MINIMUM ALTERNATE TAX: IS THERE ANY ALTERNATIVE?

Sanjay Kumar[*]

Minimum alternate taxation is a measure to address the growing problem of companies that declare high profits, but pay low or no taxes ('zero-tax' companies). Parliament has experimented with its approach to MAT since 1983 and continues to do so in the proposed Direct Tax Code. This paper charts the various changes in the MAT regime made over the years and the interpretational problems that have arisen with provisions for MAT credit, advance payment of MAT and calculation of book profits. It then considers the merits of this taxation regime with reference to the economic effects of the burden of this tax, and the attendant compliance and record-keeping costs. With this in mind, this paper argues that the MAT regime should be modified and puts forth two proposals for reform to make the corporate taxation regime clear and efficient.

I. INTRODUCTION

Over the course of the last twenty years, Parliament has experimented with various approaches to address the problem of disproportionately low tax revenue collected from highly profitable companies. The primary cause of this problem is not tax evasion or a lack of adequate government enforcement, but the statutory features of the tax system – incentives, deductions and exemptions. These policies have made it possible for companies to greatly reduce their taxable income, leading observers to coin the phrase 'zero-tax' companies. Parliament has responded by amending the Income Tax Act, 1961 ('ITA') to introduce a system of Minimum Alternate Tax ('MAT'). This paper analyses the MAT regime in terms of its legal and economic effects and examines the relative merits of other proposed solutions. In Part II, the paper analyses the objectives of the Indian MAT regime and brings out its parallels with the first such regime- the American alternate minimum tax model. Part III then traces the changes in the MAT regime over time, from its early precursor in 1983 to the proposed Direct Tax Code Bill ('DTC'). Part IV describes the detailed operation of the current MAT regime under §115JB of the ITA, and Part V compares this with the DTC regime. In Part VI, the paper examines the problems with the MAT regime in terms of its effect on earnings management practices and on the industry as a whole. Finally, Part VII proposes two solutions that could replace the present regime for corporate taxation.

[*] Assistant-Professor, the W.B. National University of Juridical Sciences, Kolkata. I thank Jenisha Parikh and Nihal Joseph for their research assistance. Any omissions or errors, however, remain mine alone.

II. OBJECTIVES OF A MINIMUM ALTERNATE TAX REGIME

The concept of MAT was introduced under the ITA to tax 'zero-tax' companies, *i.e.*, companies that make high book profits and declare substantial dividends to their shareholders but have no or insignificant taxable income under the ITA because of the exemptions, deductions and incentives provided therein in the form of a liberal rate of depreciation, sector and region-specific exemptions, deductions etc. MAT is in consonance with a fundamental canon of taxation– all entities must be taxed in proportion to their ability to pay.[1]

The current MAT regime under the ITA is similar to the first such regime– the US Alternate Minimum Tax ('AMT').[2] As with the Indian law, the legislative intent for introducing this kind of taxation was to ensure that "no taxpayer with substantial economic income can avoid significant tax liability by using exclusions, deductions and credits".[3] It is pertinent to note that AMT applies to 'all taxpayers' including individuals and companies. In contrast, the provisions of MAT under the ITA are applicable only to companies and limited liability partnerships.[4]

A taxpayer is liable to pay under the AMT regime if the Tentative Minimum Tax ('TMT') is in excess of the 'regular taxable income' for a particular year. The starting point for the calculation of the TMT is the regular taxable income itself.[5] This income is recalculated through various 'adjustments'[6] and 'preferences'[7] mentioned under the provisions of the Internal Revenue Code. One of the most important adjustments is made through the process of business untaxed reported profits ('BUP') and adjusted current earnings ('ACE'). Both these adjustments entail an addition of a certain percentage[8] of the difference between its tentative adjusted minimum tax income (which consists of the minimum income base before the calculation of BUP or ACE) and its net book income, to the calculation of the minimum tax income.[9]

---

1 Adam Smith, Wealth of Nations 499 (2007) (which states that "the subjects of every state ought to contribute towards the support of the government … in proportion to the revenue which they respectively enjoy under the protection of the state").

2 The Tax Reform Act, 1986 (which introduced AMT in the US).

3 House Ways and Means Committee Report and Senate Finance Committee Report, S.Rep. No. 313, 99th Cong., 2nd Sess.518 (1986); H.R.Rep. No. 426, 99th Cong., 2nd Sess.305-06 (1985).

4 ITA, Chapter XIIB.A, §115JC-115JF, by Finance Act 2011, w.e.f. April 1, 2012.

5 John M. Janiga, *Corporate Alternative Minimum Tax: A critique and exploration of Alternatives*, 20 Loy. U.Chi. L.J. 21 (1988-1989).

6 Internal Revenue Code, 1986, §56 and §58.

7 *Id.*, §57.

8 *Id.*, (50 percent from 1987-1989 with respect to business untaxed reported profits and 75 percent with respect to adjusted current earnings from 1989 onwards).

9 Janiga, *supra* note 5.

As will be seen, the TMT is a parallel of book profit under the Companies Act in the Indian MAT system, although they may differ in their computation. The intention of the taxation regime in both jurisdictions is, however, the same– to curtail the benefits of various exemptions and deductions if they results in little or no tax liability.

III. HISTORY OF THE MINIMUM ALTERNATE TAX REGIME

The first legislative step towards addressing the problem of zero-tax companies was made in 1983, with the addition of §80VVA to the ITA.[10] §80VVA provided that the aggregate amount of deductions (under specified heads) that a company could make in one year could not exceed 70 percent of the pre-incentive total income.[11] In effect, there was a ceiling on the total amount of incentives or allowances that a company was allowed to avail of in a given year. It, however, allowed companies to carry forward these unabsorbed allowances and set it off against taxable income in the future.[12]

This provision, however, proved to be unsuccessful in preventing companies from avoiding tax liability and a new solution was sought.[13] In 1987, this provision was replaced with §115J,[14] by which for the first time, the quantum of taxable income was determined with respect to the 'book profits'. Under §115J, if the total taxable income of a company was less than 30 percent of its book profits, then the total income to be taxed was deemed to be 30 percent of the book profits, and such total income was taxed at the applicable rate. Book profits were defined as the "the net profit as shown in the profit and loss account for the relevant previous year"[15] as determined by the provisions in Parts II and III of Schedule VI to the Companies Act, with certain positive and negative adjustments.[16] Depreciation losses also had to be calculated as per the provisions of the Companies Act.[17] Thus, the concept of 'deemed total income' was introduced. Consequently, companies now had to maintain two sets of accounts– one for calculating total taxable income under the general provisions of the ITA and the second for book profits under the provisions of the Companies Act. At the end of the year, companies were liable to pay tax on the amount calculated under the general provisions of the ITA or on the book

---

[10] Finance Act, 1983 w.e.f. Assessment Year 1984-85.
[11] ITA, §80VVA (1).
[12] ITA, §80VVA (3).
[13] Rajiv Gandhi, Union Minister of Finance, Budget Address before the Lok Shabha: Union Budget for the Year 1987-88, (February 28, 1987); *Also quoted in* Apollo Tyres LTD v. Commissioner of Income Tax, (2002) 9 SCC 1 : [2002] 255 ITR 273 (SC).
[14] Finance Act, 1987, w.e.f. Assessment Year 1988-89.
[15] ITA, §115J (1A).
[16] *Id*.
[17] Commissioner of Income Tax v. Dynamic Orthopedics, (2002) 176 CTR (Ker) 432.

profits calculated under the MAT provisions, whichever was higher. This provision was, however, eventually repealed in 1990.[18]

Provisions relating to MAT were re-introduced in the ITA in 1997 *vide* §115JA, in a modified form, introducing the concept of 'MAT credit'.[19] Under §115JA, MAT credit accrues to a company each year, as the difference (if any) between the tax calculated under the provisions of MAT and the tax calculated under the general provisions of the ITA.[20] This credit would be carried forward and may be set-off when the tax amount calculated under the general provisions is higher (and hence payable) than the tax amount under the MAT provisions subject to MAT. The MAT credit was, however, allowed to be carried forward and set-off only for five assessing years immediately succeeding the assessing year in which the MAT credit was first computed.[21]

These provisions were eventually replaced by §115JB in 2000,[22] which is the provision of law embodying the current MAT regime. The provisions relating to MAT credit were repealed in 2000 with this amendment, but re-introduced in 2005 in §115JAA. §115JB is a complete conceptual change from 'deemed total income' to 'deemed tax' on book profits. This means that while the previous regimes[23] focused on the determination of minimum deemed income to be taxed under the prevailing rate, the new regime under §115JB laid emphasis on computing the minimum deemed tax. This section was amended by the Finance Act, 2002, with retrospective effect from April 1, 2001, substituting the words "the tax payable for the relevant deemed year shall be 7.5% of the book profit"[24] for the words "such book profit shall be deemed as total income of an assessee and the tax payable by the assessee for the total income shall be the amount of 7.5%".[25]

The main difference between the initial and amended provision is that the former provided for an obligation to pay tax on 7.5 percent of the book profits without deeming book profits to be total income.[26] The MAT rate was initially fixed at 7.5 percent of book profits but has gradually been increased to 18.5 percent by the Finance Act, 2011.[27] As of 2005, §115JB does not apply

18 Finance Act, 1990, w.e.f. Assessment Year 1991-2.
19 Finance Act, 1996, w.e.f. Assessment Year 1997-8.
20 ITA, §115JA.
21 ITA, §115JAA(3).
22 Finance Act, 2000, w.e.f. Assessment Year 2001-2.
23 ITA, §80VVA, §1115J, §115JA.
24 Finance Act, 2002, w.e.f. Assessment Year 2003-4.
25 *Id*.
26 VN Mittal & Varsha Likhite, *Are MAT Companies Liable to Pay Advance Tax?*, August, 2009, available at http://www.bcasonline.org/articles/artin.asp?891 (Last visited on November 15, 2011).
27 Finance Act, 2011, w.e.f. Assessment Year 2012-13 (From 2001-2007, the MAT rate was 7.5 percent, then from 2007-2010, it was 10 percent. It was then increased to 15 percent in 2010-2011, and finally is 18 percent for the year 2011-12).

to the income from any business carried on in or any services rendered by a company in a Special Economic Zone.[28]

IV. MINIMUM ALTERNATE TAX UNDER §115JB

Under the provisions of the ITA, every company, domestic or foreign, is required to pay MAT. As per §115JB, where the income tax computed under the Act in respect of any previous year relevant to the assessing year, is less than 18.5 percent of its book profits, such book profit shall be deemed to be the total income of an assessee and tax payable on such total income shall be 18.5 percent of the same.[29] The term book profit has been defined in the ITA itself. Book profit means the net profit as shown in the profit and loss account for the relevant previous year as determined by the provisions of Parts II and III of Schedule VI to the Companies Act, 1956, with certain positive and negative adjustments.[30]

The objective of making these positive and negative adjustments with net profit is to ascertain the true and genuine profit of the company. Under the Companies Act, this profit and loss account must be maintained as per provisions of the said Act and be presented before its shareholders at its annual general meeting. As this is the basis on which investments in the company are made, there is a low chance of the company manipulating this account to show a lower profit and making investment in the company less attractive. Certain important features and controversial provisions of the current MAT regime are explained below.

A. CONSTITUTIONALITY OF THE MAT REGIME

At the outset, it would be relevant to analyse the constitutional validity of the MAT. Several arguments have been raised against the constitutionality of MAT. First, it has been argued that by leaving it to the government to decide what constitutes 'deemed income', the provision may suffer from potential arbitrariness in the exercise of this power by the government. In addition, it only singles out the 'zero-tax companies' for the purpose of taxation under MAT, thereby ignoring the fiscal burden discharged by them generally.

---

28 ITA, §115JB(6).

29 Finance Act, 2011 w.e.f. Assessment Year 2012-13. In addition, companies are also liable to pay surcharge if their total income exceeds Rs. 1 crore. The surcharge rate, as amended by Finance Act, 2011, for domestic companies and companies other than domestic companies, *i.e.*, foreign company is 5 percent and 2 percent of such income tax respectively. Like other assesses, companies also pay education cess @ 3 percent.

30 ITA, Explanation 1 to §115JB.

In a number of decisions, however, courts have rejected any such constitutional challenge to the MAT provisions.[31]

B. MAT CREDIT

MAT credit is a beneficial provision for companies based on principles equity. In a given assessing year, when a company pays tax under the MAT provisions as opposed to the general provisions of the ITA, the excess of tax so paid over and above the tax payable under the general provisions of the Act, accrues as tax credit to the company.[32] Thus, MAT credit is the difference between the tax calculated under the provisions of MAT and the tax calculated under the general provisions of the ITA (*i.e.*, normal tax liability). Such credit is allowed to be carried forward and set-off against the income tax liability in an assessment year in which the company is liable to pay tax under the general provisions of the ITA (and not under the MAT provisions), to the extent of such tax payable over and above the book profits in that assessment year. MAT credit can be carried forward and set-off for ten assessment years immediately succeeding the assessment year in which the tax credit was first computed.[33] Thus, companies must always calculate their normal tax liability and their liability under the MAT and pay whichever is higher. If, however, the company pays MAT in an assessment year, then it can avail of credit over and above normal tax liability. This means that in no year will the company pay tax less than the MAT tax rate. The table below shows how MAT credits accrue to companies and how they may be set-off:

Assessment Year	Tax under the general provisions of the ITA i.e. normal tax liability	Tax payable under §115JB, i.e. MAT	Tax payable by the company	MAT credit	MAT Credit Set-off	MAT Credit Carried forward
2008-09	100	120	120	20	-	20
2009-10	150	160	160	10	-	20+10= 30
2010-11	200	190	190	-	10	10+10= 20
2011-12	300	200	280	-	20	-

31 Karimtharuvi Tea Estates Ltd. v. Deputy Commissioner of Income Tax, 247 ITR 22 (Ker); Suryalatha Spinning Mills Ltd. v. Union of India, 223 ITR 713 (AP); National Thermal Power Corporation Ltd. v. Union of India, 192 ITR 187 (Del).

32 ITA, §115JAA.

33 ITA, §115JAA(3A).

C. ADVANCE PAYMENT OF TAX

Under the ITA, every assessee is required to pay an advance tax on their income (*i.e.*, current income) if advance tax liability as computed in accordance with the provisions of Chapter XVII of the ITA, is Rs. 10,000 or more during the financial year.[34]

One of the interpretational quandaries that has arisen with respect to §115JB is whether companies that pay MAT are liable to pay advance tax. Companies that make default in the payment of advance tax are subject to penalties under §§234B and 234C of the ITA. The Karnataka High Court, in *Kwality Biscuits Ltd*. v. *Commissioner of Income Tax*, held that the penalties prescribed under §§234B and 234C do not apply where a company pays the MAT.[35] It held that since the exercise of computing income under §115JA can only be done at the end of a financial year, the provisions relating to advance payment of tax were not applicable. This is because until accounts are audited and balance sheets prepared, the assessee will not be able to determine whether §115JA is applicable or not.[36] The respondent filed a Special Leave Petition before the Supreme Court against this decision. The Supreme Court dismissed the petition through a non-speaking order on April 26, 2006.[37] This case has subsequently been followed in a number of disputes.[38] On the other hand, some courts have not shared the view of the Karnataka High Court and decided the issue against the assessee. For instance, in *Jindal Thermal Power Company Limited* v. *Deputy Commissioner of Income Tax*, the Karnataka High Court distinguished its own decision in *Kwality Biscuits* and held that §115JB is a self-contained code regarding the MAT liability of companies.[39] Therefore, where such companies defaulted in the payment of advance tax, they were liable for payment of penalties under §§234B and 234C of the ITA.[40] Finally, the Supreme Court in its speaking order dated January 7, 2011 has brought to an end the controversy, deciding that companies paying tax under the MAT provisions had to pay advance tax and were liable for penalties in case of default as per law.

---

[34] ITA, Chapter XVII.

[35] (2000) 243 IT 519 (Kar.).

[36] *Id*.

[37] Commissioner of Income Tax v. Kwality Biscuits Ltd., (2011) 2 SCC 415 :(2006) 284 IT 434 (SC).

[38] Deepak Fertilizers and Petrochemical Corporation v. Commissioner of Income Tax, 304 ITR (AT) 167; Snowcam India Limited vs. Deputy Commissioner of Income Tax, (2009) 313 ITR 170 (Bom.); Escapade Resorts Pvt. Ltd. v. Assistant Commissioner of Income Tax, [2007] 13 SOT 300; IBM India Ltd. v. Commissioner of Income Tax, 290 ITR (AT) 183 (Bangalore).

[39] (2006) 154 Taxman 547 (Kar).

[40] *Id*.

D. PROCEDURE OF INCOME TAX RETURNS

Every company to which MAT is applicable is required to furnish a report in the prescribed form (Form 29B) from an accountant as defined in the Explanation to §288, certifying that the book profits have been calculated in accordance with the provisions of MAT along with the return of income filed under §139(1) or along with the return of income pursuant to a notice send under §142(1)(i).[41] Accounting treatment of MAT is done according to the 'Guidance Note of Credit under MAT under the Income Tax Act'[42] issued by the Institute of Chartered Accountant of India (ICAI).

E. NON-APPLICABILITY OF MAT

The provisions of §115JB initially did not apply to income from any business carried on in or any services rendered by a company in a Special Economic Zone.[43] §115JB(6) was, however, amended by the Finance Act, 2011 and a proviso was added making the provisions of §115JB applicable even to Special Economic Zones with effect from April 1, 2012. Thus, even the Special Economic Zones which were enjoying immunity from MAT so far have been subjected to MAT from 2012.

V. MAT UNDER THE DIRECT TAX CODE BILL, 2010

The Direct Tax Code Bill as introduced in the Lok Shabha on August 30, 2010, aims to replace ITA and improve the efficiency and equity of the direct tax system by eliminating distortions in tax structure, introducing moderate levels of taxation and expanding the tax base.[44] The numerous amendments to the ITA and multitude of judgements, often conflicting, have made the ITA very complicated for the tax payers and the department. Given that the cost of compliance is essentially regressive in nature, the equity of the tax system is undermined. The DTC seeks to move towards a simplified and rational regime for direct taxes.

The provisions relating to MAT are, however, largely similar to those in the current ITA. The current draft of the DTC Bill provides, *inter alia*, for the levy of MAT on companies at the rate of 20 percent of the book profits

---

41 ITA, §115JB(4).

42 Institute of Chartered Accountant of India, Guidance Note on Accounting for Credit Available in respect of Minimum Alternative Tax Under The Income-Tax Act, 1961, available at http://www.icai.org/post.html?post_id=1407 (Last visited on November 15, 2011).

43 ITA, §115JB(6).

44 The Direct Tax Code Bill, 2010, available at http://164.100.24.219/BillsTexts/LSBillTexts/asintroduced/DTC%20(110%20of%202010)%20To%20be.pdf (Last visited on November 15, 2011).

of the company without any surcharge and cess.[45] §105 provides that companies must maintain a profit and loss account in accordance with the provisions of the Companies Act and that such an account shall be treated as the book profit of that company.[46]

The DTC also includes a provision for MAT credit. While the initial draft of the DTC did not contain any provision for MAT credit, the current draft, in §106(4), provides that MAT credit accrues to a company in a financial year in which a company is liable to pay tax under MAT. This credit can be carried forward and set-off for five financial years immediately succeeding the financial year in which the credit was first computed. Under §205, the DTC also provides for the payment of advance tax with respect to the total income, if such tax is more than ten thousand rupees during any financial year. §205(2) provides for the calculation of advance tax. Moreover, §205(4) provides that a company is liable to pay this advance tax in four instalments according to the schedule prescribed therein.

VI. PROBLEMS WITH THE CURRENT MAT REGIME

As discussed above, MAT was first introduced in the ITA in order to address the problem of zero-tax companies by ensuring that such companies pay an adequate amount of tax to the government. The regime has, however, made the ITA more complicated, leading to high cost of compliance and administration. Some of these problems are analysed below.

A. EFFECT ON EARNINGS MANAGEMENT PRACTICES - DIFFICULTIES IN COMPLIANCE

As outlined above, the introduction of MAT requires companies to calculate their taxable income by both the general provision of the ITA and by the provisions of the Companies Act relating to calculation of book profits. This increases the costs for record-keeping and compliance on companies. When the AMT was introduced on companies in the US, studies showed that firms spent 18 percent more on compliance costs where such tax was applicable to them.[47] In India as well, MAT is identified as a 'legal hot spot' that increases costs of compliance.[48]

---

45 Direct Tax Code Bill, 2010, §104(1) and the Second Schedule, available at http://164.100.24.219/BillsTexts/LSBillTexts/asintroduced/DTC%20(110%20of%202010)%20To%20be.pdf (Last visited on November 15, 2011).

46 *Id*., §105.

47 M. Gujarathy & S.K. Barua, *Minimum Alternate Tax in India: Lessons to be Learnt from the Foreign use of Alternate Minimum Tax*, 24 Int'l Tax J. 65 1998.

48 Arindam Dasgupta, *The Income Tax Compliance Cost of Corporations in India*, 2000-01, available at http://ssrn.com/abstract=466041 (Last visited on November 15, 2011).

This is further complicated by the fact that all companies that are liable to be taxed under §115JB are also liable for payment of advance tax.[49] Therefore, these two sets of accounts must be maintained and submitted periodically by a company over the year and under §§234B and 234C, they can be subject to penalties for default of such payments.[50]

In addition, liability under the MAT has prompted companies to post lower profits by changing their accounting policies.[51] These accounting practices would undoubtedly have an adverse impact on companies, investors and stakeholders because displaying lower book profits lowers their reputation with the potential investors and shareholders do not receive adequately accurate information regarding the financial operation of the company.

B. ECONOMIC CONSEQUENCES – THE ECONOMIC BURDEN OF MAT

Another problem with the MAT is that it creates unintended adverse effects on investment. Some companies that show 'zero' or low tax liability are highly capital intensive and are able to avail of tax deductions through depreciation of machinery and goods in the initial years. These companies make high investments and are crucial to the economy and in providing employment. These companies also pay high indirect taxes like customs duty, excise and VAT.[52] Due to the introduction of MAT, however, these companies are faced with a higher tax burden. This in turn disincentives high investment in capital goods, which is crucial for economic growth.[53] Moreover, previously under §115JA, profits derived by industrial undertakings from the business of developing, maintaining and operating any infrastructure facility covered by §80-IA, was exempted from computing book profits. Under the current §115JB, however, this exemption has been removed.

Further, companies with low depreciation (like finance companies) but who are making consistent losses will have to pay MAT despite heavy carry forward losses.[54] Companies with high depreciation will be liable for MAT in the year in which there is net profit after depreciation irrespective of the fact of heavy unabsorbed depreciation.[55]

49 Central Board of Direct Taxes, *Circular on Section 115JA/115jb/Minimum alternate tax (No. 13 of 2001)*, November 9, 2001.
50 ITA, §234B and §234C.
51 *Money Illusion*, Economic Times, May 13, 1997.
52 Ganesh Raj, *Mat: A Strong Case for Abolition*, Mint, June 25, 2009.
53 *Id*.
54 *Id*.
55 *Id*.

C. OTHER DIFFICULTIES IN THE COMPUTATION OF MAT

The co-existence of deemed total income (book profits under the Companies Act) along with the statutory income calculated under the ITA, has itself been a source of confusion for the assesses and the revenue authorities.

One such example is with respect to §80HHC. §80HHC provides for the deduction of an amount equivalent to 80 percent of the 'eligible profits' from the exports, from the gross total income. Under §115JB, however, one of the deductions that could be made from the book profit was on the 'eligible profit from exports' as computed under §80HHC(3)(a)/(b)/(c) and under §80HHC(3A). The dispute that arose was with respect to the position taken by the revenue authorities, whereby they claimed that the amount deductible under §80HHC from the gross income, should also be the amount that can be deducted from the book profit (as opposed to the deduction of 'eligible profit' from the book profits). The dispute was, however, settled by the Supreme Court in *Ajanta Pharma Ltd* v. *CIT*,[56] whereby it made a distinction between the computation of 'eligible profits' that could be deducted from the book profits and the 'amount of deduction allowed' under §80HHC (which is a certain percentage of the eligible profits) for the purpose of the gross total income.[57]

VII. SUGGESTIONS FOR REFORM

As shown above, the MAT regime has raised significant problems in terms of the burden of tax and the difficulties in compliance and record-keeping. Companies are required to maintain two sets of accounts and submit them periodically in order to pay advance tax. It is a basic canon of taxation law that procedure of taxation must be certain and clear.[58] The present MAT regime falls short in this regard. Further, in some cases, the MAT is an excessive burden on companies. Moreover, the provisions of the proposed DTC also eliminate a number of exemptions, deductions and incentives, which are available under the ITA. Unfortunately, MAT has emerged as an imperfect solution to an imperfect system of unmanaged tax deductions.

In order to address the problems of the present complex and irrational corporate taxation regime (MAT), this paper proposes two solutions. The first is to abolish MAT and reduce the tax incentives and make the depreciation

---

[56] (2010) 9 SCC 455 : [2010] 327 ITR 305 SC.

[57] Dev Kumar Kothari, *Supreme Court Decision on §115JB in Ajanta Pharma Ltd. and its applicability after phasing out of §80 HHC: An Analysis*, available at http://www.bcasonline.org/articles/artin.asp?963 (Last visited on November 5, 2011).

[58] Smith, *supra* note 1 ("The tax which each individual is bound to pay, ought to be certain, and not arbitrary. The time of payment, the manner of payment, the quantity to be paid, ought all to be clear and plain to the contributor and to every other person").

provisions (depreciation rate) in the ITA or DTC at par with the Companies Act and to continue with the ITA or DTC as the case may be. The second is to have a separate legislation for corporate taxation based solely on book profits. Certain incentives can, however, be provided to certain particular sectors if the State desires. These two proposals are explored in further detail below.

A. ABOLITION OF MAT AND REDUCTION OF SUBSIDIES AND INCENTIVES

The problem of 'zero-tax' companies is a result of the reduction in the tax base of certain companies because of exemptions, deductions and allowing high rates of depreciation for certain industries. One way to address this problem is to increase the tax base of companies so that their taxable income increases. The high rate of depreciation under the ITA, for instance, is a significant cause for the reduction of tax base. Depreciation can be claimed by any company irrespective of its output or location, and hence, covers a greater number of companies than Special Economic Zones, tax holidays or export promotion measures. The rate of deprecation under the ITA is much higher than the rate of depreciation that can be claimed under the Companies Act. The tax base can be significantly increased if the rate of depreciation is brought on par with that in the Companies Act.

In addition, the number and extent of deductions and exemptions given to companies should be reduced. The Kelkar Committee has also recognised this as a problem, and has suggested that the MAT regime be abolished and the procedure for taxation be simplified by a reduction in the exemptions and deductions granted to companies.[59] Similar arguments for reform have been made in the American AMT system.[60]

These changes will result in an increased tax base and a reduction in the amount of exemptions that companies may avail of and thus, address the problem of zero-tax companies without resorting to a MAT system.

---

59 Report of the Task Force on Direct Taxes, November 2, 2002, available at www.finmin.nic.in/kelkar/Full_Report.pdf (Last visited on November 5, 2011) (which recognises that "the present scheme of corporate income tax is riddled with a large number of deductions and exemptions. As a result, the base is considerably lower than the book profit declared to shareholders. In effect, this has led to a non-transparent tax subsidy regime, complexity of the tax law, revenue loss, increased compliance cost and has encouraged rent seeking behaviour").

60 Andrew B. Lyon, Cracking the Code: Making Sense of the Corporate Alternative Minimum Tax (which argues that reducing deductions to increase tax base would simplify the procedure for corporate taxation); Janiga *supra* note 5 (which argues that a deductions, credits and exclusions which originally generated the tax avoidance problem should be removed).

B. A SEPARATE ACT FOR CORPORATE TAXATION BASED ON BOOK PROFITS

As discussed above, one of the main difficulties with MAT is the maintenance of two different sets of accounts for determining taxable income. These two accounts, moreover, must be submitted periodically for the payment of advance tax as well as at the time of filing final income tax return. Thus, the corporate taxation regime has become much more complicated and irrational. The corporate taxation regime can be simplified and made more rational, either by eliminating MAT and simplifying the existing ITA with less deductions, incentives and with broad tax base or to scrap the ITA, as is applicable to companies, and to have separate legislation for corporate taxation based only on book profits. This would have the advantage of reducing the confusion and cost of compliance with MAT and further, streamline the regime of corporate taxation and bring about convergence of these two systems. The regime can, however, be modified to allow certain tax incentives in the form of deductions, exemptions in order to promote a particular sector of an industry or backward region. This would have the advantage of being a simpler and more transparent procedure for corporate taxation.

In conclusion, considering the inflow of foreign direct investment in India and the growth of domestic companies, both in size and revenue, it would be more efficient to have a separate legislation on corporate taxation based on book profits. If, however, there is any need to promote a particular sector of industry or a backward region, additional negative adjustment may be provided while calculating book profit.