IN THE INCOME TAX APPELLATE TRIBUNAL
Bangalore ‘A‘ Bench, Bangalore

Before Shri Rajpal Yadav, Judicial Member
and Shri Jason P. Boaz, Accountant Member

ITA No.258/Bang/2014
(Assessment year: 2009-10)

M/s. Subhash Kabini Power Corporation Limited 8/2 Ulsoor Road Bangalore PAN: AACCS 0881 J	Vs.	Commissioner of Income Tax, Bangalore-III Bangalore
(Appellant)		**(Respondent)**

Assessee by: Shri Sajjan Kumar Tulsiyan, Advocate
Department by: Shri C.H. Sundar Rao, CIT (DR)

Date of Hearing: 19/11/2014
Date of Pronouncement: 28/11/2014

O R D E R

Per Rajpal Yadav, J.M.

The present appeal is directed at the instance of the assessee against the order of the learned Commissioner dated 27.01.2014 passed u/s 263 in assessment year 2009-10. The solitary grievance of the assessee is that the learned CIT has erred in taking congnizance u/s 263 of the Income Tax Act and thereby setting aside the assessment order dated 22.08.2011 passed u/s 143(3) of the Income Tax Act and directing the Assessing Officer to reframe the assessment order de novo.

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2. The assessee had filed an applicatin to raise additional ground of appeal, whereby, on the strength of ITAT order in the case of My Home Power Ltd vs. DCIT (151 TTJ 616) upheld by the Hon'ble Andhra Pradesh High Court), it has pleaded that the receipts from the sale of carbon credit is capital in nature and thus neither in the nature of the income chargeable to tax nor in the nature of business profit/income arising from business, therefore, no prejudice caused to the Revenue and accordingly the order u/s 263 is nto sustainable.

3. The brief facts of the case are that the assessee has filed its return of income for assessment year 2009-10 on 30.09.2009 declaring an income of Rs.22,89,820/-. This return was revised on 31.3.2011 wherein income was declared at Rs.22,66,320/-. According to the assessee, a mistake in the computation of total income crept in pertaining to the brought forward losses set off against the taxable income, therefore, it has to revise the return. The Assessing Officer had issued notice u/s 143(2) dated 23.08.2010 and 142(1) dated 1.6.2011. The assessee is in the line of power generation business. It has undertaken project during the year under consideration for a hydel power project at Kabini Dam, Heggadadevanakote, Mysore district allotted by the Govt. of Karnataka. The assessee has claimed deduction u/s 80IA of the I.T. Act at Rs.7,66,87,094/-. The Assessing Officer after considering the issue with regard to forex gain has considered the issue with regard to admissibility of deduction u/s 80IA and determined the income as underL

"4. The assessee has claimed deduction of Rs.7,66,87,094/- u/s 80IA of the Income Tx Act after adjusting a sum of Rs.1,79,40,907/- being unabsorbed depreciation brought forward from assessment year 2004-05. However, during the course of assessment proceedings, the assessee has made a written submission tha the said unabsorbed depreciation of Rs.1,79,40,907/- has been inadvertently claimed since it was already claimed for the assessment year 2006-07. Therefore, this is added back to the assessee's income as a result of which the total income is to be taken at Rs.2,02,30,730/- instead of Rs.22,66,320/-.

5. After verification of the details, the assessment is concluded accepting the income returned.

Tax payable as per normal provisions

Total income returned	*Rs.22,66,320*
Total income assessed	*Rs.2,02,30,730*
Tax Thereon 30%	*Rs.60,69,219*
Add: Surcharge @ 10%	*Rs.6,06,922*
Total	*Rs.66,76,141*
Add: Education Cess @ 3%	*Rs.2,00,284*
Net Tax	*Rs.68,76,425*

4. The learned Commissioner after going through the record formed an opinion that the assessment order passed by the learned Assessing Officer is erroneous and prejudicial to the interest of the Revenue. He observed that on verification, it was noticed that there was incorrect allowance of deduction u/s 80IA of the Income Tax Act. The copy of the show cause notice is available on page No.123 of the paper book. After hearing the assessee, the learned Commissioner has observed that the assessee has received a sum of Rs.4,88,61,721/- on sale of carbon credits. According to the CIT, this income was not derived from the eligible business, therefore, it does not qualify

for grant of deduction 80IA of the Income Tax Act. The learned Commissioner has made reference to the judgment of the Hon'ble Supreme Court in the case of M/s Liberty India vs. CIT reported in 317 ITR 218 and in the case of M/s Sterling Food reported in 237 ITR 579.

5. The learned Counsel for the assessee while impugning the order of the Commissioner contended that the receipts received on sale of carbon credit is a capital receipt as held by the ITAT Hyderabad Bench in the case of My Home Power Ltd vs. DCIT reported in 151 TTJ 616 (Supra). This order has been followed by the ITAT Chennai in the case of Ambica Cotton Mills Ltd vs. DCIT reported in 27 ITR 44. It has been further followed by ITAT Chennai in the case of Velayudhaswamy Spinning Mills (P) Ltd vs. DCIT (2013) 27 ITR (Trib.) 106. Further both these orders have been followed in the case of Shree Cement Ltd vs. ACIT (ITAT Jaipur). The learned Counsel for the assessee placed on record copies of these orders. He further contended that the Hon'ble Andhra Pradesh High Court has upheld the order in the case of My Home Power Ltd and it is reported in 2014 (6)TMI/82. On the strength of these orders, he contended that the assessee has raised an additional ground of appeal, pleading therein that receipt from the sale of carbon credit being capital in nature would not form part of the total income, therefore, there is no prejudice to the Revenue. For buttressing his contention that this ground ought to be taken into consideration, he relied upon the judgment of the Hon'ble Supreme Court in the case of NTPC vs. DCIT reported in 229 ITR 383, wherein it has been held that the Tribunal has

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jurisdiction, as to examine the question of law which arose from the fact as found by the Income Tax Authorities and having a bearing on tax liability of the assessee. The learned Counsel for the assessee further contended that in order to take action u/s 263, the twin conditions i.e. assessment order should be erroneous and prejudicial to the interests of the Revenue should be fulfilled. In the present case, even if it is found that the assessment order is erroneous, but if it does not cause any prejudice to the Revenue, then that order cannot be set aside u/s 263 of the Income Tax Act. He relied upon the judgment of the Hon'ble Supreme Court in the case of Malabar Industries Ltd. Vs. CIT, 243 ITR 83(SC) and the decision of the Hon'ble jurisdictional High Court in the case of CIT vs. D.G. Gopala Gowda 354 ITR 501. He further made reference to the following decisions:

a) Hon'ble Calcutta High Court in the case of Dawjee Dadabhoy and Co. v. S.P. Jain (1957) 31 ITR 872
b) Hon'ble Gujarat High Court in the case of Add. CIT vs. Mukur Corporation (1978) 111 ITR 312
c) Hon'ble Allahabad High Court in the case of Add.CIT vs. Saraya Distillery, 115 ITR 34 (1978)
d) Hon'ble Bombay High Court in the case of CIT vs. Gabriel India Ltd, 203 ITR 108 (Bom.)
e) Hon'ble Gujarat High Court in the case of CIT vs. Minalben S. Parikh (Smt.) 215 ITR 812 Guj. (1995)
f) Hon'ble Madras High Court in the case of CIT vs. G.R. Thangamaligai, 259 ITR 129 (Mad.) 2003.

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6. The learned DR on the other hand contended that the assessment order was passed in 2011 and at that point of time there was no decision of ITAT Hyderabad as well as Hon'ble Andhra Pradesh High Court were available with the Assessing Officer. The assessment order, whether erroneous and prejudicial to the interests of the Revenue is or not? is to be seen when it was passed?. The position of law at that point of time was that receipt on sale of carbon credit would not be considered as derived from the undertaking eligible for deduction u/s 80IA. Therefore, a prejudice to the Revenue for grant of deduction u/s 80IA qua those receipts is there and the assessment order is erroneous. He further contended that at this stage, the additional ground be not permitted to be raised.

7. We have duly considered the rival contentions and gone through the record carefully. Before embarking upon an inquiry about the facts available on record and how to construe them, we deem it pertinent to take note of the fundamental principles for judging the action of the CIT taken u/s 263. The ITAT in the case of M/s Khatiza S. Oomerbhoy Vs. ITO, Mumbai reported in 101 TTJ 1095, analyzed in details various authoritative pronouncements including the decision of the Hon'ble Supreme Court in the case of Malabar Industries Co. vs. CIT 243 ITR 83 and propounded the following broader tests:

(i) The CIT must record satisfaction that the order of the AO is erroneous and prejudicial to the interest of the Revenue. Both the conditions must be fulfilled.

(ii) Sec. 263 cannot be invoked to correct each and every type of mistake or error committed

by the AO and it was only when an order is erroneous that the section will be attracted.

(iii) An incorrect assumption of facts or an incorrect application of law will suffice the requirement of order being erroneous.

(iv) If the order is passed without application of mind, such order will fall under the category of erroneous order.

(v) Every loss of revenue cannot be treated as prejudicial to the interests of the Revenue and if the AO has adopted one of the courses permissible under law or where two views are possible and the AO has taken one view with which the CIT does not agree. If cannot be treated as an erroneous order, unless the view taken by the AO is unsustainable under law

(vi) If while making the assessment, the AO examines the accounts, makes enquiries, applies his mind to the facts and circumstances of the case and determine the income, the CIT, while exercising his power under s 263 is not permitted to substitute his estimate of income in place of the income estimated by the AO.

(vii) The AO exercises quasi-judicial power vested in his and if he exercises such power in accordance with law and arrive at a conclusion, such conclusion cannot be termed to be erroneous simply because the CIT does not fee stratified with the conclusion.

(viii) The CIT, before exercising his jurisdiction under s. 263 must have material on record to arrive at a satisfaction.

(ix) If the AO has made enquiries during the course of assessment proceedings on the relevant issues and the assessee has given detailed explanation by a letter in writing and the AO allows the claim on being satisfied with the explanation of the assessee, the decision of

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> the AO cannot be held to be erroneous simply because in his order he does not make an elaborate discussion in that regard.

8. Before adverting to the facts of the present case, we would like to make a reference to the decision of the Hon'ble jurisdictional High Court in the case of CIT vs. D.G. Gopala Gowda, 354 ITR 501 (2013). In this case, the facts noticed by the Hon'ble High Court read as under:

> *"2. The assessee had purchased a site at Rupena Agrahara in the financial year 1995-96 for a consideration of Rs.3,46,520/-. He started construction of the building in April 1999. He agreed to sell the said property under the agreement dated 9-9-2000 in unfinished condition. Under the terms of agreement, the assessee should complete the construction of the building before execution of sale deed with the help of the funds provided by the purchaser. On 22-11-2000 the assessee executed a sale deed in favour of the purchaser for a consideration of Rs.1,38,00,000/-. The assessee received a sum of Rs.40,00,000/- at the time of agreement. The total cost of construction was Rs.1,04,30,425/-. Thereafter, the assessee purchased another property at Koramangala. The Assessing Officer computed the income from the long term capital gains at Rs.22,17,940/- for the sale of the property. However, the assessee was exempted from paying tax since the fund was utilized fully towards purchase of another property at Koramangala. The Commissioner of Income Tax issued notice under Section 263 of the Act stating that the Assessing Officer was not justified in treating the sale as long term capital gain and according to him, it should have been treated as short term capital gain. The assessee filed his reply to the show cause notice. Thereafter, the Commissioner proceeded to pass the order setting aside the order of assessment on the ground that it is prejudicial to the interest of the revenue. Aggrieved by the said order, the assessee preferred an appeal to the Tribunal. The Tribunal went into the factual aspects and took note of the legal position as settled in various judgments of the courts and in fact, calculated both the short term and long term capital gain and then found that the assessee is not liable to pay any tax. Therefore, it recorded the finding that even if the order of the Assessing Authority is erroneous, it is not prejudicial to the interest of the revenue. Therefore, set aside the order of the revisional authority and granted relief to the assessee".*

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9. The Hon'ble High Court while upholding the order of the ITAT has observed as under:

> *" Even if it is erroneous, unless the said erroneous order is prejudicial to the interest of the Revenue, the Commissioner could not have exercised the said power. From the admitted material on record, the amount that is ordered to be refunded to the assessee is not the amount, which is lawfully due to the Revenue at all, it was an amount which is Revenue legitimately should have refunded if only the claim had been in the return enclosing the certificates under Section 203. the said amount should have been refunded to the assessee. Because he was handicapped by such certificates not being forwarded to him, consequently not able to make the claim, such a claim was not made. The moment he got possession of those certificates on 12.02.2001, within two years from the date of the end of the assessment year he has put forth the claim. The said amount was not a lawful amount to the Government. It was an amount which should have been refunded to the assessee.*
>
> *Therefore, the condition precedent for exercising the revisional power under Section 263 of the Act is that the order under revision should not only be erroneous, but such erroneous order should result in prejudice to the interest of the revenue. Mere error would not confer jurisdiction to exercise revisional power under Section 263 of the Act.*
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> *We have gone through the order passed by the revisional authority. It is a very cryptic order. It neither points out an error nor prejudice which has caused to the revenue. After declaring that the order is prejudicial, it refers to the notice being issued to the assessee and the assessee filing reply to the said notice and then review authority feels that it is a matter to be readjudicated by the Assessing Authority and therefore, the matter was remanded for fresh consideration. This is not the way, the revisional authority should exercise their power under Section 263 of the Act. The order of revisional authority should indicate the error committed by the Assessing Authority and consequential prejudice caused to the revenue because of the erroneous order. Unless these two conditions exist, the revisional authority does not get jurisdiction to pass any order under Section 263 of the Act. Once these two conditions are set out in the order, then it is open to the revisional authority to consider the case on merits and pass final order or in its view, requires some adjudication or enquiry, the matter can be remanded to Assessing Authority. But such remand should be only after setting out the facts which show erroneous nature of*

> *the order and the consequential prejudice to the revenue which confer jurisdiction on the revisional authority.*
>
> *Seen from that angle, in the impugned order though we could make out what is the error committed by the revisional authority, certainly there is no iota of evidence to show how it is prejudicial to the interest of the revenue. On the contrary, in the reply to the notice, the assessee had filed a statement. Even if the assessment is to be made separately for the land on long term basis and to the building on short term basis, the assessee is not liable to pay any tax for the building. The assessee has demonstrated that in no event the order passed by the Assessing Officer is prejudicial to the interest of the revenue. That aspect has not been considered and there is no reference to that aspect in the entire order passed by the revisional authority and by a cryptic order, the matter is remanded to the Assessing Authority. Though the Tribunal was not expected to go into the merits of the case, in order to demonstrate that the order passed by the Assessing Authority even if it is erroneous, is not prejudicial to the interest of the revenue, they have set out computation of capital gains and demonstrated that the order was not prejudicial. Therefore, the order passed by the revisional authority is illegal and rightly it has been set aside.*
>
> *In the light of what we have stated above, the substantial question of law is answered in favour of the assessee and against the revenue".*

10. The Hon'ble High Court has held that fulfillment of twin condition is must i.e. assessment order should be erroneous and it should cause a prejudice to the Revenue. If any one condition is lacking, then action u/s 263 would not be justified. In the above case, the assessment order was erroneous because the learned Assessing Officer failed to compute the long term capital gain and short term capital gain separately. But the Tribunal ultimately arrived at a conclusion that even if this exercise is being done, then there will not be any tax liability and therefore, there is no need to set aside the assessment order. The Hon'ble High Court has upheld this finding of the Tribunal. In the light of the above, let us examine the facts of

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the present case. There is no dispute that the assessee is in the business of Hydro Power Project. It has earned carbon credit which has been rated by the agency and it has sold those carbon credit to a Japanese Company. The details indicating service from carbon management service, allotment of letter of carbon credit, sale bill for sale of carbon credits are available on page Nos. 102 to 110 of the paper book. The ITAT Hyderabad has decided this issue for the first time and the discussion made by the ITAT Hyderabad Bench worth to note, it read as under:

> *"24. We have heard both the parties and perused the material on record. Carbon credit is in the nature of "an entitlement" received to improve world atmosphere and environment reducing carbon, heat and gas emissions. The entitlement earned for carbon credits can, at best, be regarded as a capital receipt and cannot be taxed as a revenue receipt. It is not generated or created due to carrying on business but it is accrued due to "world concern". It has been made available assuming character of transferable right or entitlement only due to world concern. The source of carbon credit is world concern and environment. Due to that the assessee gets a privilege in the nature of transfer of carbon credits. Thus, the amount received for carbon credits has no element of profit or gain and it cannot be subjected to tax in any manner under any head of income. It is not liable for tax for the assessment year under consideration in terms of sections 2(24), 28, 45 and 56 of the Income-tax Act, 1961. Carbon credits are made available to the assessee on account of saving of energy consumption and not because of its business. Further, in our opinion, carbon credits cannot be considered as a bi-product. It is a credit given to the assessee under the Kyoto Protocol and because of international understanding. Thus, the assessees who have surplus carbon credits can sell them to other assessees to have capped emission commitment under the Kyoto Protocol. Transferable carbon credit is not a result or incidence of one's business and it is a credit for reducing emissions. The persons having carbon credits get benefit by selling the same to a person who needs carbon credits to overcome one's negative point carbon credit. The amount*

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received is not received for producing and/or selling any product, bi-product or for rendering any service for carrying on the business. In our opinion, carbon credit is entitlement or accretion of capital and hence income earned on sale of these credits is capital receipt. For this proposition, we place reliance on the judgment of the Supreme Court in the case of CIT vs. Maheshwari Devi Jute Mills Ltd. (57 ITR 36) wherein held that transfer of surplus loom hours to other mill out of those allotted to the assessee under an agreement for control of production was capital receipt and not income. Being so, the consideration received by the assessee is similar to consideration received by transferring of loom hours. The Supreme Court considered this fact and observed that taxability of payment received for sale of loom hours by the assessee is on account of exploitation of capital asset and it is capital receipt and not an income. Similarly, in the present case the assessee transferred the carbon credits like loom hours to some other concerns for certain consideration. Therefore, the receipt of such consideration cannot be considered as business income and it is a capital receipt. Accordingly, we are of the opinion that the consideration received on account of carbon credits cannot be considered as income as taxable in the assessment year under consideration. Carbon credit is not an offshoot of business but an offshoot of environmental concerns. No asset is generated in the course of business but it is generated due to environmental concerns. Credit for reducing carbon emission or greenhouse effect can be transferred to another party in need of reduction of carbon emission. It does not increase profit in any manner and does not need any expenses. It is a nature of entitlement to reduce carbon emission, however, there is no cost of acquisition or cost of production to get this entitlement. Carbon credit is not in the nature of profit or in the nature of income.

25. Further, as per guidance note on accounting for Self-generated Certified Emission Reductions (CERs) issued by the Institute of Chartered Accountants of India (ICAI) in June, 2009 states that CERs should be recognised in books when those are created by UNFCCC and/or unconditionally available to the generating entity. CERs are inventories of the generating entities as they are generated and held for the purpose of sale in ordinary course. Even though CERs are intangible assets those should be accounted as per AS-2 (Valuation of inventories) at a cost or market price, whichever is lower. Since CERs are recognised as inventories, the generating assessee should apply AS-9 to recognise revenue in respect of sale of CERs.

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> *26. Thus, sale of carbon credits is to be considered as capital receipt. This ground is allowed.*
>
> *27. As we have decided the main issue, the alternate ground of the assessee becomes infructuous and the same is dismissed.*
>
> *28. In the result, assessee's appeal is allowed.*
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> Order pronounced in the open court on 2nd November, 2012".

11. This decision has been upheld by the Hon'ble Andhra Pradesh High Court. This decision has been subsequently followed by the ITAT Chennai and Jaipur Benches. There is no decision either from the Hon'ble Supreme Court or from the Hon'ble jurisdictional High Court. These decisions indicate that sale of carbon credit would result capital receipt which is not taxable. When we confronted the learned DR with regard to this position, it was contended that the position as on the day when the assessment order was passed, is to be seen and on that day these orders were not available. Therefore, the assessee cannot claim the benefit of these orders. However, we do not concur with this proposition of the learned CIT, because the Full Bench of the Hon'ble Punjab & Haryana High Court in the case of Aruna Luthra reported in 254 ITR 76 has held that a Court decide a dispute between the parties. The case can involve decision on facts. It can also involve a decision on point of law. Both may have bearing on the ultimate result of the case. When a Court interprets a provision, it decides as to what is the meaning and effect of the words used by the Legislature, it is the declaration regarding the statute. In other words the judgment declares as to what the legislature had said at the time of promulgation of the law, the declaration is.........., this

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was the law, this is the law, this is how the provision shall be construed. Therefore, he cannot plead that the view taken by the Tribunal and upheld by the Hon'ble Andhra Pradesh High Court could be considered as if applicable from the date of the decision. In the decision only the position of the law as to how receipts from sale of carbon credits are to be treated, has been explained. One of the argument raised by the DR was that at this stage, the additional ground ought not to be permitted to be raised. It is pertinent to mention here that basically, it is not a separate ground, it is a limb of arguments, which is affecting the ultimate tax liability of the assessee. The Hon'ble Supreme Court in the case of NTPC Ltd (Supra) has held that the Tribunal had jurisdiction to examine a question of law which arose from the fact as found by the Income Tax authorities and having a bearing on the tax liability of the assessee. As far as the nature of the receipt from sale of carbon credit is concerned, it is available from the assessment stage. It is not disputed even by the learned Commissioner, the dispute is, whether it has been derived from the eligible industrial undertaking for qualifying the grant of deduction u/s 80IA. The learned Commissioner felt that this receipt has not been derived from the industrial undertaking which will be eligible for grant of deduction u/s 80IA and the Assessing Officer committed an error in including the receipt in the eligible profit. Those facts are already on the record. It is to be seen, whether the receipt is of capital nature or of a revenue nature. Even in case the order of the CIT is upheld, then, in law, it will affect the computation of income, ultimately because the receipt will not be taxable, it will not come under the ambit of computation

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of income. Simultaneously it will be excluded from the deduction u/s 80IA as well as of the total income. The result will remain as it is. It is a revenue neutral case. Therefore, in view of the ratio laid down by the Hon'ble jurisdictional High Court in the case of Gopala Gowda (Supra), the second condition for taking action u/s 263 does not exist. The assessment order is not prejudicial to the interests of the Revenue. In view of the above discussion, we allow the appeal of the assessee and quash the impugned order of the learned CIT passed u/s 263 of the Income Tax Act.

Order pronounced in the Open Court on 28th November, 2014.

Sd/-	Sd/-
(Jason P. Boaz)	**(Rajpal Yadav)**
Accountant Member	**Judicial Member**

Bangalore dated 28th November, 2014.

Vnodan/sps

Copy to:

1. *The Appellant*
2. *The Respondent*
3. *The concerned CIT(A)*
4. *The concerned CIT*
5. *The DR, ITAT, Bangalore*
6. *Guard File*

By Order

ASSISTANT REGISTRAR
Income Tax Appellate Tribunal,
Bangalore Benches, Bangalore

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