) (T.M.,J.)
25.08.2015

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To

1. The Income Tax Appellate Tribunal
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2. The Joint Commissioner of Income Tax
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