



Treatment of Capital Receipts in computing Book Profit u/s 115JB of Income Tax Act, 1961

Provision of Sec. 115JB – Underlying principle

In case of a corporate assessee, if income tax payable on total income is less than 18.5% of book profit, than such book profit shall be deemed to be the total income of the assessee and tax shall be payable by the assessee on such total income @18.5%. “Book profit” is defined in Explanation 1 to Sec. 115JB as net profit as shown in P&L a/c plus specific upward/downward adjustment of items mentioned therein. In unequivocal term, leaving no doubt or room for ambiguity, the “net profit” for this purpose to be sourced from P&L a/c which is:

- (a) Prepared in accordance with the provisions of Part II of Schedule VI to the Companies Act, 1956 and
- (b) Laid before the company at its Annual General Meeting in accordance with the provision of Sec. 210 of the Companies Act, 1956.

This suggests that the computation of “book profit” is sacrosanct and very much similar to rule based system where there is no room for further logic, interpretation or maneuvering. The Apex Court in **Ajanta Pharma Ltd. [Civil Appeal No.7518 of 2010]** has held that Sec. 115JB is a Self Contained Code in itself for computing book profit which signifies that it is a mini Act within the Income Tax Act.

It is in the above background that the recent decision of

Kolkata ITAT in **Binani Industries Ltd [ITA No. 144/Kol/2013]** dated 02-03-2016 needs to be analyzed.

Facts of the case

The facts of the case was very interesting and require due attention. The assessee was a listed company and assessment year involved was AY 2009-10. The assessee had credited Rs. 12.66 Crs. in its P&L a/c in respect of receipt on account of forfeiture of share warrants. For computing book profit, assessee treated the above receipt as under:

- In Original Return of Income, assessee excluded the above receipt of Rs. 12.66 Crs.
- In Revised Return, changing its stand, assessee included above receipt of Rs. 12.66 Crs. and computed higher book profit.
- Again at assessment stage before the AO, the assessee stated that the above receipt of Rs. 12.66 Crs. was erroneously included in the Computation of book profits reported in the revised return and pleaded for exclusion of the same on the ground that it is capital receipt.

Assessee’s Contention

The argument advanced by assessee before the ITAT was as under:

- By applying Rule of purposive construction (i.e.

purpose or rationale of introducing Sec. 115J/115JA/115JB), it was never the intention of the Legislature to bring to tax such receipt which otherwise is not taxable under the provisions of the Act.

- There are two kinds of receipts a) receipts which are not taxable at all and b) receipts which are taxable but subject to exemption/deduction on fulfilling certain conditions. It is only second kind of receipt that would be liable to be taxed u/s 115JB of the Act.
- Decision of Hyderabad Special Bench in Rain Commodities Ltd. [131 TTJ 514 (Hyd)] will not be applicable as in this case issue before the Bench was whether Capital Gain which is otherwise exempt u/s 47(iv) was liable to tax in computing book profit or not, unlike the assessee case where the receipt is Capital receipt in nature which is not chargeable to tax at all.
- Provision of Sec. 115JB(5) will be applied and when the forfeiture of share warrants is not taxable under any other provisions of this Act, then same would not be taxable under book profits u/s 115JB of the Act.

Revenue's Contention

For our erudite reader & professional colleagues, it needs to be pointed out that it was a Departmental appeal against the order of CIT (Appeals) which has allowed the assessee claim. The basis on which CIT (A) has allowed the claim finds no mention in the order of Hon'ble ITAT. It further needs to be noted that, it was also not an exparte order as CIT-DR was present for Department, but more surprisingly, his argument does not find mention in the order although that of AR has been discussed at length.

ITAT decision

Decision has been given solely on the basis of Lucknow Division Bench decision of ITAT in **L.H. Sugar Factory Limited [ITA Nos. – 417,418 & 339/LKW/2013]** dated 09-02-2016 which in turn like this very Bench has relied upon decision of Jaipur Division Bench of ITAT in **M/s Shree Cement Ltd** & decision of Mumbai ITAT in **Shivalik Venture (P) Ltd. [173 TTJ 238 (Mum.)]**.

In all the three cases, amount in respect of Carbon Credit/Sales tax exemption/profit on sale of capital asset has been credited in P&L a/c and auditor has certified the accounts which has been then placed before the shareholders in AGM and thereafter filed to Registrar of Companies.

The main contention of the assessee was that Capital Receipts or Receipt which is not qualified as income u/s 2(24) of the Act needs to be excluded in computing 'book profit'. The ITAT has decided the issue in favor of the assessee's holding as under:

- A receipt which is neither 'Profit' nor 'Income' and which does not have any element thereof embedded therein, cannot be part of 'Profit' as per P&L a/c prepared in terms of Part II of Schedule VI to Companies Act.
- Decision of Rain Commodities (supra) is not applicable as it dealt with the issue of taxability of capital gains in computing Book Profit u/s 115JB of the Act. These capital gains were otherwise income u/s 2(24) of the Act and exclusion was claimed in computing Book Profit u/s 115JB on the ground that the said capital gains was exempt either u/s 47(iv) or u/s 54EC of the Act, which the Tribunal did not agree.
- The genesis of Sec 115J, thereafter section 115JA and now section 115JB was to ensure that the assessee, while making profit from operations, should not enjoy tax free status due to various deductions available under the Income Tax Act. There was never any intention of the legislature to tax what is not income at all. Reliance placed upon Indo Rama Synthetics (I) Ltd [330 ITR 363 (SC)].
- Decision of SC in Apollo Tyres [255 ITR 273 (SC)] will be applicable if the accounts are prepared in accordance with Part II and Part III to Sch.VI of the Companies Act. If however the P&L accounts are not in accordance with Part II and III of Sch. VI to the Companies Act, the said decision cannot be applied and in that situation it does not prohibit the needful adjustment
- Since, the fact that the above sum of receipt is credited to P&L a/c is disclosed in the notes



therefore, same needs to be excluded in computing book profit to arrive at working results of the company.

Our Comments

- The basis of charge u/s 115JB is “book profit” and not “Income”, therefore, whether Capital Receipt/Exempt Capital gain are income or not or enters computation provision or not will not have any bearing whatsoever in computing book profit.
 - Sec. 115JB overrides all provisions of the Act including Sec. 2(24) which defines “income” to the extent of computation of book profit is concerned. In other words, for computation of “book profit” Sec. 115JB should be treated like a Self Contained Code as held by Apex Court in Ajanta Pharma (supra).
 - Under Companies Act, it is responsibility of management of company to prepare accounts as per the relevant provisions of the said Act and same is required to be audited and certified by the Auditor. In case Auditor, not agrees with treatment regarding booking any income or charging any expenditure in P&L a/c it qualifies its audit report. In none of the cases, any qualification is made by the auditor regarding inclusion or crediting of Forfeiture of share warrant/Sales Tax exemption/Profit on transfer of Capital assets/Carbon credit to P&L a/c. It is rightly done so as part II of Schedule VI also provides as under”
 - The P&L a/c should disclose every material feature, including credits or receipts and debits or expenses in respect of non recurring transactions or transactions of exceptional nature
 - Income shall include Profit or Loss in respect of transactions of a kind, not usually undertaken by the company or undertaken in circumstances of an exceptional or non recurring nature, if material in amount.
- Therefore, it is difficult to accept that accounts which is certified by auditors and placed before the AGM and filed to registrar is not prepared in accordance with Part II of the Companies Act, 1956.
- Both under Companies Act as well as Income Tax Act, Statutory Auditor is qualified person to judge and comment whether the accounts are prepared in accordance with the Part II & III of the Companies Act. Apex Court in Apollo Tyres (supra) has clearly held that It is not open to the AO to make fresh enquiry when the accounts of an assessee company is prepared in accordance with Part II Schedule VI of the Companies Act and scrutinized and certified by Statutory Auditor who has the statutory obligations to examine and be satisfied that the accounts of the company are maintained in accordance with requirements of Companies Act. Therefore, in view of decision of SC in Apollo Tyres (supra) is difficult to exclude the above items of receipts in computing book profit u/s115JB.
 - The principle of purposive construction of Sec. 115JB does not assist the assessee’s case as by including the said receipt on account of forfeiture in its P&L a/c, profits in books increases and so the dividend payment capacity but for the purpose of computing book profit exclusion is claimed. A line or Para cannot from here and there can be picked to argue or contented that Supreme Court has decided the issue. It is the ratio of decision which is important and not any observation made by judge. This is precisely what has been done by assessee by placing relying on decision of Indo Rama Synthetic (supra).
 - If an item of income or expenditure which is required to be disclosed in the P&L a/c prepared as per Part II of Schedule VI to the Companies Act but instead disclosing the said item in P&L a/c, it was disclosed in notes to the accounts, then such item will be treated as part of the P&L a/c. Once, item is credited in P&L a/c it cannot be excluded merely a note in this regard is appended in accounts.
 - There are umpteen numbers of decisions on the



very issue where the ITATs have taken contrary view following the decision of Apollo Tyres & Rain Commodities (supra).

- Duke Offshore [ITA No. 5810/Mum./2008] dated 05-01-2011

It has been held that any receipt even if it is a capital receipt, which may or may not be taxable under the normal provisions of the Income tax Act, if it is credited to the profit and loss account cannot be excluded in computing the book profit, unless it is specifically excluded under any of the Explanations found in that section.

- M/s B&B Infotech [ITA No. 726/Bang/2014] dated 07-10-2015

It has been held that remission of loan from Bank which is also Capital Receipt in nature cannot be excluded in computing book profit u/s 115JB of the Act.

- Western India Cashew Company [ITA No. 829/Che./2015] dated 12-08-2015

The decision of Shivalik Venture is also seems to be not in sync with the law laid

down by the Special Bench in Rain Commodities.

- Sec. 115JB(5) also do not have any application as computation of book profit is governed by Explanation to said section itself and other provision like provision relating to definitions, recoveries, payment, assessment, etc., would apply as usual. Decision of Karnataka HC in Jindal Thermal Power Ltd. [286 ITR 182] supports this view.
- In the recent budget, Hon'ble Finance Minister has given much emphasis on reducing litigation. CBDT has also issued various Circulars or Guideline to achieve this end. ITAT should also play their part as by giving divergent views on identical issue adds to litigation. Last week only, The Hon'ble Bombay HC while entertaining Writ petition filed by HDFC Ltd. Had taken strong objection to the decision of ITAT which has refused to follow the binding precedent. It is well accepted principle that for taking a view which is contrary to the other decision the Bench should record a reason as to why it is taking such view or refer the issue to Larger Bench.

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