YGM

Minimum Alternate Tax

An Insight

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MAT Simplified

Glossary

Terminology	Form
MAT	Minimum Alternate Tax
The Act	Indian Income Tax Act, 1961
Co.	Company
P&L a/c	Profit and Loss Account
LTCG	Long Term Capital Gains
CBDT	Central Board of Direct Taxes
r/w	Read with
Prov.	Provision
DTAA	Double Tax Avoidance Agreement
u/s	Under Section
ICAI	Institute of Chartered Accountants of India
AS	Accounting Standard

MAT Basics

- Since 1997, a self contained code specified in Chapter XII-B of the Act
- A mechanism to compute the book profits which is considered as total income of the company by deeming fiction of law prescribed u/s 115 JB from 1.4.2001 onwards
- A conditional tax liability
- The provisions, in effect, take back the various deductions otherwise allowable to a company

Rationale:

- Increase in the zero tax companies despite substantial book profits
- To capture under MAT the huge profits distributed as dividends on which no tax has been paid to the exchequer

Applicability:

- All Indian and Foreign Companies
- *"MSEB is a Corporation but not a company. It is required to prepare accounts as per Electricity Supply Act, 1948 and is not expected to declare dividends. Hence, not taxable u/s 115J of the Act" - Hon'able Mumbai ITAT*

MAT Mechanism

Tax Payable

Higher of

Normal Tax Liability

10% (7.5% for A.Y 06-07) **of BOOK PROFITS (MAT)**

Mechanism for MAT:

i. Compute the total income of Co. as per the normal provisions of the Act

ii. Compute the Income Tax Payable on such income

iii. Work out <u>BOOK PROFITS</u> u/s 115JB

iv. Calculate 10% of Book profits as mentioned in point (iv)

v. MAT computed under (iv) would be the tax payable if it is more than amount of tax worked out in point (ii) above

Computation of Book Profits

Net Profits as per Annual Report after all appropriations:

<u>Add Items:</u>

A1. Income Tax paid, payable or provision thereof

A2. Amount carried to reserves (other than reserves u/s 33AC)

A3. Provision for unascertained liabilities

A4. Provision for losses of Subsidiary Companies

A5. Dividends paid or proposed

A6. Expenses related to income u/s 10, 10A, 10B, 11 or 12

A7. Amount of Depreciation attributable to revaluation of assets

<u>Less Items:</u>

L1. Reserves or provisions credited back to P&L a/c

L2. Income u/s 10 (except LTCG u/s 10(38)), 10A, 10B, 11 or 12

L3. Write back of Revaluation Reserve not exceeding A7 above

L4. Brought forward loss (other than Depreciation) or Depreciation, which ever is less

L5. Profits of sick companies during period of sickness

L6. Amount of profits eligible for deduction u/s 80HHC/80HHE/80HHF

"Add Items" - Insight

A1. Income Tax Paid, Payable or Provision thereof

- Addition only to the extent the amount is debited to P&L a/c

Tax Item in P&L	Treatment	Important Observations
Wealth Tax Paid	Not to be added back	Echjay Forgings Pvt. Ltd. in 251 ITR 15 (Bom).
Interest, Penalty etc. under the Act	Not to be added back	Harshad Shantilal Mehta v. Custodian in 231 ITR 871 (SC).
Gift Tax / Surtax	Not to be added back	Not a part of income tax
Fringe Benefit Tax	Not to be added back	As per the CBDT circular dated August 29, 2005
STT, BCTT	Not to be added back	
Deferred Tax Liability	Not to be added back	A notional liability that never gets paid, but only gets reversed.
Corporate Dividend Tax	Debatable	Based on Conservatism, should be added back
Tax paid for Employees u/s 192(1A) r/w section 10(10CC)	Not to be added back	

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“Add Items” - Insight

A2. Amount carried to the Reserve

- Add back sums carried to reserves by whatever name called other than u/s 33AC
- Reserves should be created by debiting the Profit and Loss Account
- Even Statutory reserves would be eligible for MAT adjustments. Hence, reserves created by Financial Institution u/s 36(1)(viii) would have to be properly adjusted
- Transfers to capital reserves out of revaluation reserve which is not created by debiting P&L won’t be added back
- Debenture Redemption Reserve though created by debiting P&L won’t be added back

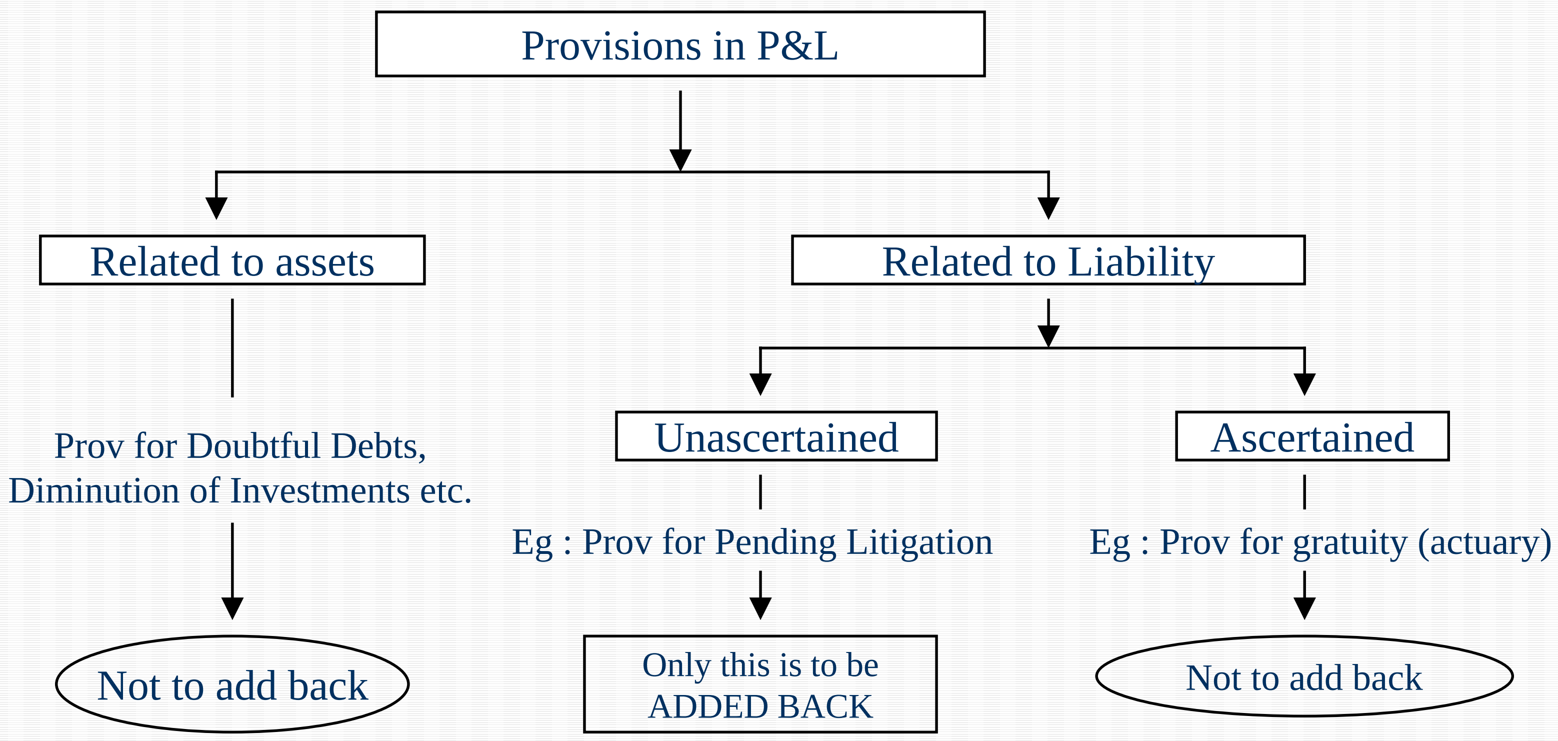
A3. Provision for Liabilities other than Ascertained Liabilities

- The idea is to increase the book profits in a case where deduction is made to the book profits for the contingent liability
- Only the items satisfying the following conditions to be added back to profits:

 - There should be a provision
 - The provision should be for a liability
 - The liability should be other than the ascertained liability

“Add Items” - Insight

A3. Provision for Liabilities other than Ascertained Liabilities



Prior Period items – Not to be added back

"Add Items" - Insight

A4. Provision for Losses of Subsidiary Companies

- Adding back the provision made for losses of subsidiary companies to net profits as per the books

A5. Dividends paid or proposed

- Adding back the amount of dividend paid/proposed to the net profits

A6. Expenses u/s 10, 10A, 10B, 11 or 12

- Expenses directly relating to the income exempt under the said sections would be added back
- Long term Capital Gains on Securities u/s 10(38) shall not be exempt for MAT purposes, the expense related to such LTCG is allowed as expense in calculating Book Profits

A7. Depreciation attributable to Revaluation of Assets (New Amendment)

"Under the normal provisions of the Income-tax Act, claim of higher depreciation on account of revaluation of assets is not allowed. However, companies do resort to revaluation of assets to claim such higher depreciation. ***With a view to plug the leakage of revenue on account of claim of higher depreciation through revaluation of assets*** *by certain companies, it is proposed to insert (this) new clause."*

-Memorandum to Finance Bill 2006

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"Less Items" - Insight

L1. Reserves/ Provision credited to P&L

- Reducing net profits by the amount withdrawn from any reserve / provision if such amount is credited to P&L a/c
- Exceptions:
  - Credit is from reserve created on or before 31st March 1997 (MAT Date) ***and*** the reserve was created without debiting P&L a/c
  - Credit is from reserve created after 31st March 1997 ***and*** in the year in which such reserve was created, it was not added back to the profits as per annual report as required in item A2 under additions
- Excess Depreciation relating to earlier years is written back to the P& L a/c for change in method of depreciation from diminishing balance to straight line method to be reduced from book profits – not liable to MAT
- For change of law since 1997, only the provision of depreciation made prior to 1-4-97, if written back can be excluded from profit and loss account

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“Less Items” - Insight

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L2. Incomes u/s 10, 10A, 10B, 11 or 12

- Reduction from book profits of the items of income for MAT purposes that are covered in the above sections
- Similarly, expenses of the concern falling under these sections were also added back to the profits under item A6
- Transactions under the above heads are kept out of MAT liability completely. Hence, they are fully exempt from tax
- Dividend income not covered by section 115O of the Act is liable to MAT (eg. an Indian Co. receives dividends from a company incorporated in the foreign company)

The amendment – Long Term Capital Gains u/s 10(38) – *Back door entry*

- The exemption for long term capital gains can be availed on equity shares and units of equity oriented mutual funds subject to the payment of STT
- Since Finance Act, 2006 the above exemption shall be available for normal purposes, it shall be disallowed under MAT
- A potential tax exposure of MAT on the said exemption

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“Less Items” – Insight

L3. Revaluation Reserve not exceeding depreciation on revalued assets

- Since depreciation on revalued assets is now disallowed, a write back of revaluation reserve upto such depreciation can be claimed as deduction from book profits for MAT purposes

L4. Brought forward losses before depreciation or depreciation, whichever is less

- Reduction in book profits by the amount of loss brought forward or unabsorbed depreciation, whichever is less
- Loss not to include depreciation. Hence, to work out the position of carried forward loss, only pure / cash loss before depreciation shall be considered
- A co. with huge investments and having a high amount of unabsorbed depreciation may be denied of the reduction claim in the absence of cash losses
- The unabsorbed depreciation and loss shall be as per books of accounts are not as per the Act

L5. Profits of Sick Industries during the period of Sickness

- To provide relief to the Sick Industries during the period of sickness

“Less Items” – Insight

L4. An Illustration

Amount in Rs.

Cases (A)	Losses After Depn (B)	Dep.(C)	Losses Before Dep.(D) (B – C)	Reduction (Lower of C or D)
1	16,00,000	10,00,000	6,00,000	6,00,000
2	21,00,000	8,00,000	13,00,000	8,00,000
3	3,00,000	5,00,000	Profit of 2,00,000	Nil
4	4,00,000	NIL	4,00,000	Nil

Important:

- If company does not have depreciable Fixed Assets, deduction = Nil
- If there is no loss before depreciation, deduction = Nil

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L6. Profits eligible for deduction u/s 80HHC, 80HHE, 80HHF

- A deduction from book profits by the amount of profits eligible for deduction under the above sections
- As provided in the Act:

  - Section 80 HHC relates to deduction in respect of profits from export business

  - Section 80 HHE relates to deduction in respect of computer software etc.

  - Section 80 HHF relates to deduction in respect of export or transfer of film software
- If the company is unable to claim the deduction under the above sections due to non-availability of profits or any other reason, whether the amount be deductible for MAT purposes – *Vital Observation in DCIT v. Govind Rubber Pvt. Ltd. 82 TTJ 615 (Mum).*
- The computation mechanism of the above sections restrict the benefits to a certain percentage, for the purposes of book profits under MAT, whether 100% of the profits to be considered - *Issue Unresolved*

MAT Calculation – We Illustrate

Profit & Loss a/c of X Ltd. for the year ended March 31, 2005

Particulars	Amount	Particulars	Amount
Manufacturing Expenses	626,000	Sales	2,700,000
Entertainment Expenses	51,000	Interest on Debentures	100,000
Provision for Income Tax:		Dividend Income	200,000
Current Tax	320,000		
Deferred Tax	30,000		
Wealth Tax paid	8,000		
FBT	4,000		
STT	8,000		
Provision for Gratuity	17,500		
Provision for Unascertained Liability	70,000		
Loss of Subsidiaries	71,000		
Managerial Remuneration	180,000		
Net Profit before appropriations	1,614,500		
Proposed Dividend	85,000		
Corporate Dividend Tax	12,000		
Net Profit after appropriations	1,517,500		
	3,000,000		3,000,000

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MAT Calculation – We Illustrate

Calculation of Book Profits

Particulars	Amount	Amount
Net Profits as per Profit and Loss a/c		1,517,500
Add Back:		
Provision for Income Tax	320,000	
Proposed Dividend	85,000	
Dividend Tax	12,000	
Provision for unascertained liabilities	70,000	
Loss for subsidiary companies	71,000	558,000
Reduce:		
Incomes u/s 10 (Dividend)	(200,000)	(200,000)
Book Profits		1,875,500
10% for A.Y 07-08 of Book Profits		187,550

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MAT Compliance

- All Companies are liable to pay Advance tax having regard to MAT provisions
- A Chartered Accountant's report in form 29B certifying that the Book Profits have been computed as per the Act is to be furnished along with the Return
- ICAI has prescribed the accounting methodology for MAT *vide* Guidance note on Report u/s 115JB of the Act
- Capital profits are not to be included for MAT purposes, however, there are instances of inclusions on account of revaluation of fixed assets
- Assessing Officer cannot challenge the profits as per annual report, not even provision for Income Tax if the same complies AS and approved by statutory auditors
- Assessing officer can challenge the items of additions and deletions for arriving at the Book Profits
- MAT provisions shall not affect amount to be carried forward as losses or unabsorbed depreciation u/s 72, 73, 74 and 74A
- Exemptions: 1) Units in SEZ; 2) Developer of SEZ; 3) Income under Tonnage Tax scheme are exempt from MAT liability

MAT on Foreign Entities

Foreign Companies:

i. Compute the total tax liability of PE in India

ii. Prepare the final accounts as per schedule VI of the Companies Act, 1956

iii. Make the adjustments as prescribed in MAT

iv. Exclude from book profits the items of income on which there is a provision in Double Tax Avoidance Treaty not to levy the tax in India

v. Apply MAT % to the book profits so computed above and pay tax higher of (i) and (iv)

Branch of Indian Company abroad:

- Accounts of foreign branch to be incorporated in Books of Head Office. Hence, profits of branch liable to MAT.
- As per section 90 of the Act r/w DTAA, credit for tax paid in said country would be applicable.
- Even if there is no DTAA, credit would be available under MAT by resorting to section 91 of the Act

MAT Credit - The Recent Relief

- Under section 115 JAA of the Act tax credit allowed for MAT
- If in any year, MAT tax is more than Normal Tax, then

MAT Credit = MAT Paid - Normal Tax

Calculation for MAT Credit:

i. Compute the total income of Co. as per the normal provisions of the Act

ii. Compute the book profit under provisions of section 115JB

iii. Find out tax payable on (i)

iv. Find out tax payable on (ii)

v. The amount of tax credit is equal to the tax paid under step (iv) as reduced by the tax computed under step (iii).

MAT Credit – We Illustrate

SET OFF OF MAT CREDIT:

Lower of

Balance of MAT Credit

Normal Tax – MAT Tax

Financial Year	Normal Tax	MAT	B/F MAT Credit	MAT Credit	Credit S/O	C/F	Tax Liability
05-06	150	180	0	30	0	30	**180**
06-07	210	190	30	0	20	10	**190**
07-08	220	230	10	10	0	20	**230**
08-09	250	235	20	0	15	5	**235**

- The above credit can be carried forward for **Maximum 7 years**
- Set off of MAT Credit can be availed from Tax ONLY in the year in which Normal Tax > MAT

THANK YOU