

IN THE INCOME TAX APPELLATE TRIBUNAL
COCHIN BENCH, COCHIN
BEFORE S/SHRI CHANDRA POOJARI, AM&GEORGE GEORGE K., JM

ITA Nos. 60 & 61/Coch/2015
Assessment Year: 2006-07

Aspinwall and Company Limited, 926/AI-A5, Total Towers, Devankulangara, Edapally, Kochi-682 024. [PAN: AACCA 2655G]	Vs.	The Assistant Commissioner of Income-tax, Circle-1(1), Kochi.
(Assessee -Appellant)		(Revenue-Respondent)

ITA No. 128/Coch/2017
Assessment Year: 2012-13

Aspinwall and Company Limited, 926/AI-A5, Total Towers, Devankulangara, Edapally, Kochi-682 024. [PAN: AACCA 2655G]	Vs.	The Assistant Commissioner of Income-tax, Circle-1(1), Kochi.
(Assessee -Appellant)		(Revenue-Respondent)

ITA No. 133/Coch/2017
Assessment Year: 2012-13

The Deputy Commissioner of Income-tax, Circle-1(1), Kochi.	Vs.	Aspinwall and Company Limited, 926/AI-A5, Total Towers, Devankulangara, Edapally, Kochi-682 024. [PAN: AACCA 2655G]
(Revenue-Appellant)		(Assessee-Respondent)

Assessee by	Shri Raja Kannan, Adv.
Revenue by	Shri Mritunjaya Sharma, Sr. DR

Date of hearing	05/03/2020
Date of pronouncement	19/05/2020

ORDER

Per CHANDRA POOJARI, AM:

The appeals filed by the assessee in ITA Nos. 60& 61/Coch/2015 and 128/Coch/2017 are directed against different orders of the CIT(A) and pertain to the assessment year 2006-07 and 2012-13. The Revenue has also filed appeal in ITA No.133/Coch/2017 for the assessment year.

2. Since the issues involved in these appeals are common, they were heard together and are being disposed of by this common order.

ITA No. 133/Coch/2017: Revenue's Appeal : AY 2012-13

3. At the time of hearing, the Ld. DR filed a letter dated 05/03/2020 stating that the tax effect in this appeal is less than the monetary limit prescribed in the CBDT's Circular No. 17/2019 vide F.No.279/Misc/14 dated 08/08/2019. Hence, the Ld. DR pleaded for withdrawal of the appeal. Accordingly, we dismiss the appeal of the Revenue as withdrawn.

ITA No. 60/Coch/2015 :Assessee's Appeal : AY 2006-07

The assessee has raised the following grounds of appeal:

1. The learned Commissioner of Income Tax (Appeals) [CIT(A)] erred in confirming the disallowance of Interest amounting to Rs. 18,43,500/- under Section 14A of the Income Tax Act, 1961 r.w.r 8D of the Income Tax Rules, 1962.
 2. The learned CIT (A) ought to have observed that the appellant has not incurred any expenditure to earn exempt income of Rs. 6,59,278/-.
 3. The learned CIT (A) ought to have observed that the investments from which the exempt income has earned are made either before 2002 or taken over on amalgamation of erstwhile The Pullangode Rubber and Produce Company Limited, on account of amalgamation of the company with Appellant w.e.f 01.01.2006.
 4. The learned CIT(A) ought to have noted that the Rule 8D is not applicable for A.Y. 2006-07, as the same was inserted vide Finance Act, 2008 and hence would apply prospectively. In this regard, reliance is placed on the decision of the High Court of Bombay in the case of Godrej and Boyce Mfg. Co. Ltd vs. Deputy Commissioner of Income Tax [2010] 328 1TR 008.
 5. The learned CIT (A) ought to have observed that the interest bearing funds of Rs. 22,17,68,481/- as on 31st March 2006 were availed by the appellant after the year 2002 and hence there is no nexus between interest bearing funds and exempt income yielding investments.
 6. The learned CIT (A) ought to have observed from the records that there were sufficient own funds available with the appellant for making the said investments. In this regard, reliance is placed on the decision of the High Court of Bombay in the case of CIT Vs. Reliance Utilities & Power Limited reported in 313 ITR 340.
3. The facts of the case are that the assessee earned exempt income of Rs.6,59,278/- and against total investment of Rs.4,17,46,194/- in the mutual funds of the sister concerns, the interest bearing funds were to the tune of Rs.22,17,68,481/-. Since assessee had huge interest bearing funds and investments were made in the mutual funds of sister concerns from where tax dividend was also earned, the

Assessing Officer disallowed interest amounting to Rs.18,43,500/- under section 14A r.w.r. 8D of the Income Tax Rules, 1962.

4. On appeal, the CIT(A) observed that exact dates and documentary evidence to show that investments were made out of surplus funds were not furnished. According to the CIT(A), the year and analysis of cash flow does not establish that the investment was made from any surplus funds, till the same is shown with relation to any sequential cash flow alongwith any identifiable bank transactions. The CIT(A) observed that the incidental administrative expenses relating to earning of income are imbedded in the indirect expenses and thus, there was a cost inbuilt into the passive investments. The CIT(A) relied on the judgment of the Punjab & Haryana High Court in the case of CIT vs. Abhishek Industries Ltd. (286 ITR 1) wherein it was held that the onus to prove that there was no nexus between the borrowed funds and investment in sister concerns, was on the assessee. The CIT(A) also relied on the judgment of the Kerala High Court in the case of CIT vs. V.I. Baby & Co. (254 ITR 248). The CIT(A) held that disallowance can be more than earned income by placing reliance on the CBDT Circular No. 5/2014 dated 11.02.2014 wherein it was stated that provisions of section 14Ar.w. rule 8D would be applicable even in a year in which taxpayer has not earned any exempt income. Thus, the CIT(A) confirmed the action of the Assessing Officer in invoking the provisions of section 14A r.w. Rule 8D and making disallowance of Rs.18,43,500/-.

5. Against this, the assessee is in appeal before us. The Ld. AR submitted that the provisions of sub-section (2) and (3) of section 14A were inserted by the Finance Act, 2006 with effect from April 1, 2007. Hence, it was submitted that the provisions of sub-section (2) and (3) of section 14A of the Act are operative only from AY 2007-08. Accordingly, it was submitted that Rule 8D which has been prescribed under sub-section (2) would also be applicable from AY 2007-08. In view of the above, it was submitted that Assessing Officer could not determine expenses attributable to earning of exempt income, which is governed by the provisions of sub-section (2) and (3) of section 14A, as the same were not applicable for the year in question. For this proposition, the relied on the following judgments:

- i) Vidyut Investments Ltd. vs. ITO (10 SOT 284) (Delhi Trib.)
- ii) Dhanalakshmi Bank Ltd. vs. ACIT (12 SOT 625) (Cochin Trib.)

5.1 Further, the Ld. AR submitted that section 14A was introduced with the intent to disallow those expenses which have nexus to tax free/exempt income. The Ld. AR submitted that for the purpose of application of provisions of section 14A of the Act, nexus between the expense and the income is the first and foremost condition to be satisfied. It was submitted that the investments were made prior to 2004 and were acquired on account of amalgamation of the assessee company with Pullangode Rubber & Produce Company Ltd. and Aspinwall & Co. (Travancore) Ltd. during the financial year 2005-06. Hence, it was submitted that there was no nexus between borrowed funds and investments. It was submitted that the Assessing Officer has not recorded his dissatisfaction with the claim made by the assessee that no expenditure

was incurred in relation to income which does not form part of total income. Regarding propriety of business decisions, the Ld. AR submitted that the business man is the best judge of its business expediency and that the Assessing Officer can only question whether expenditure is real, whether it is related to the business and is wholly spent for that purpose and not otherwise. For this, the Ld. AR relied on the following judgments:

- 1) CIT vs. Dalmia Cement (P) Ltd. (254 ITR 377) (Delhi)
- 2) CIT vs. M/s. Walchand & Co. (Pvt.) Ltd. (65 ITR 381 (SC)
- 3) CIT vs. M/s. Edward Keventer (Private) Ltd. (115 ITR 149) (SC)

5.3 The Ld. AR submitted that disallowance computed u/s. 14A should not exceed the exempt income earned during the year under consideration. In this context, the Ld. AR relied on the following judgments:

- i) Joint Investments Pvt. Ltd. vs. CIT (59 taxmann.com 295) (Delhi)
- ii) Daga Global Chemicals Pvt. Ltd. vs. ACIT (ITA No.5592/Mum/2012 dated 01/01/2015) (Mum Trib.)

6. The Ld. DR relied on the orders of the lower authorities.

7. We have heard the rival submissions and peruse the record. In this case, the assessment year involved is 2006-07. Rule 8D was introduced with effect from 24/03/2008 which was prospective in operation and cannot be applied retrospectively as held by the Delhi High Court in the case of Maxopp Investment Ltd. vs. CIT (347 ITR 272) wherein it was held as follows:

"Section 14A was inserted by the Finance Act, 2001, with retrospective effect from April 1, 1962. Prior to the introduction of section 14A, the law was that when an assessee had a composite and indivisible business which had elements of both taxable and non-taxable income, the entire expenditure in respect of the business was deductible and, in such a case, the principle of apportionment of the expenditure relating to the non-taxable income did not apply. However, where the business was divisible, the principle of apportionment of the expenditure was applicable and the expenditure apportioned to the "exempt" income or income not exigible to tax, was not allowable as a deduction. Sub-section (1) of section 14A clearly stipulates that for the purposes of computing the total income under Chapter IV, no deduction shall be allowed in respect of expenditure "incurred" by the assessee "in relation to" income which does not form part of the total income under the Act. The expression "in relation to" is, ordinarily, of wide import. In the normal course, the expression would have an expansive meaning unless, of course, the context would otherwise suggest. The context does not suggest that a narrow meaning ought to be given to the expression. The provision was inserted by virtue of the Finance Act, 2001, with retrospective effect from April 1, 1962. In other words, it was the intention of Parliament that it should appear in the statute book, from its inception, that expenditure incurred in connection with income which does not form part of total income ought not to be allowed as a deduction. The factum of making the provision retrospective makes it clear that Parliament wanted that it should be understood by all that from the very beginning, such expenditure was not allowable as a deduction. Of course, by introducing the proviso it made it clear that there was no intention to reopen finalised assessments prior to the assessment year beginning on April 1, 2001.

The expression "in relation to" does not have any embedded object. It simply means "in connection with" or "pertains to". If the expenditure in question has a relation or connection with or pertains to exempt income it cannot be allowed as a deduction even if it qualifies under other provisions of the Act. The actual expenditure that is in contemplation under section 14A(1) of the Act is the "actual" expenditure in relation to or in connection with or pertaining to exempt income. The corollary to this is that if no expenditure is incurred in relation to the exempt income, no disallowance can be made under section 14A of the Act.

Sub-sections (2) and (3) were inserted by the Finance Act, 2006, with effect from April 1, 2007. However, the expression "such method as may be prescribed" got meaning only by the introduction of rule 8D of the Income-tax Rules, 1962.

Sub-section (2) of section 14A of the Act provides the manner in which the Assessing Officer is to determine the amount of expenditure incurred in relation to income which does not form part of the total income. The requirement of the

Assessing Officer embarking upon a determination of the amount of expenditure incurred in relation to exempt income would be triggered only if the Assessing Officer returns a finding that he is not satisfied with the correctness of the claim of the assessee in respect of such expenditure. Therefore, the condition precedent for the Assessing Officer entering upon a determination of the amount of the expenditure incurred in relation to exempt income is that the Assessing Officer must record that he is not satisfied with the correctness of the claim of the assessee in respect of such expenditure.

Sub-section (3) is nothing but an offshoot of sub-section (2) of section 14A. Sub-section (3) applies to cases where the assessee claims that no expenditure has been incurred in relation to income which does not form part of the total income under the Act. In other words, sub-section (2) deals with cases where the assessee specifies a positive amount of expenditure in relation to income which does not form part of the total income under the Act and sub-section (3) applies to cases where the assessee asserts that no expenditure had been incurred in relation to exempt income, in both cases, the Assessing Officer, if satisfied with the correctness of the claim of the assessee in respect of such expenditure or no expenditure, as the case may be, cannot embark upon a determination of the amount of expenditure in accordance with any prescribed method, as mentioned in sub-section (2) of section 14A of the Act. It is only if the Assessing Officer is not satisfied with the correctness of the claim of the assessee, in both cases, that the Assessing Officer gets jurisdiction to determine the amount of expenditure incurred in relation to such income which does not form part of the total income under the Act in accordance with the prescribed method. The prescribed method is the method stipulated in rule 8D of the Rules. While rejecting the claim of the assessee with regard to the expenditure or no expenditure, as the case may be, in relation to income, the Assessing Officer would have to indicate cogent reasons for the same. It is, therefore, clear that determination of the amount of expenditure in relation to exempt income under rule 8D would only come into play when the Assessing Officer rejects the claim of the assessee in this regard.

If one examines sub-rule (2) of rule 8D, the method for determination of expenditure in relation to exempt income has three components. The first component is the amount of expenditure directly relating to income which does not form part of the total income. The second is being computed on the basis of the formula given therein in a case where the assessee incurs expenditure by way of interest which is not directly attributable to any particular income or receipt. The formula essentially apportions the amount of expenditure by way of interest (other than the amount of interest included in clause (i)) incurred during the previous year in the ratio of the average value of investment, income from which does not or shall not form part of the total income, to the average of the total assets of the assessee. The third component is an artificial figure—one half

per cent, of the average value of the investment, income from which does not or shall not form part of the total income, as appearing in the balance-sheets of the assessee, on the first day and the last day of the previous year. It is the aggregate of these three components which would constitute the expenditure in relation to exempt income and it is this amount of expenditure which would be disallowed under section 14A of the Act. It is, therefore, clear that in terms of the rule, the amount of expenditure in relation to exempt income has two aspects— (a) direct, and (b) indirect. The direct expenditure is straightaway taken into account by virtue of clause (i) of sub-rule (2) of rule 8D. The indirect expenditure, where it is by way of interest, is computed through the principle of apportionment.

Section 14A even prior to the introduction of sub-sections (2) and (3) would require the Assessing Officer to first reject the claim of the assessee with regard to the extent of such expenditure and such rejection must be for disclosed cogent reasons. It is then that the question of determination of such expenditure by the Assessing Officer would arise. The requirement of adopting a specific method of determining such expenditure has been introduced by virtue of sub-section (2) of section 14A. Prior to that, the assessee was free to adopt any reasonable and acceptable method. So, even for the pre-rule 8D period, whenever the issue of section 14A arises before an Assessing Officer, he has, first of all, to ascertain the correctness of the claim of the assessee in respect of the expenditure incurred in relation to income which does not form part of the total income under the Act. Even where the assessee claims that no expenditure has been incurred in relation to income which does not form part of the total income, the Assessing Officer will have to verify the correctness of such claim. In case, the Assessing Officer is satisfied with the claim of the assessee with regard to the expenditure or no expenditure, as the case may be, the Assessing Officer is to accept the claim of the assessee in so far as the quantum of disallowance under section 14A is concerned. In such eventuality, the Assessing Officer cannot embark upon a determination of the amount of expenditure for the purposes of section 14A(1). In case, the Assessing Officer is not, on the basis of the objective criteria and after giving the assessee a reasonable opportunity, satisfied with the correctness of the claim of the assessee, he shall have to reject the claim and state the reasons for doing so. Having done so, the Assessing Officer will have to determine the amount of expenditure incurred in relation to income which does not form part of the total income under the Act. He is required to do so on the basis of a reasonable and acceptable method of apportionment.”

7.1 Accordingly, by placing reliance on the judgment of the Madras High Court in the case of Simpson and Company Ltd. in T.C. No. 26212/2006 dated 15/10/2012, we

direct the Assessing Officer to disallow only 2% of expenses incurred towards exempted income. Thus, this ground of appeal of the assessee is partly allowed. Thus, appeal of the assessee is partly allowed.

ITA No. 61/Coch/2015 :Assessee's Appeal : AY 2006-07

8. The assessee has raised the following grounds of appeal:

Under Normal Provisions of the Income Tax Act, 1961 (The Act)

- a) The learned Commissioner of Income Tax (Appeals)[CIT(A)] erred in confirming the addition of sale proceeds of Rubber Trees amounting to Rs. 17,60,000/- and of timber amounting to Rs.3,36,817 under Rule 7A of the Income Tax Rules.1962.
- b) The learned CIT(A) ought to have observed that Rule 7A was formulated by the Central Board of Direct Taxes (CBDT) to determine income which is derived from composite activity of manufacturing value added rubber products by the cultivator of rubber trees.
- c) The learned CIT(A) ought to have observed that perusal of Rule 7A clearly shows that the said Rule is applicable for assessment of income from rubber manufactured or processed from field latex obtained from rubber plants grown by the seller in India.
- d) The learned CIT(A) ought to have observed that the condition precedent for invoking of Rule 7A is that the revenue receipt should have live and direct nexus with sale of rubber manufactured from field latex obtained from rubber plants.
- e) The learned CIT(A) ought to have observed that Rule 7A has application only to "Revenue receipts" having "income character and not to capital receipts". Further, where a particular receipt does not have revenue character then Rule 7A cannot have any application whatsoever.
- f) The learned CIT(A) ought to have observed that Rule 7A has application only to income realised from sale of rubber products which are manufactured or processed from filed latex obtained from rubber plant grown by the seller in India. Rule 7A does not have any application if manufacturing and processing is not carried out by the grower of the rubber plant.

- g) The learned CIT(A) ought to have observed that the said Rule 7A does not have application to income derived by an assessee from sale of field latex obtained from rubber plants grown by the seller. In such case the income is purely agricultural in nature.
- h) The learned CIT(A) ought to have observed that if no profit can be assessed to Central Income Tax in respect of filed latex then by equal measure the sale of rubber trees which were yielding agricultural produce in the form of latex cannot also fall within the mischief of Rule 7A.
- i) The learned CIT(A) ought to have placed reliance on the basic judicial principle laid down by supreme court in the case of Commissioner of Agricultural Income Tax vs. Kailas Rubber Co. Ltd reported in [60 ITR 435].
- j) The learned CIT(A) ought to have observed that even after introduction of Rule 7A the nature of receipt from sale of rubber trees and timber sales continues to remain "capital receipt " and not "revenue receipt". Further there being no "manufacture of rubber' involved in the sale of old and unyielding trees planted by the grower, Rule 7A has no application to such sale.
- k) The learned CIT(A) ought to have also placed reliance on the decision of the Income Tax Appellate Tribunal, Cochin Bench in the case of Harrisons Malayalam Limited vs. Deputy Commissioner of Income Tax for the assessment year 2006-07 wherein it was held that the amount received on sale of old rubber trees constitutes capital receipts.

2. Under the provisions of Section 115JB

A. Provision for loss incurred due to Capital Reduction :Rs.1,45,18,200/-

- (a) The learned CIT (A) erred in confirming the addition by treating provision for loss due to capital reduction as Provision for diminution in the value of investment amounting to Rs.1,45,18,200/- for the purposes of arriving at the book profits u/s 115JB of the Act. The learned CIT(A) ought to have observed that the provision is made in accordance with the order dated 7th June, 2006 passed by the Kerala High Court accepting the capital reduction scheme of Aspinwall Technologies Ltd.
- (b) The learned CIT(A) ought to have observed that the provisions made by the appellant is not towards any diminution in the value of asset but represents actual loss incurred in respect of a loss on account of reduction in the value of investment and accordingly the same will not fall under any of the adjustments as specified in the Explanation to Section 115JB of the Act.

(c) The learned CIT(A) ought to have appreciated the substance of the transaction (i.e. loss on account of capital reduction) rather than merely concluding based on the nomenclature of the accounting entries.

B. Provision for Lease Rent: Rs.61,00,000/-

(a) The learned CIT(A) erred in confirming the addition of Provision for Lease Rent amounting to Rs.61,00,000/- by treating it as Provision for unascertained liability for the purposes of arriving at the book profits u/s 115 JB of the Act.

(b) The learned CIT(A) ought to have observed that any liability capable of being estimated with reasonable certainty, though the actual quantification may not be possible should be allowed as an ascertained liability.

(c) The learned CIT (A) ought to have observed that the provision has been made in the accounts based on lease rent demand notice received from Tahasildar, Taluk Office, Kochi based on revised rate of Lease rent.

(d) The learned CIT(A) ought to have observed that merely because the appellant is disputing the lease rent at revised rates, the same cannot be construed to be unascertained liability u/s 115JB(2)(c) of the Act.

The Appellant craves leave to add, alter, rescind and modify the grounds herein above or produce further documents, facts and evidence before or at the time of hearing of this appeal.

For these and other grounds that may be raised at the time of hearing, it is humbly prayed that this appeal may be allowed.

8.1 The first ground is with regard to addition of sale proceeds of Rubber Trees amounting to Rs. 17,60,000/- and of timber amounting to Rs.3,36,817 under Rule 7A of the Income Tax Rules.1962.

8.2 The facts of the case are that the assessee had received an amount of Rs. 17,60,000/- on sale of rubber trees which was credited directly to the rubber replantation and rehabilitation reserve. Similarly, an amount of Rs.3,36,817/- was

received on sale of timber. The assessee had not considered these receipts for computation of income from rubber in view of various decision of courts wherein it was held that the said receipts are in the nature of capital receipts. The Assessing Officer, applying Rule 7A, computed the total income after making additions on account of sale proceeds of rubber trees amounting to Rs. 17,60,000/- and sale proceeds of timber amounting to Rs.3,36,817/-. The Assessing Officer stated that Rule 7A specifies the method to arrive at the income from value added rubber products, as per which the income from the rubber estate has to be determined as a whole and then apportioned in the ratio of 65:35 to arrive at agricultural income and business income taxable under the Act. The Assessing Officer stated that the salvage value of old and unyielding rubber trees has to be considered to arrive at the income from the estate and then the division in the ratio of 65:35 is to be made. The Assessing Officer was of the view that trees are not capital assets and compared the income from sale of trees to the salvage value got from an exhausted stock. The AO further stated that the purchase price of a capital item is never allowed as deduction in determining the income; thus, the fact that the assessee had claimed deduction in respect of replanting expenses in earlier years showed that rubber trees are not capital assets.

8.3 On appeal, the CIT(A) confirmed the addition of Rs.17,60,000/- and Rs.3,36,817/- on account of sale proceeds of rubber trees and timber respectively as made by the Assessing Officer. The CIT(A) placed reliance on the judgment of the Kerala High Court in the case of Thiruvambadi Rubber (ITA Nos.15,31,37 and 43 of 2010 dated

27/06/2011) which had reversed the decision of the Tribunal which held that sale value of old rubber trees is agricultural income

8.4. Against this, the assessee is in appeal before us. The Ld. AR submitted that Rule 7A was inserted with effect from 1st April 2002 to tax income from the manufacture of rubber. It was submitted that Rule 7A prescribes that 35% of certain income from the produce of rubber trees would be treated as income derived from business. Rule 7A provides asunder:

(1) "Income derived from the sale of centrifuged latex or cenex or latex based crepes (such as pale latex crepe) or brown crepes (such as estate brown crepe, remitted crepe, smoked blanket crepe or flat bark (crepe) or technically specified block rubbers manufactured or processed from field latex or conglulum obtained from rubber plants grown by the seller in India shall be computed as if it were income derived from business, and thirty-five per cent of such income shall be deemed to be income liable to tax.

(2) In computing such income, an allowance shall be made in respect of the cost of planting rubber plants in replacement of plants that have died or become permanently useless in an area already planted, if such area has not previously been abandoned, and for the purpose of determining such cost, no deduction shall be made in respect of the amount of any subsidy which, under the provisions of clause (31) of section 10, is not includible in the total income.

8.5 The Ld. AR submitted that the above Rule covers incomes which are derived from the sale of certain items which are obtained from rubber plants grown. It was submitted that the above rule does not cover incomes which have been derived from the sale of the rubber plants/trees. Therefore, the Ld. AR submitted that the AO has erred in bringing the income from the sale of rubber trees under Rule 7A. The Ld. AR placed reliance on the decisions of the Cochin Bench of the Tribunal in the case of

Harrisons Malayalam Limited vs. DCIT (24 taxmann.com 59) and Thirumbadi Rubber Company Limited vs. DCIT in ITA No. 626 to 628/Coch/2013 dated 3rd January, 2014. The Ld. AR relied on various decisions wherein it was held that income from sale of trees is capital in nature. However, the AO held that all the decisions relied upon by the assessee were rendered before the insertion of Rule 7A. The Ld. AR submitted that the CIT(A) rejected the appeal of the assessee by placing reliance on the judgment of the Jurisdictional High Court in the case of Thiruvambadi Rubber Co. Ltd. in ITA No. 15/2010, 31/2010, 37/2010 and 43/2010 dated 27th June, 2011. According to the Ld. AR, the question before the Court was whether the sale proceeds from the sale of old and unyielding rubber trees can be excluded in the computation of book profits u/s. 115JA of the Act. Moreover, in this case, the Court held that the sale proceeds from sale of rubber trees is not agricultural income. Accordingly, it was submitted that the case relied upon by the CIT(A) does not cover the issue of taxability of sale of rubber trees under the normal provisions of the Act . Thus, it was contended that Rule 7A cannot be applied as the income from sale of rubber trees is not agricultural income. The Ld. AR relied on the judgments of various Courts in support of his contention that sale of rubber trees is capital receipt:

- 1) Commissioner of Agricultural Income-tax vs. Kailas Rubber Company Limited (60 ITR 435) (SC).
- 2) Kalpetta Estate Limited vs. CIT (221 ITR 601) (SC)
- 3) Harrisons Malayalam Limited vs. DCIT (24 taxmann.com 59) (Kochi Trib.)
- 4) CIT vs. Rajagiri Rubber & Produce Co. Ltd. (189 ITR 182) (Ker.)

8.6 The Ld. DR submitted that decision relied upon by the assessee was given in an entirely different context. At that point of time income from value added rubber was never considered for Central Income Tax and the question thereon was whether any capital gains arise on sale of rubber trees. According to the Ld. DR with the amendment brought in by IT (Second Amendment) Rules, 2001 the scenario has changed and now by Rule 7a an altogether new method to arrive at the income from value added rubber products, which is assessable under Central Income Tax has been evolved. The Ld. DR submitted that in that case, income from a rubber estate as a whole was first determined and then it was apportioned in the ratio of 65:35 to arrive at the agricultural income and income taxable under Central Income Tax. Here, according to the Ld. DR, all expenditure for growing the rubber like replanting expenses, estate expenses etc. were taken into account and then, the salvage value of old and unyielding rubber trees also has to be taken into account to arrive at the correct income from the estate and then the division in the ratio 65:35 is to be made. The Ld. DR noted that this income is only a salvage value got from an exhausted stock – Just like the money got on sale of empty gunny bags by a cement dealer or of empty bottles by a bar hotel. There is no point in calling the trees a capital asset. According to the Ld. DR whenever an article or thing is considered as capital, its purchase price is never allowed as a deduction in determining the income. Here, the Ld. DR submitted that the assessee itself has deducted the estate expenses and replanting expenses which shows that rubber trees are not capital assets so far as an estate is considered. According to the Ld. DR, the cost price relating to the buildings,

Plant and Machinery etc. belonging to an estate is never allowed as a revenue expenditure and it is not right on the part of the assessee to categorize the cost of acquisition of a thing as a revenue expenditure and the thing, as a capital asset. Therefore, the Ld. DR submitted that the proceeds of rubber trees amounting to Rs.17,60,000/- and income from sale of timber amounting to Rs.3,36,817/- was rightly taken into account for computing income from rubber.

8.7 We have heard the rival submissions and perused the material on record. This issue was considered by the Tribunal in the case of *Harrisons Malayalam Ltd. vs. DCIT* (24 taxmann.com 59) wherein it was held as follows:

“10. We have gone through Rule 7A of Income Tax Rules and for the sake of convenience, we extract the same below:-

“Income from the manufacture of rubber

7A (1) Income derived from the sale of centrifuged latex or cenex or latex based crepes (such as pale latex crepe) or brown crepes (such as estate brown crepe, remilled crepe, smoked blanket crepe or flat bark crepe) or technically specified block rubbers manufactured or processed from field latex or coagulum obtained from rubber plants grown by the seller in India shall be computed as if it were income derived from business, and thirty-five per cent of such income shall be deemed to be income liable to tax”.

On a careful perusal of Rule 7A, we notice that the said rule talks about computation of income derived from sale of centrifuged latex or cenex or latex based crepes (such as pale latex crepe) or brown crepes etc. The said rule does not talk about the taxability of income from sale of old rubber trees. According to Ld A.R, the Rule 7A provides for ascertainment of business income obtained on sale of centrifuged latex etc. when manufactured or processed from field latex or coagulum obtained from rubber plants grown by the seller in India, i.e., when there is a combined activity of growing rubber trees and also manufacturing or processing of field latex or coagulum obtained from rubber plants, Rule 7A provides for segregation and ascertainment of agricultural income and the business income. On a plain reading of Rule 7A, we are inclined to accept the contentions of Ld A.R. Thus, the said Rule 7A does not take in its ambit the

question of sale of old rubber trees and accordingly, in our view, the Ld. CIT has placed incorrect interpretation on Rule 7A and has taken the view that the said Rule 7A shall apply to the sale proceeds of old rubber trees. Hence, it cannot be said that there is incorrect application of law on the part of the AO. Accordingly, we are of the view that the Ld. CIT was not correct in assuming jurisdiction over this issue by making incorrect interpretation of law.”

8.8 Further, this issue travelled to the High Court. The High Court observed in the case of *Harrisons Malayalam Ltd.* in 103 CCH 442 that sale of old and unyielding trees would not give rise to the exempt income. If there is no exempt income, then there is no question of application of Rule 7A. In such circumstances, the claim of the assessee is to be allowed. Further, The Jurisdictional High Court considered its own judgment in the case of *CIT vs. Thiruvambadi Rubber Co. Ltd.* (203 taxman 63). Being so, the reliance placed by the CIT(A) on the judgment of the Jurisdictional High Court in the case of *CIT vs. Thiruvambadi Rubber Co. Ltd.* (supra) is totally misplaced. Accordingly, we hold that the sale proceeds on sale of rubber trees and timber cannot be brought to tax under Rule 7A of the I.T. Rules. Thus, this ground of appeal of the assessee is allowed.

9. The next ground in ITA No. 61/Coch/2015 is with regard to addition of provision for diminution in the value of investment of Rs.1,43,18,200/-, provision for lease rent of Rs.61,00,000/- and provision for bad debts of Rs.36,55,248/- for the purposes of arriving at the book profit u/s. 115JB, treating the same as a provision for an unascertained liability.

9.1 The AO made this addition observing that the provision towards lease rent is an unascertained liability and diminution in the value of assets and bad debts are to be added back to the book profit u/s 115JB.

9.2 On appeal, the CIT(A) upheld the findings of the Assessing Officer by observing that section 115JB requires that any liability debited to profit and loss account other than an ascertained liability needs to be added to the net profit for arriving at book profits chargeable to MAT. The CIT(A) relied on the judgment of the Madras High Court in the case of DCIT vs. Beardsell Ltd. (244 ITR 256) holding that the provision for bad debts cannot be termed as an ascertained liability, and therefore needs to be added back to the net profits for arriving at the book profit subject to MAT. However, distinguishing this decision, the Special Bench of ITAT, Kolkata in the case of JCIT vs. Usha Martin Industries (104 ITD 249) held that the provision for bad debt is not liability per se, as no liability would be fastened upon the tax-payer even if the underlying debt is not recovered. The Supreme Court in the case of CIT vs. HCL Comnet systems & Services Limited (305 ITR 409) held that the provision of doubtful debts is akin to the provision of diminution in value of assets.

9.3 However, according to the CIT(A), this provision in the Act has been amended by the Finance Act, 2008 and 2009 w.e.f. 1.4.2001 wherein the Explanation 1, clause (c) and (i) read as under:

Explanation (1) – For the purposes of this section “book profit” means the net profit as shown in the profit and loss account for the relevant previous year prepared under sub-section (2) as increased by:-

- (a).....
- (b).....
- (c) the amount or amounts set aside to provisions made for meeting liabilities, other than ascertained liability, or
- (d).....
- (i) the amount or amounts set aside as provision for diminution in the value of any asset.

Accordingly, the CIT(A) confirmed the addition of provision for diminution in the value of investment of Rs.1,45,18,200/-, provision for lease rent of Rs.61,00,000/- and provision for bad debts of Rs.36,55,248/- for the purposes of arriving at the book profits u/s. 115JB of the Act.

9.4 Against this, the assessee is in appeal before us. The Ld. AR submitted that the loss so incurred on capital reduction is a capital loss which cannot be added while computing book profits under section 115JB. In order to give rise to a capital gains / losses in India, two key ingredients have to be satisfied -

There should be a 'capital asset'
There should be a 'transfer'

In the current case, it was submitted that the assets in question are shares of a company which are capital assets. The term 'transfer'¹ as defined u/s 2(47) of the Act includes, inter-alia, sale, exchange or relinquishment of the asset or extinguishment of any rights therein.

9.4.1 The Ld. AR submitted that the loss so incurred on capital reduction there is an extinguishment of rights/relinquishment in the underlying shares. In this regard, the Ld. AR placed reliance on the following judgments of the Supreme Court:

Kartikeya Sarabhai v. CIT (1997) 228 ITR 164 (SC)
CIT v. G Narasimhan (1999) 102 Taxman 66 (SC)

Considering the above, the Ld. AR submitted that the assessee company had suffered capital losses and the same was disallowed while computing the business income under the normal provisions of the Act but no adjustment was made while computing book profits. The Ld. AR submitted that the provisions of section 115JB, only certain items are to be added or removed which have been specified under various clauses. None of the clauses require capital gains/losses. The Ld. AR relied on the judgment of the Bombay High Court in the case of CIT vs. Veekaylal Investments Co. Ltd. vs. CIT (116 Taxmann 104). Considering the above, the loss so incurred on capital reduction is not required to be added back while computing the income under the provisions of section 115JB. The Ld. AR prayed that if the loss incurred on capital reduction is not allowed in the year under consideration, the same be allowed to be claimed in the computation of book profits in AY 2007-08 when the order of Kerala High Court was passed.

10. Regarding provision for lease rent of Rs. 61,00,000/-, the facts of the case are that the assessee debited an amount of Rs. 61,00,000/- in the statement of profit and loss for the year ended on 31st March, 2006 on account of provision for lease rent.

The government had unilaterally increased the lease rent of the land held by the assessee. The assessee received a demand notice amounting to Rs.1,59,80,172/- from Tahasildar, Taluk Office, Kochi, based on revised rate of Lease rent. The provision made by the assessee was based on rent rates which prevailed before the revision made by the revenue authorities. This revision was challenged by the assessee before the High Court of Kerala. While granting stay, the Court directed the assessee to make payment of Rs. 40,00,000/-. The applicant made the said interim payment as per direction of Court. The case filed by the assessee company for the increase in rent was disposed off by the High Court of Kerala, directing the Government of Kerala to issue fresh orders after giving an opportunity of being heard. Accordingly, the Government of Kerala issued an order dated 26th April, 2013 rejecting the request of the assessee for reduction of lease rent.

10.1 The AO added back the sum of Rs. 61,00,000/- in the computation of book profit u/s 115JB, treating the same as a provision for an unascertained liability. The CIT(A) confirmed the addition of Rs. 61,00,000/- made by the AO in the computation of profit u/s 115JB, treating the same as a diminution in the value of an asset.

11. Against this, the assessee is in appeal before us. The Ld. AR submitted that the provision was made towards an ascertained liability based on the notice received by the assessee company from the Tahasildar, Taluk Office, Kochi, the provision was for Rs. 61,00,000/- only, which according to the assessee would be the reasonable amount to cover the liability, even though the demand was for a higher amount as

per the notice. The provision so made was not on an estimated basis and was towards an ascertained liability being lease rental payment. The Ld. AR referred to the term 'ascertained' which has not been defined under the Act. As per the Webster's II New Riverside University Dictionary, the term "ascertained" means 'to make certain'. In this connection, the Ld. AR drew our attention to the judgment of the Supreme Court in the case of *Bharat Earth Movers v. Commissioner of Income-tax* (112 Taxman 61) in which the following principles was laid;

"The law is settled: if a business liability has definitely arisen in the accounting year, the deduction should be allowed although the liability may have to be quantified and discharged at a future date. What should be certain is the incurring of the liability. It should also be capable of being estimated with reasonable certainty though the actual quantification may not be possible. If these requirements are satisfied, the liability is not a contingent one. The liability is in praesenti though it will be discharged at a future date. It does not make any difference if the future date on which the liability shall have to be discharged is not certain."

11.1 Applying the aforesaid principles to the facts of the assessee, it was submitted that the assessee company had received a notice from the revenue authorities wherein the assessee was required to pay the revised rent. The Court also in the interim order directed the assessee to pay Rs. 40,00,000/-. Further, the liability of the assessee company had also become final based on the order of the Government of Kerala as mentioned above. Further, as held by the Supreme Court in the above mentioned case, the fact that the liability would be discharged at a future date would not convert the nature of liability into that of contingent or unascertained so long as such liability can be quantified or estimated with reasonable certainty. In the instant

case, the assessee company had quantified its liability towards lease rent based on the revised rates of rent. In this regard, the Ld. AR relied on the judgment of the Supreme Court in the case of Metal Box Co. of India Ltd. v. Workmen (73 ITR 53) wherein it was held that:

"For an assessee maintaining his accounts on mercantile system, a liability already accrued, though to be discharged at a future date, would be a proper deduction while working out the profits and gains of his business, regard being had to the accepted principles of commercial practice and accountancy. It is not as if such deduction is permissible only in case of amounts actually expended or paid;

Just as receipts, though not actual receipts but accrued due are brought in for the income-tax assessment, so also liabilities accrued/due would be taken into account while working out the profits and gains of the business;

A condition subsequent, the fulfilment of which may result in the reduction or even extinction of the liability, would not have the effect of converting that liability into a contingent liability;

11.2 Further, the Ld. AR relied on the judgment of the Supreme Court in the case of *Calcutta Co. Ltd. v. CIT* (37 ITR1) wherein it was held that the liability on the assessee having been imported, the liability would be an accrued liability and would not convert into a conditional one merely because the liability was to be discharged at a future date. There may be some difficulty in the estimation thereof but that would not convert the accrued liability into a conditional one. Thus, it was submitted that merely because the assessee had filed an appeal before the High Court against the order received for increase in rent, the liability would not become a liability which is unascertained. Considering the above, the assessee prayed that the provision made for lease rent not be treated as an unascertained liability.

11.3 The Ld. AR submitted that if it is held that the provision made in the year under consideration be added to the book profits, the same may be allowed a deduction on computation of book profits in the year in which the order of the High Court has confirmed the liability for lease rent.

11.4 The Ld. DR submitted that in view of clause (i) (c) of section 115JB(2) of the I.T. Act, the amount is to be added back to the book profit as shown in the profit and loss account of the assessee.

11.5 We have heard the rival submissions and perused the record. It is pertinent to reproduce the provision of 115JB(2)(i)(c) which reads as follows:

115JB Notwithstanding anything contained in any other provision of this Act wherein the case of an assessee being a company, the income tax payable on the total income as computed under this Act in respect of any previous year relevant to the assessment year commencing on or after the 1st day of April, 2012, is less than eighteen and one-half per cent of its book profit, such book profit shall be deemed to be the total income of the assessee and the tax payable by the assessee on such total income shall be the amount of income shall be the amount of income-tax at the rate of eighteen one-half per cent.

(2) Every assessee –

Explanation (1) –For the purpose of this section, “book profit” means the net profit as shown in the profit and loss account for the relevant previous year prepared under sub-section (2), as increased by –

(a) the amount of income-tax paid or payable, and the provision therefor; or

(b) the amounts carried to any reserves, by whatever name called (other than a reserve specified under section 33AC); or

- (c) the amount or amounts set aside to provisions made for meeting liabilities, other than ascertained liabilities; or
- (d) the amount by way of provision for losses of subsidiary companies; or
- (e) the amount or amounts of dividends paid or proposes; or
- (f) the amount or amounts of expenditure relatable to any income to which section 10 (other than the provisions contained in clause (38) thereof) section 11 or section 12 apply; or
- (g) the amount of depreciation.
- (h) the amount of deferred tax and the provision therefor;
- (i) the amount or amounts set aside as provision for diminution in the value of any asset,
- (j) the amount standing in revaluation reserve relating to revalued asset on the retirement or disposal of such asset.

Prior to the substitution, clause (i) and the proviso read as under:

- (i) the amount withdrawn from any reserves or provisions, if any such amount is credited to the profit and loss account.

Provided that, where this section is applicable to an assessee in any previous year(including the relevant previous year), the amount withdrawn from reserves created or provisions made in a previous year relevant to the assessment year commencing on or after the 1st day of April, 2001 shall not be reduced from the book profit unless the book profit of such year has been increased by those reserves or provisions (out of which the said amount was withdrawn) under that Explanation or be reduced from the book profit unless the book profit of such year has been increased by those reserves or provisions (out of which the said amount was withdrawn) under this Explanation or Explanation below the second proviso to section 115JA as the case may be.

11.6 On going through the above provisions, we are of the opinion that the amount set aside as provision for diminution in the value of investment is to be added back to

the book profit as shown in the profit and loss account in view of the retrospective amendment introduced by Finance Act No. 2, 2009 by introducing clause (i) (c) . By virtue of the said amendment the amount set aside as provision for diminution in the value of any asset is to be added back in view of the specific clause (i) in the said Explanation. Being so, we do not find any infirmity in the order of the lower authorities in adding back the said amount to the book profits shown in the profit and loss account .

11.7 Further, Hon'ble ITAT Mumbai E-Bench has considered the similar issue in the case of ITO vs TCFC Finance Ltd. reported in (2011) 11 ITR (TRIB) 153 (MUM) after discussing the factual and legal position it was held as under:

"Section 115JB has to be considered as code in itself. This section is a special provision for payment of tax by certain companies and opens with non-obstante clause thereby excluding any other provisions 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 Explanation. 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 provisions, 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. [Para 11]

Explanation 1 to section 115JB(2) in no uncertain terms states that any amount set aside as provision for diminution in the value of asset debited to the profit and loss account is to be added to the amount of net profit for the purpose of computing book profit. As the relevant condition 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 was required to be added for determining book profit. [Para 12] 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 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 precondition for adding it to the net profit. 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 fact whether or not there is any balance value of asset. In view of the foregoing discussion it is manifest that 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. [Para 14]

12. A similar provision was made for lease rent of Rs.61,00,000/- as unascertained liability which is hit by the provisions of clause (c) in Explanation (2) of section 115JB of the Act. The contention of the Ld. AR is that the assessee is following mercantile system of accounting and therefore, the provision is to be allowed, though it was

crystallized in the year in which the order of the Government of Kerala in G.O. (Ms) No.162/13/RD dated 26-04-2013 was passed. We are not in agreement with this contention of the Ld. AR. Being so, we are not in agreement with the Ld. AR's contention that this ascertained liability is to be allowed in view of mercantile system of accounting followed by the assessee. In other words, the provision for lease rent is unascertained liability in the assessment year under consideration and it is to be allowed in the year of crystallization of the expenditure. This ground of appeal of the assessee is dismissed. The appeal of the assessee in ITA No.61/Coch/2015 is partly allowed.

ITA No. 128/Coch/2017 :Assessee's Appeal : AY 2012-13

13. The assessee has raised the following grounds of appeal:

A. The order passed by the first appellate authority, to the extent challenged hereunder, is contrary to the law, facts and circumstances of the case. The order, if allowed to continue, would occasion travesty of justice and cause irreparable loss and hardship to the appellant.

B. The appellant would submit that, based on the order dated 16.11.2006 passed by the Hon'ble High Court of Kerala, erstwhile "The Pullangode Rubber and Produce Company Ltd. (PRPCL)," along with other Group Companies, got merged with the appellant. As per the scheme approved by the Hon'ble High Court of Kerala, all the liabilities existing in respect of the merged Companies were to be borne by the appellant. At the time of merger, PRPCL had returned a brought forward unabsorbed Agricultural Loss of Rs. 4,89,30,939/-, up to 31.12.2005 (A.Y 2006-07). Consequent to the date of merger, the appellant started filing returns from 01.01.2006 onwards, declaring agricultural income earned from the estate previously owned by PRPCL, after setting off the said unabsorbed brought forward loss. The authorities under the AIT Act, disallowed the set off of unabsorbed loss, under the AIT Act, and therefore, the appellant was mulcted with the liability to pay agricultural income tax and interest thereon. The appellant has remitted all the AIT demand along with interest up to the AY 2009-10. The loss arisen on account of disallowance of carry forward and set off of the

Act. The disallowance of set off of unabsorbed loss of PRPCL against the income earned by the appellant is pending adjudication before the Hon'ble Supreme Court.

C. The first appellate authority erred in not considering the fact that when valuing the shares of erstwhile the PRPCL at the time of merger, the availability of carry forward agricultural loss has also been taken into consideration. The learned CIT (A) ought to have observed that if some assets, taken over at the time of merger, ceases to exist or fails to realize the value adopted at the time of merger, the same is only an incidental business loss eligible for deduction in computing the income. Similarly if over and above the liability disclosed or considered at the time of merger, additional amounts are payable, the same is also eligible for deduction u/s. 37 as an incidental business loss. The crucial aspect that the appellant was bound by the terms of scheme of merger approved by the Hon'ble High Court, which covered the set off of brought forward losses, was overlooked by the first appellate authority. Similarly, the first appellate authority lost sight of the fact that the liability incurred by the appellant was on account of transactions entered into prior to the date of merger. Therefore, the appellant was entitled, in law and on facts to claim the interest paid on the agricultural income tax, as business loss admissible under Section 37 of the Act.

D. The first appellate authority erred grossly in not considering the decisions relied on by the appellant, that if the interest is compensatory in nature, the same is an allowable deduction under Section 37 of the Act (Ref; Bhai Jaspal Singh (2011) 1 SCC 39, Consolidated Coffee Ltd. - (2001) 1 SCC 278, Prakash Cotton Mills P. Ltd.(1993) (201 ITR 684), Hoshiari Lal Kewal Krishan (2009) (311 ITR 336), and Padmavathy Raje Cotton Mills Ltd., (1999) (239 ITR 355). The decisions governing the above aspect, relied on by the appellant are highly brushed aside by the first appellate authority, and further, the first appellate authority holds that it is not clear as to whether the interest in the instant case is compensatory or not. (Ref: Page 32 Paragraph (ii)). The first appellate authority states that whether, the interest under AIT Act, is entirely compensatory or not is not clear. The first appellate authority' erred in not considering the phraseology under the AIT Act, relating to the levy of interest. (Ref; Section 39 read with Section 37(4) of AIT Act). When the language of the provision is clear and unambiguous, the first appellate authority ought not to have stated that there is lack of clarity. Furthermore, if there was any ambiguity, then the benefit of doubt should yield in favour of the appellant.

E. The decision relied on by the first appellate authority is divorced of the facts and circumstances of the case of the appellant, and very well distinguished by the appellant before the first appellate authority. There is no infraction of law, as stated by the first appellate authority. With reference to the decision in East India Pharmaceutical Works Ltd. (cited supra), the appellant would submit that the said

decision was rendered based on the particular conspectus of the facts and circumstances arising therefrom. The said decision cannot have a universal application, especially in cases where the facts and circumstances stand on a different footing, as in the instant case. It goes against the settled legal principle relating to "precedents" that the factual situation in the case at hand should fit in with the case relied on. The appellant would submit that the case cited supra, cannot be relied on for confirming the disallowance of the interest paid on belated payment of AIT, for more than one reason.

E In East India case, the assessee availed "Over draft" facility to pay Income Tax, and claimed interest paid on availing O.D facility, as deduction under Section 37 of the Act, which was disallowed. In the case of the appellant, the AIT dues were paid from the Agricultural income derived from the rubber estate, and therefore, out of funds/revenue generated from the business and not from any borrowed funds. The source of funds and the nature of payment strike the differential note in the case of the appellant, from that in East India case.

There is no question of retention of funds by the appellant till the payment of AIT dues. As already explained, the appellant started filing returns pursuant to the order of the Hon'ble High Court of Kerala, approving the scheme consequently the dues were paid with interest. There was no question of retention of money, let alone retention of public funds, in the instant case. Consequent to the merger approved by the Hon'ble High Court of Kerala, the returns were filed, and the brought forward unabsorbed agricultural loss of PRPCL, was set off against the agricultural income generated from the rubber estate. The contention of retention of public money in the instant case, is not correct, and will not have any application.

The Tribunal decision (Ahmedabad Tribunal in Shree Saras Spices & Foods (P) Ltd.), which followed East India Case, will also be not applicable, since the facts and circumstances therein are divorced from the case of the appellant.

For these and other grounds and documents to be submitted at the time of hearing, it is humbly prayed that this Hon'ble Tribunal be pleased to set aside the first appellate order, to the extent impugned in this Appeal.

13.1 The facts of the case are that the assessee incurred interest expenses totaling Rs.94,00,179/- on delayed payments of Agricultural Income Tax (AIT) demanded by the Kerala AIT Department (and paid by the assessee in the impugned F.Y. 2011-12)

owing to non-allowance of set-offs of losses brought forward from the earlier A.Y's 2006-07 to 2009-10 relating to the business of the erstwhile Pullangode Rubber and Produce Company Limited (PRPCL) which was subsequently taken over by the assessee. At the time of merger with ACL, PRPCL had brought forward unabsorbed Agricultural losses of Rs. 4,89,30,939/- up to 31.12.2005 (viz. A.Y. 2006-07) that were disallowed from being set off by the Kerala AIT Department who levied the impugned interest. The expenses totaling Rs. 94,00,179/- as above were added by the AO to the composite (business-cum-agricultural) income and 35% of that (under Rule 7A) computed at Rs. 32,90,063/- was added back and assessed in the hands of the assessee. According to the Assessing Officer, the interest amounts as above that was claimed as deduction by the assessee cannot be allowed as wholly and exclusively incurred for the purposes of the assessee's business. The AO's arguments are based on the position that any income tax, penalty or interest amounts paid could not be allowed as deduction under the Central Income-tax and the Kerala Agricultural Income Tax. The Assessing Officer was of the view that as the interest amounts paid as above were due to the delay in paying the Agricultural Income Tax to the Government of Kerala, these were part of tax and also impliedly contained a penal element. The Assessing Officer applied Rule 7A which provides that incomes from agricultural and non-agricultural activities were to be computed as if the same were incomes from business, following which 35% of such incomes were to be brought to tax. This impliedly meant that only business expenses that stood the lie test of Section 37 (or other applicable provisions of the Act) could be allowed.

13.2 On appeal, the CIT(A) observed that though the ratio of the Supreme Court in the case of East India Pharmaceutical Works Ltd. (224 ITR 627) related to interest payments on borrowed funds to pay statutory income-tax dues, the situation was *Para Materia* with the facts in the case of the assessee in as much as that moneys being statutory dues (AIT payments) that needed to be paid in time were retained by the assessee beyond stipulated due dates, thereby causing an increase in its operating funds and capital at the expense of public funds of respective equivalent amounts. The CIT(A) observed that in the case of East India Pharmaceutical Works Ltd. (*supra*) the assessee concerned had made interest payments to independent private parties (being banks and financial institutions) for the income tax amounts that were paid out of funds borrowed from such third parties. The CIT(A) observed that the moment the borrowed funds entered the financial system of the assessee, as per the judgment of the Supreme Court (*supra*), they were effectively public funds since the intent to borrow very clearly stated such to be the purpose. In that case, the amounts were borrowed because the assessee did not possess the necessary funds to make the payments of the statutory dues being income taxes and the intention thereafter stood authenticated and proved by the assessee actually making the payments of the income taxes. Therefore, in the case of East India Pharmaceutical Works Ltd. (*supra*), the CIT(A) observed that the amounts borrowed and the interest accruals thereupon constituted public moneys from the date of such borrowals. However, in the instant case, the CIT(A) observed that the assessee held

on to moneys that were liable to be paid as AIT and therefore, constituted and represented public funds from the dates from which such liabilities statutorily commenced and benefitted from such retention through the returns generated that can be readily computed on the basis of financial time-value-for-money principle. According to the CIT(A), the returns manifested in the form of interest payments due to the AIT authorities should be offered to tax through the instrument of their disallowance and assessment u/s. 37 of the Act. Thus, the CIT(A) held that the assessee has no case in making deductible claim of the payments of interest amounts that do not belong to it and never belonged from the dates of their generation/accrual. Accordingly, he upheld the disallowance made by the Assessing Officer.

13.3 Against this, the assessee is in appeal before us. The Ld. AR submitted that the payment of interest under the AIT Act had arisen on account of the scheme of amalgamation approved by the High Court of Kerala vide order dated 16.11.2006, wherein "The Pullengode Rubber and Produce Company Ltd. (PRPCL)" along with some other Companies were amalgamated with the assessee. The Ld. AR submitted that as per the approved scheme, all liabilities of PRPCL became the liabilities of the assessee and the assessee in the returns filed, declared income earned by PRPCL and availed set off of the unabsorbed brought forward losses of PRPCL. The set off of unabsorbed brought forward losses was rejected by the AIT authorities. The Ld. AR submitted that the assessee remitted the dues along with interest u/s. 37(4) r.w.s. 39

of the AIT act and claimed it as a deduction u/s. 37 of the Act. According to the Ld. AR, the payment of interest under the AIT Act is compensatory in nature and hence allowable as a deduction u/s. 37 of the Act. The Ld. AR relied on the judgments of the Supreme Court in the case of Bhai Jaspal Singh (2011) 1 SCC 39, Consolidated Coffee Ltd. (2001) 1 SCC 278. He also relied on the decision in the case of Prakash Cotton Mills P. Ltd.(1993) (201 ITR 684), Hoshiari Lal Kewal Krishan (2009) (311 ITR 336), and Padmavathy Raje Cotton Mills Ltd. (1999) (239 ITR 355). The Ld. AR also relied on the judgment of the Kerala High Court in the case of CIT vs. Dhanalakshmi Bank Ltd. (2003) 2 KLT 1076. The Ld. AR submitted that the judgment relied on by the CIT(A) in the case of East India Pharmaceutical Works Ltd. (supra) was clearly distinguishable on facts and hence, cannot be applied to the facts of the present case.

13.4 The Ld. DR relied on the order of the lower authorities.

13.5 We have heard the rival submissions and perused the material on record. In the present case assessee is claiming the payment of interest for delay in payment of agricultural income tax as a deduction while computing the income of assessee under Income Tax Act. It cannot be said that it has any connection with the business income of the assessee on which the assessee is liable to pay income tax under Income tax Act. If agricultural income tax is not a permissible deduction under

section 37 of the Income Tax Act, any amount payable for default committed by the assessee in discharging its statutory obligation under Agricultural Income Tax cannot be allowed as a deduction while computing income under Income Tax Act. The Ld. AR submitted that the payment of interest under the AIT Act had arisen on account of the scheme of amalgamation approved by the High Court of Kerala vide order dated 16.11.2006, wherein "The Pullengode Rubber and Produce Company Ltd. (PRPCL)" along with some other Companies were amalgamated with the assessee. The approval of amalgamation by High Court can not lead to conclusion that disallowable expenditure under Income Tax Act is allowable as a deduction and it won't confer any entitlement for allowability of such an expenditure. The allowability of interest expenditure is governed by provisions of S. 37 and 36(1)(iii) of the Income Tax Act. Interest incurred for delay in payment of Agricultural income tax also cannot be allowed u/s 36(1)(iii) of the Act as the condition laid down u/s 36(1)(iii) has not been fulfilled. In other words, interest paid is not for the purpose of the business of the assessee on which income assessee is paying income tax. In our opinion, the interest paid is having direct nexus with agricultural income which is exempt from tax u/s 10(1). Therefore, such payment of interest cannot be allowed u/s 36(1)(iii) also. We have also carefully gone through all the case law cited by the Ld. AR, which have no relevance to the facts of the case. In view of this discussion, we are inclined to dismiss all the grounds of appeal of the assessee. The assessee appeal in ITA No.128/Coch/17 is dismissed.

14. In the result, the appeal of the Revenue in ITA No.133/Coch/2017 and the appeal of the assessee in ITA No.128/Coch/2017 are dismissed. The appeals of the assessee in ITA No. 60 & 61/Coch/2015 are partly allowed.

Order pronounced in the open court on 19th May, 2020.

sd/-
(GEORGE GEORGE K.)
JUDICIAL MEMBER

sd/-
(CHANDRA POOJARI)
ACCOUNTANT MEMBER

Place: Kochi

Dated: 19th May, 2020

GJ

Copy to:

1. Aspinwall and Company Ltd., Post Box No. 560, Subramanian Road, Willingdon Island, Kochi-682 003.
2. The Assistant Commissioner of Income-tax, Circle-1(1), Kochi.
3. The Deputy Commissioner of Income-tax, Circle-1(1), Kochi.
4. The Commissioner of Income-tax(Appeals)-II, Kochi
5. The Pr. Commissioner of Income-tax-II, Kochi.
6. D.R., I.T.A.T., Cochin Bench, Cochin.
7. Guard File.

By Order

(ASSISTANT REGISTRAR)
I.T.A.T., Cochin

I.T.A. Nos. 60&61/Coch/2015
& 128 & 133/Coch/2017