आयकर अपीलीय अधिकरण, 'डी' न्यायपीठ, चेन्नई

IN THE INCOME TAX APPELLATE TRIBUNAL
"D" BENCH, CHENNAI

श्री चंद्र पूजारी, लेखा सदस्य एवं श्री जी. पवन कुमार, न्यायिक सदस्य के समक्ष

BEFORE SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER
AND SHRI G. PAVAN KUMAR, JUDICIAL MEMBER

आयकर अपील सं./ITA Nos.1469/Mds/2009, 2019/Mds/2010,
12/Mds/2011, 560/Mds/2011 & 256/Mds/2015
निर्धारण वर्ष /Assessment Years: 2004-05 to 2008-09

The Assistant Commissioner of Income-tax, Large Tax Payer Unit/The Dy. CIT, Large Payer Unit-II Chennai – 600101. (अपीलार्थी/Appellant)	v.	**M/s. Shree Ambika Sugars Ltd**., Eldorado, 5th floor, 112, N.H.Road, Chennai 600 001. **PAN** AABCS 5163 J (प्रत्यर्थी/Respondent)

आयकर अपील सं./ITA Nos. 162/Mds/2015
निर्धारण वर्ष /Assessment Year : 2008-09

M/s. Shree Ambika Sugars Ltd., Chennai -600001. **PAN** AABCS 5163 J (अपीलार्थी/Appellant)	v.	The Assistant Commissioner of Income-tax , LTU / The Dy. CIT, LTU-II, Chennai. (प्रत्यर्थी/Respondent)

Revenue by : Shri Jairam Raipura, CIT
Assessee by : Shri R. Vijayaraghavan, Advocate

सुनवाई की तारीख/Date of Hearing : 22.09.2016
घोषणा की तारीख/Date of Pronouncement : 19.12.2016

आदेश /O R D E R

PER CHANDRA POOJARI, ACCOUNTANT MEMBER

The appeals in ITA Nos. 1469/Mds/2009, 2019/Mds/2010, 12/Mds/2011, 560/Mds/2011 are filed by the Revenue for the assessment years 2004-05, 2005-06, 2006-07 and 2007-08. There are cross appeals for the assessment year 2008-09 by the Revenue in ITA No.256/Mds/2015 and by the assessee in ITA No.162/Mds/2015. They are directed against different orders of the CIT(Appeals).

2. First, we take up the appeal in ITA No.1469/Mds/2009 (Revenue) for AY 2004-05.

2.1 The first ground is that the CIT(Appeals) erred in holding that restriction of the depreciation claim of the assessee in terms of Explanation 2 to sec.43(6) was not called for, thus, deleted the addition of ₹58,66,647/-.

3. The facts of the case are that certain capital assets had been acquired by the assessee company through the process of amalgamation of its subsidiary companies with

it. The assessee company had claimed depreciation on the actual cost as provided in Rule 5(1A) as provided in Appendix-1A. The assessee company relied on Explanation 7 to sec.43 of the Act in support of such computation of the eligible depreciation allowance. The AO, on the other hand, relied upon Explanation 2 to sec.43(6) of the Act, which stipulated that in the case of an amalgamation the actual cost of a block of assets in the case of the amalgamated company shall be the written down value of the value of the block of assets as in the case of the amalgamating company for the immediately preceding previous year as reduced by the amount of depreciation actually allowed. Thus, by changing the base for computation of depreciation allowance from the actual cost of acquisition as claimed by the assessee to the written down value of such block of assets for the period under consideration, the excess depreciation was computed by the AO at ₹ 58,66,647/- and the same was disallowed and added to the returned income. Aggrieved by the order of A.O., the assessee

carried the appeal before the Ld. Learned Commissioner of Income Tax(A).

3.1 On appeal, the Ld. CIT(A) observed that the AO while concluding, has missed out the fact that the concerned assets are power plant equipment for which depreciation allowance in terms of sec.32(1)(i) is permissible at such percentage on the actual cost thereof to the assessee as may be prescribed if such assets are of an undertaking engaged in generation or generation and distribution of power. Since specific provisions applicable to the facts of the assessee's case would override the general provisions dealt by Explanation 2 to sec.43(6) of the Act, restriction of the depreciation claim in terms of Explanation 2 to sec.43(6) was not called for. Accordingly, the CIT(Appeals) allowed the appeal of the assessee on this ground. Against this, Revenue is in appeal before us.

4. Before us, the Ld. AR submitted that special treatment of depreciation for the machinery in business of generating electricity to be considered. According to him, as per Sec.32(i) and Rule 5(1A), depreciation is to be computed on the actual cost on a straight line basis. Further, the ld.A.R submitted

that it does not form part of any block assets u/s.32(ii) of the act. He drew out attention to the provision of section-41(2) of the Act which prescribes the method of computation of depreciation on assets acquired on merger of electricity generating machinery. According to him, Explanation-2 to Sec.43(6) applies to only transfer of block assets. Explanation-7 to Sec.43(1) deals with the cost of acquisition on amalgamation.

4.1 On the other hand, ld.D.R relied on Explanation-2 to Sec.43(6) of the Act. According to him, as per this Explanation, the in case of an amalgamation the actual cost of a block of assets in case of a the amalgamated company shall be the written down value of the block of assets as in the case of the amalgamating company for the immediately preceding previous year as reduced by the amount of depreciation actually allowed, as such there is an excess depreciation claimed by the assessee at ₹58,66,647/-.

5. We have heard both the parties and perused the material on record. In this case, assessee-company acquired certain fixed assets from its subsidiary company through amalgamation, which includes certain power plant equipments. In case of

power plant equipments, depreciation to be considered in terms of sec.32(1)(i) of the Act, which prescribes depreciation at certain percentage on actual cost thereof, in respect of undertaking engaged in generation or generation and distribution of power. The AO applies Explanation-2 to Sec.43(6) of the Act. This is a general provision. There is a specific provision in respect of assessee engaged in generation or generation and distribution of power, i.e Explanation-7 to Sec.43(1) read with Rule-5(1A) of the Income Tax Rules. Being so, Ld.CIT(A) directed the AO to apply Explanation-7 to Sec.43(6) of the Act to grant Depreciation on actual cost to assessee and we do not find any infirmity in applying this provisions to this section and Rule-5(1A) giving option to the assessee to adopt actual cost to claim the depreciation on the amalgamation. Accordingly, we confirm the order of the Ld.CIT(A) and dismiss the ground taken by the Revenue.

6. The next ground is that the CIT(Appeals) erred in holding that it cannot be said that any receipt or benefit had accrued to the assessee company on account of reduction of face value of equity shares from ₹10 each to ₹2.50 each,

as understood by sec.28(iv) of the Act, thus, deleting the addition of ₹ 74.27 crores.

7. The facts of the case are that through a scheme of arrangement between Shree Ambika Sugars Ltd., the assessee company, and Supreme Renewable Energy Ltd. And Auro Energy Ltd., two of its subsidiaries, approved by the Madras High Court, the face value of equity shares held by the respective shareholders was reduced from ₹10 each to ₹2.50 each. Such reduction had been effected by cancellation of paid-up equity share capital of the face value of ₹7.50 per equity share and the resulting balance of ₹74,27,37,750/- was utilised by adjusting against debit balance in the profit and loss account, unamortized balances of miscellaneous expenditure, and by transfer to revaluation reserve and general reserve.

7.1 After considering the implication of the accounting entries made, the AO observed that respective shareholders had agreed for reduction of the value of their share capital which had, in turn, resulted in a gain of ₹7.50

per share to the assessee company. As a result of such reduction of share capital, the assessee company's liability got reduced by ₹74.27 crores and its assets got enhanced to that extent. For the surrender of a portion of the share capital by the shareholders the assessee company had not paid anything in return to such shareholders. Therefore, the assessee company had derived a benefit in the course of running its business which was taxable in terms of sec.28(iv) of the Act.

7.2 The assessee company in the course of appellate proceedings has contended that by reduction of share capital no benefit accrued to the assessee company and that there was no reduction of liability of the assessee company to its shareholders, as the paid-up value of the shares represented only the amount subscribed by the shareholders and does not represent any liability of the assessee company.

7.3 The relevant accounting entries made were in pursuance of a decision of the Madras High Court. It is a

basic fact that accumulated losses represent eroded capital. Hence, instead of showing the full capital on one side and accumulated losses on the other side of the balance sheet, what the assessee company did was to adjust the accumulated losses against the share capital. This was only an adjustment entry. It does not affect the assets, liabilities, net worth or the value of shares or the rights of the shareholders. Again, the share capital was reduced and a corresponding increase has been reflected in the reserves. Both share capital and reserves appeal under the head 'liabilities' in the balance sheet. Reducing one and increasing the other has no effect on the overall sum of liabilities reflected in the balance sheet. The number of shareholders and their proportion of holding has remained the same even after the adjustment entries presently under discussion. The voting powers and the right to returns are also unchanged. To put the facts in their proper perspective, the entire exercise was meant only to re-draw the balance sheet to represent the fair net worth of the assessee company after adjusting the accumulated

losses and the impact of amalgamation. Such accounting treatments represents only a “dressing up” of the balance sheet and has no material impact on the net worth of the assessee company or its rights and obligations towards its shareholders. Mere accounting entries passed, by themselves; do not create a benefit or an income chargeable to tax. Therefore, according to the CIT(A) any receipt or benefit accrued to the assessee company as understood by the provisions of sec.28(iv) of the Act and assessment of such reduction in share capital is not justified. Accordingly, Ld. Learned Commissioner of Income Tax(A) allowed this ground of appeal. Aggrieved, the Revenue is in appeal before us. The ld. A.R placed reliance in the following cases:-

i) In the case of Benett Coleman & Co.Ltd., in 133 ITR 1 (Mum SB)

ii) In the case of Quintegra Solutions P Ltd Vs. ITO in 148 TTJ 471(Chennai)

iii) In the case of Learned Commissioner of Income Tax Vs. TVS Motor Ltd in 128 ITD 47 (Chennai)

iv) In the case of Learned Commissioner of Income Tax Vs. G.Narasimhan in 236 ITR 327 SC

v) In the case of Bhavanga Bone & Fertilizers Co. In 166 ITR 316(Guj.)

vi) In the case of Learned Commissioner of Income Tax Vs. General Industrial Society Ltd. In 261 ITR 01 (Calcutta)

vii) In the case of Elscope P Ltd. Vs. Learned Commissioner of Income Tax in 313 ITR 293(Guj.)

viii) In the case of Mahindra & Mahindra Ltd Vs. Learned Commissioner of Income Tax in 262 ITR 501(Bom.)

ix) In the case of Learned Commissioner of Income Tax Vs. Chetan Chemicals in 267 ITR 770(Guj.)

7.4 The ld.D.R submitted that as per scheme of arrangement, the assessee who had share capital worth of ₹99,03,17,000/- was reduced to ₹24,75,79,250/-, in other words ₹9,90,31,700/- shares of ₹10.00 each reduced to share of ₹2.50/-. Thus, the assessee got the benefit of ₹74,27,37,750/-, which is to be considered as business profit u/s.28(iv) of the Act.

8. We have heard both the parties and perused the material on record. As seen from the facts of the case, there is a reduction of share capital and there is no distribution of assets for the benefit of any person. The right of share holders as well as the assessee company continued to be the same and this is only a notional in nature. Being so, loss/profit arising of

reduction in share capital cannot be subject to any taxation either sec.28(iv) of the Act, or u/s.45 r.w.s.48 of the Act as being only notional loss. Further, similar issue came for consideration before this Tribunal in the case of Benett Coleman & Co. Ltd in 133 ITR 1 (Mum.SB) wherein held that deduction in share capital is only a notional profit/loss. It cannot be subject to the provisions of the Income Tax Act, 1961. Following the same, we are of the opinion that Ld. Commissioner of Income Tax(A) is justified in holding that there is no gain to the assessee in terms of sec.28(iv) of the Act on reduction of share capital. This ground of appeal of the Revenue is dismissed.

9. The next ground is that the CIT(A) erred in holding that the AO's action was not correct while disallowing set off of book loss of earlier years of ₹18.27 crores on the ground that entire book loss as on 31.3.2003 was wiped out by adjustment against reconstruction reserve generated by revaluation of assets and reduction of share capital.

10. The facts of the case are that in the course of appellate proceedings, the assessee had filed a letter stating that during the period relevant to the immediately preceding assessment year interest of ₹6.37 crores had been converted into a term loan and if the same was disallowed in the assessment for that period, then the interest paid out of the above amount for the period under consideration amounting to ₹79,62,062/- may be allowed. The AO had not permitted such deduction as no such disallowance had been made for the preceding assessment year up to the date of the assessment order under consideration. The assessee company has contended before the CIT(A) that interest converted into loan was disallowed for the preceding assessment year and therefore, claim of interest on such part of the loan should be allowed for the period under consideration. The relevant facts are not available with the CIT(A). Therefore, the CIT(A) directed the AO to verify if interest converted into term loan in the preceding assessment year was disallowed

or not and carry out the consequential effect for the period under consideration after such verification.

10.1 In the computation of book profits chargeable to tax under sec.115JB of the Act, the assessee in its return of income had claimed set off of brought forward losses of ₹18.27 crores. The AO noted that the assessee company as a result of revaluation of the assets and reduction of share capital had generated a reconstruction reserve of ₹142.57 crores. Out of such reconstruction reserve the debit balance in the profit and loss account had been adjusted and consequentially the entire book loss had been wiped out as on 31.3.2003. Accordingly, no book loss brought forward from earlier years was available to the assessee for set off against the book profits of the period under consideration as on the date of drawing up of the balance sheet.

10.2 Before the CIT(A), the assessee company has relied on the decision of this Tribunal, Hyderabad 'B' Bench in ITA No.442/Hyd/2001 dated 27.6.2008 in the case of DCIT,

Central Circle-1, Hyderabad vs. Raasi Cement Limited, wherein it was held that :

> *"In fact, it is merely a matter of presentation prescribed by Schedule VI of the Companies Act to the effect that the debit balance of profit and loss account is to be shown after deduction of uncommitted reserves, if any. This does not mean that the debit balance is written off or adjusted against the reserves. The debit balance remains as it is, it has only to be shown in the balance sheet net of general reserve. This being the case, the debit balance of RCII and TPML (subsidiaries which had been merged with the assessee company and hence as per clause (iii) of the Explanation to section 115 JA, the same will have to be reduced from the profit shown in the profit and loss account."*

10.3 According to the CIT(A), this Tribunal was of the view that the manner of presentation of the statement of affairs in the balance sheet does not obliterate the fact that losses had been incurred in the preceding years. Such losses, if they had been incurred and computed, would be available for carrying forward to the subsequent assessment year and would be available for set off in spite of being shown in the balance sheet as a reduction from the general or uncommitted reserves. Manner of presentation cannot change the fact of loss having been incurred. The

CIT(Appeals) observed that the losses quantified in the preceding year would be available for set off against the book profits of the period under consideration in terms of Explanation (iii) to sec.115JB of the Act and mere accounting entries cannot erase the fact that losses had been incurred in the preceding years and were permitted to be carried forward. According to the CIT(A), the AO's action in denying such set off for the period under consideration was not correct in view of the decision of this Tribunal, Hyderabad Bench cited supra and allowed the appeal of the assessee on this ground. Against this, the Revenue is in appeal before us.

11. The Ld. D.R submitted that book loss available with the assessee to set off with the present assessment year's book profit and there is no question of carried forward of such loss in the assessment year under consideration.

11.1 On the other hand, ld. A.R submitted that as on 31.03.2003, there was a loss and this loss has been in

brought forward and such brought forward losses has been correctly set off and accordingly he relied on the following judgements:-

i) in the case of Sumi Matherson Innovative Engg. In 336 ITR 321(Del.)

ii) in the case of Peico Electronics & Electrical Ltd. In 339 ITR 596(Kol.)

iii) in the case of DCIT Vs. Beck India Ltd in 26 SOT 141 (Bom.)

iv) in the case of Rangnathan Industries order in ITA No.2434/Chen/04

v) in the case of Raasi Cements order in Income Tax Act, 1961 (in short 'the Act') No.442/Chen/01

12. We have heard both the parties and perused the material on record. According to the AO, the assessee company has generated reconstruction reserve of ₹142.57 crores and out of this reconstruction reserve, the loss in P & L A/c to be adjusted, thus as on 31.03.2003, there was no brought forward loss to set off in the current assessment year. In our opinion, this methodology followed by the AO is not proper while computing the book profit under Explanation (iii) to sec.115JB of the Act, brought forward loss on the last date of the immediately preceding year, which is to be brought forward to the

financial year in question is to be reduced; what happens during the course of assessee is not relevant. Therefore, Ld. Commissioner of Income Tax(A) is justified in deleting that the A.O taking such set off for the period under consideration was not correct. Hence, the same is confirmed and the ground taken by the Revenue stands dismissed.

13. Now, we take up the cross appeals in ITA Nos.162/Mds./15 (Assessee's appeal) & 256/Mds./15 (Revenue's appeals)

14. The first common ground in these appeals is that the CIT(Appeals), LTU erred in upholding the disallowance of ₹26,00,376/- made by the AO under sec.14A r.w.r. 8D(2)(iii) of the Act.

15. The facts of the case are that the AO observed that the assessee has claimed exemption of dividend income of ₹1,53,203 as exempt from tax. The AO asked the assessee as to how much expenses have been debited to

profit and loss account on account of earning of this income and as to why the provisions of sec.14A of the Act r.w. Rule 8D should not be invoked. The assessee replied that it has not accounted any expenditure as there is no expenditure incurred in connection with earning such exempted income. The AO was not satisfied with the correctness of the claim of the assessee in respect of such expenditure in relating to the exempted income considering the voluminous transaction involved and substantial amount of expenses debited to profit and loss account under various head. Therefore, the AO made disallowance of ₹2,37,79,071/- u/s.14A by invoking Rule 8D by relying on (i) CBDT Instruction in F.No.173/172/2008-ITA-I dated 4.2.2009, (ii) decision of this Tribunal Special Bench, Mumbai in the case of M/s. Daga Capital Management P. Ltd. for AY 2001-02 vide ITA No.8057/Mum/03 dated 20.10.2008 and the decision of the Delhi Bench in the case of M/s. Cheminvest Ltd. V. ITO (121 ITD 318). Aggrieved, the assessee carried the appeal before the Ld. Learned Commissioner of Income Tax(A).

15.1 On appeal, the CIT(Appeals) observed that the disallowance made by the AO by invoking the provisions of Rule 8D(2)(ii) will not survive and he confirmed the disallowance made by the AO by invoking the provisions of Rule 8D(2)(iii) of the I.T.Rules. Accordingly, he directed the AO to rework the disallowance and partly allowed the ground of appeal. Against this, both, the assessee and the Revenue is in appeal, before us.

16. We have heard both the parties and perused the material on record. For assessment year 2008-09 Rule-8D is not applicable as it was inserted with effect from 24.03.2008. Accordingly, in our opinion for these assessment years we direct the A.O to disallow 2% of the exempted income on placing reliance on the jurisdiction High Court in the case of Simpson & Co. Ltd. V. DCIT in Tax case No.2621 of 2006 dated 15.10.2002. This ground is allowed in assessee's appeal and is dismissed in Revenue's appeal.

17. The next ground in Revenue's appeal is that the CIT(A) has erred in deleting the disallowance of excess depreciation made by the AO by applying the WDV method, by relying upon the decision of his predecessor for the A.Y. 2004-05 to 2007-08.

18. The facts of the case are that the AO observed that M/s. Supreme Renewable Energy Ltd. And M/s. Auro Energy Ltd. were amalgamated with M/s. Shree Ambika Sugar Ltd. w.e.f. 01.04.2003. While claiming depreciation, the assessee claimed depreciation on the assets of these companies on Straight Line Method. The AO further observed that for earlier years the depreciation has been worked out on WDV basis and for A.Y. 2007-08 similar stands was taken by the AO. However, the assessee stated that though the AO for earlier years have granted depreciation on WDV basis, that has been contested by the assessee in further appeals. The assessee further stated that for AY 2004-05, the CIT(A) has allowed relief to the assessee. The AO did not accept the reply and observed

that the department is consistently taking this stand which has not been finally settled down and the appeal is pending before the Tribunal, Chennai and with due respect to the decision of the CIT(A) on A.Y 2004-05, the A.O worked out the excess depreciation claimed at ₹ 4,25,71,722/-. Aggrieved, the assessee carried the appeal before the Ld. Learned Commissioner of Income Tax(A).

19. On appeal, the CIT(Appeals) observed that the identical issue was already decided in favour of the assessee by his predecessor in assessee's own case for the AY 2004-05 in ITA No.659/06-07 dated 28.11.2008 and based on the same decision, the issue was decided in favour of the assessee for A.Ys. 2005-06 to 2007-08 also. Further, the CIT(Appeals) observed that in the order passed for AY 2007-08 vide ITA No.49/09-10/LTU(A) dated 19.11.2010, it was held as under:

> *"4.2 I have carefully considered the facts of the case and the submissions of the ld. AR. I have also gone through the decisions relied on by the AR in this regard. I find that identical issue in the earlier year*

for AY 2004-05 in ITA 659/06-07 dated 28.11.2008 was decided as under:

> *8. The Assessing Officer in coming to his conclusion has missed out the fact that the concerned assets are power plant equipment for which depreciation allowance in terms of section 32(1)(i) is permissible at such percentage on the actual cost thereof to the assessee as may be prescribed if such assets are of an undertaking engaged in generation or generation and distribution of power. Specific provisions applicable to the facts of the assessee's case would override the general provisions dealt by explanation 2 to section 43(6) of the Act. On the facts of the present case restriction of the depreciation claim in terms of Explanation 2 to section 43(6) was not called for and the same is hereby deleted. Appeal filed by the assessee on this ground may be treated as allowed."*

Accordingly, following the above decision, ld. Learned Commissioner of Income Tax(A) allowed this ground for A.Y. 2008-09. Against this, the Revenue is in appeal before us.

20. We have heard both the parties and perused the material on record. As discussed in earlier para-5, this ground is decided in favour of the assessee. Accordingly, this ground raised by the Revenue is dismissed.

21. ITA Nos.219/Mds./2010, 12/Mds./11 & 560/Mds./11 /Mds/2011(Revenue's appeal for assessment year 2005-06, 2006-07 & 2007-08)

21.1. The first common ground in these appeals is with regard to deletion of addition due to restricting depreciation of assets acquired on merger.

22. At the outset, the ld. A.R pointed out that this issue came for consideration in Revenue's appeal in ITA No.1469/09 for the AY 2004-05. As discussed in earlier para-5, this ground is decided in favour of the assessee Accordingly, this ground raised by the Revenue is dismissed.

23. The next ground in Revenue's appeal in ITA No.560/Mds./2011 is with regard to disallowance u/s.14A read with Rules 8D of Income Tax Act, 1961.

24. We have heard both the parties and perused the material on record. Admittedly, this issue is covered by the decision of jurisdictional High Court in the case of Simpson & Co. Ltd. V. DCIT in Tax case No.2621 of 2006 dated 15.10.2002. Accordingly, we direct the AO to disallow 2% of exempted income towards notional expenditure incurred for the purpose of earning this income. As discussed in earlier para-16, this ground is dismissed.

25. In the result, the all the appeals by the Revenue are dismissed and all the appeals by the assessee are allowed.

Order pronounced on 19th Decembe, 2016 at Chennai.

Sd/-	Sd/-
(जी. पवन कुमार)	(चंद्र पूजारी)
(G. Pavan Kumar)	(Chandra Poojari)
न्यायिक सदस्य/Judicial Member	लेखा सदस्य/Accountant Member

चेन्नई/Chennai,
दिनांक/Dated, the 19th December, 2016.

K S Sundaram आदेश की प्रतिलिपि अग्रेषित/Copy to:

1. अपीलार्थी/Appellant
2. प्रत्यर्थी/Respondent
3. आयकर आयुक्त (अपील)/CIT(A)
4. आयकर आयुक्त/CIT
5. विभागीय प्रतिनिधि/DR
6. गार्ड फाईल/GF