IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO.367 OF 2018

Pr.Commissioner of Income Tax-2 ..... Appellant

Vs.

Varun Corporation Limited ..... Respondent

Mr.Suresh Kumar for the appellant

Mr.Tanmay Varadkar for the Liquidator of Varun Corporation Limited

Mr.Prakash K. Pandya – Liquidator present

CORAM: K.R. SHRIRAM, J & FIRDOSH P. POONIWALLA, J.

DATED : 5TH JULY, 2023

P.C.

1. Mr.Tanmay Varadkar undertakes to file Vakalatnama for respondent during the course of this week. Undertaking accepted.

2. Respondent was called Khatau International Limited till 04.01.2009. Respondent was carrying on business activities through three divisions, viz., (1) Resort Division, (2) Travel Division, and (3) Investment Division.

3. Under the Resort Division, respondent was running a resort namely “Infinity Resort” at Corbett, Ramnagar, w.e.f., 15th July

2008. Respondent demerged its resort division to a company called "Khatau Resorts Pvt.Ltd. in accordance with section 391 to 394 of the Companies Act, 1956. The demerged scheme was approved by Company Court on 19th September 2008.

4. Pursuant to the demerger, respondent transferred its resort division along with all assets and liabilities, except, remaining business. As part of remaining business, respondent retained certain investments in shares of companies and borrowings from financial institutions. As per the scheme approved, respondent reduced the book value of all the assets and liabilities relating to the hospitality business from its books of accounts. The difference being the excess of the book value of the assets transferred over the book value of liabilities transferred was to be adjusted by respondent in its profit and loss account. While approving the demerger, the Company Court also noted that no party has come forward to oppose the scheme and the Regional Director has also stated that the scheme as proposed is not prejudicial to the interest of shareholders, creditors and the public. The Court also has noted that all requisite statutory compliances have been fulfilled.

5. Respondent, in its annual accounts prepared for year ending 31st March 2009, *interalia,* debited loss of Rs.145,23,56,165/- which arose on transfer of asset on demerger. This loss was fully disclosed

by respondent as extraordinary item in its profit and loss account. This loss was arrived at by reducing the book value of the asset transferred to the tune of Rs.146,93,56,165/-. The book value of the liabilities transferred was Rs.1,70,00,000/-. The treatment given by respondent to the loss arising on demerger, it appears from the annual accounts, was in accordance with the provisions of the Companies Act and as well as accounting standards 5 dealing with "net profit or loss for the period prior period items and changes in the accounting policies" issued by the Institute of Chartered Accountants of India (ICAI).

6. On 05th October 2010, respondent declared nil income for Assessment Year 2009-2010, in regular computation of income and loss of Rs.64,21,12,555/- was computed under section 115JB of the Act. This computation of income was based on the annual accounts prepared for the year ending 31st March 2009, which was audited by its statutory auditors and approved by share holders. Audit report does not contain any adverse observation regarding treatment given in the accounts for this item. Auditors have accepted the book treatment in respect of loss arising on account of demerger. While framing the assessment under section 143(3), the Assessing Officer (AO) accepted the income as NIL, as per the regular computation of income, but, on computation of book profit under section 115JB of

the Act, Assessing Officer started with the net profit as reflected in the profit and loss account of Rs.78,37,68,201/-, i.e., such profit before provisions of fringe benefit tax, prior period adjustment and extraordinary adjustment.

7. It was respondent's case that such computation should start with net loss of Rs.66,86,13,773/- being loss as shown in the Profit and Loss Account after extraordinary adjustment. Assessing Officer took a stand that such loss ought to be adjusted against reserves of respondent and cannot be debited to the profit and loss account. The Assessing Officer also observed that the accounting treatment was not in accordance with the provisions of the Companies Act.

8. On Appeal, the Commissioner of Income Tax (Appeal) upheld the findings of the Assessing Officer. Respondent, aggrieved by the order of the Commissioner of Income Tax (Appeal), approached the Income Tax Appellate Tribunal (ITAT) which by the impugned order dated 22nd April 2016 allowed the appeal. The admitted position is that as per explanation to section 115JB(2) of the Act, only adjustment as permitted to the book profit are those as provided in the explanation thereto.

9. It is respondent's case that there is no adjustment prescribed in the said explanation with respect to increasing the book profit by loss arising on transfer of assets and liabilities upon demerger. But

the Assessing Officer as also Commissioner of Income Tax (Appeals) took the starting point for the purpose of section 115JB of the Act as the net profit as disclosed before provision for fringe benefit tax, prior period adjustment and extraordinary adjustment which is not provided in Explanation 1.

10. Having heard the counsel and having considered the impugned orders and the memo of Appeal, we have to observe that the treatment given by respondent in its accounts have been approved by the Company Court while approving the scheme of demerger. Moreover, the statutory auditors have accepted the book treatment in respect of loss that arise on account of demerger.

11. It is well settled that as per Explanation 1 below section 115JB(2) of the act, only adjustment as permitted to the book profit are those as provided in the said explanation. The purpose of section 115JB of the Act is to provide an alternative method of computation of tax by accepting the book profits as shown by Respondent, after certain adjustments as specified in Explanation 1 of section 115JB(2) and levying tax thereon as alternative to the tax computed under the other provisions of the Act. Further the Apex Court in the case of ***Apollo Tyres Ltd. vs. Commissioner of Income Tax, Kochi***[1] has held that the only power the Assessing Officer has is the power of examining whether the books of account

1 (2002) 255 ITR 273 (SC)

are certified by the authorities under the Companies Act as having been properly maintained in accordance with the Companies Act. Thereafter, the Assessing Officer has a limited power of making increase and reduction as provided for in the explanation to section 115JB. The Assessing Officer does not have jurisdiction to go behind the net profit shown in the profit and loss account except to the extent provided in the explanation.

12. The Apex Court in the case of *Apollo Tyres* (Supra) also held that while so looking into the accounts of the company, an assessing officer has to accept the authenticity of the accounts with reference to the provisions of the Companies Act which obligates the company to maintain its accounts in a manner provided by that Act, the same to be scrutinised and certified by statutory auditors and approved by the company in its General Meeting and, thereafter to be filed before the Registrar of Companies who has a statutory obligation also to examine and be satisfied that the accounts of the company are maintained in accordance with the requirements of the Companies Act. It does not empower the Assessing Officer to mark upon a fresh enquiry in regard to the entries made in the books of account of the Company.

13. Section 115JA was changed to 115JB pursuant to Finance Act, 2000, w.e.f., 1st April, 2001. We also find that the conditions

given in explanation 1 in section 115JB is the same as explanation 1 in section 115JA, barring few minor differences. But the undisputable position is once the accounts of the company have been scrutinized and certified by statutory auditors and approved by the Company in general meeting and the Registrar of Company is also satisfied that the accounts of the Company are maintained in accordance with the requirement of the Companies Act, the Assessing Officer cannot embark upon a fresh enquiry in regard to the entries made in the books of account of the company. This is exactly what the ITAT has also held in the impugned order.

14. In the circumstances, we see no reason to entertain the Appeal. Appeal dismissed.

(FIRDOSH P.POONIWALLA, J.) **(K.R. SHRIRAM, J.)**