

IN THE INCOME TAX APPELLATE TRIBUNAL  
“J” BENCH, MUMBAI  
BEFORE SHRI PRASHANT MAHARISHI, ACCOUNTANT MEMBER &  
SHRI PAVAN KUMAR GADALE, JUDICIAL MEMBER

ITA No. 5875/Mum/2017

(A.Y: 2013-14)

M.Pallonji Shipping Pvt Ltd.46A Veetrag Chambers, Cawasji Patel Street, Fort, Mumbai-400001	Vs.	DCIT – 5(2)(2) Mumbai
स्थायी लेखा सं./जीआइआर सं./PAN/GIR No. : AAECM4615L		
Appellant	..	Respondent

Appellant by :	Dr.K. Shivaram, & Shri Rahul Hakani.AR
Respondent by :	Ms.Vatslaaa Jha.CIT.DR

Date of Hearing	08.06.2022
Date of Pronouncement	28.06.2022

आदेश / O R D E R

**PER PAVAN KUMAR GADALE JM:**

The assessee has filed the appeal against the order of the A.O passed u/s 143(3) r.w.s 144C(13) of the Act, 1961 in pursuance to directions of the Dispute Resolution Panel (DRP) u/sec 144C(5) of the Act. The assessee has filed the following grounds of appeal as under:

1. On the facts and in the circumstances of the case and in law, the Hon'ble Dispute Resolution Panel (DRP) erred in upholding the proposed transfer pricing addition of notional interest of Rs. 4,44,67,107/- (net) on account of loan given to M Pallonji Shipping Singapore Pte Ltd (MPS Singapore) without appreciating the fact that the advance to subsidiary was in the nature of a quasi capital advance and this being a way of doing business.

(B) Without prejudice to Ground 1(A) above, the DRP erred in directing the AO to make addition of notional interest at the LIBOR rates. The appellant submits that since the loan was given in Singapore, it ought to be benchmarked at SIBOR rates.

(C) Without prejudice to Ground 1(A) above, the DRP erred in directing the AO to make addition of notional interest at a spread of 500 bps. The appellant submits that a spread of 200 bps was held to be reasonable by the Hon'ble Bombay High Court in the case of CIT v Aurionpro Solutions Ltd. (ITA 1869 of 2014).

2 (A) On the facts and in the circumstances of the case and in law, the Hon'ble DRP erred in upholding the proposed addition on account of foreign exchange gain of Rs5,18,56,618/-.The Hon'ble DRP failed to appreciate that the gain arose on account of loan given to MPS Singapore which was used to acquire a capital asset i.e. ships, therefore, capital in nature.

B) Without prejudice to Ground 2(A) above, the DRP failed to appreciate that such exchange gain is notional in nature, therefore, not liable to be taxed.

3. The appellant craves leave to add, alter or amend any ground of appeal at the time of hearing or before.

At the time of hearing the Ld. AR submitted that the assessee is not pressing ground of appeal No.1(B). Accordingly the ground of appeal is treated as withdrawn and is dismissed.

2. The brief facts of the case are that the assessee company is engaged in the business of shipping owners, charter of ships and allied activities. The assessee company is a holding company of M. Pallonji Shipping Singapore Pte Ltd. The assessee has filed the return of income for the A.Y 2013-14 on 30.11.2012 disclosing a total income of Rs. 42,19,660/-. Subsequently the case was selected for scrutiny and notice u/s 143(2) and 142(1) of the Act was issued. In compliance to notice, the Ld. AR of the assessee appeared for time to time and submitted the details and information. The Assessing Officer (AO) on perusal of Audit Report in FormNo.3CEB and the financial statements found that the assessee has international transactions exceeding Rs.15 crores, therefore the matter was referred to the Transfer Pricing Officer(TPO) for determination of Arm's Lengths Price (ALP) in relation to international

transactions with its AEs. Since the assessee company is engaged in the business of hire, charter and lease of all kind of ships, boats, barges etc, the income of the assessee computed under chapter XIIG of the Income Tax Act. During the F.Y 2012-13 the assessee has received income of Rs. 5,45,69,192/- in the shipping business and the assessee is covered under tonnage tax and it has offered income of Rs. 36,95,000/- under chapter XIIG of the Act.

3. The TPO has issued notice u/s 92CA(2) of the Act along with the questionnaire to furnish the necessary documents and details in support of ALP. The assessee has international transactions with its AE as per Form.No.3CEB as under:

4. *International Transactions:*

*The assessee has reported following international transactions with the Associate Enterprises (AE) in Form 3CEB:*

<i>S. No</i>	<i>Nature of international Transctons</i>	<i>AE</i>	<i>Amount</i>	<i>Method adopted by assessee</i>
1	<i>Purchase of Ship</i>	<i>M Pallonji Shipping Singapore Pte</i>	<i>54,29,00,000</i>	<i>CUP</i>
2	<i>Purchase of</i>	<i>M Pallonji</i>	<i>4,26,53,264</i>	<i>CUP</i>

	<i>Fuel</i>	<i>Shipping Singapore Pte Ptd.</i>		
3	<i>Charter Ship Services Provided</i>	<i>M Pallonji Shipping Singapore Pte Ptd.</i>	<i>1,08,78,000</i>	<i>CUP</i>
4.	<i>Amount advanced</i>	<i>M Pallonji Shipping Singapore Pte Ptd.</i>	<i>169,85,15,124</i>	<i>Other method</i>
5.	<i>Corporate Guarantee obtained</i>	<i>M Pallonji Shipping Singapore Pte Ptd.</i>	<i>128,94,96,246</i>	<i>Other method</i>

4. The assessee has submitted the documentary evidences and detailed explanations in respect of international transactions in support of Form.No.-3CEB. On perusal of the information, the TPO found that the assessee has provided interest free advances to its AEs i.e M. Pallonji Shipping Singapore Pte Ltd and the amount of Rs.169,85,15,124/- is outstanding advance as on 31.03.2013. The TPO has called the assessee to explain the benchmark to ALP with relevant supporting documents. Whereas the assessee has submitted, the details of terms loans obtained from HDFC bank and advances to its AE. The TPO considered the facts that the loan was given out of the own funds and were converted into shares in the F.Y 2014-15 and the assessee has submitted the

documents supporting the claim. The TPO has summaries the submissions of the assessee on the reply filed at page 4 Para 6.3 of the order as under:

*6.3 The assessee filed its reply vide its AR letter dated 31.08.2016. The arguments of the assessee can be summarized as under:-*

- (i) The assessee has obtained secured loans from HDFC Bank wholly and exclusively for and on behalf of the AE which were used by the AE exclusively for purchase of ships.*
- (ii) The A being 100% subsidiary of the assessee, the assessee had provided capital by way of shareholder loan funds rather than by way of share capital due to ease of repatriation of capital contribution in future and on account of commercial expediency and has relied on the decision of Hon ble Supreme Court in the case of S.A.Builders. Therefore, the loans advanced by the assessee to its AE are in the nature of quasi capital.*
- (iii). The AE MPS Singapore created charge over its assets i.e. ships with the bankers and AE has also provided corporate guarantee to the lending bank.*
- (iv) The assessee has not even claimed deduction for interest expenditure incurred in respect of the aforesaid loans obtained from HDFC bank.*
- (v) In financial year 2014-15, the outstanding loans have been converted into share capital by the assessee.*
- (vii) If any addition made for notional interest, the same should be made as per LIBOR.*
- (viii) If any addition is made for notional interest, the deduction for interest of Rs. 9,91,92,004/- paid to HDFC bank should be allowed u/s 57(iii) of the Act.*

*(ix) Considering the commercial substance of the transaction between assessee and its AE, the loan advanced are in the nature of capital contribution which on arms length basis would not have been subject to any charge of interest. (x) The economic substance of the transaction is in the nature of quasi equity capital rather than a commercial loan and is in fact \*disguised equity capital.*

*(xi) The determination of arms length price of this transaction does not have bearing on income and hence the ALP determination is not in accordance with principles of TP Regulations.*

5. The TPO find that the assessee has applied the Comparable uncontrolled Price (CUP) method as a Most Appropriate Method (MAM) for determination of ALP rate of interest. The TPO has discussed on the internal/external CUP method transactions at page 5 to 15 of the order and relied on the judicial decisions. Finally the TPO has determined the ALP of the interest transactions at page 18 Para 7 & 8 as under and passed the order u/s 92CA(3) of the Act dated 30.09.2016.

*7. In view of the same, a search for comparable was done on Bloomberg database by using the following criteria*

*i) Loans of the same currency in which loan given by assessee*

*(ii) Loans pertaining to the FY in which loan given to AE.*

*(iii) Loans pertaining to the country where loan has been given to the AE by assessee.*

*(iv) Secured loans (as loan given to AE by assessee is also considered secured).*

*7.1 The average loan spread of the comparable selected from the database on the above criterions then used for fixing the same into a fixed rate interest as would have been done in a third party unrelated transaction. For doing this the Average Spread data of the comparable loans is fed into the Swap Manager application of the Bloomberg Database, which converts the Average Spread into a Fixed Coupon Rate of interest.*

*7.2 Accordingly, total Transfer Pricing adjustment in respect of notional interest income has been worked out at Rs. 13,38,78,991/- as per the rates obtained from Bloomberg database (working of interest chargeable to A is enclosed herewith as Annexure A) . Thus, a transfer pricing adjustment of Rs. 13,38,78,991/- is made in respect of the aforesaid transaction.*

*8. It is hereby clarified that the findings and discussions made in this order are applicable only for this assessment year being referred, i.e., A. Y. 2013-14 and not for subsequent years.*

6. The Assessing Officer (A.O.) after receiving the TPO order u/sec92CA (3) dated 30.09.2016 has passed the draft assessment order with (i) the transfer pricing adjustment of Rs. 13,38,78,991/- (ii)

the addition in respect of foreign exchange gain of Rs. 5,18,56,617/- earned in respect of loan given to its foreign subsidiaries in the foreign currency and which cannot be part of Tonnage Tax Scheme.(iii) the disallowance u/s 14A r.w.r 8D(2)(ii)&(iii) of I T Rules of Rs.47,33,547/- and determined the total income of Rs.19,46,88,820/- u/s 143(3) r.w.s 144C(1) of the Act dated 30.12.2016.

7. Whereas the assessee has filed the objections in Form.no. 35A against the draft assessment order with the Dispute Resolution Panel (DRP), where the DRP after considering the objections and findings of the TPO has issued the directions and passed the order u/s 144C(5) of the Act dated 30.06.2017. Based on the directions of the DRP, the AO has passed the order u/s 143(3) r.w.s 144C(13) of the Act determining the total income which includes TP adjustment on account of notional interest of Rs. 14,36,59,111/- and foreign exchange gain of Rs. 5,18,56,618/- and further allowed the interest expenses paid to HDFC Bank Rs.9,91,92,004/- and assessed the total income of Rs.10,05,43,393/- and

passed the order u/s 143(3) r.w.s 144C(13) of the Act dated 31.08.2017. Aggrieved by the final assessment order, the assessee has filed an appeal before the Hon'ble Tribunal.

8. At the time of hearing, the Ld. AR has restricted his arguments on the two grounds of appeal being 1(A) & 1(c) and 2(A) & (B). The Ld. AR on the first disputed issue with respect to addition on notional interest mentioned that DRP has overlooked the facts in holding the TP adjustment without appreciating that advance/loan provided to subsidiary company and is in the nature of capital advance and is form part of business operations/ transactions therefore no notional interest has to be computed and levied. On the second disputed issue of the foreign exchange gain, the Ld.AR submits that it is in the nature of capital receipt and arises in the course of business, where the loans are advanced to its subsidiary for buying the ships and to carry on the shipping business. The Ld. AR substantiated the submissions with the judicial decisions and voluminous factual paper book and prayed for allowing the appeal. Contra

the Ld.DR supported the order of the lower authorities.

9. We heard the rival submissions and perused the material on record. The Ld.AR emphasized that the lower authorities and the DRP has erred in overlooking the factual aspects that the loan /advance was provided to subsidiary company at Singapore in the ordinary course of business and assessee is connected with the business operations of the subsidiary company. We find that the assessee has obtained term loans from the HDFC Bank and advances to its subsidiary/Associate Enterprises .i.e M.PallonjiShipping Singapore Pte Ltd (MPS Singapore). The assessee in the financial statements has not provided any interest on the loan given to MPS Singapore and interest paid on the HDFC Bank loan was not claimed as deduction. The assessee has filed the submissions that the notional interest should not charged on MPS Singapore Loan and the Ld.AR demonstrated the correspondence placed at page 152 to 163 of the paper book. Whereas the TPO has computed the interest free advance to MPS Singapore with the bench marking of LIBOR+ on the

loan from HDFC Bank and also on the own funds with the T P adjustment of Loan from HDFC bank Rs.10,45,01,917/- and adjustment of loan from own funds Rs2,93,77,704/- both aggregating to Rs.13,38,78,991/-.

10. Whereas, the DRP has observed that the T P adjustment needs to be made on account of the non charging of interest to the AE by adopting LIBOR + 500BPS and directed the A.O. to grant deduction of Rs.9,91,92,004/- being interest paid to HDFC Bank against the notional interest income on the loans advanced to the AE .i.e. MPS Singapore. The Ld. AR explained that the loan was given to subsidiary in the earlier years and not in the A.Y.2013-14 and for the first time notional interest was assessed. The outstanding loans provided out of the own funds of the assessee are converted in to the share capital and the shares were allotted out of the own funds. We find that the Ld.AR has substantiated the submissions with the voluminous information of the loan provided to the subsidiary and the shares allotment. The contentions raised by the Ld. AR that

the TPO has not considered these facts and the assessee has substantial evidences and information that this loan was provided in the earlier years and the TPO has over looked the facts while computing the TP adjustment and the notional interest was calculated. We considering the facts, circumstances and the information filed and the judicial decisions envisaged by the Ld. AR are of the opinion that the loans which are given in the earlier years are to be categorized separately and it was provided for business purpose by the assessee. Further the loans have been granted as a business participation and the same has to be considered in the line of commercial expediency. The loan was directly provided to the subsidiary by the HDFC Bank and the assessee did not claim interest while computing the income. Accordingly, we restore this disputed issue to the file of the TPO as discussed in the above paragraphs to relook afresh and recomputed the TP adjustment. The assessee should be provided adequate opportunity of hearing and shall co operate in submit the information and we allow the grounds of appeal for statistical purpose.

11. On the second disputed issue, with respect to foreign exchange gain, where the DRP has erred in holding foreign exchange gain on account of loan given to MPS Singapore, which was used for the purpose of capital asset. The contention of the Ld. AR that there cannot be any foreign exchange gain on these transactions and further substantiated with the ledger accounts and the assessment orders for the earlier years and subsequent years. The Ld.AR referred to the financial statements and details in the paper book and emphasized that these facts play a vital role in determination of ALP. The A.O has observed that the assessee has earned foreign exchange gain in respect of loan given to foreign subsidiaries in foreign currency. We found that the assessee has obtained the loan from HDFC Bank for the purpose of onward lending to its subsidiary M/s. Pallonji Singapore PTE Pvt Ltd and the main business of the assessee is shipping and the assessee has provided the loan in the course of regular business transactions and not in money lending. Therefore the income and loss has to be generated based on this information and the submissions that the assessee's

core business is shipping but not the lending. The fact remains that the assessee has provided the loan for the purposes of capital asset to its subsidiary which is on record.

12. The assessee is not in the business of finance, and the loan was utilized for purchase of ships and not for any working capital necessity. The loan given to the subsidiary was disclosed in the balance sheet as a non current asset and the ships are disclosed in the balance sheet of the subsidiary as plant & machinery. We are of the opinion that the facts are not emerging out of the assessment order or draft assessment order where the assessee has submitted the various details but the AO has only considered the fact that the assessee is not a money lending business and is not a NBFC and it cannot be part of the business transaction.

13. Prima-facie the assessee has disclosed the information in the balance sheet and it is in the nature of business. Further there is no consistency of taxing of the foreign exchange gain by the revenue and the Ld.AR has demonstrated the issue of foreign exchange gain in the A.Y. prior to the present

Assessment year and subsequent A.Y.s, and in few cases the A.O. has not taxed the net gain and in some cases the appeals are pending before the First Appellate authorities (CIT(A)). Therefore, in the interest of justice, we restore this issue to the file of the A.O. for limited purpose to adjudicate fresh on merits considering the information, details and judicial decisions. The assessee should be provided adequate opportunity of hearing and shall cooperate in submitting the information and allow the grounds of appeal of the assessee for statistical purposes.

14. In the result, the appeal filed by the assessee is partly allowed for statistical purposes.

Order pronounced in the open court on 28.06.2022.

Sd/-  
(PRASHANT MAHARISHI)  
**ACCOUNTANT MEMBER**

Sd/-  
(PAVAN KUMAR GADALE)  
**JUDICIAL MEMBER**

Mumbai, Dated 28.06.2022

KRK, PS

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :

1. अपीलार्थी / The Appellant

2. प्रत्यर्थी / The Respondent.
3. संबंधित आयकर आयुक्त / The CIT(A)
4. आयकर आयुक्त(अपील) / Concerned CIT
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, अहमदाबाद / DR, ITAT, Mumbai
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

सत्यापित प्रति //True Copy//

1.

( Asst. Registrar)  
ITAT, Mumbai