IN THE INCOME TAX APPELLATE TRIBUNAL
"B" BENCH : BANGALORE

BEFORE SHRI N.V. VASUDEVAN, VICE PRESIDENT
AND SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER

IT(TP)A No.560/Bang/2016
Assessment year : 2011-12

The Deputy Commissioner of Income Tax, Circle 7(1)(1), Bangalore.	Vs.	M/s. Tata Coffee Pvt. Ltd., No.57, Railway Parallel Road, Kumara Park West, Bangalore – 560 020. **PAN: AABCC 0241R**
APPELLANT		RESPONDENT

IT(TP)A No.647/Bang/2016
Assessment year : 2011-12

M/s. Tata Coffee Pvt. Ltd., No.57, Railway Parallel Road, Kumara Park West, Bangalore – 560 020. **PAN: AABCC 0241R**	Vs.	The Deputy Commissioner of Income Tax, Circle 7(1)(1), Bangalore.
APPELLANT		RESPONDENT

Revenue by	:	Dr. Manjunath Karkihalli, CIT(DR)(ITAT), Bangalore.
Assessee by	:	Shri K.R. Vasudevan, Advocate

Date of hearing	:	26.10.2021
Date of Pronouncement	:	29.11.2021

O R D E R

Per N V Vasudevan, Vice President

IT(TP)A No.647/Bang/2016 is an appeal by the assessee, while IT(TP)A No.560/Bang/2016 is an appeal by the revenue. Both these appeals are directed against the order of assessment dated 27.01.2016 for the assessment year 2011-12 passed by the DCIT, Circle 7(1)(1), Bangalore u/s. 143(3) r.w.s. 144C(13) of the Income-tax Act, 1961 [the Act] for the assessment year 2011-12.

2. We shall first take up the **appeal of the assessee**. Grounds relating to TP issues has been raised in ground No. I (1) to (10). We deem it appropriate to consider ground I (3) raised by the assessee with regard to adoption of Most Appropriate Method (MAM) for determination of ALP of the international transactions in dispute. The said ground reads as follows:-

> "I. Transfer Pricing Grounds
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> 3. The learned AO, learned TPO, and the Hon'ble DRP have erred in not considering Comparable Uncontrolled Price (*CUP') as the most appropriate method applied by the Appellant in respect of the international transactions with the AEs. While doing so, the learned AO, learned TPO, Hon'ble DRP have erred in:
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> a) not appreciating the fact that CUP method is more superior and reliable in comparison to Transactional Net Margin Method (`TNMM') with respect to the international transaction of sale of instant coffee by the Appellant to the AE.
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> b) ignoring the justification and the documentary evidences provided by the Appellant in the TP documentation and during the transfer pricing audit, in support of the application of CUP method."

3. The assessee is engaged in the business of growing of coffee and tea, curing and marketing them after value addition. The assessee purchased Robusta and Arabica coffee and produced instant coffee. The assessee entered into international transaction with its Associated Enterprise (AE) in respect of purchase of Robusta green coffee. It also entered into transaction of sale of instant coffee with its AE. The transaction of purchase and sale between the assessee and the AE was as follows:-

Sl. No	Type of transaction	Amount (Rs) Paid	Amount (Rs) received	Quantity sold
1	Purchase of Robusta Green Coffee	13,87,43,124		22,17,203
2	Sale of Instant Coffee	-	50,72,01,366	15,76,08
3	Commission paid	1,23,36,810		
4	recovery of Expenses	-	2,90,767	

4. Since as per the provisions of section 92 of the Act, income arising from any transaction between the assessee and its AE has to be determined having regard to the arm's length price (ALP), the assessee filed a TP analysis justifying the price it paid for purchase of Robusta green coffee and the price it received on sale of instant coffee from and to its AE. The asse adopted Comparable Uncontrolled Price (CUP) method as the MAM for determining the ALP of the international transactions in question. In respect of purchase of Robusta green coffee, the assessee relied on the price at which 8'O Clock coffee Co., USA which was the AE of the assessee purchased identical quantity of coffee from a third party. Similarly, in respect of sale of instant coffee, the assessee had sold instant coffee to OOO Sunty Ltd., Russia. The assessee had sold similar type of coffee in the same geographical region and the weighted average sale price to 3rd party customers was used as a benchmark for justifying the sale price by the assessee to the AE. The TPO had proposed to reject the TP analysis on the claim of assessee that international transaction was at

arm's length price. The assessee in reply to the same highlighted as to how the CUP was the MAM and in this connection placed reliance on the decision of the ITAT Pune Bench of the Tribunal in the case of *ACIT v. MSS India Pvt. Ltd., 123 TTJ 657 (Pune)* wherein it was held that a method cannot be disputed in preference over Transaction Net Margin Method (TNMM) unless the revenue authorities are able to demonstrate the fallacies in application of standard methods and that preference of one method over the other method must be justified by the TPO. The assessee also pointed out that in the light of the data available for applying the CUP method, TNMM should not be applied.

5. The TPO, however, rejected the CUP method without assigning reasons and by merely observing that CUP method requires high degree of comparability of products and functions. He also observed that the TPO document contains various defects without pointing out as to what are those defect and he finally concluded that the assessee failed to apply TNMM, even though there were comparable companies. Thereafter, the TPO proceeded to apply TNMM and ultimately made an addition and consequently determined the ALP of a sum of Rs.14,49,12,600.

6. The assessee filed objections to the draft assessment order wherein addition suggested by the TPO was incorporated by the AO. The DRP in its directions with regard to MAM by a cryptic order upheld the action of the TPO in adopting the TNMM. The observations of the DRP in this regard are as follows:-

> "2.1 The assessee has made detailed submissions on these issues and the same have duly been considered. These issues have been discussed in detail by the TPO in his order. Although the assessee used CUP method to determine ALP of the international transactions, however it failed to analyze and summit comparable companies having FAR profile similar to it. In absence of same CUP method cannot be used. So the TPO is right in adopting

> TNMM as the most appropriate method. As regards assessee's claim that for AY 2010-11 CUP was considered as the most appropriate method and TNMM was not accepted, it is observed that the international transaction involved in AY 2010-11 was entirely of different nature and so the most appropriate method for the same was found to be CUP. The method to be adopted depends upon the nature of transaction and the availability of data of comparables. Even for a single year different methods can be used for different types of transactions and for same type of transactions in different years, different methods can be used depending upon availability of relevant data. So the submissions of the assessee are devoid of any merit. While rejecting the TP study of the assessee, the TPO has given detailed reasons for the same in para 7 of his order and the same cannot be faulted with. Considering above the objections of the assessee are not accepted."

7. Aggrieved by the aforesaid order of the DRP which was incorporated in the final order of assessment of the AO, the assessee has preferred ground No.3 before the Tribunal. The ld. counsel for the assessee brought to our notice several decisions of the Tribunal wherein it was held that in the light of available data to apply CUP method, TNMM should not be resorted to. It was also brought to our notice that the TPO himself in the subsequent assessment year i.e., AY 2010-11 accepted the CUP as the MAM for benchmarking some international transactions.

8. On the other hand, the ld. DR placed reliance on the observations of the Tribunal.

9. We have heard both the parties and perused the material on record. From a perusal of the orders of the TPO and the DRP, it is seen that no valid reasons have been assigned by the revenue authorities for not accepting the CUP method as the MAM. The law with regard to selection of comparables when CUP is sought to be applied as the MAM has been laid down in several decisions as follows:-

(a) The Delhi Tribunal in the matter of *Hughes Systique India (P.) Ltd. v. Asstt. CIT [2013] 36 taxmann.com 41 (Delhi - Trib.)*, *inter alia* held that:—

> "6.5 The CUP method provides the most direct comparison for the purpose of determining the arm's length price of international transactions and is to be preferred over the other profit based methods. Reliance is placed in this regard on the following decisions:
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> - Aztec Software & Technologies Services Ltd. v. Asstt. CIT [2007] 107 ITD 141/162 Taxman 119 (Bang.) (SB)
>
> - UCB India (P.) Ltd. v. Asstt. CIT [2009] 30 SOT 95 (Mum.)
>
> - Gharda Chemicals Ltd. v. Oy. CIT [2010] 35 SOT 406 (Mum.)
>
> - Intervet India (P.) Ltd. v. Asstt. CIT [2010] 39 SOT 93 (Mum.)
>
> - Asstt. CIT v. Dufon Laboratories [2010] 39 SOT 59 (Mum.) 11"

(b) The Mumbai Tribunal in the case of *Serdia Pharmaceuticals (India) (P.) Ltd. v. Asstt. CIT [2011] 44 SOT 391/9 taxmann.com 13* while dealing with the priority of applications of methods for the determination of ALP, has held as under:—

> "64. . . as long as CUP method can be reasonably applied in determining the arm's length price of an international transaction in a particular fact situation, and unless another method is proven to be more reliable a method vis-a-vis the fact situation of that particular case, the CUP method is to be preferred. The reason is simple. When associated enterprises enter into a transaction at such conditions in commercial and financial terms, which are different from commercial and financial terms imposed in comparable transaction between independent enterprises, the difference in these two sets of conditions in financial and commercial terms re attributed to inter relationship

> between the associated enterprises that is sought to be neutralized by the transfer pricing regulations. As long as CUP method can be reliably applied on the facts of a case, it does offer most direct method of neutralizing the impact of inter- relationship between AEs on the price at which the transactions have been entered into by such AEs. "

(c) Relying on the decision of *Serdia Pharmaceuticals India (P.) Ltd. (supra)*, the Delhi Tribunal in the case of *Clear Plus India (P.) Ltd. v. Dy. CIT [2011] 10 taxmann.com 249*, inter alia held that:—

> "7 . . . . In the case of Serdia Pharmaceuticals India (P) Limited, it has been held that CUP method is a preferred method and it leads to more reliable results vis-a-vis the results obtained by applying transaction profit method. In the case of SNF (Australia) Pty. Limited, it has been held that the focus is on the market in which products are acquired. The ratio of this case is applicable mutatis-mutandis to the facts of the case as the focus is on the market in which products are sold."

(d) In the case of *Gharda Chemicals Ltd. (2010) 35 SOT 59 (Mum)*, the Tribunal held that internal comparable should be preferred over external comparables. The relevant extract of the judgment is furnished here in below:—

> "Internal CUP method envisages comparing the uncontrolled transactions of the appellant itself with other unrelated parties so as to determine the ALP with the AE. However the External CUP method disregards the price charged or paid by the appellant to or from its unrelated parties and contemplates the comparison of the price so charged from or paid to its AE with some external independent reliable price data under similar circumstances of transactions with AE. Ordinarily the Internal CUP method should be preferred over the External CUP method as it neutralizes several distinguishing factors, such as the local factors and the economies available or unavailable to the appellant in particular, having bearing over the comparison of price charged from unrelated parties and AE."

10. In view of the above judicial precedents, we find that the CUP method provides the most direct comparison for the purpose of determining the arm's length price of international transactions and is to be preferred over the other profit based methods. Accordingly in the instant case internal CUP method should be preferred over the external CUP method. Hence, we hold that in the instant case, the CUP Method (internal) is the most appropriate method in determining the arm's length price of the international transaction.

11. In the light of the law as explained above and the admitted factual position that the TPO in AY 2010-11 has himself accepted the CUP as the most appropriate method (MAM) for determining the ALP of the international transactions, we are of the view that the CUP method ought to have been accepted as the MAM. We therefore set aside the order of the DRP insofar as it relates to the determination of the ALP of the international transactions and remit the issue to the AO/TPO for fresh consideration by applying CUP as the MAM.

12. The other grounds of appeal with regard to application of TNMM are therefore rendered academic. Hence the issue of determination of ALP under TNMM is left open.

13. The next issue that arises for consideration in the assessee's appeal is the disallowance of R&D Expenses of Rs.38,10,000. This issue has been raised in ground No.11 by the assessee. The assessee incurred this expenditure towards R&D. The following activities were treated as R&D:-

- Soil Nutrient Index.
- Varietal trial of Coffee. Pepper and Cardamom.
- Bio-Control Research.
- Pests and Disease Control Research.
- Coffee effluent Treatment.
- Compost - Vermicompost Experiment.

- Quality Analysis of Coffee & Pepper.
- Analysis of Agro-inputs for quality standards.
- Water management Research-- Drip irrigation for coffee.
- Crop Diversification.

14. It is undisputed that the R&D expenses pertain to activities relating to business of the company like coffee effluent treatment, pests and disease control research, water management research, etc. The AO held that the expenditure in question results in acquiring rights and therefore has to be treated as capital in nature. The view of the AO was confirmed by the DRP and hence ground No.11 by the assessee before the Tribunal.

15. The ld. counsel for the assessee brought to our notice that identical issue was considered in assessee's own case for AY 2010-11 in IT(TP)A No.568 & 729/Bang/2015, order dated 22.3.2021 by the Bangalore Bench of the ITAT and in para 6 to 6.4, the Tribunal ultimately concluded that the expenses had to be allowed as a deduction. The following were the relevant observations of the Tribunal:-

> "**6.** The next issue relates to disallowance of Research & Development expenses incurred by the assessee. The A.O. noticed that assessee has claimed a sum of Rs. 42.95 lakhs towards Research & Development expenses. The details of the said expenses have been tabulated by Ld. DRP as under:

Particulars	*Amount (Rs.)*
Salaries, Wages & Bonus-R&D	2,650,408
Contribution to P F/Other Fund. R&D	122,392
Workmen & Staff Welfare Expenses-R&D	5,211
Repairs To Buildings -Stores—R&D	9,603
Repairs To Machinery- Wages-R&D	8,272
Repairs To Machinery -Stores-R&D	3,986
Repairs To Machinery -Others-R&D	4,115

Insurance-R&D Exps	83,693
Miscellaneous Expenses-R&D Exps	241,442
Cos contri SAS to R&D Off	138.508
Medical expenses-officers R&D	111,486
Medical expenses-staff & artisen - R&D	130
Travelling expenses-air/bus/train/auto fare - R&D	13,083
Travelling Expenses-R &D	51,771
Biological Control Laboratory	1,103
Library Books & Periodicals-R&D	6,331
Coffee Plants Plot Exprnt Exps-R&D	2,500
Total	**4,295,176**

6.1 Before the A.O., the assessee submitted that these expenses have been incurred in connection with the routine business activities carried on by it on the following activities:

- Soil Nutrient Index
- Varietal trial of Coffee, Pepper and Cardamom
- Bio-Control Research
- Pests and Disease Control Research
- Coffee effluent Treatment
- Compost-Vermicompost Experiment
- Quality Analysis of Coffee & Pepper
- Analysis of Agro-inputs for quality standards
- Water management Research - Drip irrigation for Coffee
- Crop diversification.

Accordingly, it was submitted that this expenditure is revenue in nature and allowable as deduction u/s 37(1) of the Act. In the alternative, it was submitted that the assessee has obtained approval from Department of Scientific & Industrial Research, Government of India and hence, these are allowable u/s 35 r.w.s. 43(4)(*ii*) of the Act. It was submitted that this expenditure does not create any rights. The A.O. however, took the view that incurring of R&D expenses results in creation/acquisition of

rights to the assessee. Accordingly, he disallowed the above said amount of Rs. 42.95 lakhs incurred by the assessee. The Ld. DRP also concurred with the view taken by the A.O.

6.2 The Ld. A.R submitted that the assessee has been incurring expenditure on research & development activities in a routine manner year after year and it has not developed any "copy right" as presumed by the A.O. He further submitted that the capital expenditure incurred in connection with the R&D activities have been duly capitalized by the assessee and details of the same have been reported in the annual report of the assessee. He submitted that revenue expenses have been charged to profit and loss account. He further submitted that major portion of the R&D expenses is the expenditure incurred on salaries & wages paid to its staff. He submitted that the assessee is constrained to maintain "R & D department" in the normal course in order to meet the competition and to remain upto date with the changes in the market. Accordingly, the Ld. A.R. submitted that there is no justification for treating this expenditure as capital in nature.

6.3 On the contrary, the Ld. D.R. submitted that the assessee has not been able to substantiate before the A.O. that it has obtained approval from DSIR, Govt. of India. The assessee also failed to establish that this expenditure does not create any rights.

6.4 We heard the rival contentions on this issue and perused the record. From the details of expenditure furnished by the assessee, we notice that the assessee has claimed salary & wages expenses, repairs expenses, *etc*. under the head "R & D expenses". From the annual report furnished by the assessee, we notice that the assessee has duly capitalized the capital expenditure incurred by it. We also noticed that the A.O. has observed that these expenses have resulted in creation of copy right in the hands of the assessee. However, the A.O. has not brought any material on record to show that these expenses has resulted in creation "copy right", meaning thereby, the A.O. has made his observations on surmises and conjectures. We also agree with the contentions of Ld A.R that it is a business necessity to maintain R & D department in order to meet the competition and changing business circumstances. Unless it is established that the R & D department has undertaken a mission to invent something new which would give a copy right to the assessee, in our view,

routine expenses cannot be considered as capital in nature. Accordingly, we are of the view that the A.O. was not justified in treating the above expenses as capital in nature. Accordingly, we direct the A.O. to delete the addition."

16. The facts and circumstances in the present year are identical and the nature of expenses are also identical. Hence following the decision of the Tribunal for AY 2010-11 in assessee's own case, we direct the expenses to be allowed as a revenue expenditure and allow ground Nos.11 raised by the assessee.

17. Ground No.12 is with regard to disallowance made u/s. 14A of the Act. The facts on this issue are that the assessee received dividends amounting to Rs.2,33,42,160 during the relevant previous year. The assessee had disallowed Rs.1,76,477 u/s. 14A of the Act being a portion of salary cost of employees managing the investment portfolio of the assessee. It was the case of the assessee that investments were made out of its own surplus funds and there was no other interest costs. The details of investments which yielded dividend income claimed as exempt were as follows:-

Particulars	Amount of dividend (Rs.)	Financial Year of purchase of investments	Remarks
Tata Tea Limited	39,65,000	1999-2000	Acquired on amalgamation
Tata Chemicals Limited	4,38,650	1994-95	Acquired on amalgamation
Joonktolle Tea & Industries Ltd.	28,810	1999-2001	Acquired on amalgamation
Industrial Development Bank of India	48,480	1999-2000	Acquired on amalgamation
Alliance Coffee Ltd.	1,78,61,20	2006-07	Acquired from Surplus Fund
			Fund
Total exempt income	**2733,42,160**		

18. The AO did not agree with the submissions of the assessee and by applying the provisions of section 14A of the Act r.w.s. Rule 8D of the Rules, he disallowed a sum of Rs.6,80,643. The DRP confirmed the action of the AO by following its own order for the AY 2010-11 wherein identical disallowance was confirmed by the DRP.

19. Aggrieved by the order of the DRP, the assessee has raised ground No.12 before the Tribunal. At the time of hearing, it was brought to our notice that for AY 2010-11 in IT(TP)A No.568 & 729/Bang/2015, order dated 22.3.202, the issue of disallowance u/s. 14A has also been discussed by the Tribunal and the issue was restored by the Tribunal to the AO with the following observations:-

> "7. The next issue urged by the assessee relates to disallowance made by the A.O. u/s 14A of the Act. The assessee earned exempt dividend income of Rs. 1.51 crores. The assessee voluntarily disallowed a sum of Rs. 1,78,013/- u/s 14A of the Act. The A.O. took the view that the disallowance should be computed under rule 8D of I.T. Rules. Accordingly, he disallowed a sum of Rs. 6,83,989/-from out of interest expenditure under rule 8D(2)(ii) of I.T. Rules and Rs. 3,05,800/- out of administrative expenses under rule 8D(2)(iii) of I.T. Rules. Out of the aggregate amount of disallowance of Rs. 9,89,789/- so computed, the A.O. gave set off of Rs. 1,78,013/- voluntarily disallowed by the assessee and made further disallowance of Rs. 8,11,776/- u/s 14A of the Act. The Ld. DRP also confirmed the same. The Ld. A.R. submitted that the A.O. had made identical disallowances u/s 14A of the Act in assessment years 2006-07 to 2008-09. Before the Tribunal, the assessee had submitted that the investments have been made by the assessee in the past out of own surplus funds and hence, there is no requirement of making any disallowance out of interest expenses. Hence, the ITAT, vide its order dated 6-9-2013 passed in ITA No. 1462 to 1464/Bang/2012, has restored the matter to the file of the A.O. for examining the issue afresh. The Ld. A.R. submitted that the A.O. has since passed the order giving effect to the order passed by the Tribunal and he did not make any disallowance out of

interest expenditure. The Ld. A.R. submitted that the facts are identical in the instant case and accordingly, prayed that the matter may be restored to the file of the A.O. with similar directions.

7.1 The Ld. D.R. on the contrary, submitted that the assessee has not demonstrated that the investments have been made out of surplus funds in the past. Further, the assessee is maintaining its accounts in a consolidated manner, whereby all funds and receipts are intermingled in a common pool. Hence, it will be difficult to relate the investment to a particular receipt. Accordingly, the Ld. D.R. submitted that the A.O. was justified in making disallowance out of interest expenses under rule 8D(2)(ii).

7.2 We heard the parties on this issue and perused the record. We notice that the issue of disallowance under rule 8D(2)(ii) out of interest expenses have been restored to the file of the A.O. by the coordinate bench in the assessee's own case for assessment years 2006-07 to 2008-09. It is the submission of the Ld. A.R. that the investments have been made by the assessee in the past out of surplus funds and these aspects have been verified by the A.O. in the restored the said proceedings. Accordingly, the A.O. did not make any disallowance out of interest expenditure in the above said year. In view of the above said facts, we are of the view that, consistent with the decision taken by the coordinate bench in the assessee's own case, the issue of disallowance of interest expenditure under rule 8D(2)(ii) requires fresh examination at the end of the A.O. Accordingly, we set aside the order passed by the A.O. on the above said issue and restore the same to the file of the A.O. for examining it afresh. The disallowance made under rule 8D(2)(iii) was out of administrative expenses shall stand sustained. While giving effect, the AO shall give set off of the disallowance voluntarily made by the assessee."

20. We are of the view that identical direction in the present assessment year should be given as the facts of the case are identical. We therefore restore this issue to the AO for fresh consideration as directed by the Tribunal in AY 2010-11.

21. In ground No.13, the assessee has sought that credit for tax deducted at source was not given properly. We are of the view that it would be just and appropriate to direct the AO to give proper credit for TDS in accordance with the law.

22. The other grounds of appeal are purely consequential and academic and do not require any consideration.

23. Accordingly, the appeal by the assessee is partly allowed.

Revenue's appeal

24. The grounds of appeal raised by the revenue are as follows:-

> "1. The directions of the Dispute Resolution Panel are opposed to law and facts of the case.
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> 2. Whether on the facts and in the circumstances of the case, the DRP was justified in law in direction the AO to treat the shade trees as capital asset and to allow the claim of long term capital loss of the assessee.
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> 3. Whether the DRP is correct in law in placing reliance on the decision of the Hon'ble jurisdictional High Court of Karnataka in assessee's own case for AY:200-304 and 2004¬05 in ITA No.110 & 111 of 2009 and in directing the AO to allow the long term capital loss in spite of the fact that the department didn't accept the decision of the Hon'ble High Court of Karnataka and filed SLP.
>
> 4. For these and other grounds that may be argued at the time of hearing, it is prayed that the directions of Dispute Resolution Panel in so far as it relates to the above grounds may be reversed.
>
> 5. The appellant craves leaves to add, alter, amend and /or delete any of the grounds mentioned above."

25. The only that arises for consideration in the revenue's appeal is as to, whether the DRP was justified in directed the AO to treat the loss on sale of shade trees as long term capital loss. A the time of hearing, it was brought to our notice that identical issue was considered by the Tribunal in assessee's own case for the AY 2010-11 in IT(TP)A No.568 & 729/Bang/2015, order dated 22.3.2021 wherein the Tribunal held that the loss/gain on sale of shade trees gives rise to capital gain and does not give rise to business income as contended by the revenue. The following were the relevant observations of the Tribunal:-

> "**10.1** The facts relating to the above issue are stated in brief. During the year under consideration, the assessee had sold Rosewood, Silver Oak, Eucalyptus and other trees. The assessee computed capital gain on sale of Rosewood &Silver Oak after considering indexed cost of acquisition by taking fair market value as on 1-4-1981. In respect of Eucalyptus and other trees 70% of the sale consideration was considered as the cost of acquisition based on the decision rendered by Hon'ble Kerala High Court in the case of *CIT* v. *Pullangode Rubber Produce Co. Ltd.* [1992] 62 Taxman 298/189 ITR 580. Accordingly, the assessee declared a capital loss of Rs. 30.67 lakhs. The A.O. took the view that the activities carried on by the assessee in nurturing/growing and selling of trees is normal business activities of the assessee. Accordingly, the AO took the view that the gain arising on sale of trees should be assessed as normal business income. The Ld. DRP however, accepted the contentions of the assessee that the income arising from sale of trees is Capital gains in the hands of the assessee on noticing that the Hon'ble Karnataka High Court has upheld the view of the assessee in its own case relating to assessment years 1997-98 to 1999-2000 and 2001-02 *Lata Coffee Ltd.*. v. *Jt. CIT* [2012] 27 taxmann.com 98 (Kar.). Accordingly, the Ld. DRP directed the A.O. to compute capital gains adopting fair market value of the asset as on 1-4-1981. Aggrieved, the revenue has filed this appeal.

10.2 We heard the parties on this issue and perused the record. We notice that the Ld. DRP has decided the issue in favour of the assessee with the following observations:

> "8.3 The tax payer disagreed with the above treatment and submitted that these trees are maintained as shade trees for the coffee bushes since shade trees are absolutely essential for the protection of coffee bushes. It is not possible to grow coffee in India without the necessary shade trees. It was submitted that amongst other trees only Silver oak is converted into stock in trade and transferred to the value addition division for processing and manufacture of plywood's. As regards other trees, the subsequent treatment is tabulated below:

Rosewood	Compulsorily sold through Government auction
jungle Wood	Compulsorily sold after Government approval
Eucalyptus	Sold to third parties
Miscellaneous timber	Internally consumed by the company

To protect the coffee bushes, the company cuts the old shade trees. Usage of such cut trees (alter than rosewood and Eucalyptus) in its timber division was claimed to be incidental to Its coffee plantation business.

8.4 It was submitted that sale of rosewood to government depot and transfer of silver oak and other trees to Timber division is shown as sale of capital asset and offered to tax as capital gains. Further, sale of marine plywood, fire retardant plywood, phenol formaldehyde black board, commercial plywood produced in timber division are shown as business income. It was submitted that the reason for the different treatment is the difference in characterization of the item of sale *i.e.,* trees. As regards Rosewood, Eucalyptus and other trees which are used for shade of coffee bushes are in the nature of capital assets and hence, income/loss from their sale is computed under the head "Capital gains" once the income is recognized in the books of the company based on its accounting.

As regards, Silver Oak the income is computed under the head "Capital gains" upon their conversion into stock in trade of

timber value addition division. The subsequent sale in the timber division is of the stock in trade of the business of the timber division and hence, income from their sale is computed under the head "Business income".

8.5 The following case laws were relied upon by the assessee:

- Decision of Honourable Karnataka High Court in Assessee's own case for AY 1997-98, 1998-99, 1999-2000 and AY 2001-02 reported in 27 taxmann.com 98
- Decision of Honourable Karnataka High Court in Assessee's own case for AY 2003-04 and AY 2004-05 in ITA No. 110 and 111 of 2009
- *Emerald Valley Estates Ltd*. [1996] 222 ITR 799 (Karnataka HC)
- *Travancore Tea Estates* v. *CIT* [1974] 93 ITR 314 (Kerala HC)
- *State of Kerala* v. *Karimtharuvi Tea Estate Ltd*. [1964] 51 ITR 129 (Kerala HC)
- *C. Hanumantharao (Deceased)* v. *CIT (Madras HC)* (Tax case appeal No. 44/2004)
- The Honourable Bangalore Tribunal in the assessee's own case for AY 2006-07, 2007-08 and 2008-09 [ITA 1462 to 1464/Bang/2012]
- *CIT* v. *Pullangode Rubber Produce Company Limited* (189 ITR 580)

8.6 We have considered the submissions as above and find that the facts regarding treatment of shade trees as capital assets is squarely covered by the decision of the Hon'ble jurisdictional High Court in the tax payer's own case apart from the Hon'ble ITAT's order cited. The computation of capital gains and the fair market value of the asset as on 1-4-1981 will be considered by the AO in this regard."

10.3 We notice that the Ld. DRP has followed the binding decision rendered by Hon'ble Karnataka High Court in the assessee's own case referred (*supra*). Under these circumstances we do not find any infirmity in the directions so given by Ld. DRP."

26. Following the decision of the Tribunal referred above, we uphold the order of the DRP and dismiss the appeal of the revenue.

27. In the result, the appeal of the assessee is partly allowed, while the appeal by the department is dismissed.

Pronounced in the open court on this 29th day of November, 2021.

Sd/-	Sd/-
(CHANDRA POOJARI)	(N V VASUDEVAN)
ACCOUNTANT MEMBER	VICE PRESIDENT

Bangalore,
Dated, the 29th November, 2021.

/*Desai S Murthy /*

Copy to:

1. Assessee 2. Revenue 3. CIT 4. CIT(A)
5. DR, ITAT, Bangalore.

By order

Assistant Registrar
ITAT, Bangalore.