DENIAL OF CARRIED FORWARD MAT CREDIT TO COMPANIES OPTING FOR CONCESSIONAL RATE OF 22% - DISCRIMINATION AND BREACH OF PROMISE

The Taxation Laws (Amendment) Ordinance, 2019 has inserted two new sections 115BAA and 115BAB to provide an option for domestic companies to pay tax concessional rate of taxes of 25.17 per cent and 17.16 per cent respectively inclusive of surcharge and health and education cess. The option to pay tax at concessional rate of 25.17 per cent under new section 115BAA will be available to all domestic Companies whereas the option to pay tax at concessional rate of 17.16 per cent will be available only to new domestic companies that are set up and registered on or after 1st October 2019 and are engaged solely in the business of manufacturing or production of any article or thing.

Post this Ordinance, there was some confusion going on as to whether the credit of carried forward MAT credit against the new rate of 22 per cent will be allowed or not to a company which opts for new rate of 22 per cent. There is no bar or restriction in the Ordinance for claiming such MAT credit. The Ordinance has amended only section 115JB relating to MAT on Book Profit by inserting a new sub clause (ii) in sub section (5A) to provide that the provision of section 115JB i.e. MAT shall not be applicable to a company which has exercised the option to be taxed at the rate of 22 per cent under this new section 115BAA. There is no reference to MAT credit. This credit of carried forward MAT is allowed under section 115JAA. No amendment is made in this section 115JAA by the Ordinance so as to restrict such credit in any manner. As per this section 115JAA, credit is allowed of tax paid under MAT i.e. section 115JB of the difference between the tax payable by the assessee on his total income in the subsequent year and the MAT liability of that subsequent year.

The CBDT has now issued a circular no 29/2019 dated 2nd October, 2019, clarifying that the benefit of MAT Credit will not be allowed to those companies which opt for new tax rate of 22 per cent under Section 115BAA. It has advised such companies having MAT credit to continue under existing rates i.e. 30 per cent if its turnover exceeds Rs. 400

crores in FY 2017-18 or 25 per cent if its turnover does not exceed Rs. 400 crores, in case it intends to avail MAT credit. The implication of this will be that a company will be required to compute its tax liability at the effective rate, which will be 34.94 per cent for companies having turnover more than 400 crores and 29.12 per cent for companies whose turnover does not exceed Rs. 400 crores, and liability on account of MAT which under new rate of MAT will be 17.47 per cent. The difference of these two i.e. 17.47 per cent (34.94-17.47) or 11.65 per cent (29.12-17.47), as the case may be, will be eligible for adjustment with carried forward MAT credit. This will compel companies having substantial MAT credit to continue under the old rates.

Thus, apparent net benefit to a company, whose turnover exceeds Rs. 400 crores, having MAT credit after this Circular will be that such company will be able to take credit of 17.47 per cent instead of 13.39 per cent (34.94-21.55) presently available against its tax liability on the tax rate of 34.94 per cent applicable to it. Thus, such companies will save net 4.08 per cent outgo in tax. To this extent of 4.08 per cent, there will be faster adjustment of MAT credit. This benefit is arising as MAT rate for all companies have been reduced from 18.5 per cent (effective rate after including surcharge and Cess being 21.55 per cent) to 15 per cent (effective rate being 17.47 per cent). Further, such companies shall continue to have benefits of all exemptions and incentives also as these will continue to be governed by old provisions. After exhausting MAT credit, such company shall be eligible to opt for reduced rate of 22 per cent (effective tax rate of 25.17 per cent).

The above benefit may be apparently good. But in substance, there is a discrimination against such companies which are having carried forward MAT credit vis-à-vis companies which don’t have such carried forward MAT credit. A company without carried forward MAT Credit will be paying tax at the rate of 25.17 per cent as against 34.94 per cent to be paid by a company which has MAT credit. There is a net saving of 9.77 per cent in tax rate to a company which does not have MAT credit. As against this, a company with MAT credit either will have to forego/ surrender all the carried forward MAT credit, which is valuable asset with it, or such company will be compelled to pay tax at the rate of 34.94 per cent to avail MAT credit which otherwise is its asset. Thus, in one option, entire carried forward MAT is lost and in the other option, carried forward MAT credit (being carried as an asset) gets utilized against higher 9.77 per cent tax liability (34.94-25.17) which otherwise would not have been payable had this company be allowed to opt for new rates. In substance, carried forward MAT credit asset to the extent of 9.77 per cent of income every year virtually will get written off/ adjusted and only remaining 7.70 per cent will be real benefit of MAT credit asset to such companies. Further, this benefit of 7.70 credit will be available only to the extent of credit left after first adjusting 9.77 towards the rate difference. Thus, in percentage terms, the real benefit of total amount of carry forward MAT asset will only be 44.07 per cent approximately (7.70/17.47*100). This means a company having MAT credit asset say of Rs 100 crores will get real benefit of such MAT credit of Rs 44.07 crore only and Rs 55.93 crore asset will get set off against difference in tax rates as this company shall be required to pay tax at the rate of 34.94 per cent as against 25.17 per cent.

For better understanding the implication of the above analysis, take a case of a company having taxable income and also book profit of Rs 100 crore with carried forward MAT credit of 8 crore. The tax liability on regular income of Rs 100 crore will be 34.94 crore and MAT liability on same as book profit will be 17.47 crore. Thus, this company can avail credit of the difference of the two i.e. 17.47 crore restricted to actual MAT credit available which is 8 crore. If it does so and doesn't opt for the new tax rate, it will end up paying tax of 26.94 crore (Rs 34.94 - 8.00) as against Rs 25.17 crore payable under the new rate. Since by not opting to go for new rates for availing carried forward MAT credit, it has to pay tax more than which it would be liable had it opted to surrender MAT credit, it will be compelled to opt for new rates and forego and write off the carried forward MAT asset of Rs 8 crore and pay tax of Rs 25.17 crore. Thus, the carried forward MAT credit as an asset stands discounted at least to the extent of 55 per cent and in some cases, such percentage may be more than 55 per cent as can be seen from the above example. Accordingly, all such companies carrying MAT credit as asset and falling in this situation will have to write off the MAT credit and take a hit on its profit and many such companies may end up with negative profit after tax (PAT).

The impact of denial of carried forward MAT credit in respect of other companies which at present are being assessed on the basis of its turnover and income amount at different rate can be understood from the following table:

Income	**Tax liability under normal provisions**	**MAT liability under section 115JB**	**Effective tax liability**	**Effective tax liability under section 115BAA**	**Virtual benefit on adjustment of carried forward MAT credit**	**Real Benefit on adjustment of carried forward MAT credit**
	A	**B**	**C=A-B**	**D**	**E=A-D**	**F=D-C**
Domestic Companies whose turnover in Previous Year 2017-18 exceeds Rs. 400 crores						
Upto Rs. 1 crore	31.2%	15.6%	15.6%	25.17%	6.03%	9.57%
More than Rs. 1 crore but upto Rs. 10 crores	33.38%	16.69%	16.69%	25.17%	8.21%	8.48%
More than Rs. 10 crores	34.94%	17.47%	17.47%	25.17%	9.77%	7.70%
Domestic Companies whose turnover in Previous Year 2017-18 does not exceed Rs. 400 crores						
Upto Rs. 1 crore	26.00%	15.6%	10.40%	25.17%	0.83%	14.77%
More than Rs. 1 crore but upto Rs. 10 crores	27.82%	16.69%	11.13%	25.17%	2.65%	14.04%
More than Rs. 10 crores	29.12%	17.47%	11.65%	25.17%	3.95%	13.52%

This apparently is a discrimination as when MAT was paid by the taxpayer to the Government, there was a promise made in law that such MAT paid will be available as credit against its future regular tax liability. Now by enacting a law in a manner as stated in the Circular, virtually this promise is not being kept. It may be difficult to challenge this restriction of claiming credit of carried forward MAT credit on the doctrine of promissory estoppel as there cannot be promissory estoppel against the exercise of legislative power. However, such restrictions do create uncertainty in the minds of taxpayer as to whether the advantage/benefit promised under the law today will be honored by the Government tomorrow or not.

Restricting MAT credit in this manner as stated in the Circular as analysed hereinabove may not be appropriate. Ideally, credit of carried forward MAT should be allowed to be adjusted in full as MAT is a carried forward asset. However, in case Government has a concern that with full MAT credit, many companies will end up paying zero tax this year after adjusting regular tax liability against carried forward MAT credit and fiscal deficit may get wider, it may consider allowing carried forward MAT on staggered basis every year to the extent a company would have claimed carried forward credit had MAT been payable by such companies i.e. 7 per cent (22 per cent-15 per cent) instead of denying option of tax rate of 22 per cent to such companies. This way Government will be able to collect taxes to the extent of MAT rate and there will be no discrimination and companies will be able to avail full credit though over a longer period.

As regards the apprehensions that this Circular denying MAT credit at present may not be legally in consonance with the provisions stated in Ordinance, the same may be correct. However, legal challenge to the Circular will not be sustainable as Government has to introduce and get the Bill passed in the parliament to replace this Ordinance. While introducing and passing the Bill in winter session of the Parliament, the Government will amend the Ordinance and insert specific provision in the Bill denying MAT credit if a company exercises option of new concessional rate of 22 per cent. Once such Bill is passed by the Parliament and notified in the Gazette, the Circular obviously will have legal backing of such Act.