CORPORATE TAX PLANNING

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Himalaya Publishing House
ISO 9001 : 2008 CERTIFIED
Offered at the lotus feet of Reverend Mother Ma Indira Devi

Jai Guru

PRADIP
PREFACE

The topics in the text are covered from the perspective of a person who wishes to learn about the corporate tax planning of a growth oriented business. However, it is important that managers also understand corporate tax planning developments on an overall macroeconomic level. Such an understanding enables managers to anticipate economic changes and adjust to what they expect to occur. Of late, the international financial developments that are happening are nothing short of spectacular. For example, new markets and instruments are emerging at a frantic pace that at times has been so volatile, that they grab headlines in the financial news. Great fortunes have been made and lost due to the compounded complexities of the taxation laws. It is therefore necessary that these are understood and advance tax planning is adopted.

It is also heartening and encouraging to note that Utkal University, Sambalpur, Bhubaneswar and Ravenshaw University have included Corporate Tax Planning in their B.Com. (Hons.) curriculum.

The book is divided into five units covering certain terms, Corporate Tax Planning concepts and various tax planning devices, which will have impact on decision making.

An introduction to the structure of the Corporate Tax Planning, meaning, objectives, types and factors on which Tax Planning is done is covered in Unit 1. The unit also covers Corporate Tax in India including types of companies, residential status of companies, tax incidence, tax liability and minimum alternate tax and additional tax on distributed profits.

Unit 2 explains Tax Planning with reference to: (i) Setting up new business — locational aspect, nature of business, form of organization; (ii) Financial Management decisions and (iii) Sale of scientific research assets.

Tax Planning with reference to: (i) managerial decisions such as buying out of borrowed funds or from own funds, purchase vs. leasing/hire, make or buy, repairs/renewal/renovation, etc., (ii) employees’ remuneration, (iii) receipt of insurance compensation and (iv) distribution of assets at the time of liquidation, are covered in Unit 3.

Unit 4 deals with Tax liability in respect of non-residents, relief for double taxation, computation of arms length prices in case of international transactions and Advance Ruling and Advance Pricing agreements.

Unit 5 explains the following in connection with business restructuring: (i) tax provisions relating to amalgamation, demerger, slump sale of companies, (ii) conversion of sole proprietary concern/partnership firm into company, and (iii) conversion of company into LLP and (iv) transfer of assets between holding company and subsidiary company so that relevant concessions can be availed through proper tax planning.

I would like to express my sincere thanks to Himalaya Publishing House Pvt. Ltd. and their staff for the encouragement and help in bringing out this publication.

Finally, I am grateful to my wife Shukla and children Pritish and Sanchari for their untiring support and patience without which the publication of this book would not be possible.

Comments from the readers are welcome.

Dr. PRADIP KUMAR SINHA
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UNIT 1
INTRODUCTION TO CORPORATE TAX PLANNING

OBJECTIVES

Reading this chapter would enable you to understand —

- the meaning of tax planning and how it is different from tax evasion, tax management and tax avoidance
- corporate tax in India including types of companies, residential status of companies, tax incidence, tax liability and minimum alternate tax and additional tax on distributed profits

STRUCTURE

1.1 Introduction to Corporate Tax Planning
1.2 Meaning of Tax Planning
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1.1 INTRODUCTION TO CORPORATE TAX PLANNING

The practical concept of taxation laws is to realize the revenue by way of tax to the maximum. Therefore, the perception of tax payer (including company) and tax collector are different. The tax payer spares no efforts in maximizing his profits and attracting the least incidence of tax. The tax collector, on the other hand, tries to maximize revenue within the framework of law. It is here that tax planning has assumed far reaching importance in the complexities of the taxation laws.

The Indian Income Tax law is a highly complicated piece of legislation. Hence knowledge about its key features is useful for business managers and others because under the law, a taxpayer is legitimately entitled to plan his taxes in such a manner that his tax liability is minimal and net income from the business and other sources is maximum.
1.2 MEANING OF TAX PLANNING

Tax Planning is the arrangement of financial activities in such a way that maximum tax benefits are enjoyed by making use of all beneficial provisions in the tax laws. It entitles the assessee to avail certain exemptions, deductions, rebates and reliefs, so as to minimise its tax liability.

1.3 OBJECTIVES OF TAX PLANNING

The primary objectives of tax planning are as follows:

(i) **Reduction of tax liability:** One of the supreme objectives of tax planning is the reduction of the tax liability of the payer and the resultant saving of the earnings for a better enjoyment of the fruits of hard labour. By usage proper tax planning, a tax payer can oblige the administrators of the taxation laws to keep their hands off from his earnings.

(ii) Minimization of litigation and the tax payer may be saved from the hardships and inconveniences caused by unnecessary litigations.

(iii) **Productive investment:** Tax planning is a measure of awareness of the taxpayer to the intricacies of the taxation laws and it is the economic consciousness of the income earner to find out the ways and means of productive investment of the earnings which would go a long way to minimize its tax burden.

(iv) **Healthy growth of economy:** The saving of earnings is the only basement upon which the economic structure of human life is founded.

(v) **Economic stability:** Productive investment increase contours of the national economy embracing in itself the economic prosperity of not only the tax payers but also of those who earn the income not chargeable to tax. The planning thus creates economic stability of the nation and its people by even distribution of economic resources.

1.4 TYPES OF TAX PLANNING

Tax planning can be divided into two heads:

(a) Short term planning is normally for a period up to a year and it is done from year to year to achieve some particular objective.

(b) Long term planning is for a longer period and it may not pay immediately.

1.5 FACTORS ON THE BASIS OF WHICH TAX PLANNING IS DONE

The following factors are essential for effective tax planning:

(i) **Residential status and citizenship of the assessee:** We know that a non-resident in India is not liable to pay income-tax on incomes which accrue or arise and are also received outside India, whereas a resident in India is liable to pay income-tax on such incomes. Therefore, every assessee would like to be a non-resident in India, if he has any income which accrues or arises outside India.
(ii) **Heads of income/assets to be included in computing net wealth:** Before the Tax-planner goes in for his task; he has to have a full picture of the sources of Income of the tax payer and the members of his family. Though total income includes all income from whatever source derived, the scope of tax planning is not similar in respect of all sources of income. The assessee can avail the benefits of exemption and deductions under each head of income. Further he can avail the benefit of rebate and relief under the Act.

(iii) **Latest legal position:** It is the foremost duty of a tax-planner to keep him fully conversant with the latest position of the taxation laws along with the allied laws and also the judicial pronouncements in respect thereof. For this purpose he must have a thorough and up-to-date understanding of the annual finance Acts, the Taxation Laws Amendments, the amendments, if any, of the allied laws, the latest judicial pronouncements of the High Courts and the Supreme Court, various Circulars of the Central Board of Direct Taxes which seek to clarify the legal position in so far as the Revenue is concerned.

(iv) **Form vs Substance:** A tax planner has to bear in mind the following principles enunciated by the courts on the question whether form or substance of a transaction should prevail in Income-tax matters.

(a) **Form of transaction:** When a transaction is arranged in one form known to law, it will attract tax liability while, if it is entered into another form which is equally lawful, it may not.

(b) **Genuineness of transaction:** In deciding whether the transaction is a genuine or colourable one because in such a situation, it is not the question of form and substance but of appearance and truth. It will be open to the authorities to pierce the corporate veil and look behind the legal facade, at the reality of the transaction.

(c) **Expenditure:** In the case of expenditure, the mere fact that the payment is made under an agreement does not preclude the department from enquiring into the actual nature of the payment.

1.6. **METHODS COMMONLY USED BY COMPANIES TO MINIMISE TAX LIABILITY**

The following three methods are commonly used to reduce taxes:

1. Tax evasion
2. Tax avoidance
3. Tax planning

**Tax Evasion**

Some of the methods used to evade/reduce tax liability are:

(a) Concealment of income
(b) Inflation of expenses to suppress profits
(c) Falsification of accounts
(d) Conscious violation of rules
Tax evasion is sheer non-payment of tax even when it is due to be paid in the circumstances of the case. Tax Evasion is illegal and can result into penalties and prosecution for the perpetrator. When financial transactions are arranged in a way that it becomes obvious that they were entered with a malafide intention of either not paying taxes or with a view to defeat the genuine spirit of law, they cannot be accepted. Twisting of facts or taking a very strict and literal interpretation of law without understanding the basic purpose of the law can only lead to punishable offence.

**Tax Avoidance**

Tax avoidance is minimising the incidence of tax by adjusting the affairs in such a manner that although within the four corners of the taxation laws, the advantage is taken by finding out loopholes in the laws.

As to the ethics of Taxation, the learned judge in McDowell & Co. Ltd. vs. CTO (1985) 154 ITR 148(SC) at page 160, observed: “We now live in a welfare State whose financial needs, if backed by the law, have to be respected and met. We must recognise that there is behind taxation laws as much moral sanction as behind any other welfare legislation and it is pretence to say that avoidance of taxation is not unethical and that it stands on no less moral plane than honest payment of taxation.”

### 1.7 TAX PLANNING AND TAX EVASION

Tax Planning thus can be defined as an arrangement of the financial affairs within the scope of law in a manner that derives maximum benefit of the exemptions, deductions, rebates and relief and reduces tax liability to the minimal. As long as one is within the framework of law, one can plan financial affairs in such manner which keeps tax liability at its minimum. However, in the name of tax planning, one should not indulge in Tax Evasion, and the line between Tax Planning and Tax Avoidance is very thin, so one needs to tread carefully. Tax evasion is sheer non-payment of tax even when it is due to be paid in the circumstances of the case. It should be remembered that while tax planning is perfectly legal, Tax Evasion is illegal and can result in penalties and prosecution for the perpetrator. When financial transactions are arranged in a way that it becomes obvious that they were entered with a malafide intention of either not paying taxes or with a

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<tr>
<th><strong>Tax Planning</strong></th>
<th><strong>Tax Evasion</strong></th>
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<tr>
<td>1. Tax planning is an act within the permissible range of the Act conducted to achieve social and economic benefits.</td>
<td>1. Tax evasion is an attempt to avoid tax by misrepresentation of facts and falsification of accounts.</td>
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<tr>
<td>2. Tax planning is a legal right which enables the tax payer to achieve social and economic objectives.</td>
<td>2. Tax evasion is a legal offence which may lead to penalty and prosecution.</td>
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<td>3. Tax planning accelerates development of the economy of a country by generating funds for investment in desired sectors.</td>
<td>3. Tax evasion retards the development of economy of a country by generating black money which works as a parallel economy.</td>
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<tr>
<td>4. Tax planning promotes professionalism and strengthens economic and political situation of the country.</td>
<td>4. Tax evasion encourages bribery and weakens economic and political situation of the country.</td>
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view to defeat the genuine spirit of law, they cannot be accepted as legitimate Tax Planning. Twisting of facts or taking a very strict and literal interpretation of law without understanding the basic purpose of the law can only lead to punishable offence.

1.8 TAX AVOIDANCE AND NOT TAX PLANNING

Tax Avoidance

Tax avoidance is minimising the incidence of tax by adjusting the affairs in such a manner that although within the four corners of the taxation laws, the advantage is taken by finding out loopholes in the laws.

In the words of Justice O. Chinnappa Reddy of Supreme Court in McDowell &Co. Ltd. vs. CTO (1985) 154 ITR 148(SC) at page 160, the evil consequences of Tax Avoidance are manifold and can be summarised as follows —

(a) Substantial loss of much needed public revenue, particularly a welfare state like ours.
(b) Serious disturbance caused to the economy of the country by piling up of black money directly causing inflation.
(c) Large hidden loss to the community by some of the best brains in the country being involved in the perpetual war waged between tax avoider and his expert team of advisers, lawyers, and accountants on one side, and the Tax adviser and his perhaps not so skillful advisers on the other side.
(d) Sense of injustice and inequality which tax avoidance arouses in the breasts of those who are unwilling or unable to profit by it.
(e) Ethics (or lack of it) of transferring the burden of tax liability to the shoulders of guideless, good citizens from those of artful dodgers.

Tax Management: Tax Management refers to the compliance with the statutory provisions of law. While tax planning is optional, tax management is mandatory. It includes maintenance of accounts, filing of return, payment of taxes, deduction of tax at source, timely payment of advance tax, etc. Poor tax management may lead to levy of interest, penalty, prosecution, etc. In some cases it may lead to heavy financial loss if proper compliance is not made, e.g., if a loss return is not filed in time it will result in a financial loss which will not be allowed to be carried forward.

**Difference between Tax Avoidance and Tax Evasion**

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<td>1. Tax avoidance means planning for minimisation of tax according to legal requirements but it defeats the basic intention of the legislature.</td>
<td>1. Tax evasion means avoiding of tax liability illegally.</td>
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<tr>
<td>2. Tax avoidance takes into account various lacunas of law.</td>
<td>2. Tax evasion involves use of unfair means.</td>
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<td>3. Tax avoidance is lawful but involves the elements of mala fide intention.</td>
<td>3. Tax evasion is unlawful.</td>
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<td>4. Tax avoidance is planning before the actual liability for tax comes into existence.</td>
<td>4. Tax evasion involves avoidance of payment of tax after the liability of tax has arisen.</td>
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1.9 TAX PLANNING AND TAX MANAGEMENT

**Tax Management:** Tax Management refers to the compliance with the statutory provisions of law. While tax planning is optional, tax management is mandatory. It includes maintenance of accounts, filing of return, payment of taxes, deduction of tax at source, timely payment of advance tax, etc. Poor tax management may lead to levy of interest, penalty, prosecution, etc. In some cases it may lead to heavy financial loss if proper compliance is not made, e.g., if a loss return is not filed in time it will result in a financial loss which will not be allowed to be carried forward.

### Difference between Tax Planning and Tax Management

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<tr>
<td>1. Tax planning is a wider term and includes tax management.</td>
<td>1. Tax management is a narrower term and is first term towards tax planning.</td>
</tr>
<tr>
<td>2. Tax planning emphasizes on minimisation of tax burden.</td>
<td>2. Tax management emphasis the compliance of legal formalities for minimisation of tax.</td>
</tr>
<tr>
<td>3. Every person may not require tax planning.</td>
<td>3. Tax management is essential for every person.</td>
</tr>
<tr>
<td>4. Tax planning helps in decision making.</td>
<td>4. Tax management helps in complying with the conditions for effective decision making.</td>
</tr>
<tr>
<td>5. Tax planning helps to claim various benefits of tax.</td>
<td>5. Tax management helps in complying the conditions for claiming tax benefits</td>
</tr>
<tr>
<td>6. Tax planning involves comparison of various alternatives before selecting the best one.</td>
<td>6. Tax management involves maintenance of accounts in prescribed form, filing of returns, payment of taxes, etc.</td>
</tr>
<tr>
<td>7. Tax planning looks at future benefits.</td>
<td>7. Tax management relates to the past, present and future.</td>
</tr>
</tbody>
</table>

1.10 INTRODUCTION AND DEFINITION OF COMPANIES

A company has been defined as, *'a juristic person having an independent and separate legal entity from its shareholders’*. Income of the company is computed and assessed separately in the hands of the company. The company is liable to pay tax at a flat rate like a firm. If any amount is distributed or paid by the company as dividend to the shareholders, the company shall be liable to pay tax on such dividends distributed or paid including a surcharge, as applicable. However, the shareholder shall not be liable to pay Income Tax on such dividends.

### 1.10.1 Types of Companies

1. **Company:** As per Section 2(17), of the Income Tax Act, a company means:
   - (i) any Indian company, or
   - (ii) any body, corporate/incorporated by/under the laws of a country outside India, or
   - (iii) any institution, association or body which was assessed as a company for any assessment year under the Income tax Act, 1922 or was assessed under this act as a company for any assessment year commencing on or before 1.4.1970, or
(iv) any institution, association or body, whether incorporated or not and whether Indian or non-Indian, which is declared by a general or special order of the CBDT to be a company.

2. A company in which the public is substantially interested: Section 2(18) of the Income Tax Act has defined a company in which the public is substantially interested to include:

(i) A company owned by the Government or the Reserve Bank of India.

(ii) A company having Government participation, i.e., a company in which not less than 40% of the shares are held by the Government or the RBI or a corporation owned by the RBI.

(iii) Companies registered under Section 25 of the Indian Companies Act, 1956: Companies registered under Section 25 of the Companies Act, 1956 are companies which are promoted with the special object, such as to promote commerce, art, science, charity or religion or any such useful object and these companies do not have a profit motive. However, if at any time these companies declare dividend, they would lose the status of a company in which the public is substantially interested.

(iv) A company declared by the CBDT: It is a company without share capital and which, having regard to its object, nature and composition of its membership or other relevant consideration is declared by the board to be a company in which the public is substantially interested.

(v) Mutual Benefit Finance Company, where the principal business of the company is acceptance of deposits from its members and which has been declared by the Central Government to be a Nidhi or a Mutual Benefit Society.

(vi) A company having cooperative society participation: It is a company in which at least 50% or more equity shares have been held by one or more of the cooperative societies.

(vii) A Public Limited company: A company is deemed to be a public limited company if it is not a private company as defined by the Companies Act, 1956 and is fulfilling either of the following two conditions:

(a) Its equity shares were listed on a recognised stock exchange, as on the last day of the relevant previous year; or

(b) Its equity shares carrying at least 50% of the voting power (in the case of an industrial company the limit is 40%) were beneficially held throughout the relevant previous year by the Government, a statutory corporation, a company in which the public is substantially interested or a wholly owned subsidiary of such a company.

An industrial company means a company whose business consists mainly of the construction of ships or the manufacturing or processing of goods or in mining or in the generation or distribution of electricity or any other form of power.

3. Widely held company: It is a company in which the public is substantially interested.

4. Closely held company: It is a company in which the public is not substantially interested.

5. Indian company [Section 2(26)]: An Indian Company means a company formed and registered under the Companies Act, 1956 and includes:
(i) a company formed and registered under any law relating to the companies formerly in force in any part of India (other than the State of Jammu and Kashmir and the Union Territories):
   (a) a corporation established by or under a Central, State or Provincial Act;
   (b) any institution, association or body which is declared by the Board to be a company;
(ii) in the case of the state of Jammu and Kashmir, a company formed and registered under any law for the time being in force in that state;
(iii) in the case of any of the Union Territories of Dadra and Nagar Haveli, Goa, Daman and Diu and Pondicherry, a company formed and registered under any law for the time being in force in that Union Territory.

Provided that the registered or as the case may be, the principal office of the company, corporation, institution, association or body, in all cases is in India.

6. Domestic Company [Section 2(22A)]: A domestic company means an Indian company or any other company which in respect of its income, liable to tax under the Income Tax Act, has made the prescribed arrangements for the declaration and payment within India, of the dividends (including dividends on preference shares) payable out of such an income.

7. Foreign Company [Section 2 (23A)]: Foreign Company means a company which is not a domestic company.

8. Investment Company: Investment Company means a company whose gross total income consists mainly of income which is chargeable under the heads ‘Income from House Property’, ‘Capital Gains’ and ‘Income from Other Sources’.

1.10.2 Residence of a Company [Section 6(3)]

A company is said to be a resident in India during the relevant previous year if: (a) it is an Indian company, or (b) if it is not an Indian company then, the control and the management of its affairs is situated wholly in India.

The company is said to be non-resident in India, if it is not an Indian company and some part of the control and management of its affairs is situated outside India.

Thus the residential status of a company can be either resident or non-resident.

1.10.3 Scope of Total Income and Incidence of Tax

The following table indicates the tax incidence on income in different situations depending on the residential status of the corporate assessee
Table 1.1: Income Tax in Different Situations

<table>
<thead>
<tr>
<th>Place of Income</th>
<th>Resident</th>
<th>Non-resident</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income received or deemed to be received in India whether earned in India or elsewhere.</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Income accruing or arising in India whether received in India or elsewhere.</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Income deemed to accrue or arise in India whether received in India or elsewhere.</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Income received / accrued outside India from a business controlled from India.</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>Income which accrues or arises outside India and received from outside India from any other source.</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>Income which accrues or arises outside India and received outside India during the years preceding the previous year and remitted to India during previous year.</td>
<td>No</td>
<td>No</td>
</tr>
</tbody>
</table>

The term ‘business connection’ has been explained below.

Section 9(1)(i):

**Income from Business Connection:** The Income Tax Act does not define the term ‘business connection’. A business connection involves a relation between a business carried on by a non-resident that yields profits and gains and some activity in India which contributes directly or indirectly to the earning of those profits and gains. It implies an intimate relation between trading activity carried on outside India and trading activity within India and such relation is contributing to the earning of profit by non-residents. To illustrate the term ‘business connection’, following are some instances:

1. Maintaining a branch office, factory, agency receivership or management for the purchase and sale of goods or transacting any other business.
2. Appointing an agent in India for the systematic and regular purchase of raw materials or other commodities or for sale of the non-resident’s goods for business purposes or for securing orders in India.
3. Erecting a factory in India where the raw products purchased locally is worked into a form suitable for export abroad.
4. Forming a local subsidiary company to sell the products of the non-resident parent company.
5. Having financial association between a resident and non-resident company.
6. Granting a continuing license to a resident to exploit for profit an asset belonging to a non-resident even if the transaction might be disguised as out and out sale.

In B.P. Ray vs. ITO, the Supreme Court held that the expression ‘business connection’ u/s 9(1)(i) would refer to ‘Professional Connection’ also.
Exception to Section 9(1)(i):

In the case of a non-resident, no income shall be deemed to accrue/arise in India in the following situations:

1. Where the business connection is confined only to the purchase of goods in India for the purpose of exports. (This exception is made to encourage exports).
2. Where the business connection is confined only to collection of news and views in India for transmission out of India.
3. Where the business connection is confined to the shooting of any cinematography firm in India. (This exception is also available to a firm and company which does not have any partner/shareholder who is a citizen of India or who is resident in India).
4. Where all operations of a business are not carried out in India, the extent of income of the business relating to operations not carried out in India.

1.10.4 Computation of Total Income of a Company

The total income of a company is also computed in the manner in which income of any other assessee is computed.

The first and the foremost step in this direction is to ascertain Gross Total Income.

**Gross Total Income:** As per Section 14, income of a person is computed under the following five heads:

1. Salaries
2. Income from house property
3. Profits and gains of business or profession
4. Capital gains
5. Income from other sources

The aggregate income under these heads is termed as “gross total income”. In other words, gross total income means total income computed in accordance with the provisions of the Act before making any deduction under Chapter VIA. (Section 80C to 80U)

Further Section 14 A provides that no deduction shall be made in respect of expenditure incurred by the assessee in relation to income which does not form part of the total income under the Act.

**How to compute total income:** The steps in which the total income for any assessment year is determined as follows:

1. Determine the residential status of the assessee to find out which income is to be included in the computation of his total income
2. Classify the income under each of the following five heads. Compute the income under each head after allowing deductions prescribed for each head of income:
(a) Income from salaries
Salary/Bonus/Commission, etc. __________
Taxable Allowance __________
Value of Taxable perquisites __________
Gross salary __________
Less: Deductions u/s 16 __________
Net taxable income from salary __________

(b) Income from House Property
Net annual value of house property __________
Less: Deduction under section 24 __________
Income from house property __________

(c) Profits & gains of business & profession
Net profit as per P&L A/c __________
Less/Add: Adjustments required to be made to the profit as per provisions of Income tax Act __________
Net profit and gains of business & Profession __________

(d) Capital gains
Capital gains as computed __________
Less: exemptions u/s 54/54B/54D etc. __________
Income from capital gain __________

(e) Income from other sources:
Gross income __________
Less: Deductions __________
Net income from other sources __________

Gross Total Income [(a) + (b) + (c) + (d) + (e)] __________
Less: Deductions available under chapter VIA Sections 80 C to 80 U) __________

Total Income __________

Income computed under four heads (salary head is not applicable), is aggregated. While aggregating the income, section 60 and 61 shall be applicable. Further, effect to set off of losses and adjustment for brought forward losses will also be done. From the gross total income so computed, the following deductions of Chapter VIA should be allowed:

80G Donations to certain funds/charitable institutions, etc.
80GGA Certain donations for scientific research or rural development
80GGB Contribution to political parties
80IA Profits and gains of new industrial undertakings or enterprises engaged in infrastructural development, etc.
80IAB Deductions in respect of profits and gains by an undertakings or enterprises engaged in development of Special Economic Zone
80IAC Profits and gains derived from eligible start-up
80IB Profits gains from certain industrial undertakings other than infrastructure development undertakings
### INTRODUCTION TO CORPORATE TAX PLANNING

- **80IC** Deductions in respect of certain undertakings or enterprises in certain special category states
- **80ID** Deduction in respect of profits and gains from business of hotels and convention centres in specified area
- **80IE** Deduction in respect of certain undertakings in North Eastern States
- **80JJA** Deduction in respect of profits and gains from business of collecting and processing of bio-degradable waste
- **80JJAA** Deduction in respect of employment of new workmen
- **80LA** Deductions in respect of certain incomes of Offshore Banking Units and International Financial Services Centre

The resulting sum is net income.

### 1.10.5 Computation of Tax Liability of a Company

Tax liability of a company is calculated as follows:

<table>
<thead>
<tr>
<th>Computation 1 — Under normal provisions</th>
<th>Computation 2 — Under minimum alternate tax</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Step 1</strong> Find out taxable income under normal provisions</td>
<td><strong>Step 8</strong> Find out book profits</td>
</tr>
<tr>
<td><strong>Step 2</strong> Find out income-tax at the rate of 30% per cent (40 per cent in case of foreign company) of income computed under (1). There is no exemption limit.</td>
<td><strong>Step 9</strong> Find out 18.5 per cent of book profit</td>
</tr>
<tr>
<td><strong>Step 3</strong> Add Surcharge</td>
<td><strong>Step 10</strong> Add surcharge</td>
</tr>
<tr>
<td><strong>Step 4</strong> Find out (2) + (3)</td>
<td><strong>Step 11</strong> Find out (9) + (10)</td>
</tr>
<tr>
<td><strong>Step 5</strong> Add education cess at the rate of 2% on (4) and secondary and higher education cess at the rate of 1 per cent of (4)</td>
<td><strong>Step 12</strong> Add education cess at the rate of 2% on (4) and secondary and higher education cess at the rate of 1 per cent of (11)</td>
</tr>
<tr>
<td><strong>Step 6</strong> Deduct tax rebate or tax credit under sections 86, 90, 90A and 91</td>
<td><strong>Step 13</strong> Find out (11) + (12)</td>
</tr>
<tr>
<td><strong>Step 7</strong> Find out (4) + (5) – (6)[ it cannot be less than zero]</td>
<td></td>
</tr>
</tbody>
</table>

Tax Liability of a company is (7) or (13) whichever is more.

### 1.10.6 Tax on the income received from Venture Capital Companies/Venture Capital Funds [Section 115U and Rule 12C]

1. Notwithstanding anything contained in any other provisions of this Act, any income received by a person out of investments made in a venture capital company or venture capital fund shall be chargeable to income tax in the same manner as if it were the income received by such person had he made investments directly in the venture capital undertaking.

2. The person responsible for making payment of the income on behalf of a venture capital company or a venture capital fund and the venture capital company or venture capital fund shall furnish, by 30th November of the Financial Year following the previous year
during which such income is distributed, to the person receiving such income and to the jurisdictional Chief Commissioner/Commissioner, a statement in Form No. 64 and duly verified by an accountant in the manner indicated therein, giving details of the nature of income paid during the previous year and such other relevant details as may be prescribed.

3. The income paid by the venture capital company and the venture capital fund shall be deemed to be of the same nature and in the same proportion in the hands of the person receiving such income as it had been received by, or had accrued to, the venture capital company or the venture capital fund, as the case may be, during the previous year.

4. The provisions of Chapter XII D (relating to dividend distributed by domestic companies or chapter XIIE (relating to TDS) or chapter XVII-B shall not apply to the income paid by a venture capital company or venture capital fund.

**Important Points**

(a) “Venture capital company” means such company —
   (i) which has been granted a certificate of registration under the Securities and Exchange Board of India Act, 1992 and regulations made hereunder;
   (ii) which fulfills the conditions as may be specified, with the approval of the Central Government, by the Securities and Exchange Board of India, by notification in the Official Gazette, in this behalf;

(b) “Venture capital fund” means such fund —
   (i) operating under a trust deed registered under the provisions of the Registration Act, 1908;
   (ii) which has been granted a certificate of registration under the Securities and Exchange Board of India Act 1992, and regulations made hereunder;
   (iii) which fulfills the conditions as may be specified, with the approval of the Central Government, by the Securities and Exchange Board of India, by notification in the Official Gazette, in this behalf; and

(c) “Venture capital undertaking” means a domestic company —
   (i) whose shares are not listed in a recognized stock exchange in India;
   (ii) which is engaged in the business for providing services, production or manufacture of an article or thing but does not include such activities or sectors which are specified, with the approval of the Central Government, by the Securities and Exchange Board of India, by notification in the Official Gazette, in this behalf.

**1.10.7 Carry Forward and Set Off of Losses in Case of Certain Companies (Section 79)**

In the case of closely held companies, no loss incurred in any year prior to the previous year shall be carried forward and set off against the income of the previous year unless on the last day of the previous year in which loss is set off and on the last day of the previous year in which the loss was incurred, the shares of the company carrying not less than 51% of the voting power were beneficially held by the same persons.
Where a change in voting power of more than 49% of the shareholding of a closely held company has taken place between two relevant dates (viz., the last day of the previous year in which set off is claimed and the last date of the previous year in which the loss is incurred) the assessee will not be entitled to claim set off of such losses.

This provision shall not apply to a change in the voting power consequent upon:

(a) the death of a shareholder, or
(b) on account of transfer of shares by way of gifts to any relative of the shareholder making such gift.

Further, section 79 shall not apply to any change in the shareholding of an Indian company, which is subsidiary of a foreign company arising as a result of amalgamating or demerged foreign company continue to remain the shareholders of the amalgamated or the resulting foreign company.

Section 79 applies to all losses, including losses under the head Capital gains. However, overriding provisions of section 79 do not affect the set off of unabsorbed depreciation which is governed by section 32(2). [CIT v. Concord Industries Ltd. (1979) 119 ITR 458 (Mad)].

1.10.8 Company Assessment Procedure

The principal officer of the company is required to file the return of total income of the company on or before 31st October of the assessment year. A company is assessed like any other assessee. However, its liability differs in two respects:

1. No exemption limit: A company does not enjoy any exemption limit.
2. Flat Rate of Tax: A company pays income tax at a flat rate instead of slab rate.

1.10.9 Rates of Income Tax

The rates of tax which applicable to companies for the assessment year 2017-18 are as under:

1. Short-term capital gains on equity shares in a company or units of an equity oriented fund where the transaction is chargeable to securities transaction tax 15%
2. Tax on long-term capital gains 20%
3. Dividend received by a foreign company or non-resident non-corporate assessee (it is not applicable in the case of dividends referred to in Section 115-0) 20%
4. Interest received by a foreign company or non-resident non-corporate assessee from Government or an Indian concern on money’s borrowed or debt incurred by Government or the Indian concern in foreign currency 20%
5. Royalty or fees for technical services received by a foreign company or non-resident non-corporate assessee from an Indian concern or Govt. in pursuance of an agreement approved by the Central Government and made after March 31, 1976 10%
6 Tax on any other income
   (a) Domestic company 30%
   (b) Foreign company
      (i) Royalty received from Government or an Indian concern in pursuance of an agreement made by it with the Indian concern after March 31, 1961 but before April 1, 1976 or fees for rendering technical services concern in pursuance of an agreement made by it with the Indian concern after February 29, 1964 but before April 1, 1976 and where such agreement has in either case, been approved by the Central Government 50%
      (ii) Other income: 40%

Surcharge for AY 2017-18

<table>
<thead>
<tr>
<th></th>
<th>If net income does not exceed ₹ 1 crore</th>
<th>If net income is in the range of ₹ 1 crore to ₹ 10 crore</th>
<th>If net income exceeds ₹ 10 crore</th>
</tr>
</thead>
<tbody>
<tr>
<td>Domestic Company</td>
<td>Nil</td>
<td>7%</td>
<td>12%</td>
</tr>
<tr>
<td>Foreign company</td>
<td>Nil</td>
<td>2%</td>
<td>5%</td>
</tr>
</tbody>
</table>

Education cess of 2% and Secondary and higher education cess of 1% is applicable on the amount of total tax.

1.11 DEEMED INCOME RELATING TO CERTAIN COMPANIES – ALSO KNOWN AS MINIMUM ALTERNATIVE TAX (MAT)

1.11.1 Provisions of MAT for payment of tax by certain companies [Section 115JB(1)]

Tax payable for assessment year (2011-12) cannot be less than 18.5% of book profit (plus Surcharge plus EC plus SHEC as applicable). Where in the case of a company, the income tax payable on the total income as computed under the Income Tax Act in respect of the previous year, is less than 18.5% of its book profit, such book profit shall be deemed to be the total income of the assessee and the tax payable by the assessee on such total income (book-profit) shall be the amount of the income tax at the rate of 18.5%.

Example:

Suppose the book profits a company for the assessment year 2017-18 are ₹ 10,00,000 whereas its total income as per provision of income tax is ₹ 3,00,000, then the tax shall be payable as under:

1. Tax on total income as computed from Income Tax Act 30% of ₹ 3,00,000 90,000
2. Tax @ 18.5% on book profit of ₹ 10,00,000 1,85,000
In the above case, tax payable on total income, i.e., ₹ 90,000 is less than 18.5% of the book profits, i.e., ₹ 1,85,000. Hence in this case, deemed total income shall be ₹ 10,00,000 and the tax payable shall be ₹ 1,85,000 plus Education cess and SHEC @ 3% 5,550 = 190,550.

**Exceptions:** The provisions of MAT are not applicable in the following cases:

<table>
<thead>
<tr>
<th><strong>Nature of income</strong></th>
<th><strong>Time frame when MAT provisions are not applicable</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Income from any business/services in the hands of entrepreneur/developer in a special economic zone</td>
<td>Income arising after March 31, 2005 but after April 1, 2011</td>
</tr>
<tr>
<td>2. Income of a shipping company which is subject to the provisions of 'tonnage income'</td>
<td>Income arising after March 31, 2004 (i.e., assessment year 2005-06 onwards)</td>
</tr>
<tr>
<td>3. Income which accrues and arises to a company from life insurance business referred to in Section 115B</td>
<td>Income arising after March 31, 2000 (i.e., assessment year 2001-02 onwards)</td>
</tr>
</tbody>
</table>

**Foreign Company:** With effect from assessment year 2001-02, the provisions of Minimum Alternate Tax are not applicable to a foreign company in the following two cases:

- (a) the assessee is a resident of a country/specifies territory with which India has an agreement under section 90/90A and the assessee does not have a permanent a permanent establishment in India in accordance with the provisions of such agreement.
- (b) the assessee is a resident of a country with which India does not have an agreement referred to above and the assessee is not required to seek registration in India under any law from the time being in force relating to companies.

**1.11.2 Profit and loss of the company to be prepared as per provisions of the Companies Act [Section 115JB(2)]**

Every company shall for the purpose of this section, 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.

Profits and loss account prepared for Section 115JB(2) and annual accounts including profit and loss account prepared and placed before AGM should have same accounting policies, standards, etc. [Proviso 1 and 2 to section 115JB(2)]

While preparing the annual accounts including profit and loss account:

- (i) the accounting policies of the company;
- (ii) the accounting standards followed by the company for preparing such accounts including profit and loss account;
- (iii) the method and rates adopted for calculating the depreciation by the company,

shall be the same as have been adopted for the purpose of preparing such accounts including profit and loss account as laid before the company at its annual general meeting in accordance with the provisions of Section 210 of the Companies Act, 1956.
Further, where the company has adopted or adopts the financial year under the Companies Act, 1956, which is different from the previous year under the Income Tax Act, the above three (i.e., accounting policies, accounting standards and method of calculating depreciation) shall correspond to the accounting policies, accounting standards and the method and rates for calculating the depreciation which have been adopted for preparing such accounts including profit and loss account for such financial year or part of such financial year falling with the relevant previous year.

When an Assessing Officer has power to rework the net profit: In the following cases, the Assessing officer shall have power to rework or rewrite the profit and loss account:

1. Where the profit and loss account submitted is not as per Part II and Part III of the Schedule VI of the Companies Act.
2. Where the accounting policies or accounting standards or rate of depreciation adopted are different from those adopted for the profit and loss prepared for the annual general meeting.

Assessing Officer has no power to scrutinize profit and loss account: Where the profit and loss account has been prepared in accordance with Part II and Part III of the Schedule VI of the Companies Act and which has been scrutinised and certified by the statutory auditors and relevant authorities, the Assessing officer has no power to scrutinise net profit in profit and loss account except to the extent provided in Explanation to 115J

1.11.3 How to compute book profits [Explanation to 115JB(1) and (2)]

Step 1: The net profit as shown in the profit and loss account (prepared as per Part II and III of schedule VI) for the relevant previous year, shall be increased by the following, if debited to the Profit and Loss Account:

(a) The amount of income tax paid or payable, and the provision therefore; or
(b) The amounts carried to any reserves by whatever name called
(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 section 10, (other than the provisions contained in clause (38) relating to long-term capital gain on transfer of shares through a recognized stock exchange, 11 or 12 applies (i.e., incomes which are exempt from tax).
(g) The amount of depreciation.
(h) The amount of deferred tax and provisions therefore and the amount or amounts set aside as provision for diminution in the value of any asset
(j) The amount standing in revaluation reserve relating to revalued asset on the retirement or disposal of such asset.
(j) Notional capital gain or transfer of a share in a special purpose vehicle (SPV) to a business trust in exchange of units allotted by that trust and notional gain resulting from any change in carrying amount of such units [Section 47(xvii)]
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Notes:
1. The starting figure is the net profit after tax as per profit and loss account.
2. As per clause (a) above only income tax has to be added back. Hence, any tax, penalty or interest paid or payable under Wealth tax, gift tax, or any penalty or interest paid or payable under income tax, if debited to profit and loss account should not be added back to such net profits. Dividend tax paid or payable as per Section 115-O should be added back. Further no adjustment is to be done in respect of income-tax refund.
3. Where any amount has been transferred to reserve as per the provisions of Sec. 36(1)(viii), Sec. 80-IA(6), or 10(A)(1A) or 10AA the same is also to be added back.
4. Any tax or duty which is not allowed as deduction as per provisions of Section 43B though debited to profit and loss account shall also not to be added back.
5. Any provision made to meet unascertained liabilities like provisions of Gratuity provisions for future losses, etc. should be added back to such net profit. However, if the provisions for gratuity have been made on the basis of actuarial valuation, it becomes an ascertained liability and hence should not be added back.
6. Every kind of reserve is to be added to net profit to determine book profit
7. Dividend whether on equity or preference share paid or proposed should both be added.
8. Security Transaction Tax and Banking Cash Transaction Tax are not to be added back as these are not income tax.
9. Any expense other than mentioned in Clause (5) above should not be added back even if such expense is not allowable under the Income Tax Act.
10. Deferred tax liability as per Accounting standards is an unascertained Liability, hence to be added back.
11. Loss of subsidiary company, if debited to the profit and loss account, should be added back.
12. The provisions of Section 115JB shall not apply to the income accrued or arising on or after 1-4-2005 from any business carried on, or services rendered, by an entrepreneur or a Developer, in a Unit or Special Economic Zone as the case may be [Section 115JB(6)]

Step 2: The profit as per the Profit and Loss Account shall be reduced by the following:
(i) The amount withdrawn from any reserves or provisions, if any, such amount is credited to the profit and loss account:
A clarificatory amendment has been made by the Finance Act, 2002, i.e., assessment year 2001-02 to Section 115JB to provide that the amount withdrawn from the reserve or provision, created not out of profits before 1.4.1997, if credited to the profit and loss account, shall not be deducted while computing book profit.
Similarly, the amount withdrawn from the reserve created on or after 1.4.1997 and credited to the profit and loss account shall not be deducted while computing book profit unless the book profit in the year of creation of such reserve was increased by such reserve at that time.
(ii) The amount of income to which any of the provisions Section 10 (other than the income referred to in section 10(38), 11, 12 or 80-IAB applies, if any such amount is credited to the profit and loss account; or
(iii) The amount of depreciation debited to the profit and loss account (excluding the depreciation on account of revaluation of assets); or
(iv) The amount withdrawn from revaluation reserve and credited to profit and loss account, to the extent it does not exceed the amount of depreciation on account of revaluation of assets referred to in Clause (iii) above; or
(v) The amount of loss brought forward or unabsorbed depreciation, whichever is less as per books of account. The loss shall, however, not include depreciation. Further the provision of this clause shall not apply if the amount of brought forward loss or unabsorbed depreciation is Nil; or

(vi) The amount of profits of sick industrial company for the assessment year commencing from the assessment year relevant to the previous year in which the said company has become a sick industrial company under Sub-section (1) of Section 17 of the Sick Industrial Companies (Special Provisions) Act, 1985 and ending with the assessment year during which the entire net worth of such company becomes equal to or exceeds the accumulated losses.

For the purposes of this clause, net worth shall have the meaning assigned to it in Clause (ga) of Sub-section (1) of Section 3 of the Sick Industrial Companies (Special Provisions) Act, 1985. According to Section 3(1)(ga) of the Sick Industrial Companies (Special Protection) Act, 1985 net worth means the sum total of the paid up capital and free reserves.

“For free reserve” means all reserve credited out of the profits and share premium account but does not include reserves credited out of revaluation of assets, write back of depreciation provisions and amalgamations.

(vii) The amount of profit derived from the activities of a tonnage tax company [Sec. 115VO]

(viii) Amount of income/loss in the case of units referred to in Section 47(xvii).

The amount computed after increasing or decreasing the above in Step 1 and Step 2, respectively is known as book-profit.

1.11.4 How much brought forward loss/unabsorbed depreciation are deductible from book profits?

As per Clause (v) above, the amount of loss brought forward or unabsorbed depreciation as per books of accounts whichever is less is to be deducted from the book profits. It has been however clarified that loss however shall not include depreciation. In this case, brought forward loss and unabsorbed depreciation as per income tax shall have no relevance.

It has been clarified that where the value of the amount of either loss brought forward or unabsorbed depreciation is ‘nil’, no amount on account of such loss brought forward or unabsorbed depreciation would be reduced from the book profit.

1.11.5 Furnishing of Report of an Accountant [Section 115JB(4) and Rule 40B]

Every company to which this section applies, shall furnish a report in Form No. 29B from a chartered accountant certifying that the book profit has been computed in accordance with the provisions of this section along with the return of income filed under section 139(1) or along with the return of income furnished in response to a notice under Section 142(1)(i).

It may however, be noted that the company shall have to file such report even if it furnishes the return of income under Section 139(4) instead of Section 139(1) or in response to which notice Section 142(1)(i).
1.11.6 Unabsorbed Depreciation or Losses which can be carried forward [Section 115JB]

Computing book profit the amount of (a) loss brought forward (before depreciation) or (b) unabsorbed depreciation which ever is less (as per books of account) shall be reduced from net profit.

- Adjustment only when there is ‘unadjusted loss’ before depreciation as well as unabsorbed depreciation pertaining to earlier years.
- Consolidated loss and depreciation for early years in totality to be considered.
- Adjustment is required even if deduction is not permissible under the income-tax act.

1.11.7 Carry Forward and Set off of Tax Credit

The amount of tax credit (i.e., excess of step 13 over step 7) under section 115JAA shall be carried forward and set off subject to the following propositions —

1. No interest is payable in respect of tax credit.
2. Tax credit shall be allowed set off in a future year in which tax becomes payable on the total income computed in accordance with the provisions other than section 115JB.
3. Set off in respect of brought forward tax credit will be allowed for nay assessment year to the extent of —
   (a) tax computed on income under normal provision.
   (b) 18.5 per cent (plus surcharge + education cess) of book profit
4. Carry forward shall not be allowed beyond the period given below—

<table>
<thead>
<tr>
<th>Section assessment year</th>
<th>MAT paid in the following of MAT credit</th>
<th>Time limit for carry forward</th>
</tr>
</thead>
<tbody>
<tr>
<td>115JA</td>
<td>1997-98 to 2000-2001</td>
<td>5 years</td>
</tr>
<tr>
<td>115JB</td>
<td>2001-02 to 2005-06</td>
<td>Nil, i.e., no carry forward</td>
</tr>
<tr>
<td>115JB</td>
<td>2006-07 to 2017-18</td>
<td>10 years</td>
</tr>
</tbody>
</table>

1.11.8 Other provisions of the Act shall continue to apply to such companies [Section 115 JB(5)]:

Save as otherwise provided in section 115JB, all other provisions of the Income Tax Act shall apply to such companies. Hence, all other provisions relating to Advance tax, interest chargeable in certain cases shall apply to such companies also.

1.12 SPECIAL PROVISIONS RELATING TO TAX ON DISTRIBUTED PROFITS OF DOMESTIC COMPANIES

Tax on distributed profits of domestic companies [Section 115-0]: Domestic Company shall, in addition to the income-tax chargeable in respect of its total income, be liable to pay additional income-tax on any amount declared, distributed or paid by such company by way of dividend (whether interim or otherwise), whether out of current or accumulated profits. Such additional
income-tax shall be payable @15% plus surcharge @ 10% plus education cess @ 2% plus SHEC @1% of the amount so declared, distributed or paid.

**When the additional tax should be paid:** The tax on distributed profit shall be paid within 14 days from the date of —

(a) declaration of any dividend; or
(b) distribution of any dividend; or
(c) payment of any dividend.

whichever is the earliest

**Who is liable to pay tax** - The principal officer of the domestic company and the company shall be liable to pay the aforesaid tax

**Dividend received from subsidiary company to be reduced from the above dividend to be distributed [Section 115-O(IA)]**

Section 115-0(IA) provides a relief when a holding company has received dividend from its subsidiary company and in the same financial year the holding company declares dividends to its shareholders. When dividend is declared, distributed or paid by the holding company to its shareholders, dividend tax shall be payable on the following amount —

<table>
<thead>
<tr>
<th>Description</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dividend declared, distributed or paid by the holding company to its shareholders (a)</td>
<td>xxx</td>
</tr>
<tr>
<td>Less: dividend received by holding company from its subsidiary company in the same financial year (b)</td>
<td>xxx</td>
</tr>
<tr>
<td>Balance [i.e., (a) – (b)] on which dividend tax is payable by the holding company</td>
<td>xxx</td>
</tr>
</tbody>
</table>

The aforesaid relief is available only in the situation given below:

1. Subsidiary company is a domestic company and has paid tax under section 115-0 when dividend is paid to the holding company and holding company is not subsidiary of any other company (applicable from April, 2008 to June 30, 2012).
2. Subsidiary company is a domestic company and has paid tax under section 115-0 when dividend is paid to the holding company and holding company is not subsidiary of any other company (applicable from July 1, 2012).
3. Subsidiary company is a foreign company and dividend received by the holding company from the subsidiary company is taxable in the hands of holding company under Section 115BBD (applicable from July 1, 2013)

For the aforesaid purposes, a company shall be subsidiary of another company, if such other company holds more than half in nominal value of the equity share capital of the company.

**Notes:**

(a) The expression dividend used above shall have the same meaning as is given in Section 2(22) which shall include Section 2(22)(a), (b), (c) and (d) but shall not include deemed dividends under Section 2(22)(e).

(b) The above additional tax shall be payable by such company on its total income.
No tax on distributed profits by an undertaking or enterprise engaged in developing, operating and maintaining a Special Economic Zone [Section 115-O(6)]

(b) **Time limit for deposit of additional income-tax**: Such additional tax will have to be paid by the principal officer of the domestic company and the company within 14 days from the date of declaration of dividend, or distribution or payment of any dividend.

(c) **Tax on distributed profits not allowed as deduction**: The company or the shareholder shall not be allowed any deduction in respect of the amount which has been charged to tax or the tax thereon under any provisions of the income-tax Act.

(d) **Interest payable for non-payment of tax by domestic companies [Section 115P]**: In case of default simple interest @ 1% shall be liable for every month or part thereof beginning on the date immediately after the last date on which tax was payable and ending with the date on which the tax is actually paid.

(e) **When companies deemed to be in default [Section 115Q]**: If the principal officer of a domestic company and the company does not pay tax on distributed profits in accordance with the provisions of Section 115-O, then he or it shall be deemed to be an assessee in default in respect of the amount of tax payable by him or it and all the provisions of the Income-tax Act for the collection and recovery of income-tax shall apply.

(f) **Penalty under section 271C**: If any person fails to pay the whole or any part of the tax as required u/s 115-O(2), then such person shall be liable to pay, by way of penalty a sum equal to the amount of tax which such person failed to pay as aforesaid.

### 1.13 SPECIAL PROVISIONS RELATING TO TAX ON DISTRIBUTED AMOUNT TO UNIT HOLDERS [Sections 115R TO 115T]

(a) **Tax on income distributed to unit holders by the specified company or a Mutual Fund [Section 115R(2)]**

(I) where the income is distributed by money market mutual fund or a liquid fund, additional income-tax @ 25% + 10% SC + 2% EC + 1% SHEC will be liable to be paid.

(Ia) 30% + 10% SC + EC + SHEC on income distributed to any other person by a non market mutual fund or a liquid fund.

(II) Where the income is distributed by a fund other than a money market mutual fund and such income is distributed to —

   (i) individual or HUF — additional income-tax @ 25% + 10% SC + 2% EC + 1% SHEC will be liable to be paid.

   (ii) any person other than individual or HUF — additional income-tax @ 30% + 10% SC + 2% EC + 1% SHEC will be liable to be paid.

(b) **Time limit for deposit of additional income-tax [Section 115R(3)]** within 14 days from the date of distribution or payment of such income whichever is earlier.

(c) **Income charged to tax not allowed as deduction [Section 115R(4)]** to the specified company or to a Mutual Fund in respect of which income has been charged to tax.
(d) Interest payable for non-payment of tax [Section 115S]: In case of default simple interest @1% shall be liable for every month or part thereof beginning on the date immediately after the last date on which tax was payable and ending with the date on which the tax is actually paid.

(e) When specified company or Mutual Fund shall be deemed to be the assessee in default [Section 115T]: If any person responsible for making payment of the income distributed by the specified company or a mutual fund and the specified company or the Mutual Fund shall be deemed to be an assessee in default in respect of the amount of tax payable by him or it and all the provisions of the Income-tax Act for the collection and recovery of income-tax shall apply.

(f) Provisions of Section 115R shall not apply in respect of any income distributed:
(i) by the Administrator of the specified undertaking to the unit holders; or
(ii) to a unit holder of an equity oriented fund (whether open ended or close ended) in respect of any distribution made from such fund.

(g) Exemption of income in the hands of unit holder [Section 10(35)]: The following income shall be exempt in the hands of unit holders.
(a) income received in respect of units of a Mutual fund specified under Clause 23D; or
(b) income received in respect of units from the Administrator of the specified undertaking;
or
(c) income received in respect of units from the specified company.

1.14 PROBLEMS

1. R Ltd., a closely held Indian company is engaged in the manufacture of insecticides and fertilizers (value of the plant and machinery owned by the company is ₹ 55 lakhs). Its profits and loss account for the year ended 31-3-2017 is as under:

<table>
<thead>
<tr>
<th>Profit and Loss Account</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>₹</strong></td>
</tr>
<tr>
<td>Depreciation</td>
</tr>
<tr>
<td>Salaries and wages</td>
</tr>
<tr>
<td>Entertainment expenses</td>
</tr>
<tr>
<td>Traveling expenses</td>
</tr>
<tr>
<td>Miscellaneous expenses</td>
</tr>
<tr>
<td>Income tax</td>
</tr>
<tr>
<td>Wealth tax</td>
</tr>
<tr>
<td>Outstanding customs duty</td>
</tr>
<tr>
<td>Prov. For unascertained liabilities</td>
</tr>
<tr>
<td>Proposed dividend</td>
</tr>
<tr>
<td>Loss of subsidiary company</td>
</tr>
<tr>
<td>Consultation fees paid to a tax expert</td>
</tr>
<tr>
<td>Salaries &amp; Perquisites to MD</td>
</tr>
<tr>
<td>Excise duty of 2014-15</td>
</tr>
<tr>
<td>Net profit</td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>

Wealth tax 8,000
Outstanding customs duty 17,500
Prov. For unascertained liabilities 70,000
Proposed dividend 60,000
Loss of subsidiary company 30,000
Consultation fees paid to a tax expert 21,000
Salaries & Perquisites to MD 1,80,000
Excise duty of 2014-15 75,500
Net profit 15,86,500
30,00,000
For tax purposes the company wants to claim the following:
— Deduction under section 80IB (30% of ₹ 15,86,500)
— Excise duty pertaining to 2014-15 paid during 2016-17 (amount actually paid ₹ 75,500)
— Depreciation u/s 32 ₹ 5,36,000

The company wants to set off the following losses/allowances —

<table>
<thead>
<tr>
<th>For tax Purposes</th>
<th>For accounting purposes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brought forward loss of 2014-15</td>
<td>11, 80,000</td>
</tr>
<tr>
<td>Unabsorbed depreciation</td>
<td>2,45,000</td>
</tr>
</tbody>
</table>

Determine tax payable under Section 115JB.

**Solution:** Book Profit under Section 115JB:

<table>
<thead>
<tr>
<th>₹</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net profit as per profit &amp; loss account (assumed to be prepared according to Part II and III of Schedule VI to the Companies Act)</td>
<td>15,86,500</td>
</tr>
<tr>
<td><strong>Add:</strong></td>
<td></td>
</tr>
<tr>
<td>Income tax</td>
<td>3,50,000</td>
</tr>
<tr>
<td>Prov. For unascertained liability</td>
<td>70,000</td>
</tr>
<tr>
<td>Loss of subsidiary co.</td>
<td>30,000</td>
</tr>
<tr>
<td>Proposed dividend (appropriation of profit)</td>
<td>60,000</td>
</tr>
<tr>
<td><strong>Less:</strong> Unabsorbed depreciation</td>
<td></td>
</tr>
<tr>
<td>Book profit</td>
<td>18,51,500</td>
</tr>
</tbody>
</table>

**Computation of taxable income:**

<table>
<thead>
<tr>
<th>₹</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net profit as per profit &amp; loss account</td>
<td>15,86,500</td>
</tr>
<tr>
<td><strong>Add:</strong></td>
<td></td>
</tr>
<tr>
<td>Income Tax</td>
<td>3,50,000</td>
</tr>
<tr>
<td>Wealth tax</td>
<td>8,000</td>
</tr>
<tr>
<td>Outstanding customs duty</td>
<td>17,500</td>
</tr>
<tr>
<td>Provision for unascertained liability</td>
<td>70,000</td>
</tr>
<tr>
<td>Proposed dividend</td>
<td>60,000</td>
</tr>
<tr>
<td>Loss of subsidiary co.</td>
<td>30,000</td>
</tr>
<tr>
<td><strong>Less:</strong> Depreciation, i.e., (5,36,000 – 4,16,000)</td>
<td></td>
</tr>
<tr>
<td>Balance</td>
<td>20,02,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance</td>
</tr>
<tr>
<td><strong>Less:</strong> Brought forward business loss</td>
</tr>
<tr>
<td>Gross Total Income</td>
</tr>
<tr>
<td><strong>Less:</strong> Deduction u/s 801B (i.e., 30% of ₹ 8,22,000)</td>
</tr>
<tr>
<td>Net income rounded off</td>
</tr>
</tbody>
</table>
Tax on net income 30% of ₹ 5,75,400
   Add: Surcharge Nil
   Add Education cess +SHEC 3% ₹ 5,179
Total Tax Liability ₹ 1,77,799

Computation of tax u/s 115JB

<table>
<thead>
<tr>
<th>Description</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>18.5% of book profit (18,51,500)</td>
<td>3,42,528</td>
</tr>
<tr>
<td>Add: Education cess +SHEC 3%</td>
<td>10,275</td>
</tr>
<tr>
<td></td>
<td>3,52,803</td>
</tr>
</tbody>
</table>

Since tax payable under other provisions, i.e., all provisions ignoring Section 115JB is lower than as determined u/s 115JB, Section 115JB is applicable and the tax liability of the company shall be ₹ 3,52,803.

2. A domestic company, R Ltd., has an undertaking newly established for export of computer Software in a free trade zone, the profits of which have been merged in the net profit of the company as per profit and Loss Account prepared in accordance with the provisions of Parts II and III of Schedule VI to the Companies Act. It furnishes the following particulars in respect of assessment year 2017-18 and seeks your opinion on the application of Section 115JB. You are also required to compute the total income and tax payable.

<table>
<thead>
<tr>
<th>Description</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) Net profit as per Profit and Loss account as per schedule VI</td>
<td>2,00,00,000</td>
</tr>
<tr>
<td>(2) Profit and Loss Account includes:</td>
<td></td>
</tr>
<tr>
<td>(a) Credits:</td>
<td></td>
</tr>
<tr>
<td>(i) Dividend income</td>
<td>20,00,000</td>
</tr>
<tr>
<td>(ii) Excess realized on sale of land held as Investment</td>
<td>30,00,000</td>
</tr>
<tr>
<td>(iii) Net profit of the undertaking for export of computer software</td>
<td>1,00,00,000</td>
</tr>
<tr>
<td>(b) Debits:</td>
<td></td>
</tr>
<tr>
<td>(iv) Depreciation on straight line basis</td>
<td>1,00,00,000</td>
</tr>
<tr>
<td>(v) Provision of losses of subsidiary company</td>
<td>60,00,000</td>
</tr>
<tr>
<td>(3) Depreciation allowable as per income-tax Act and Rules</td>
<td>1,50,00,000</td>
</tr>
<tr>
<td>(4) Capital gains as computed under Income-tax Act</td>
<td></td>
</tr>
<tr>
<td>(5) Losses brought forward as per books of account —</td>
<td></td>
</tr>
<tr>
<td>Business Loss</td>
<td>50,00,000</td>
</tr>
<tr>
<td>Unabsorbed depreciation</td>
<td>60,00,000</td>
</tr>
</tbody>
</table>

The company has represented to you that the excess realised on sale of land cannot form part of the book profit for purposes of Section 115JB. You will have to deal with this issue.