

HIGH COURT OF MADRAS

Tamil Nadu Cements Corporation Ltd.

v.

Joint Commissioner of Income-tax, Special Range II, Chennai*

MRS. CHITRA VENKATARAMAN AND K. RAVICHANDRA BAABU, JJ.

TC(A). No. 1123 of 2005†

June 5, 2012

JUDGMENT

Mrs. Chitra Venkataraman, J. - The assessee has preferred the appeal as against the order of the Income Tax Appellate Tribunal relating to assessment year 1997-98. The above Tax Case (Appeal) was admitted on the following substantial question of law:-

"Whether the Tribunal was right in holding that for the purpose of computation under Section 115JA of the Act, the prior years expenses should not be deducted since the same was not debited in the profit and loss account?"

2. It is seen from the narration of facts that the book profit shown by the assessee was computed after deducting prior period expenses of Rs.96,94,693/-. While processing the return, the Assessing Authority viewed that as per the provisions of the Companies Act, prior year adjustments could not be reduced for arriving at the net profit of that particular year. As per Section 115JA of the Act, the Profit and Loss Account for the relevant previous year should be in accordance with the provisions of Parts II and III Schedule VI of the Companies Act. Consequently, it was held that the computation done by the assessee was not in accordance with Section 115JA of the Act. Thus the Officer viewed that the net profit as per the profit and loss adopted by the assessee was not in order. Aggrieved by the same, the assessee went on appeal before the Commissioner of Income Tax (Appeals), who confirmed the order of the Assessing Authority by holding that prior year's expenditure could not be adjusted in the book profit of the current year. The assessee went on further appeal before the Income Tax Appellate Tribunal, who confirmed the view of the Commissioner of Income Tax (Appeals) once again. Aggrieved by this, the assessee is before this Court.

3. Learned counsel for the assessee placed reliance on the decision of the Apex Court in *Apollo Tyres Ltd. v. CIT* [2002] 255 ITR 273/122 Taxman 562 only to contend that while computing the book profit under Section 115JA, the jurisdiction of the Assessing Officer is limited to examine whether the books of account are certified by the authorities under the Companies Act as having been properly maintained in accordance with the Companies Act. The Assessing Officer, thereafter, has the limited power of making increases and reductions as provided for in the *Explanation* to Section 115JA. Thus, when once the assessment is sought to be made under Section 115JA, the said provision does not empower the Assessing Officer to embark on a fresh enquiry in determining the book profit so as to arrive at a re-computation.

4. Learned counsel for the assessee pointed out that the said decision was once again reiterated in the decision of the Apex Court in *Malayala Manorama Co., Ltd v. CIT* [2008] 300 ITR 251/169 Taxman 471. Learned counsel for the assessee pointed out that in the

decision in *Dynamic Orthopaedics (P.) Ltd v. CIT* [2010] 321 ITR 300/190 Taxman 288 (SC), the Apex Court referred the case rendered in the decision *Malayala Manorama Co., Ltd (supra)* to a larger Bench. The said decision however does not in any manner stand in the way of applying the law laid down in the decision of the Apex Court in *Apollo Tyres Ltd. (supra)*. Pointing out to the fact that the profit and loss account computed for the year under consideration was made after taking into consideration the prior year expenses as given under Schedule 'S', she submitted that the issue in question, apart from being concluded by the decision of the Apex Court reported in *Apollo Tyres Ltd. (supra)* is also covered by decision of the Delhi High Court in *CIT v. Khaitan Chemicals & Fertilizers Ltd.* [2008] 307 ITR 150/175 Taxman 195.

5. Per contra, supporting the order of the Tribunal, learned standing counsel for the Revenue submitted that the assessee had not charged the prior year expenses to the profit and loss account. It was deducted from the profit after computing the same. After arriving at the net profit after tax, the assessee has charged prior period expenses. Consequently, no exception could be found in the order of the Tribunal.

6. Heard learned counsel for the assessee as well as learned standing counsel for the Revenue.

7. Before going into the various submissions of learned counsel for the assessee and learned Standing Counsel for the Revenue, the facts herein need to be seen as disclosed in the papers filed before this Court. A perusal of the profit and loss account which is filed before the authorities below and before this Court shows that profit for the year to a tune of Rs.1456.44 was reckoned after taking into account, the prior year expenses which are enumerated under Schedule 'S'. It is seen from the order of the Assessing Authority that the Assessing Authority also did not dispute the above said fact that in computing the net profit of the company, the assessee had considered the deduction of the prior year expenses. The only ground on which the claim of the assessee was rejected was that the prior year adjustments could not be reduced for arriving at net profit for the year under consideration.

8. In contrast to the said fact, the Tribunal held that after arriving at the net profit after tax, the assessee has charged "prior period expenses" and in their opinion, it was charged to appropriation account. We do not think such statement of facts is supported by any material. Thus, the facts as seen from the documents show that the computation of the net profit for the year under consideration was made after adjusting prior year expenses and it was not by way of appropriation account.

9. The authority of an Assessing Officer to go beyond the book profit under Section 115JA for the Officer to go beyond the book profit, in the decision in *Apollo Tyres Ltd. (supra)* the Apex Court pointed out to the objects of the introduction of the said provision of Section 115J with a deeming provision which makes the company liable to pay tax on at least 30 percent of its book profits as shown in its own account. The Apex Court pointed out that Sub-section (1A) of Section 115J does not empower the Assessing Officer to embark upon a fresh inquiry with regard to the entries made in the books of account of the company. The said sub-section mandates the company to maintain its account in accordance with the requirements of the Companies Act for the limited purpose to find out whether the computation is done in accordance with the provisions of the Companies Act. The Assessing Authority has a limited jurisdiction to satisfy himself that the accounts are maintained in accordance with the provisions of the Companies Act. Beyond that, the Assessing Authority has no jurisdiction to go further into accounts. The Apex Court further held as follows:-

"..... If the statute mandates that income prepared in accordance with the Companies Act shall be deemed income for the purpose of Section 115J of the Act, then it should be

that income which is acceptable to the authorities under the Companies Act. There cannot be two incomes one for the purpose of Companies Act and another for the purpose of income-tax both maintained under the same Act. If the Legislature intended the Assessing Officer to reassess the company's income, then it would have stated in Section 115J that "income of the company as accepted by the Assessing Officer" "

10. The said decision came up for consideration, although in the different context as regards the working out of the depreciation in the decision in *Malayala Manorama Co. (supra)*., the Apex court upheld the contention of the assessee therein that the net profit prepared by the assessee after working out the depreciation as per the Income Tax Rules was correct in law.

11. In the decision *Dynamic Orthopaedics (P.) Ltd (supra)* the Apex Court however questioned the correctness of the working out of the depreciation as per the Income Tax Rules as against the rates given in the Companies Act in terms of Parts II and III of Schedule VI to the 1956 Act. Thus, the Supreme Court referred the decision in *Malayala Manorama Co., Ltd. (supra)* to a larger Bench.

12. Leaving this aspect aside, the Apex Court pointed out that by legislative incorporation, only Parts II and III of Schedule VI to the 1956 of the Companies Act have been incorporated legislatively into Section 115J of the Act. The question hence that came up before the Apex Court in the decision in *Dynamic Orthopaedics (P.) Ltd. (supra)* is as regards the computation of the depreciation for the purpose of net profit determination. Hence, as rightly contended by learned counsel for the assessee, the said decision does not seriously stand in the way of this Court considering the issue as regards the deduction of prior year expenses in the matter of computing the net profit of the company for the year under consideration. In fact, similar question came up for consideration before the Delhi High Court in the decision in *Khaitan Chemicals & Fertilizers Ltd. (supra)* The facts therein is that the assessee prepared its net profit as per the profit and loss account after reducing the prior period expenses/ extraordinary items and thus arrived at the resultant book profit. The Revenue contested the claim of the assessee for reducing the prior period expenses on the ground that such expenses did not find mention in any of the clauses (i) to (ix) of the *Explanation* to Section 115JA(2). Dealing with such contention, the Delhi High Court pointed out that to the Accounting Standard (AS-5) and stated that Accounting Standards clearly stipulates that prior period items are income or expenses which arise "in the current period" as a result of errors or omissions in the preparation of the financial statement of one or more prior periods. Referring to paragraph 7 of AS 5, the Delhi High Court pointed out that the net profit or loss comprises of extraordinary items and the same should be disclosed on the face of the statement of profit and loss. The Delhi High Court further held as follows:-

" From this, it is clear that both, "prior period items" as well as "extraordinary items" are to be included in the determination of net profit or loss. If a prior item is an expense, it is obvious that it will go towards reducing the net profit or increasing the loss, as the case may be. On the other hand, if the prior period item is an income, it would go towards increasing the net profit or reducing the loss, as the case may be. The same is the position with extraordinary items which may be income or expenses. The conclusion that one can arrive at from this discussion is that prior period items and extraordinary items form part of the net profit or loss. "

13. Prior period items are also enumerated in paragraphs 15 and 19 of Accounting Standard. Dealing with the above said Accounting Standard-5, the Delhi High Court pointed out that the income or expenses relating to prior period items, merit to be included in the determination of net profit or loss. It reasoned out that both the prior period items and extraordinary items are to be included in the determination of the net profit or loss and as per

paragraphs 15 of the AS 5, that prior period items should be separately disclosed in the statement of profit and loss and held as follows:-

"..... Two approaches have been indicated in paragraph 19 of the said Accounting Standard (AS 5). The normal approach is to include prior period items in the determination of net profit or loss for the current period. The alternative approach is to show such items in the statement of profit and loss after determination of current net profit or loss. As indicated in the accounting standard, in either case, the objective is to indicate the effect of such items on the current profit or loss."

14. Thus, the Delhi High Court held that whether the prior period expenses were shown separately or not, the assessee would nevertheless be entitled to have the adjustment of the prior period expenses in the matter of computing the net profit of the assessee. Thus on mere fact that the assessee had shown its prior period expenses in the extra ordinary items separately, did not mean the net profit was arrived at de hors these items. The Delhi High Court further pointed out that the assessee had not claimed any deduction with the net profit on the basis of any clauses given in the *Explanation* to Section 115JA(2). Consequently, the question was answered in favour of the assessee. We are in agreement with the view expressed by the Delhi High Court and we do not have any hesitation in applying the said decision to the case before us.

15. It is relevant to note herein that the said decision rendered by the Delhi High Court was considered by this Court in the decision in *CIT v. Swamiji Mills Ltd.* [2012] 342 ITR 250 (Mad.), wherein in preference to the decision of the Delhi High Court in *Khaitan Chemicals & Fertilizers Ltd. (supra)*, this Court applied the decision of the Kerala High Court in *Sree Bhagawathy Textiles Ltd. v. Asstt. CIT* [2012] 342 ITR 244 (Ker.), on the facts available that it was more about appropriation account. In considering the nature of the expenses charged on the appropriation account, this Court held that the assessee was not entitled to have the deduction of amounts debited in the profit and loss appropriation account in the computation of the net profit. As such, the decision of this Court *Swamiji Mills Ltd. (supra)* has no application to the facts of the case herein and it is totally distinguishable.

16. Thus, going by the decision of the Apex Court in *Apollo Tyres Ltd. (supra)* and applying the facts thus found that in computing the net profit the assessee had adjusted prior period expenses, rightly, the assessee offered the book profit for assessment. No exception could be taken to the course adopted by the assessee in adjusting the prior period expenses in computing the net profit. In the light of the law declared by the Apex Court as to the jurisdiction of the officer in respect of the matter of MAT assessment, we have no hesitation in holding that once the officer accepts the book profit, he cannot travel beyond what had been disclosed in the book profit. In the matter of granting adjustment to the prior period expenses, we have no hesitation in applying the decision of the Delhi High Court in *Khaitan Chemicals & Fertilizers Ltd. (supra)* thereby set aside the order of the Tribunal and allowed the Tax Case Appeal and answered the substantial question of law in favour of the assessee. No costs.