THE INCOME TAX APPELLATE TRIBUNAL
AHMEDABAD "B" BENCH
(Conducted Through Virtual Court)

Before: Shri P.M. Jagtap, Vice President
And Shri Siddhartha Nautiyal, Judicial Member

ITA No. 249/Ahd/2019 **Assessment Year 2015-16**

Neptune Polymers Pvt. Ltd. 529/10/1 Old Daliya Building Opp. Town Hall, Ellis Bridge, Ahmedabad Ltd. PAN: AAACN9080A (Appellant)	Vs	The ITO, Ward-3(1)(1), Ambawadi, Ahmedabad (Respondent)

Assessee by: **Shri S.N. Divatia, A.R.**
Revenue by: **Shri R.R. Makwana, Sr. D.R.**

Date of hearing : 16-03-2022
Date of pronouncement : 30-05-2022

आदेश/ORDER

PER : SIDDHARTHA NAUTIYAL, JUDICIAL MEMBER:-

This is an appeal filed by the assessee against the order of the ld. Commissioner of Income Tax (Appeals)-9, Ahmedabad in Appeal no. CIT(A)-9/10340/ITO. Wd. 3(1)(1)Abd/17-18 vide order dated 09/01/2019 passed for the assessment year 2015-16.

2. The assessee has taken the following grounds of appeal:-

"1.1 The order passed u/s.250 on 09.01.2019 for A.Y. 2015-16 by CIT(A)-9, A'bad, confirming the addition of Rs.3,23,99,007/- towards STCG and Rs.5,55,186/- towards business profit is wholly illegal, unlawful and against the principles of natural justice.

1.2 The Ld. CIT(A) has grievously erred in law and or on facts in not considering fully and properly the explanations furnished and the evidence produced by the appellant.

2.1 The Ld. CIT(A) has grievously erred in law and or on facts in upholding the following additions:

a) Short term capital loss on sale of plan and machinery Rs.30,45,512/-(loss)

b) STCG on sale of buildings Rs.3,54,44,519/-

c) Business profit @2.5% Rs.5,55,186/-

2.2 That in the facts and circumstances of the case as well as in law, the Ld. CIT(A) ought not to have made above said additions.

3.1 The Ld. CIT(A) has grievously erred in law and or on facts in upholding the sale consideration of building and office at Rs.3,99,06,000/- without making allowance for the liability owed to Cosmos Cooperative Bank ltd. of Rs.380 lakhs. Therefore, the sale consideration accruing or arising to the appellant was only Rs.19,06,000/- and the STCG ought to have been worked out thereon. Thus, the Ld. CIT(A) has grievously erred in confirming STCG of Rs.3,54,44,519/- as against the loss of Rs.25,05,481/-.

3.2 That in the facts and circumstances of the case as well as in law, the ld. CIT(A) has grievously erred in not allowing the loan liability aggregating to Rs.380 lakhs owed to Cosmos Coop. Bank Ltd. The Ld. CIT(A) has failed to appreciate that the actual sale consideration accruing or arising to the appellant Was only Rs.19,06,000/- so that the appellant had correctly computed STCG.

4.1 The Ld. CIT(A) has grievously erred in law and or on facts in working out short term capital loss of Rs.30,45,512/- in respect of plant and machinery as against the loss of Rs.21,29,284/- declared in the return.

4.2 That in the facts and circumstances of the case as well as in law, the ld. CIT(A) has grievously erred in working out short term capital loss of Rs.30,45,512/- in respect of plant and machinery as against the loss of Rs.21,29,284/- declared in the return.

5.1 The Ld. CIT(A) has grievously erred in law and or on facts in confirming the rejection of book result and upholding the addition to the extent of Rs.5,55,186/- by estimating NP @ 2.5% as against the business loss of Rs.2,32,88,938/-. The entire action on part of both the lower authorities is wholly arbitrary and unlawful.

6.1 Without prejudice to the above and in the alternative, the additions confirmed by CIT(A) are highly excessive.

It is therefore prayed that the additions confirmed by the CITCA) should be deleted."

3. The brief facts of the case are that the assessee company was engaged in the business of manufacturing and trading of woven fabrics. During the year, the assessee had sold properties comprising of factory building, plant and machinery, furniture and fixture etc. and claimed a short-term capital loss of ₹ 46,34,765/- along with business loss under the normal provisions of the Act. During the course of assessment, the AO noted that the assessee had executed a sale deed for Rs. 3,99,06,000/- in respect of its factory premises in favour of M/s Sukruti Polymers. The assessee also made another sale deed towards plant and machinery for ₹ 70,69,359/- with the same concern. The AO found that the working of capital gains was not proper and prepared a revised working. In the said working, the AO disallowed the sum

of ₹ 3,80,00,000/- from the sale consideration of ₹ 3,99,06,000/ received on sale of factory premises, which was claimed by the assessee as a deduction towards amount of principal and interest paid on the outstanding loan from M/s Cosmos cooperative Bank Ltd, which was paid directly by the purchaser to the bank, for the purpose of issuing NOC by the said bank and releasing the mortgaged properties with this bank. Accordingly, after making the adjustments, the AO worked out the net short term capital gain of ₹ 3,23,99,007/- on sale of factory premises, plant and machinery, furniture and fixtures etc. to M/s Sukruti Polymers. Further, the AO rejected the book loss declared by the assessee and estimated the net profit @5% of the turnover, in absence of the assessee causing appearance before him during the course of assessment proceedings and producing books of accounts for verification.

3.1 In appeal, the counsel for the assessee submitted that the claim of the assessee for deduction of ₹ 3,80,00,000/- which was for clearing the dues of Cosmos Bank was an allowable deduction since the property was mortgaged with the bank for claiming credit facilities during the course of business, but since due to severe cash crunch, assessee could not repay the debt of the bank, it decided to sell the property in order to clear the bank dues. Accordingly, Cosmos Bank agreed to issue NOC for sale of this mortgaged property, provided the purchaser would repay the outstanding bank liability. Therefore, counsel for the assessee submitted that as soon as the buildings are mortgaged with the bank, the ownership rights of the appellant were reduced from full ownership rights to the rights of a mortgagor and therefore the assessee had rightly claimed deduction of this amount of ₹ 3,80,00,000/- directly paid by the purchaser M/s Sukruti Polymers directly to the bank.

Further, the counsel for the assessee relied on the case of **CIT v Virtual Soft System 404 ITR 409 (SC)** to contend that the assessee can only be charged on the "real income" which can be calculated only after applying the prescribed method. The assessee also challenged the rejection of declared book loss and its substitution by net profit computed @5% of turnover of the assessee. The Ld. CIT(Appeals) rejected the assessee's arguments and held that the AO had rightly disallowed deduction of ₹ 3,80,00,000/- since it is an undisputed fact that the loan was taken from the bank for the purpose of business of the assessee and the loan was used for discharging the trading liabilities. Further, Cosmos Bank was not an owner of the assets so sold but it had created a charge or interest in lieu of granting the loans to the assessee company and the amounts realised by the bank were not the absolute sale consideration for which it had borne the cost of acquisition but was recovered amounts of loan together with interest charged from time to time. Regarding the ground in relation to rejection of book results and estimation of profits at 5% of total turnover/receipts, Ld. CIT(Appeals) partly allowed the assessee's appeal and reduced the net profit to 2.5% of the gross trading receipts.

4. The assessee is in appeal before us against the aforesaid additions confirmed by Ld. CIT(Appeals). Before us, counsel for the assessee primarily reiterated the same submissions made before Ld. CIT(Appeals), which are to the effect that effectively the amount of ₹ 3,80,00,000/- was diverted by way of an overriding title in favour of Cosmos Bank, being the mortgagee of the property and this amount never accrued to the assessee in the first instance. The purchaser directly paid this consideration of ₹

3,80,00,000/- in favour of the bank and this amount did not form part of the sale consideration of the assessee and hence should have been allowed by way of deduction while computing capital gains. He also took the argument that only the "real income" which accrues to the assessee could be taxed in his hands. The counsel for the assessee reiterated the judgements on which reliance was placed before Ld. CIT(Appeals) in support of the above arguments. He also contended that Ld. CIT(Appeals) has erred in restricting the net profit to 2.5% of the turnover. The counsel for the assessee placed reliance on the case of **Gopee Nath Paul & Sons 278 ITR 240 (Calcutta)**, wherein it was held that where in the instant case, without removing the liability of the bank, the title of the purchaser could not be perfected. Having regard to the facts and circumstances of the case, and the position in law, the meeting of the liability of the bank relating to the assets of 'GS' was an expenditure incurred wholly and exclusively in connection with the transfer. On the issue of taxability of "real income", the assessee placed reliance on the case of **Balbir Singh Maini [2017] 86 taxmann.com 94 (SC)** in which it was held that this income must have been received or have 'accrued' under section 48 as a result of the transfer of the capital asset. In response, the Ld. DR submitted that the argument of the counsel for the assessee that there is diversion by overriding title is unacceptable for the simple reason that the charge of the property is self-created by the assessee company. The amount of ₹ 3,80,00,000/- is not an expense in relation to transfer of the impugned property and hence the assessee cannot claim deduction thereof while computing capital gains. It is effectively the charge on the property which the purchaser directly paid to the Cosmos Bank instead of paying it to the seller i.e. the assessee company. On the issue of rejection of the books and

action of the Ld. CIT(Appeals) restricting net profit to 2.5% of the turnover, the Ld. DR submitted that since the books were not produced before the lower authorities for verification at any stage, the question of rejecting the same does not arise in the first instance.

5. We have heard the rival contentions and perused the material on record.

5.1 Ground the number 1 (1.1 and 1.2) are a general in nature and do not require any specific adjudication.

5.2 Ground number 2 (2.1 and 2.2) has been dealt with specifically in the succeeding Grounds of Appeal.

5.3 Ground number 3 (allowability of ₹ 3,80,00,000/- paid to Cosmos bank against the total sale consideration of ₹ 3,99,06,000). The issue for consideration in this ground before us is the allowability of deduction of ₹ 3,80,00,000/- from the sale consideration received on account of sale of factory premises, plant and machinery, furniture and fixture etc. on slump sale basis to M/s Sukriti Polymers. In our considered view, it is difficult to accept the argument of the assessee that this amount of ₹ 3.8 crores is a charge by overriding title and hence this sum never accrued to the assessee in the first instance. In a considered view, this charge on property was created by the assessee company itself since it took business loan from M/s Cosmos Bank Ltd by mortgaging the impugned property. Therefore, clearly this amount represents application of income and not diversion by overriding

title and the assessee cannot claim deduction thereof from the sale consideration. In the case of **CIT vs. Attili N. Rao (2001) 119 taxman 1030 (SC)**, on which reliance has been placed by the Revenue, the facts were that the assessee mortgaged his immovable property to the State Excise Department to provide security for the amounts of 'kist' which were due by him to the State. The State sold the immovable property by public auction to realize its dues. A sum of Rs. 5,62,980 was realized at the auction. Out of that, the State deducted the amount of Rs. 1,29,020, due to it towards 'kist' and interest and paid over the balance to the assessee. It was the assessee's contention that the amount due to the State Excise Department, i.e., Rs. 1,29,020, should be deducted while computing capital gains besides allowing other deductions. Neither ITO nor the appellate authority agreed with the assessee. The Tribunal upheld the assessee's claim. The High Court upheld the Tribunal's order. In appeal, the Supreme Court held that what was sold by the State at the auction **was the immovable property that belonged to the assessee**. **The price that was realised, therefrom, belonged to the assessee. From out of that price, the State deducted its dues towards 'kist' and interest due from the assessee and paid over the balance to him. The capital gain that the assessee made was on the immovable property that belonged to him. Therefore, it was on the full price realised that the capital gain and the tax thereon had to be computed.** Therefore, the High Court was not correct in holding that amount realised by the sale of the assessee's interest in the property was only Rs. 4,33,960, i.e., Rs. 5,62,980 minus Rs. 1,29,020. Again, the Mumbai ITAT (TM) Bench in the case of **Perfect Threads Mills V. DCIT [2020] 113 taxmann.com 384 (Mumbai - Trib.) (TM)** held that where on account of non-payment of

corporate loan as per agreed terms, a charge on mortgaged property was created by assessee in terms of section 13(2) of SARFAESI Act, 2002, in such a case, upon sale of property so mortgaged, assessee could not claim deduction of principal amount of loan either as expenditure under section 48 or as 'diversion of income by overriding title'. The Madras High Court in the case of **Smt. D. Zeenath v. ITO [2019] 1taxmann.com 298 (Madras)** held that where property was mortgaged by assessee after he had acquired property, amount paid by assessee to discharge mortgage debt by sale of said property could not be treated as cost of acquisition so as to allow same as deduction under section 48 of the Act. In the case of **Sri Kanniah Photo Studio v ITO [2015] 62 taxmann.com 357 (Madras)**it was held that Amount spent on discharge of mortgage created by assessee after acquiring property, would not be deductible as expense under section 48(1)(i) of the Act. In the case of **CIT v. Roshanbabu Mohammed Hussein Merchant [2005] 144 Taxman 720 (Bombay)/[2005] 275 ITR 231 (Bombay),** the Bombay High Court held that **where a property is acquired by assessee free from encumbrances and, thereafter, an encumbrance by way of mortgaging said property is created by him, then assessee is not entitled to deduction under section 48(i) on account of repayment of mortgage debt or expenditure incurred to remove said encumbrance.** The Bombay High Court made the following relevant observations while giving the judgment which are directly relevant to the issue in hand before us:

> *There is a distinction between the obligation to discharge the mortgage debt* ***created by the previous owner and the obligation to discharge the mortgage debt created by the assessee himself****. Where*

the property acquired by the assessee is subject to the mortgage created by the previous owner, the assessee acquires absolute interest in that property only after the interest created in the property in favour of the mortgage is transferred to the assessee, that is, after the discharge of mortgage debt. In such a case, the expenditure incurred by the assessee to discharge the mortgage debt created by the previous owner to acquire absolute interest in the property is treated as 'cost of acquisition' and is deductible from the full value of consideration received by the assessee on transfer of that property. ***However, where the assessee acquires property which is unencumbered****, the assessee gets absolute interest in that property on acquisition.* ***When the assessee transfers that property, the assessee is liable for capital gains tax on the full value realized, even if an encumbrance is created by the assessee himself on that property and the assessee is under an obligation to remove that encumbrance for effectively transferring the property. In other words, the expenditure incurred by the assessee to remove the encumbrance created by the assessee himself on the property which was acquired by the assessee without any encumbrance is not allowable deduction under section 48****. [Para 14]*

It was not in dispute that the property on which the encumbrance was created by the assessee was acquired by the assessee free from encumbrances. Therefore, it must be said that the assessee was not entitled to the deduction of the expenditure incurred to remove the encumbrance created by the assessee herself. *[Para 15]*

The contention that the assessee had not received a pie from the transfer and the entire sale proceeds realised on transfer of the mortgaged asset had been appropriated towards discharge of mortgage was also without any merit. When the property belonging to the assessee was sold in discharge of the mortgage created by the assessee herself, then irrespective of the amount actually received by her, the capital gain had to be computed on the full price realised (less admissible deduction) on transfer of the asset*. [Para16]*

Therefore, repayment of the mortgage debt created by the assessee was not an expenditure incurred in connection with the transfer of mortgaged asset allowable under section 48(i). *[Para 18]*

In light of the above analysis and the case of **CIT vs. Attili N. Rao (2001) 119 taxman 1030 (SC)** and **CIT v. Roshanbabu Mohammed Hussein Merchant [2005] 144 Taxman 720 (Bombay)/[2005] 275 ITR 231 (Bombay)**, which are directly and squarely applicable to the assessee's set of facts, we are of the considered view, that the said amount of ₹ 3,80,00,000/- represents application of income and does not qualify as "diversion of income by overriding title" and the assessee is not entitled in the instant set of facts to claim deduction thereof from the sale consideration received on the impugned property in question. The cases relied upon by the assessee are not directly applicable to the assessee's set of facts and are distinguishable in the instant set the facts. In the result, we hold that the Ld. CIT (Appeals) has not erred in facts and law in confirming the action of the AO in disallowing the sum of ₹ 3,80,00,000/-from the sale consideration.

5.4 In the result, ground number 3 of the assessee's appeal is dismissed.

Ground number 4:

5.5 The assessee has submitted that it shall not be pressing Ground number 4 and hence the same is being dismissed as not pressed.

Ground number 5 (estimation of net profit @ 2.5% as against business loss of 2,32,88,938/-)

5.6 The next issue before us is whether the Ld. CIT(Appeals) has erred in facts and in law in partly allowing the assessee's appeal and restricting the net profit to 2.5% of the turnover of the assessee as against the business loss of ₹ 2,32,88, 938/- declared by the assessee in the return of income. We note that the assessee did not produce the books of accounts at any point in time before the Revenue Authorities for their consideration/perusal. Therefore, in the instant set of facts, in our considered view, Ld. CIT(Appeals) has been quite reasonable in restricting the net profit of the assessee to 2.5% of the turnover. In the case of **Swayambhu Furniture1988 taxmann.com 783 (Allahabad)**it was held that when there was non-production of accounts at time of survey as well as at time of assessment, then authorities were justified in making best judgment assessment on estimate basis taking into account number of persons employed on date of survey, labor cost, production and capital employed. In the case of **Smt. Jayaben K. Ghelani [2017] 79 taxmann.com 249 (Rajkot - Trib.)**, the ITAT held that where assessee failed to produce relevant books of account

in scrutiny assessment, Assessing Officer was justified in rejecting book results and making addition on estimation basis under section 145(3) of the Act. In the case of **Zora Singh v. CIT [2008] 173 Taxman 76 (Punjab & Haryana)**, the Punjab and Haryana High Court held that where the assessee, failed to produce books of account and vouchers to justify expenses made against gross receipts, the Tribunal was justified in confirming estimation of 6.5% as net profit as against 1.52% shown by assessee. In our view, it is seen that the books of account were never produced either before the AO or Ld. CIT(Appeals) for their consideration. Accordingly, in absence of production of books of account, in our considered view, the Ld. CIT(Appeals) has been quite reasonable in restricting the net profit @2.5% of the total turnover. Therefore, we are of the view that Ld. CIT(Appeals) has not erred in facts and law in restricting the net profit @2.5% of the total turnover in instant set of facts.

5.7 In the result, Ground Number 5 of the assessee's appeal is dismissed.

6. In the result, the assessee's appeal is dismissed.

Order pronounced in the open court on 30-05-2022

Sd/-	**Sd/-**
(P.M. JAGTAP)	**(SIDDHARTHA NAUTIYAL)**
VICE PRESIDENT	**JUDICIAL MEMBER**

Ahmedabad : Dated 30/05/2022

आदेश की प्रतिलिपि अग्रेषित / Copy of Order Forwarded to:-

1. Assessee
2. Revenue
3. Concerned CIT
4. CIT (A)
5. DR, ITAT, Ahmedabad
6. Guard file.

By order/आदेश से,

उप/सहायक पंजीकार
आयकर अपीलीय अधिकरण,
अहमदाबाद