IN THE INCOME TAX APPELLATE TRIBUNAL "I" BENCH, MUMBAI

BEFORE SRI MAHAVIR SINGH, JM AND SRI RAJESH KUMAR, AM

ITA No. 430/Mum/2015

(A.Y. 2011-12)

Five Star Shipping Co. Pvt. Ltd Unit No. 3, Brady Gladys Plaza, Senapati Bapat Road, Lower Parel, Mumbai-400 013	Vs.	The Asst. Commissioner of Income Tax Center Circle, 6th Floor, Room No. 658, Aayakar Bhavan, M.K. Road, Mumbai-400 020
Appellant	..	**Respondent**
PAN No. AAACF0530B		

ITA No. 2709/Mum/2015

(A.Y. 2011-12)

The Asst. Commissioner of Income Tax Center Circle, 6th Floor, Room No. 658, Aayakar Bhavan, M.K. Road, Mumbai-400 020	Vs.	Five Star Shipping Co. Pvt. Ltd Unit No. 3, Brady Gladys Plaza, Senapati Bapat Road, Lower Parel, Mumbai-400 013
Appellant	..	**Respondent**

Assessee by : Nikhil S Pathak, AR

Revenue by : Saurabh Kumar Rai, DR

Date of hearing: 26-12-2017 **Date of pronouncement :** 16-02-2018

O R D E R

PER MAHAVIR SINGH, JM:

These cross appeals are arising out of the order of Commissioner of Income Tax (Appeals)-50, Mumbai, [in short CIT(A)] in appeal No. CIT(A) 50/IT-1000/2013-14 dated 18-12-2014. The Assessment was framed by the Asst. Commissioner of Income Tax, CC 47, Mumbai (in short ACIT) for the assessment year 2011-12 order dated 28-02-2014 under section 143(3) of the Income Tax Act, 1961(hereinafter 'the Act').

2. The first common issue in these cross appeals, of assessee and that of the Revenue, is as regards to the order of CIT(A) deleting the agricultural income at ₹ 14,30,190/- and restricting the addition of lease rentals of agricultural lands at ₹ 25,75,065/-. For this Revenue has raised following ground No.1: -

> *"1. On the facts and in the circumstances of the case and in the law, the ld. CIT(A) erred in holding income of Rs.14,30,1 90/-, as agricultural income, ignoring the fact that as per 7/12 extract, only special grass was grown, which did not require any agricultural operation.*

And assessee has raised following ground No. 1 to 4:

> *"1. The learned CIT(A) erred in holding that the lease rent paid '25,75,065/- would not be allowable while computing the income of the appellant.*
>
> *2. The learned CIT(A) further erred in holding that the lease rent paid in excess of the agricultural income earned by the appellant company would be disallowable u/s 14'\ of the Act.*
>
> *3. The learned CIT(A) failed to appreciate that the lease rent paid by the appellant company was incurred wholly and exclusively for its stud farm business and accordingly, the same should have been allowed while computing the income of the appellant.*
>
> *4. The learned CIT(A) failed to appreciate that the lease rent paid by the appellant company was not hit by the provisions of Section 14A and hence, no amount was disallowable u/s 14A."*

3. Briefly stated facts are that the assessee company had taken land on lease from its directors and declare agricultural income at ₹ 14,30,190/- which was claimed as exempt. The assessee has paid lease rental of ₹ 25,75,065/- which was claimed as deduction. The AO treated the agricultural income as non-genuine and accordingly, takes the entire income of ₹ 14,30,190/- as income from other sources and also further disallowed the lease rental paid of ₹ 25,75,065. The assessee preferred appeal before CIT(A) who deleted the addition of the agricultural income of ₹ 14,13,190/- and confirmed the action of the AO in disallowing the loans as rental paid of ₹ 25,75,065/-.

4. At the outset, the learned Counsel for the assessee stated that this common issue is exactly covered in assessee's own case by tribunal's decision for AY 2007-08 and 2008-09 in ITA No. 2151 & 2767/Mum/2012 for AY 2007-08, 2152 & 2766/Mum/2012 for AY 2008-09 vide order dated 11-06-2015, wherein the Tribunal vide Para 8 to 10 has allowed the claim of the assessee on both the issues and the same reads as under: -

> *"8. Rival contentions have been considered and record perused. We found that during the course of appellate proceedings, the ld. CIT(A) found that the assessee has not given due opportunity to produce the evidence, insofar as the A.O. had given notice for producing the evidence only at the fag end of the. assessment proceedings i.e. 10 to 15 days time. Under these circumstances, the ld. CIT(A) admitted the additional evidence filed before him and sent the same to the A.O. for his remand report. From the record we found that the assessee has a business of maintaining a stud farm at Nanoli near Talegaon, Pune. It has its own land and it has also taken about 133 acres of land on rent from Dhunjibhoy Family. The assessee uses the land for*

stud farm and also for agricultural operations. It has about 4 lakhs trees of Gauva, Jambhun, Mango, Coconut, etc. etc. on the land and it also grows paddock (dhoop) grass for the horses, rice, vegetables on this land. It sells some agricultural produce like vegetables and fruits in the market while part of this produce is utilised by the assessee for its employees on the farm. It has earned receipt ofRs.801,175/- from sale of such agricultural produce and which the A.O. treated as non agricultural income. After considering the remand report, the ld. CIT(A) has recorded a categorical finding to the effect that the assessee had carried on agricultural operations and earned income of Rs. 8,01,175/-. The grass is paddock grass (dhoop grass) which is specially planted as it is a feed for the horses. It does not have spontaneous growth and hence, it is an agricultural activity. In the following cases, it has been held that if the grass is planted, it is an agricultural activity.

> *a) ITO vs. Kanchanlal Mancha Ram (1988) 32 TTJ (Ahd.)(TM) 38 b) ACIT vs. PZ Estates (P) Ltd. (2005) 2 SOT 563 (Del).*

The ld. CIT(A) after considering the corroborative evidence filed on record, observed that the assessee had sold French Beans, Cabbage, Cauliflowers, Carrot, Cucumber, Ladies Finger, Mango during the relevant previous year which constituted the agricultural income which was credited to the P&L account under the head "other income". The ld. CIT(A) also recorded a finding to the effect that 7/12 extracts reflected that mango

trees, coconut trees, guava, jamun, rice, cashew nut etc. are being grown. The finding recorded by the ld. CIT(A) has not been controverted by the ld. D.R. by bringing any positive material on record, we, therefore, find no reason to interfere with the findings recorded by the ld. CIT(A) holding that the assessee had earned agricultural income of Rs. 8,01,175/-. With regard to lease rent expenditure of Rs. 26,59,140/- incurred by the assessee, the ld. CIT(A) has disallowed the same on the plea that the expenditure was incurred for earning exempt income. We also find that the lease rent was paid to the directors of the assessee company for leasing the lands to the assessee which deserves to be disallowed u/s 14A of the Act to the extend attributable to earning of exempt income.

9. The Revenue has also taken a ground with regard to additional evidence accepted by the ld. CIT(A) without giving opportunity to the A.O. In this regard, we found that the A.O. has not given sufficient opportunity to the assessee, insofar as the documents were asked at the fag end of the assessment proceedings, therefore, the assessee could not furnish the same before the A.O. These documents were filed before the ld. CIT(A) who has sent all these documents to the A.O. for his remand report. The A.O. has examined all these documents and sends his remand report. Accordingly, there is no violation of Rule 46A insofar as the A.O. has been given due opportunity by the ld. CIT(A) by examining the documents and give his report. After considering the remand report sent by the A.O., the

ld. CIT(A) has decided the issue. Thus there is no contravention of Rule 46A, we, therefore, do not find any merit in the ground taken by the Revenue.

10. In view of the above, we dismiss the grounds taken by the Revenue with respect to the agricultural income and uphold the disallowance of expenditure incurred in the form of lease rentals for earning exempt income u/s 14A of the Act."

5. We find that the Tribunal in Assessee's own case in earlier year has held that agricultural income declared by the assessee has exempt but lease rental paid should be disallowed under section 14Aof the Act. Respectfully following the Tribunal decision for earlier years, we direct the AO accordingly.

6. The next issue in these cross appeals, of assessee as well as Revenue, is as regards to the order of CIT(A) in directing the AO to set off of the business losses in respect of horses breeding activities against other business income and restricting the same against activity of owning and maintenance of horses. For this assessee has raised following ground No. 5 and 6: -

"5. The learned CIT(A) erred in holding that the Appellant Company was carrying on two separate activities viz, activity of Livestock Breeding business and activity of 'owning and maintaining race horses' as defined in Explanation to Section 74A without appreciating that the Appellant Company was engaged in the business of breeding of thoroughbred horses at the company's stud farm established at village Nanoli Dist. Pune and hence, the provisions of section 74A were not applicable to the facts of the present case.

> *6. The learned CIT(A) erred in not appreciating that provisions of section 74A were applicable only in a case where the assessee had income only from stake money and not from any other source and since in the present case, assessee's main source of income was from breeding of horses, the provisions of section 74A were not applicable to the facts of the present case and thus, the entire expenditure incurred by the assessee company was allowable as a deduction while computing the income of the assessee."*

And for Revenue has raised following ground No. 2

> *"2. On the facts and in the circumstances of the case and in the law, the Ld. CIT(A) erred in directing the A.O to set off the business loss respect of horse breeding activities amounting to ₹ 13,05,00,083 against the other business income without appreciating that the activities horse breeding and horse racing in the instant case were mixed/ interconnected, being of same nature and the income from the two activities were not separately indicated in the return of income."*

7. At the outset, the learned Counsel for the assessee stated that the same issue has been dealt by Tribunal in assessee's own case ITA No. 2151 & 2767/Mum/2012 for AY 2007-08 vide order dated 11-06-2015, wherein the Tribunal vide Para 20 has allowed the claim of the assessee on both the issues and the same reads as under: -: -

> *"20. The grievance of the assessee and Revenue relates to the disallowance of losses from activity of owning and maintaining race horses amounting to*

Rs. 3,08,56,448/-, we found that livestock breeding industry wherein the assessee has incurred expenditure and also earned revenue. The assessee is maintaining a stud farm. Its business is that of breeding and only 15% of its horses take part in the racing activity. Over all, it incurred a loss of Rs. 3,08,56,448/-. It has set off of this loss against the income from shipping business as per the P&L account. The A.O. held that breeding and racing activities constitute one activity u/s 74A the loss from the activity of owning and maintaining race horses cannot be set off against any other income and it can be carried forward and set off only against the income from the activity of owning and maintaining the race horses in the future years. Accordingly, the A.O. disallowed the set off of loss from the stud farm against the profits from the ship management activity. The CIT(A) observed that 15% of the assessee's horses take part in racing. The breeding and racing activities are separate. The major activity is that of breeding. The assessee has on an average around 300 horses and only 40 horses run in the races. He did not accept the assessee's contention that entire loss is from breeding activity as racing activity is only incidental to the breeding activity. It was also observed that assessee submitted a columner profit and loss account of the race horses owning and maintenance activity and breeding horses owning and maintenance activity for the year ended 31st March 2007. This bifurcation was done on the basis of separate cost code and ledger accounts maintained in the books of accounts to record the receipts and

expenditure in respect of race horses and breeding horses. In the remand report, the A.O. has agreed that the bifurcation is in consonance with the P & L Account. Accordingly, the CIT(A) has held that the loss of Rs. l,18,63,894/- is from racing activity and he did not allow the set off of this loss against the business income from ship management activity. While he held that the loss of Rs. l,89,92,554/- is from breeding activity and he allowed the set off of this loss against the income. The Revenue's ground is that the entire loss should be disallowed for set off as it is from the racing activity while the assessee's appeal is on the issue that the entire loss should be allowed for set off. The assessee has also shown the bifurcation of its receipts from stud farm and it is to be noted that out of the total receipts of Rs.4,75,70,112/- from this activity, stakes won in the races are amounting to Rs. 69,51,746/- only and hence, this indicates that racing income is just 15% of total income and breeding is the main activity. The assessee has given its object in the Memorandum of Association which is the breeding activity. As per turf club regulations racing and breeding are two branches and administration of these branches come from separate bodies. Thus, A.O. was not justified in holding that the entire activity is of maintaining horses for running in races. The CIT(A) has correctly appreciated that the loss from racing activity should be bifurcated from the breeding activity and that loss should only be disallowed for set off against business income. Accordingly, on the basis of facts and figures, he has correctly held the loss of Rs.1,18,63,894/-

pertains to racing activity and the same is to be disallowed for set off while the balance loss of Rs.1,89,92,554/- is from breeding activity and it is allowed to be set off against the income from ship management business as section 74A cannot be applied to the loss from breeding business. The ld. CIT(A) has recorded a categorical finding to the effect that the company had on an average 300 horses owned by it at the farm and horses of the clients at the farms out of which only 15% participated in the races, therefore, the loss incurred to the activities attributable to race horses cannot be allowed to be set of against other income in view of provisions of section 74A of the Act. The details filed by the assessee was sent by the ld. CIT(A) to the A.O. for remand report. The A.O. has verified the income and expenditure of composite livestock business as well as racing activity with books of account and found the same in consonance with the books of account submitted by the assessee company. After considering the remand report and corroborative evidences, the ld. CIT(A) recorded a categorical finding to the effect that it constitutes only around 15% of the gross receipt, therefore, only loss incurred thereon is liable to be disallowed u/s 74A to be set off against other income. Section 74A is not applicable for the activity of breeding of horses since these horses are maintained for breeding and selling and not for running horse races. The activity of breeding of horses is similar to that of poultry or piggeries etc. where the animals are bred for the purpose of selling. Section 74A is not applicable for such breeding activity. The ld.

CIT(A) also found that during the remand proceedings, the A.O. reported that income and expenditure pertaining to breeding activity and racing activity were found to be captured under two different accounting codes in respect of both the assessment years. The ld. CIT (A) also found that an amount of Rs. 1.94 crores is recovered on account of livery expenses from other horse owners, who have utilized the stables and other services of the stud farm of the assessee. After considering the remand report and corroborative evidences filed before him, the ld. CIT(A) reached to the conclusion that only the business loss in respect of horse breeding activity amounting to Rs. 1,89,92,554/- was liable to be set off against business income whereas loss of Rs. 1,18,63,894/- is from horse racing activity not eligible for set off against business income in view of provisions of section 74A of the Act. The findings recorded by the ld. CIT(A) are as per material on record, thus we do not find any reason to interfere in the findings of ld. CIT(A) and accordingly we confirm the same."

8. Respectfully following the Tribunal decision in assessee's own case in earlier years, we direct the AO to allow the claim of assessee accordingly.

9. The next issue in this appeal of assessee is as regards to the order of CIT(A) treating the activity of owning and maintenance of horses as separate activity. For this assessee has raised following ground No. 7, 7.1 and 7.2 as under: -

"7. Without prejudice to the above grounds, assuming without admitting that the activity of

owning and maintaining race horses' was a separate activity carried out by the assessee company, the learned CIT(A) erred in directing the learned Assessing Officer to verify the nature of expenditure of Rs. 2,24,77,792/- incurred on stud firm stall salaries & wages, sponsorship expenses, legal and professional fees and identify the expenses relating to horse breeding activity and the activity of owning and maintaining race horses and accordingly allow set off of expenses relating to the horse breeding activity against the other business income and carry forward the expenses relating to the activity of owning and maintaining race horse. He erred in not appreciating that as per the working filed by the appellant company during the course of assessment proceedings as well before the-learned CIT(A) Rs.2,03,18,500/- out of the aforesaid Rs. 2,24,77,792/- was allocable to the horse breeding activity and the balance Rs. 21,59,292/- was allocable to the activity of owning and maintaining race horses.

7.1 He erred in not appreciating that most of the above expenses (i.e. Rs. 2,03.18,500/- out of Rs. 2,24,77,792/-) were incurred for the breeding business of the assessee company and that the appellant company had furnished the bifurcation to the learned Assessing Officer during the assessment proceedings and to the learned CIT(A) during the appeal proceedings and hence, the same were not required to be allocated to the activity of 'owning and maintaining race horses'.

7.2 He erred in not appreciating that the Directors remuneration of Rs. 23,95,800/- would have been incurred by the assessee company irrespective of the fact that it was carrying on the activity of owning and maintaining race horses' and therefore, there was no reason to apportion Rs. 4.60.700/- (being part of the Directors' Remuneration of Rs. 23,95,800/-) between the activity of owning and maintaining race horses' and livestock breeding business carried out by the assessee."

10. At the outset, the learned Counsel for the stated that he has instructions from the assessee not to press this issue and hence, the same is dismissed as not pressed.

11. **In the Result, the appeal of assessee is partly allowed and that of the Revenue is dismissed.**

Order pronounced in the open court on 16-02-2018.

Sd/-	Sd/-
(RAJESH KUMAR)	(MAHAVIR SINGH)
ACCOUNTANT MEMBER	JUDICIAL MEMBER

Mumbai, Dated: 16-02-2018
Sudip Sarkar /Sr.PS

Copy of the Order forwarded to:

1. The Appellant
2. The Respondent.
3. The CIT (A), Mumbai.
4. CIT
5. DR, ITAT, Mumbai
6. Guard file.

//True Copy//

BY ORDER,

Assistant Registrar
ITAT, MUMBAI