

**IN THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD BENCH 'B', HYDERABAD**

**BEFORE SMT. P. MADHAVI DEVI, JUDICIAL MEMBER
AND SHRI S. RIFAUR RAHMAN, ACCOUNTANT MEMBER**

ITA Nos. 438, 439 & 440/Hyd/2016
Assessment Year: 2008-09, 2011-12 & 2012-13

Ocean Sparkle Ltd., vs. Dy. Commissioner of
Hyderabad Income-tax, Circle – 16(3),
Hyderabad.

PAN – AAACO 2519H

Appellant

Respondent

Assessee by: Shri T.S. Ajai
Revenue by: Smt. U. Minichandran

Date of hearing: 17/05/2018
Date of pronouncement: 08/06/2018

ORDER

PER S. RIFAUR RAHMAN, AM:

These appeals are filed by the Assessee against separate orders of CIT(A) - 4, Hyderabad, all dated 04/01/2016. Since identical issues are involved in these appeals, they were clubbed and heard together and, therefore, a common order is passed for the sake of convenience.

ITA No. 438/Hyd/2016 for AY 2008-09

2. Briefly the facts of the case are, assessee company, engaged in the business of Cargo Lighterage and Port O&M Operations, filed its original return of income for the AY 2008-09 on 30.09.2008 declaring a total income of Rs.6,12,82,476/- under normal provisions. Book profit u/s.115JB was admitted at Rs.14,89,67,159/-. The assessee filed revised return of income admitting total income of Rs.8,96,07,642 under normal provisions and Rs.14,65,02,499 under provisions of section

115JB. The Order u/s.143(3) of the Income-tax Act, 1961 (in short 'the Act') was passed on 14.12.2010 and assessed the total income at Rs.12,73,91,732/- and raised a demand of Rs.52,34,417/-.

2.1 Later, certain discrepancies were observed from the details submitted by the assessee and, therefore, a notice u/s.148 was issued and served on 26.03.2013 after getting approval from CIT- IV for reopening of the assessment u/s 147 of the Act. In response to the notice, the assessee company filed a letter on 02.04.2013 stating that the revised return filed may be treated as the return filed with reference to notice u/s.148 of the Income-tax. Consequently, a notice u/s 143(2) was issued on 23.07.2013, posting the case on 02.08.2013. In response to the notice, Authorized Representative of the assessee company filed the information on 05.11.2013 in support of its return of income. After examining the information, the assessment u/s.143(3) r.w.s.147 of the I.T. Act, was completed as under:

2.2 During the course of assessment, on verification of books it was found that the assessee has declared other income of Rs.5,43,03,629 in tonnage income (which is not taxable). Further, details showed that this is the other income under tonnage which is primarily profit on the sale of fixed assets and other income. The AO observed that subsection (i) and (ii) of section 115V-I have exhaustive meaning of relevant shipping income of tonnage tax from core activities and incidental activities, and hence other income shall not constitute exempted tonnage income. As per section 115VN "any profit arising from transfer of capital asset shall be computed in accordance with provision of section 45 to 51 with a specific provision that WDV of block of assets would be

substituted by WDV of block of qualifying assets". Further, AO noted that the revised depreciation chart submitted by the assessee clearly shows the sale of tonnage ships at Rs.14,59,08,000/-. A letter was addressed to the assessee calling for clarification in this regard. The assessee submitted a reply on 05/11/2013, and stated as under:

(A) We are into the business of Shipping and Port Operations:

We have opted the Tonnage tax scheme and has got both tonnage vessels and non- Tonnage vessels. The details of block of assets relating to Tonnage vessels and non- Tonnage vessels are maintained separately as required u/s.115VK.

(B) Section 115VN provides that the capital gains arising on sale of Tonnage assets shall be computed in accordance with the Sec 45 r.w.sec. 50. The proviso to section 115 VN clarifies that the provisions of section 50 shall apply for the "written down value of the block of qualifying assets" .

(C) Therefore, the capital gains if any u/s.50, in respect of the block of assets relating to Tonnage assets will have to be computed separately from the block of assets relating to non-tonnage assets.

D) In respect of sale of any vessel of the Tonnage division, the liability to capital gains arises only if anyone of the following situations are attracted;

a) If the sale value of any Tonnage vessel, results in an excess over the aggregate of the written down value of the block of assets of the Tonnage division, then such excess is chargeable to capital gains u/s.50(1).

OR

b) If the block of assets relating to Tonnage division ceases to exist then the liability to the capital gains arises u/s 50(2)

(E) In the present case it can be seen from the computation of written down value of the Tonnage division, filed along with the return of income, that none of the situations prescribed in section 50(1) or 50(2) are

attracted. The sale of the Tonnage vessel namely Ocean melody has not resulted in any credit balance of the block of assets of Tonnage ships and hence section 50(1) is not attracted. Further, the sale of the ship Ocean melody has not resulted in the block of ships of Tonnage division ceasing to exist, and hence section 50(2) is not attracted.

(F) The credit of Rs.5,43,03,629 in the books of accounts, and the statement of allocating profits division wise, is only an accounting exercise. The amount so credited to the Profit & Loss account of the Tonnage division is only "profit on sale of asset", and does not represent the amount chargeable to tax as capital gains. It is settled law and practice that capital gains is to be computed as provided in section 45 to 51, and that there is no relationship to the amount credited in the Profit & Loss account/Books of accounts as profit on sale of asset. In the present case while the profit on sale of the vessel relating to Tonnage division, is Rs.5,43,03,629/- the corresponding amount chargeable as capital gains is Rs. Nil, as per the computation envisaged u/s.50.

(G) The observation that the amount of Rs, 5,43,03,629/- is not exempt Tonnage income and hence the income is non Tonnage income and taxes payable thereon is incorrect and without any basis. There is no provision of law which converts a Tonnage division income into non Tonnage income. The reference to income from core activities is not relevant and extraneous to the issue on hand. The present case is that profit on sale of a Tonnage asset is credited to the Profit & Loss account, while the capital gains on such sale as computed under the provisions of section 50 is Nil. In other words it is not a case of an exemption, but a case of taxable capital gains being Nil on account of the specific method of computation prescribed by section 50."

2.3. In view of the assessee's reply, the AO observed that the provisions of Sec.50(1) or 50(2) of the Act cannot be invoked, however, he opined that the sale of vessel does not constitute the income exempted under tonnage/non-tonnage income and hence the same is to be shown under income from other sources. Therefore it was proposed to add back the amount of

Rs.5,43,03,629 under 'Income from Other Sources'. A show-cause letter was addressed to the assessee on 24.02.2014 and the assessee's A.R accepted for the same. Accordingly, he made an addition of Rs. 5,43,03,629/-.

3. Aggrieved by the order of AO, the assessee preferred an appeal before the CIT(A).

4. Before the CIT(A), the assessee contended that contrary to the statement of AO in the assessment order that a show cause letter was addressed to the assessee on 24/02/2014 and the assessee's AR accepted for the same, no show cause letter was sent to the assessee including any letter dated 24/02/2014 and the assessee's AR had not accepted for any proposal of addition. Further, the assessee stated that any receipt can fall only under one head of income. In this case, the profits of Rs. 5,43,03,629/- falls under the heads of capital gains. It is an exempt capital gains, this was accepted by the AO in para 5 of assessment order. It was stated that once a profit or receipt falls under a particular head of income, it can be classified as income from other sources. Therefore, the action of the AO in treating the profit of Rs. 5,43,03,629/- as income from other sources is not correct.

5. The CIT(A) rejecting the submissions of the assessee, confirmed the order passed by the AO by passing cryptic order without discussing on the main plea of the assessee.

6. Aggrieved by the order of CIT(A), the assessee is in appeal before us raising the following grounds of appeal:

"1. The CIT(Appeals) has erred in law and in the facts and circumstances of the case in confirming the addition of an amount of Rs. 5,43,03,629/- as "income from other sources", being profit on sale and vessels ignoring the contention of the assessee that the said profit on sale of

vessel pertains to Tonnage tax division of the assessee and hence is not liable to tax.

2. The learned CIT(Appeals) has completely erred in law in confirming the said amount of profit on sale of assets as income from other sources. The learned CIT(Appeals) ought to have appreciated that the Assessing Officer having held that the provisions of Section 50(1) or 50(2) of the Act are not invoked has no reason, basis or authority of law to treat the same as income from other sources.

3. The learned CIT(Appeals) ought to have noted that a receipt can fall under only one head of income, and in this case the it is "Capital Gains which is exempt" consequently, there is no authority to treat the same under any other head of income including income from other sources. The CIT(Appeals) ought to have also noted that unless a receipt is chargeable to tax it cannot be taxed under the head income from other sources, that too by merely observing that the income does not constitute income exempted under Tonnage/Non-tonnage income.

4. The CIT(Appeals) having held that the amount of Rs.5,43,03,629/- pertains to Tonnage Tax Division, has erred completely in holding that the Income is to be added under Income from other sources."

7. Considered the rival submissions and perused the material on record. It is noticed that assessee is into business of shipping and port operations. They have two divisions in the shipping business in consonance with the exemption schemes in the I.T. Act as per section 115V namely tonnage division and non tonnage division. The books are maintained separately for both the divisions. During this year, the assessee disposed of ships which falls in the tonnage division. Assessee by following company law provisions and depreciation method as per company law arrived at a profit on sale of fixed asset at Rs. 5,43,03,629/-. The same was declared in the books of account. During hearing, Id. AR also submitted respective ledger copy of the asset and depreciation schedule as per company's Act. (which is part of paper book).

During assessment proceedings, AO treated the above profit on sale of fixed asset relating to tonnage division as income from other sources, reason being this income could not be brought to tax in any other head as the asset is depreciable asset for which provisions of section 50 are attracted. Since, this income could not be brought to tax in any other head of income, it was brought to tax under 'income from other sources'.

7.1 We find it difficult to understand the views of the revenue authorities. It is a normal practice that the profit determined as per Companies Act is not considered for determining the taxable income for the purpose of income tax. It is to be determined separately as per section 14 of the IT Act by following Head of income. An income is brought to tax considering the nature of income which falls within the definition which falls under one of the heads of income. In the given case, sale of ships, which are depreciable assets will fall under the head 'income from capital gains. From the record, which is submitted before us, the assessee has sold two ships and realized sale consideration of Rs. 14,59,08,000/-. It has worked out the profit on sale of ships as below (which is taken from the depreciation schedule as per Companies Act, refer page 12 and 32 of paper book)

Sale consideration		14,59,08,000
Accumulated depreciation		
	Rs. 964,39,932	
	(-)Rs. 41,61,449	<u>9,22,78,483</u>
Profit on sale		Rs. 5,36,29,517
		=====

For the purpose of Income-tax, assessee has followed the depreciation schedule as per concept of Block assets as per section 2(11) of the Act. Since the above assets are depreciable and fall under Block I of assets in the depreciation

schedule of income as followed by assessee, which is reproduced below:

Block – I	
Ships: tonnage	
Written down value as on 01/04/2007	641,981,602
Less: Sales during the year	<u>145,908,000</u>
	496,073,602
Add: Transfer from non tonnage ships	54,829,921
Add: Additions during the year [More than 180 days]	<u>1,052,349,396</u>
	1,603,252,919
Less: Depreciation @20%	<u>320,650,584</u>
	1,282,602,335
Add: Additions during the year [less than 180 days]	<u>199,409,898</u>
	1,482,012,233
Less: Depreciation @10%	<u>19,940,990</u>
Written down value as on 31/03/2008	1,462,071,244
	=====

From the above calculation, it is clear that assessee has reduced the sale consideration of Rs. 14,59,08,000/- from the block of assets and then calculated the relevant depreciation for the year. The profit earned by the assessee in this transaction is reduced from the value of the Block of Asset. As per income tax, any gain or loss in the case of sale or transfer of an asset is adjusted in the value of the Block of assets. The net value of Block of asset is considered for the calculation of depreciation for that year.

7.1.1 For calculating capital gains, as these assets i.e. ships fall under depreciable assets category, the special provisions of section 50 is applicable, as per which, there are two situations narrated, for the sake of clarity, it is reproduced below:

“50. Special provision for computation of capital gains in case of depreciable assets:

Notwithstanding anything contained in clause (42A) of section 2, where the capital asset is an asset forming part of a block of assets in respect of which depreciation has been allowed under this Act or

under the Indian Income- tax Act, 1922 (11 of 1922), the provisions of sections 48 and 49 shall be subject to the following modifications:-

(1) where the full value of the consideration received or accruing as a result of the transfer of the asset together with the full value of such consideration received or accruing as a result of the transfer of any other capital asset falling within the block of the assets during the previous year, exceeds the aggregate of the following amounts, namely:-

(i) expenditure incurred wholly and exclusively in connection with such transfer or transfers;

(ii) the written down value of the block of assets at the beginning of the previous year; and

(iii) the actual cost of any asset falling within the block of assets acquired during the previous year, such excess shall be deemed to be the capital gains arising from the transfer of short- term capital assets;

(2) where any block of assets ceases to exist as such, for the reason that all the assets in that block are transferred during the previous year, the cost of acquisition of the block of assets shall be the written down value of the block of assets at the beginning of the previous year, as increased by the actual cost of any asset falling within that block of assets, acquired by the assessee during the previous year and the income received or accruing as a result of such transfer or transfers shall be deemed to be the capital gains arising from the transfer of short-term capital assets.”

From the above, it is clear that in one of the situation, the value of such transfer is more than the value of block of assets, the excess is chargeable to tax under the head 'capital gains'. In the given case, the excess i.e. profit is reduced from the block of assets and Block continue to have assets value and both situations highlighted in section 50(1) & 50(2) are not attracted. Therefore, as per Income Tax Act, this transaction has not generated any capital gains.

7.2 Therefore, income has to be determined strictly as per the provisions of I.T. Act and not as per Companies Act/Book profit. Only in specific situation book profit is considered for only determining the taxable income u/s 115JB. In no other

situation, the book profit is considered to bring an income which is not as per the provisions of I.T. Act. Just because a separate income is disclosed by the assessee, it does not mean that it should be brought to tax over looking the actual provisions of income tax. Therefore, the profit on sale of vessels of the division tonnage is not taxable as the provisions of section 50(1) & 50(2) are not attracted. Therefore, the addition made by the AO is deleted.

8. In AY 2011-12 (ITA No. 439/H/16) and 2012-13 (ITA No. 440/H/16), the assessee has raised a common ground which is as under:

The learned CIT(Appeals) has erred in law and in the facts and circumstances of the case Directing to allow deduction except to Karaikal Port and workout deduction u/s.80IA accordingly instead of excluding only Karaikal Port - Chemplast Sanmar limited in as much as the CIT(Appeals) was following the Order of ITAT for the AY 2009-10 & AY 2010-11 where in the deduction u/s80IA was allowed for Karaikal Port (Karaikal Port company Pvt.Ltd.) Division and the disallowance as restricted to Chempalst Sanmar - Karaikal Division due to non-furnishing of certificate from the Developer i.e. Chemplast Sanmar, Karaikal Port.”

9. Briefly the facts relating to raise this ground are that the assessee had claimed deduction u/s 80IA of Rs. 2,00,63,037/- to the extent of the income available in respect of following ports:

1. Karaikal Port Company Ltd., Karaikal
2. Gujarat Chemical Port Terminal Company Ltd., Dahej
3. Chennai Petroleum Corporation Ltd., Nagapatnam
4. Chemplast Sanmar Ltd., Karaikal.

9.1 In the return of income filed, assessee had claimed that the income was derived from operating and maintenance of Port Infrastructure and hence eligible for deduction u/s 80IA.

During the course of hearing, assessee was asked to furnish details on the nature of operations from which income was derived so as to make the assessee eligible to claim deduction u/s 80IA of the Act. In response, assessee's AR filed a letter dated 20/01/2014, the contents of which were extracted by the AO at pages 2 & 3. After considering the submissions of the assessee, the AO discussed the issue elaborately in his order and held that as per the amendment made in the Finance Bill, 2009, with a view to preventing the misuse of tax holiday u/s 80IA, it has been provide to clarify with retrospective effect that the benefit under section 80IA(4) will not be available in the case of a works contract awarded by any person and executed by an undertaking or enterprise referred to in section 80IA(1). He, therefore, concluded that as the assessee's nature of activity is execution of contract works, assessee is not eligible for claiming deduction u/s 80IA of the Act.

10. Aggrieved by the order of AO, the assessee preferred an appeal before the CIT(A), who by following the decision of ITAT in AY 2009-10 and 2010-11 in assessee's own case, directed the AO to allow deduction u/s 80IA with regard to Jamnagar, Kakinada and Dahej Ports and disallow 80IA deduction with regard to Karaikal Port, for which the CIT(A) in AY 2010-11 rejected the claim of assessee due to non submission of certificate.

11. Aggrieved, the assessee is in appeal before us.

12. Considered the rival submissions and perused the material on record. This issue is squarely covered by the decision of the coordinate bench of ITAT in assessee's own case for AYs 2009-10 and 2010-11 (Revenue's appeals) in ITA

Nos. 1615 & 1624/Hyd/2014 vide order dated 08/07/2015 wherein the coordinate bench has held as under:

“8. As far as AY 2010-11 is concerned, the issue is more or less identical, except, the fact that assessee has claimed deduction u/s 80IA for the first time in respect of Karaikal port being operated by Karaikal Port company Pvt. Ltd. In this regard, assessee has submitted a certificate from the port authority certifying that they have entered into an agreement with assessee for O&M of the port. That being the case, the decision rendered in respect of AY 2009-10 equally applies to the facts of the present case. Accordingly, we do not find any reason to interfere with the order of Id. CIT(A) in allowing assessee’s claim of deduction u/s 80IA. Therefore, upholding the order of Id. CIT(A), we dismiss the grounds raised by department.”

Since the assessee has submitted a certificate from the port authority certifying that they have entered into an agreement with the assessee for O&M of the port in AY 2009-10 itself, we set aside the order of CIT(A) and direct the AO to allow deduction u/s 80IA to Karaikal port also.

13. In AY 2012-13, the assessee has raised another ground with regard to disallowance of Rs. 25,95,980/- u/ 14A of the Act.

14. The AO disallowed an amount of Rs. 25,95,980/- by observing that the provisions of section 14A are applicable with respect of dividend income earned by assessee engaged in the business of dealing with shares and securities, on the shares held as stock-in-trade when earning of such dividend income is incidental in the trading of shares. Further, he observed that the relation was seen between the exempt income and the expenditure incurred in relation to it and not vice versa. AO also observed that the provisions of sub-section (1) of section 14A provide for not allowing deduction in

respect of expenditure incurred by the assessee in relation to exempt income. The AR filed a detailed submission of the loans attributable to investment. The AO worked out the interest payable on the loans at Rs. 25,95,980/-, which was disallowed u/s 14A. On appeal, the CIT(A) upheld the addition.

15. Considered the rival submissions and perused the material on record. We observe that the legislature has introduced Rule 8D for calculation of disallowance relating to direct expenses associated with the exempt income, interest relating to the investment and administrative expenses.

15.1 While carefully reading the rule 8D(2)(ii), the formula given are:

$A \times B/C$

Where A = amount of expenditure by way of interest other than the amount of interest included in clause (i) incurred during the previous year:

B = the average of value of investment, income from which does not or shall not form part of the total income, as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year;

C = the average of total assets as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year;

In particular, the notes for 'B' clearly states that the average value of investment, income from which does not or shall not form part of the total income. It is clear that we have to include those investments which has generated income and exclude those investments, which have not generated income. In the present case, AO had taken the total investment instead of those investments, which have generated income. Accordingly, we direct the AO to calculate the disallowance of interest as below (as per rule 8D):

$$\text{Interest X } \frac{\text{Investment(which generated income)}}{\text{Average total assets}}$$

The main reason is that as per section 14A, no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to income, which is exempt from tax. The relevance is the expenditure in relation to income. The quantification has to be undertaken in relation to the exempt income. The investment which has not generated exempt income should be excluded from the calculation of ratio to determine the disallowance.

15.2 Similarly, for the administrative expenses, 0.5% of average investments from which the exempt income is received should be considered instead of average of the total investments.

15.3 considering the above discussion, we direct AO to recalculate the disallowance as per rule 8D(iii) as per the above guidance. Accordingly, ground raised by assessee is allowed for statistical purposes.

16. In the result, both the appeals for AY 2011-12 and 2012-13 are allowed.

17. To sum up, all the three appeals under consideration are allowed.

Pronounced in the open court on 8th June, 2018.

Sd/-
(P. MADHAVI DEVI)
JUDICIAL MEMBER

Sd/-
(S. RIFAUR RAHMAN)
ACCOUNTANT MEMBER

Hyderabad, dated 8th June, 2018

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Copy forwarded to:

1. Ocean Sparkle Ltd., 1st Floor, 128 Srinagar Colony, Hyd.
2. DCIT, Circle – 16(3), Hyd.
3. CIT(A) - 4, Hyderabad
4. Pr. CIT - 4, Hyderabad
5. The DR, ITAT, Hyderabad
6. Guard File