

**IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCHES "E", MUMBAI**

Before Shri R.S.Syal, AM and Shri Vijay Pal Rao, JM

ITA No.1299/Mum/2009: Asst.Year 2004-2005

The Income Tax Officer Ward 3(3)(3) Mumbai.	Vs.	M/s.TCFC Finance Limited 502, Raheja Chambers Nariman Point, Mumbai – 400 021. PA No.AAACR2710H.
(Appellant)		(Respondent)

**Appellant by : Shri Hemant Lal
Respondent by : Shri Vijay Mehta**

ORDER

Per R.S.Syal, AM :

This appeal by the Revenue emanates from the order passed by the CIT(A) on 17.09.2008 in relation to assessment year 2004-2005.

2. First ground is against the deletion of disallowance of Rs.2,04,12,594 being the amount of loss in respect of future and options transactions (hereinafter referred to as F & O transactions). Briefly stated the facts of this ground are that the assessee-company claimed the loss from F & O transactions as business loss. The Assessing Officer came to the conclusion that it was to be treated as loss from speculation business in terms of section 43(5). He, therefore, held that such loss could not be adjusted against non-speculation business income. As the assessee had adjusted such loss against the non-speculation share trading income, the Assessing Officer did not accept this treatment. The learned CIT(A) overturned the assessment order on this issue by holding that this loss was to be considered as non speculation business loss.

3. Having heard the rival submissions and perused the relevant material on record we find that this issue has been settled by the Special Bench of the tribunal in *Shree Capital Services Limited Vs. ACIT [(2009) 125 TTJ 740 (Kol.) (SB)]* by

holding that loss on account of transactions in derivatives, that is, F & O transactions, has to be considered as speculation loss up to assessment year 2005-2006. Insertion of clause (d) of proviso to section 43(5) has been held by the Special Bench to be prospective as applicable from assessment year 2006-2007. Since the assessment year under consideration is 2004-2005, the issue is duly covered by the afore-noted Special Bench decision. We, therefore, reverse the finding given by the learned CIT(A) and restore the action of the Assessing Officer. This ground is allowed.

4. Second ground is against the deletion of disallowance of Administrative expenses admitted to have been incurred for F & O transactions amounting to Rs.4,94,649. The facts apropos this ground are that the assessee debited a sum of Rs.46,48,955 to its Profit and loss account towards administration and general expenses excluding the expenses of Rs.15.68 lakhs incurred on rented property. The assessee's business consisted of share trading, investment and dealing in future and options. In view of the decision taken by him about the loss of Rs.2.04 crores from derivatives as speculation loss, the A.O. opined that expenses relating to such F & O transactions could not be allowed against the income of non speculation business income. Taking the figure of total turnover of the assessee from share trading at Rs.75.50 crores and from F & O transactions at Rs.8.99 crores totaling to Rs.84.49 crores, the AO found out the percentage of turnover of F & O transactions to total turnover at 10.64%. Applying this percentage to the administrative expenses of Rs.46,48,955 he determined a sum of Rs.4,94,649 as relatable to F&O transactions, which was held to be not allowable against non-speculation business income. Since the learned CIT(A) held the loss from futures and options to be non-speculation, he allowed deduction for entire expenses accordingly.

5. We have heard the rival submissions and perused the relevant material on record. The action of the learned CIT(A) in treating the loss from F&O transactions amounting to Rs.2.04 crores as non-speculation loss has been set aside by us in an earlier para. In that view of the matter, the conclusion drawn by the 1st. first appellate authority on the deductibility of entire expenses against the total receipts would automatically witness reversal. *Explanation 2* to section 28 clearly provides that where speculative transactions carried on by an assessee are of such a nature as to constitute a business, the speculation business shall be deemed to be distinct and separate from any other business. The prescription of this *Explanation* mandates that speculation business and non-speculation business are to be considered as distinct from each other and consequently the common expenses debited to the profit and loss account also need bifurcation into these two segments. The learned A.R. contended that the method of quantification of such expenses, adopted by the AO, was not appropriate inasmuch as there is variation in the degree of efforts put in to earn the income from these two segments. He stated that comparatively lower time and endeavor is required for carrying out the business in F & O segment. He, therefore, pleaded that the expenses should also be allocated in such a manner that these are not in proportion to the turnover. It was suggested that some relatively lower *ad hoc* disallowance towards such administrative and general expenses be sustained.

6. We are not impressed with this submission. Adverting to the facts of the instant case it is found that the Assessing Officer has taken total administrative and general expenses which have been bifurcated on the basis of ratio of turnover of speculation and non-speculation business. The obvious reason is that the assessee had clubbed expenses in relation to both these businesses. When the income from speculation business is required to be computed separately, the expenses claimed in a consolidated manner need to be bifurcated on some reasonable basis and not on *ad hoc* basis. In our considered opinion the splitting of expenses on the basis of

turnover, in the absence of other reasonable measure suggested by the learned A.R., is reasonable and does not call for any interference. We, therefore, hold that the Assessing Officer was right in determining general administrative expenses as relatable to speculation business at Rs.4,94,649. The impugned order is set aside and this ground of the Revenue is allowed.

7. Last effective ground of the appeal is against the deletion of addition of Rs.1,25,00,000 made to the book profit, being diminution in the value of shares of "RFB Latex Limited". The Assessing Officer called upon the assessee to explain as to why the provision for diminution in the value of investments of Rs.1.25 crores should not be added to the book profit u/s.115JB. The assessee submitted that it made investment in unquoted shares of RFB Latex Limited on 11.08.2000 which was included in the earlier balance sheet under the head 'Investment'. As RFB Latex Limited had discontinued the operation, the assessee filed an application before the Company Law Board alleging that the affairs of that company were mismanaged. In that view of the matter the assessee entertained the view that the amount was irrecoverable and hence a sum of Rs.1.25 crores was written off as provision for diminution in value of investment. Not convinced with the assessee's submission, the Assessing Officer came to hold that this amount was required to be added to book profit u/s.115JB. The learned CIT(A) deleted the said addition.

8. We have heard the rival submissions and perused the relevant material on record. Section 115JB was inserted by the Finance Act, 2000, with effect from 1.4.2001. Its marginal note is :`Special provision for payment of tax by certain companies'. Sub-section (1) of this section provides that notwithstanding anything contained in any other provision of this Act, where in the case of an assessee, being a company, income-tax payable on the total income as computed under this Act in respect of any previous year relevant to the assessment year so stated is less than the specified percentage of its book profit, then such book profit shall be deemed to

be the total income of the assessee and tax payable by the assessee on such total income shall be the amount of income tax at the given rate. *Explanation 1* to sub-section (2) defines “book profit” to mean net profit as shown in the profit and loss account for the relevant previous year prepared under sub-section (2) as increased by the items set out in clauses (a) to (i) debited to the profit and loss account and as reduced by the items enumerated in clauses (i) to (viii). There is no dispute on the fact that the provisions of section 115JB are applicable in this case. The dispute only centers round the computation of ‘book profit’. The Assessing Officer computed the book profit by increasing net profit as per profit and loss account with a sum of Rs.1.25 crores debited by the assessee in its profit and loss account with the narration “Provision for diminution in the value of investments”.

9. At this juncture it would be relevant to note the judgment of the Hon’ble Supreme Court in *CIT Vs. HCL Comnet Systems and Services Limited [(2008) 305 ITR 409 (SC)]* in which the controversy was about the adding back of provision for doubtful debts to the net profits under clause (c) of the *Explanation* to section 115JA. The Hon’ble Supreme Court noted that clause (c) of *Explanation* to section 115JA talks of : “the amount or amounts set aside to provisions made for meeting liabilities, other than ascertained liabilities”. It was held that clause (c) would be applicable only if the amount is set aside as provision for meeting a liability other than ascertained liability. As the provisions for bad and doubtful debts was made to cover up the probable diminution in the value of asset, that is, debt which was an amount receivable by the assessee and hence an asset, the Hon’ble Apex Court held that such a provision could not be characterized as a provision for liability because even if a debt is not receivable, no liability could be fastened upon the assessee. It was further noted that the debt was the amount receivable by the assessee and not liability payable and hence any provision made towards non-recoverability of the debt could not be said to be a provision for liability. In the final analysis it was held that clause (c) of *Explanation* to section 115JA was not

attracted and the provisions for doubtful debts could not be added to the net profit. It is vital to note that the Finance (No.2) Act, 2009 inserted clause (g) to *Explanation* to section 115JA(2) which reads : “the amount or amounts set aside as provision for diminution in the value of asset”. This amendment, with retrospective effect, has been aimed at neutralizing the judgment of the Hon’ble Supreme Court in *HCL Comnet Systems and Services Limited (supra)*. On the same line, amendment has also been carried out to section 115JB by the same Finance (No.2) Act, 2001 and that too, with retrospective effect from 1.4.2001, by inserting clause (i) to *Explanation 1* to section 115JB(2). This clause reads : “the amount or amounts set aside as provision for diminution in the value of any asset”. The effect of amendment to section 115JB also remains the same, that is, while computing “book profit”, net profit as shown in the profit and loss account for the relevant previous year is to be increased *inter alia* by the amount or amounts set aside as provision for diminution in the value of any asset.

10. The learned A.R. has rightly not disputed the legal position as discussed above. He submitted that the narration given by the assessee to this provision of Rs.1.25 crores in its Profit and loss account as “Provision for diminution in the value of investments” should not be considered as binding on assessee, since there was difference in the actual transaction *vis-à-vis* the nomenclature given in the profit and loss account. He invited our attention towards the Balance sheet of the assessee, at page 2 of the paper book, in which the figure of Investment has been depicted at Rs.17.28 crores. Taking us through the details of the figure of such investment, at page 5 of the paper book, he submitted that in the previous year ending on 31.3.2003 the amount of provision for diminution in the value of investment was at Rs.9.08 crores and with the addition of the amount of Rs.1.25 crores, being the provision for this year, the total amount of provision as at the end of the year stood reflected at Rs.10.33 crores. He showed that the assessee had reduced the amount of such provision for diminution in the value of investment

from the gross value of investment at Rs.27.62 crores and resultantly only the net sum of Rs.17.28 crores was shown in the balance sheet. It was, therefore, argued that by reducing the amount of provision for diminution in the value of investment from the gross figure of investment, the assessee had shown net figure of investment in the asset side of the balance sheet and as such no figure of provision was appearing in the liability side. Reference was made to the judgment of the Hon'ble Supreme Court in the case of *Vijaya Bank Vs. CIT [(2010) 323 ITR 166 (SC)]* in which the question for consideration was deductibility of the provision for bad debt u/s.36(1)(vii). He read out the relevant parts of this judgment to show that the Hon'ble Supreme Court has entitled the assessee to deduction u/s.36(1)(vii) by holding that since the provision for bad and doubtful debt was reduced from the value of debtors in the balance sheet it should be construed as writing off of bad debt. It was, therefore, put forth that there was difference in two situations, viz., firstly, in which the assessee debits the amount of doubtful debts to its Profit and loss account and credits the asset account like sundry debtors which would constitute a write off of an actual debt and, secondly, in which the assessee debits provision for doubtful debts to the Profit and loss account and makes a corresponding credit on the liability side of the balance sheet, in which case it would constitute provision for doubtful debts. Drawing analogy from this judgment, the learned A.R. contended that the amount of Investments of the assessee stood at Rs.27.62 crores, which included the value of unquoted shares of RFB Latex Limited worth Rs.1.25 crores. As the entire amount was found to be unrealizable, the assessee created provision for this sum of Rs.1.25 crores and the total amount of the such provision including that of the opening balance, was shown by way of reduction from the value of Investment in its balance sheet. It was thus contended that the treatment given by the assessee to the amount of diminution in the value of investment should not be seen as a provision itself, notwithstanding the wrong nomenclature given by the assessee, but it was, in effect, writing off of

bad debt , which could not be added to the book profit. Per contra, the learned Departmental Representative strongly relied on the assessment order on this point.

11. We have heard the rival submissions and perused the relevant material on record in the light of precedents cited before us. *Explanation 1* to section 115JB(2) defines “book profit” to mean the net profit as shown in the profit and loss account for the relevant previous year prepared as per Parts II and III of Schedule VI of the Companies Act, 1956 as increased, *inter alia* by clause (i), being the amount or amounts set aside as provision for diminution in the value of any asset. Clauses (a) to (i), as set out in the first part of the *Explanation*, succeed with the expression ‘if debited to the profit and loss account’. The learned A.R. vehemently argued that section 115JB has to be considered as code in itself. We are in full agreement with this argument for the reason that this section is a special provision for payment of tax by certain companies and opens with *non-obstante* clause thereby excluding any other provision of this Act in the matter of determination of payment of tax by certain companies. Book profit is computed by adding back certain amounts to the net profit as shown in the profit and loss account which have been debited to the profit and loss account and thereafter reductions start, which have been specified in the later part of the Expl. in clauses (i) to (viii) if such amounts have been credited to the profit and loss account. From here it follows that if the amount set aside as provision for diminution in the value of any asset, appears on the debit side of the profit and loss account, which implies that the amount of net profit as per profit and loss account is after the amount of such provision, then such amount will be added back to the net profit for computing ‘book profit’ as per *Explanation 1* to section 115JB(2). There is no other requirement in the language of the section for the addition or non-addition of the amount of provision for diminution in the value of any asset to the amount of net profit as shown in the profit and loss account, depending on the way in which such provision has been shown in the balance sheet. The reflection of the amount of provision for diminution in the value of

investment separately on the liability side of the balance sheet or by way of reduction from the figure of investment on the asset side of balance sheet is totally alien for computing book profit. What is relevant for this purpose is to find out if any provision for diminution in the value of any asset has been debited to the profit and loss account. If it is so debited, the same will automatically stand added to the amount of net profit for working out the amount of book profit.

12. The judgment of the Hon'ble Supreme Court in the case of *Vijay Bank (supra)*, as heavily banked upon by the learned A.R., is in the context of deduction u/s.36(1)(vii). The Hon'ble Apex Court was called upon to decide on the deductibility or otherwise of the amount of bad debt u/s.36(1)(vii). The Department argued in that case that since the deduction could be allowed on actual write off of the bad debt, the provision made by the assessee bank without writing off the individual accounts of debtors, did not satisfy the condition for deduction. It was in that context that the Hon'ble Summit court held that there was no need to write off each account of debtor separately and it would be the sufficient compliance of the provision if the debtors have been shown in the asset side of the balance sheet as net of the provision. There was no consideration or decision on the question of computation of book profit u/s.115JB in that case. As we are dealing with a special provision contained in section 115JB, which is a code in itself even as per the arguments of the learned A.R., there is no scope for examining the judgments rendered by the Hon'ble Courts in the context of other provisions, with a view to find out whether provision for diminution in the value of asset could or could not be added to the amount of net profit as shown in the profit and loss account. It is seen from the text of *Explanation 1* to section 115JB(2) in no uncertain terms that any amount set aside as provision for diminution in the value of asset debited to the profit and loss account has to be added to the amount of net profit for the purpose of computing book profit. As the relevant conditions have been fully satisfied in the instant case in terms of the assessee debiting provision

for diminution in the value of investment to its profit and loss account, the same is required to be added for determining book profit.

13. The learned Counsel for the assessee supported the impugned order from another angle. He submitted that since section 115JB is a code in itself, only those adjustments to the net profit can be made which are clearly stipulated under *Explanation 1* to section 115JB(2). Accentuating on the language of clause (i), which talks of provision for “diminution” in the value of any asset, the learned AR contended that the term ‘diminution’ in this clause refers to reduction in the value of an asset. He submitted that this word presupposes one higher value of an asset before diminution and another lower value of the same asset after diminution. Referring to the meaning of word “diminution” in the Webster’s Dictionary and Shorter Oxford English Dictionary, the learned A.R. contended that it represents “the condition of being diminished” or “to make smaller or less”. He emphasized on the meaning of word “diminution” as suggesting having some lower value of the asset other than zero as a precondition for the attractability of clause (i) of *Explanation 1* to section 115JB. As the assessee created provision in respect of Shares of RFB Latex Limited for Rs.1.25 crores, being the full value of investment itself, he submitted that after reduction of the provision, the amount of investment *qua* these share came to Nil. It was thus argued that it was not a case of diminution in the value of any asset and hence application of clause (i) of *Explanation 1* was ousted. Countering this submission, the learned Departmental Representative contended that the word “zero” has been defined in Concise Oxford Dictionary to mean ‘lowest possible value’. He argued that reduction in the value of shares of RFB Latex Limited to zero also amounted to diminution in the value of investment and the same was rightly considered by the Assessing Officer.

14. Having regard to the rival submissions we find that the Legislature has employed the expression “provision for diminution in the value of any asset” in

clause (i) to *Explanation 1* to section 115JB(2). The expression “diminution in the value of any asset” has not been defined in this section. In common parlance the word “diminution” indicates the state of reduction. The Concise Oxford Dictionary gives the meaning of the word “diminution” as “*the act or an instance of diminishing; the amount by which something diminishes*”. Almost to the same extent is the meaning of this word, given in other dictionaries relied on by the learned A.R. If an asset worth Rs.100 is reduced to the value of Rs.10, there is diminution in the value of asset by Rs.90. If however the value of the asset is reduced to Rs.0, there is diminution in the value of asset by Rs.100. It is beyond our comprehension as to what name, other than diminution, can we give to reduction in the value of asset from Rs100 to Rs.0. The meaning of the word “diminution” in the value of any asset has to be construed as reduction from its original value which may still be a positive value or nil. If the reduced value happens to be cipher, the diminution will be the original value of the asset itself. There is not even a remotest hint in the language of clause (i) of *Explanation 1* to section 115JB that some value of the asset must remain after diminution, as a pre-condition for adding it to the net profit. It is paramount to note that we are concerned with the amount of provision for “diminution in the value of any asset” and not with the value of asset which remains after diminution. *Explanation 1* contemplates the adding back of the provision for diminution in the value of any asset to the amount of net profit. Once provision is made for diminution in the value of any asset, the same has to be added for computing book profit, regardless of the fact whether or not there is any balance value of the asset. In view of the foregoing discussion it is manifest that the as *Explanation 1* to section 115JB(2) deals with the computation of book profit and specifically provides that the net profit as shown in the profit and loss account for the relevant previous year has to be increased *inter alia* by the amount of provision for diminution in the value of any asset, the amount of provision for diminution in the value of any asset debited

to the profit and loss account before the determination of net profit has necessarily to be added. We, therefore, reject this contention raised on behalf of the assessee.

15. The learned A.R. still attempted to strengthen his case from still another angle by pointing out there are certain amounts, enumerated in clauses (i) to (viii), which are required to be reduced from the net profit as shown in the profit and loss account. He referred to clause (i), as per which the amount withdrawn from any reserve or provision, if credited to the profit and loss account, shall be reduced if the creation of the provision was by way of debit to the profit and loss account. It was argued that here is a case in which provision has been made at 100% of the value of investment. He submitted that when, at a later stage, this amount becomes bad and irrecoverable, the value of investment as well as provision to that extent will be reduced to the extent of Rs.1.25 crores and there will not be any debit or credit to the profit and loss account at that point of time. In his opinion the working out of the amount of book profit as per *Explanation 1* would, therefore, show the distorted picture.

16. On this count also we express our inability to agree with him. Later part of *Explanation 1* to section 115JB(2) enumerates certain items, which are required to be reduced from the amount of net profit, if they are credited to P&L account. Clause (i) provides that 'the amount withdrawn from any reserve or provision (excluding a reserve created before the 1st day of April, 1997 otherwise than by way of a debit to the profit and loss account), if any such amount is credited to the profit and loss account' shall be reduced from the amount of net profit as per profit and loss account for computing book profit. The upshot of this provision is that if any amount of reserve or provision has been added to the amount of net profit as shown in the profit and loss account for computing book profit, then the amount withdrawn from any reserve or provision credited to the profit and loss account should be reduced. To put it in simple words if a provision for Rs.100 was made

for diminution in the value of any asset but later on the assessee was successful in making recovery to the extent of Rs.30, then the excess provision of Rs.30 credited to the profit and loss account should be reduced from the amount of net profit for computing the book profit. The obvious reason is that when earlier the provision of Rs.100 was made, it resulted in increasing the amount of net profit by that extent for working out the amount of book profit. However, now on the reversal of the provision found to be excess, such amount should not be again allowed to increase the book profit and hence should be reduced. If the debit to the profit and loss account of provision for diminution in the value of any asset is added to the amount of net profit and thereafter the excess provision when credited to the profit and loss account is not reduced, that would amount to double addition of Rs.30 to the net profit for computing book profit as per *Explanation 1* to section 115JB(2). This contention made on behalf of the assessee is also found to be bereft of any force.

17. In view of the foregoing reasons we are satisfied that the learned CIT(A) was not justified in ordering for the reduction of the amount of Rs.1.25 crores from the book profit. We, therefore, restore the action of the A.O. on this issue and allow the ground raised by the Revenue.

18. In the result, the appeal is allowed.

Order pronounced on this **9th day of March, 2011.**

Sd/-
(Vijay Pal Rao)
JUDICIAL MEMBER

Sd/-
(R.S.Syal)
ACCOUNTANT MEMBER

Mumbai : **9th March, 2011.**
Devdas*

Copy to :

1. The Appellant.
2. The Respondent.
3. The CIT concerned
4. The CIT(A) –XXXII, Mumbai.
5. The DR/ITAT, Mumbai.
6. Guard File.

TRUE COPY.
By Order

Assistant Registrar, ITAT, Mumbai.