

Karnataka High Court Kwality Biscuits Ltd. vs Commissioner Of Income-Tax on 30 November, 1999 Equivalent citations: 2000 243 ITR 519 KAR, 2000 243 ITR 519 Karn Author: V Singhal Bench: V Singhal, T Vallinayagam JUDGMENT V.K. Singhal, J. 1. The Assistant Registrar of the Income-tax Appellate Tribunal has referred the following question of law arising out of its order dated March 3, 1994, in respect of the assessment year 1989-90, under Section 256(1) of the Income-tax Act, 1961 : “(1) Whether, on the facts and in the circumstances of the case for the purpose of Section 115J of the Act read with Section 205(1)(b) of the Companies Act, 1956, the expression ‘loss’ under the Companies Act is to be reckoned after allowance of depreciation or before it ? (2) Having regard to the scheme of Section 115J whether in an assessment year where the assessee’s income is computed by invoking the provisions of Section 115J interest under Sections 234B and 234C are leviable ? (3) Whether, on the facts and in the circumstances of the case, the amounts to be carried forward like unabsorbed depreciation, unabsorbed investment allowance and business loss from an assessment year to which the provisions of Section 115J are applied should be those Which were available to the assessee as at the commencement of the previous year relevant to the said assessment year unaltered by the making of an assessment under Section 115J for that assessment year ? (4) Whether, on the facts and in the circumstances of the case, the carried forward amounts like unabsorbed depreciation, investment allowance and business loss should be reckoned as if a regular assessment is made under Section 143(3)/144 of the Act for the year in question and only such sums as emerge after the making of such a notional assessment for that year could be carried forward ? (5) Whether, on the facts and in the circumstances of the case, the written down value as at the commencement of the relevant previous year in respect of the assets then in existence for the current assessment year should remain the same for the immediately succeeding assessment year unaltered by any notional assessment that might be made for the purpose of examining the applicability of Section 115J ? (6) Whether, on the facts and in the circumstances of the case, the amount of depreciation which is absorbed in a notional assessment under Section 143(3)/144 for the relevant assessment year reducing the income to nil should be deemed to have been actually allowed for the purpose of working out the written down value for the immediately subsequent assessment year ? (7) Whether, on the facts and in the circumstances of the case, the sum of Rs. 83,61,301 written back to the profit and loss account for the assessment year 1987-88 should not have been excluded for the purpose of computation of profits under Section 115J read with Section 205 of the Companies Act, 1956 ?” 2. The facts of the case are that the assessee is a manufacturing company and for the assessment year in question, its income was computed by invoking the provisions of Section 115J. While concluding the assessment, the Assessing Officer, for the purpose of applying the provisions of Section 205(1)(b) of the Companies Act held that the expression “loss” therein is before allowance of depreciation and not after deduction of depreciation. He also proceeded on the basis that even though the income as per the normal computation under the Income-tax Act led to a negative figure still the assessee was liable to pay advance tax and its failure

t6 pay such advance tax would invite the levy of penal interest under Sections 234B and 234C. He also determined the amounts to be Carried forward to the subsequent year like losses, unabsorbed depreciation, etc., by making a notional assessment under Section 143(3) and on the basis that such an assessment was made he proceeded to determine the amounts to be carried forward as well as the written down value to be adopted for the subsequent year for the purpose of allowance of depreciation. While computing the profits for the purpose of Section 115J and making the adjustments thereof, as provided by law, the Assessing Officer did not deduct the sum of Rs. 83,61,301 written back to the profit and loss account for the accounting year relevant to the assessment year 1987-88 by reason of the change in the method of provision of depreciation by the assessee. The assessee appealed. The Commissioner (Appeals) held that the expression “loss” has to be considered after deducting therefrom depreciation. The amounts to be carried forward to the subsequent year in respect of unabsorbed items were those which were in existence at the commencement of the accounting year. Similarly, written down value for the subsequent year has to be adopted at the value as at the commencement of the accounting year in respect of the assets in existence at that point of time. The Commissioner (Appeals) did not approve of any adjustments in respect of the sum of Rs. 83,61,301. He upheld the levy of interest under Sections 234B and 234C. Both the assessee and the Department appealed. The Tribunal, following the decision of the Andhra Pradesh High Court in W. P. No. 5408 of 1993, dated December 31, 1993 (reported as V. V. Trans-Investments (P.) Ltd. v. CIT [1994] 207 ITR 508), and disagreeing with the decision of the Special Bench of the Tribunal reported in Surana Steels Pvt. Ltd. v. Dy. CIT [1993] 201 ITR (AT) 1 (Hyd) held that the expression “loss” under Section 205 of the Companies Act must be interpreted so as to exclude depreciation. The Tribunal also held that interest under Sections 234B and 234C can be charged. The departmental appeal was allowed to the extent that the word “loss” excludes depreciation. 3. So far as question No. 1 is concerned, the controversy is now covered by the decision of the apex court in the case of Surana Steels Pvt Ltd. v. Deputy CIT [1999] 237 ITR 777, wherein it was observed that (page 786) : “Section 205(1), proviso Clause (b) of the Companies Act brings out the unabsorbed portion of the amount of depreciation already provided for computing the loss for the year. The words ‘the amount provided for depreciation’ and ‘arrived at in both cases after providing for depreciation’ make it abundantly clear that in this clause ‘loss’ refers to the amount of loss arrived at after taking into account the amount of depreciation provided in the profit and loss account. The term ‘loss’ as occurring in Clause (b) of the proviso to Section 205(1) of the Companies Act has to be understood and read as the amount arrived at after taking into account the depreciation. Then alone the formula prescribed in this clause would make sense and it would be consistent with the object sought to be achieved by enacting Section 115J of the Income-tax Act, 1961. If ‘loss’ were to be taken as pre-depreciation loss then the resultant computation will not be in conformity with the tenor of the provisions of Section 205. The language of Clause (b) of the proviso to Section 205(1) is clear. It applies to those cases where the depreciation has been pro-

vided in accordance with the provisions of Sub-section (1) of Section 205. The depreciation is provided for in the profit and loss account. The loss is arrived at after taking into account the depreciation provided. It is therefore clear that the word 'loss' as used in the proviso Clause (b) to Section 205(1) signifies the amount arrived at after taking into account the amount of depreciation and it has to be so read and understood in the context of Section 115J of the Income-tax Act, 1961." 4. In view of the judgment of the apex court we are of the view that, for the purpose of Section 115J of the Act read with Section 205(1)(b) of the Companies Act, the expression "loss" under the Companies Act is to be reckoned after allowance of depreciation. This question is answered in favour of the assessee and against the Revenue. 5. In respect of the liability of interest under Sections 234B and 234C for the income which is determined under Section 115J, learned counsel appearing for the assessee has drawn our attention to the commentary from Kanga and Palkhivala's Income TAX, eighth edition, volume I, wherein it is observed as below : "No company is required to pay advance tax on the basis of this section. The charge under this section is on the basis of the book profit shown by the accounts of the previous year, which are prepared only after the year is over, whereas advance tax, by definition, is to be paid before the close of the previous year. Further, the expressions 'total income' and 'current income' used in Sections 207 to 212 refer to 'income' and 'total income' as defined in Sections 2(24) and 2(45), respectively ; they are concepts which indicate the income and the total incomes computed under different heads specified in the Act. By contrast, Section 115J purports to tax an amount which has never been computed in the manner laid down in the Act at all. The legal fiction in this section, by which the total income is deemed to be thirty per cent. of the book profit, applies only for the purpose of this section ; a legal fiction can operate only within the field of a definite purpose for which it is created." 6. It is submitted that the deemed income cannot be considered to be income as defined under Section 2(24) of the Act and that the Explanation to Section 115J(1A) confers the power of computation of income for the purpose of this section and for other sections it is not taken. It is submitted that liability of interest in default of payment of advance tax and deferment of advance tax have not been visualised by the Legislature when Chapter XVII was brought in the statute book and there being no further declaration of liability of payment of advance tax under Section 115J, the provisions of Sections 234B and 234C cannot be invoked. 7. It is submitted that under Section 14, different heads of income have been specified and the income which is computed under section. 115J does not fall under any of the heads and the provisions of Section 115J are meant only for computation of income and cannot be extended at all. 8. On behalf of the Department, learned standing counsel, has submitted that under Section 210, an assessee has to file his own estimate and pay the tax accordingly in advance. Since the income under Section 115J is treated to be an income, therefore, all the provisions of the Income-tax Act are applicable. 9. We have considered over the matter. Section 115J as inserted by the Budget Speech of the Finance Minister was to the following" effect (see [1987] 165 JTR (St.) 14) : "80. It is only fair and proper that the prosperous should pay at least some

tax. The phenomenon of so-called ‘zero-tax’ highly profitable companies deserves attention. In 1983, a new Section 80WA was inserted in the Act so that all profitable companies pay some tax. This does not seem to have helped and is being withdrawn. I now propose to introduce a provision whereby every company will have to pay a ‘minimum corporate tax’ on the profits declared by it in its own accounts. Under this new provision, a company will pay tax on at least 50 per cent. of its book profit. In other words, a domestic widely held company will pay tax of at least 15 per cent. of its book profit. This measure will yield a revenue gain of approximately Rs. 75 crores.” 10. In the Notes on Clauses, in the Finance Bill [1987] 165 ITR (St.) 137, under Clause 43, it is stated as under : “Clause 43 seeks to insert a new Chapter XIIB containing special provisions relating to certain companies. Under the proposed amendments, in the case of any company, whose total income as computed under the other provisions of the Income-tax Act in respect of any previous year is less than thirty per cent, of its book profit, the total income of such assessee chargeable to tax shall be deemed to be an amount equal to thirty per cent. of such book profit. For the purposes of the aforesaid provision, ‘book profit’ means the net profit as shown in the profit and loss account for the relevant previous year prepared in accordance with the provisions of Parts II and III of the Sixth Schedule to the Companies Act, 1956, subject to certain adjustments. It has also been provided that the aforesaid provision shall not affect the determination of the amounts to be carried forward to the subsequent year or years under the provisions of Sub-section (2) of Section 32, or subsection (3) of Section 32A or Clause (ii) of Sub-section (1) of Section 72 or Section 73 or Section 74 or Sub-section (3) of Section 74A or Sub-section (3) of Section 80J. This amendment will take effect from 1st April, 1988, and will, accordingly, apply in relation to the assessment year 1988-89 and subsequent years.” 11. Section 234B casts the liability for payment of interest for default in payment of advance tax if the assessee is liable to pay advance tax under Section 208 and has failed to pay such tax or, where the advance tax paid by such assessee under the provisions of Section 210 is less than 90 per cent. of the assessed tax, then he is liable to pay simple interest at the rate of two per cent. for every month to the date of determination of total income under Section 143(1) and, where the regular assessment is made, to the date of such regular assessment on the amount equal to the assessed tax or, as the case may be, on the amount by which the advance tax paid has fallen short of the assessed tax. Under the Explanation, “assessed tax” means the tax on the total income as declared in the return or the tax on the total income determined under Section 143(1) or on regular assessment, as reduced by the amount of tax deducted or collected at source in accordance with the provisions of Chapter XVII. 12. Under Section 234C also, if there is liability to pay advance tax under Section 208 and if there is failure to pay such tax or if it is not paid in instalments prescribed in the section, then the liability for interest arises. 13. Section 208 contemplates the liability to pay advance tax in every case where the amount of such tax payable by the assessee during that year, as computed in accordance with the provisions of this Chapter is Rs. 1,500 or more. The computation of advance tax is provided under Section 209, Under Section 209(1)(a) firstly, the

estimate of current income is to be made. If there is no current income there is no liability for making the estimate. It is not a case where the Income-tax Officer has passed an order for payment of advance tax. 14. Under Section 115J, where the total income of the company 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. It is thus, by way of deeming fiction that this income has been considered to be the deemed income. The profit and loss account has to be prepared in accordance with the provisions of Parts II and III of Schedule VI to the Companies Act. In the Explanation under Section 115J(1A) it is provided that 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 (1A) as increased by various amounts given in the section. Thus, for the purpose of assessing tax under Section 115J, firstly, the profit as computed under the Income-tax Act has to be prepared and thereafter the book profit as contemplated by the provisions of Section 115J are to be determined and then the tax is to be levied. The liability of the assessee for payment of tax under Section 115J arises if the total income as computed under the provisions of the Act is less than 30 per cent. of its book profits. This exercise for determining the total income in accordance with the provisions of the Act and that of book profit can be only after the end of the relevant assessment year. It is only the deemed income for which the provisions of Section 115J have been incorporated. When a deeming fiction is brought under the statute it is to be carried to its logical conclusion but without creating further deeming fiction so as to include other provisions of the Act which are not specifically made applicable. Since the entire exercise of computing the income or that of book profit could be only at the end of the financial year, the provisions of Sections 207, 208, 209 or 210 cannot be made applicable, until and unless the accounts are audited and the balance-sheet is prepared even the assessee may not know whether the provision of Section 115J would be applicable or not. The liability would be after the book profits are determined in accordance with the Companies Act. The words "for the purposes of this section" in the Explanation to Section 115J(1A) are relevant and cannot be construed to extend beyond the computation of liability of tax. Accordingly, we are of the view that the Income-tax Appellate Tribunal was not justified in directing to charge interest under Sections 234B and 234C of the Income-tax Act. This question No. 2 is therefore answered in favour of the assessee and against the Revenue. 15. So far as questions Nos, 3, 4, 5 and 6 are concerned, this matter has been dealt with at length by this court in ITRC Nos. 144-145 of 1995 and connected matters, disposed of on September 29, 1999 (*Widia (India) Ltd. v. CIT* [2000] 242 ITR 678). Therefore, it is to be held that the amounts to be carried forward like unabsorbed depreciation, unabsorbed investment allowance and business loss from an assessment year to which the provisions of Section 115J are applied should be those which were available to the assessee as at the commencement of the previous year relevant to the said assessment year unaltered by the making of an assessment under Section 115J for that assessment year, and that carried forward amounts like unabsorbed

depreciation, investment allowance and business loss should be reckoned as if a regular assessment is made under Section 143(3)/144 of the Act for the year in question and only such sums as. emerge after the making of such a notional assessment for that year could be carried forward ; and the written down value as at the commencement, of the relevant previous year in respect of the assets then in existence for the current assessment year should remain the same for the immediately succeeding assessment year unaltered by any notional assessment that might be made for the purpose of examining the applicability of Section 115J; and the amount of depreciation which is absorbed in a notional assessment under Section 143/144 for the relevant assessment year reducing the income to nil should be deemed to have been actually allowed for. the purpose of working' out the written down value for the immediately subsequent assessment year. In respect of these four questions, therefore, the reference is answered in favour of the Revenue and against the asses-see. 16. In respect of question No. 7, it was observed in ITRC Nos. 144445 of 1995 and connected cases disposed of on September 29, 1999 (*Widia (India) Ltd. v. CIT* [2000] 242 ITR 678 (Kar)), that (page 685) : "According to accounting" principles, depreciation is money spent and is an expenditure as held in *Indian Leaf Tobacco Development Co. Ltd. v. CIT* . Section 32 is in respect of depreciation and Section 32A is for investment allowance. Section 72 is for cash losses, etc., and Section 80 refers to conditions under which losses cannot be carried forward which draws a distinction between cash loss, depreciation, investment allowance, speculation losses, etc. It is only for the purpose of carry forward and set-off of loss, such a distinction has been drawn. Under Section 115J, the method of computing the total income is with reference to the provisions of Section 205(1)(b) of the Companies Act and since that provision overrides any other provision. Therefore, the commercial concept as contemplated by the Companies Act has to prevail over a concept referred to in the Income-tax Act. Under Section 211(2) of the Companies Act, every profit and loss account of a company shall give a true and fair view of the profit or loss of the company for the financial year. Under Section 205 of the Companies Act, the word "loss" should be interpreted to include depreciation." 17. In these circumstances, the amount of Rs. 83,61,301 written back to the profit and loss account for the assessment year 1987-88 should not have been excluded for the purpose of computation of profits under Section 115J read with Section 205 of the Companies Act, as it was change of system of accounting by the assessee in accordance with the provisions of the Companies Act. 18. The references are disposed of with the above observations.