

IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCH 'C', BANGALORE

BEFORE SHRI. N. V. VASUDEVAN, JUDICIAL MEMBER

AND

SHRI. ABRAHAM P. GEORGE, ACCOUNTANT MEMBER

I.T.A No.634/Bang/2015
(Assessment Year : 2010-11)

Mfar Holdings P. Ltd,
No.3, Lavelle Road, Bangalore
PAN : AABCM3804C

..Appellant

v.

Principal Commissioner of Income-tax-4,
Bangalore

..Respondent

Assessee by : Shri. Cherian K Baby, CA
Revenue by : Shri. Sunil Kumar Agarwala, JCIT

Heard on : 04.08.2015
Pronounced on : .08.2015

ORDER

PER ABRAHAM P. GEORGE, ACCOUNTANT MEMBER :

In this appeal filed by assessee, it assails an order dt.27.02.2015 of the Pr. CIT -4, Bengaluru, passed u/s.263 of the Income-tax Act, 1961 ('the Act' in short), for the assessment year 2010-11.

02. Assessee has raised the following grounds :

- 1. The learned Pr. Commissioner of Income Tax-4, Bangalore has erred in acting outside the jurisdiction vested in him under section 263 of the Income Tax Act, 1961 as he has failed to establish that the impugned order of assessment under section 143(3) of that Act is erroneous in so far as it is prejudicial to the interests of the revenue.*

2. *The learned Pro Commissioner of Income Tax-4, Bangalore has erred in directing the AO to redo the assessment to check the genuineness of the business loss incurred by your appellant on sale of inventory converted into stock in trade from investment in earlier years.*
3. *The learned Pro Commissioner of Income Tax-4, Bangalore has erred in directing the AO to examine the evidence in the possession of your appellant with regard to cash payments u/s 269SS/269T of the Income tax Act, 1961 without considering the fact that the Additional Commissioner, Range 4(1), Bangalore had already initiated proceedings u/s 271D and 271E and passed an order dated 29-12-2014 after detailed verification of all records in the possession of your appellant.*

03. Facts apropos are that assessee engaged in the business of holdings and leasing of properties had filed its return for the impugned assessment year declaring income of Rs.2,11,43,020/-. This was later revised downwards to Rs.1,22,55,121/- through a revised return. Assessment was completed after scrutiny on 27.03.2013, inter alia making certain disallowances u/s.14A of the Act, read with Rule 8D of the Rules.

04. On 27.03.2014, show-cause notice was issued by the CIT u/s.263 of the Act. As per the Pr. CIT, assessee had claimed business loss of Rs.5,30,56,438/- on sale of inventory, but as per the tax audit report in form 3CD assessee had not carried on any business activity nor transferred any of its capital asset to stock-in-trade during the relevant previous year. As per the Pr. CIT, such claim of business loss was to be disallowed. Second point raised in such show cause notice was that assessee had received cash loans of Rs.1,02,83,336/- and paid back Rs.2,85,57,209/- otherwise than by account payee cheque contravening Section 269 SS and 269T of the Act. As per the Pr. CIT, AO ought to have

initiated penalty proceedings u/s.271D and 271E of the Act, which he failed to do.

05. To this show-cause notice, assessee filed a detailed reply. On the first issue reply of the assessee was that it was in the business of real estate and the buildings, sale of which resulted in profits from business or profession were in the nature of its inventory. As per the assessee, business loss of Rs.5,30,46,848/- related to sale of property held as inventory, namely, Mfar Silverline Technology Park, Whitefield, Bangalore. Assessee explained to the Pr. CIT that the said property was part of its investment up to 31.03.2007, on which date it was converted to stock-in-trade. As per the assessee, difference between fair market value as on 31.03.2007 and the actual cost of the property which came to Rs.7,23,97,464/-, was returned under the head short-term capital gains and difference between the fair market value and actual sale consideration was returned under the head 'profits and gains of business or profession'. Assessee submitted before the CIT (A) that u/s.45(2) of the Act, when an asset was converted into stock-in-trade, the difference between the fair market value and the cost of such asset had to be considered as capital gains and returned in the year in which the asset was sold. Thus according to assessee it had correctly shown the income / loss in its computation, as well as the return filed.

06. Vis-à-vis the cash receipt and repayment of loans, submission of the assessee before the Pr. CIT was that transactions considered were with its group company namely /s. Leonis Infrastructure Development P. Latd (LIDPL in

short). Assessee pointed out that the cash payments were only Rs.13,757/- and other payments were all made either through account payee cheques, or through journal entries in the ledger account, squaring up the amounts due from other parties with that of LIDPL. Assessee also produced ledger account copies and bank account copies in support of this. As per the assessee, there was no contravention of Section 269SS / 269T of the Act.

07. However, Pr. CIT was not impressed with the above reply. According to him, business loss claimed on the sale of the property was only for the purpose of taking advantage of Section 45(2) of the Act, thereby inflating the cost of asset to the fair market value. As per the Pr. CIT, there was no business loss since the assessee was holding the property only as an investment all through.

08. Vis-à-vis receipts / payment of loans in cash, as per Pr. CIT, necessary evidence in support of its claim, that there were no cash transactions, was not available. He set aside the order of assessment and directed the AO to redo it after considering the full circumstances and genuineness that the claim of the assessee as well as the evidence produced with regard to the cash payments.

09. Now before us, Ld. AR strongly assailing the order of Pr. CIT submitted that conversion of the property into stock-in-trade was done on 31.03.2007. As per the Ld. AR even in the immediately preceding year, viz., A. Y. 2009-10, there was sale of a part of the very same property and the assessee had returned short-term capital gains and business loss arising out of sale of the property in the same manner, as for the impugned assessment year. Such results for A. Y.

2009-10 were accepted by the Department. As per the Ld. AR, in the audited final accounts of the assessee filed along with the return of income for A. Y. 2007-08, reclassification of the investments to inventory was specifically mentioned. Building pending completion of construction was shown as inventory in Schedule -6 of the Balance-sheet as on 31.03.2007. Para 3.2(ii) of Schedule – 16, being notes to accounts, clearly mentioned the factum of reclassification. Ld. AR pointed out that during the course of original assessment proceedings for the impugned assessment year, assessee filed all necessary information / documents required by the AO. Relying on letter dt.11.01.2013, Ld. AR submitted that the method of computation of short-term capital gains was clearly given therein. Ld. AR pointed out that a portion of the building was sold in the year 2008-09 and this was also mentioned in the said reply. Reliance was also placed on letter dt.23.01.2013 which explained why sale consideration of the property sold was Rs.3,000/- per sft against the fair market value of Rs.3,500/- per sft as on 31.03.2007, which lead to the business loss. Thus according to Ld. AR, the AO was well aware of the transaction and had considered the computation to be lawful and valid.

10. Vis-à-vis the issue of non-initiation of penalty u/s.271D and 271E of the Act, Ld. AR submitted that such penalty proceedings were initiated by Addl. CIT. As per the Ld. AR, CIT was not correct in stating that no penalty proceedings were initiated. Relying on a penalty order u/s.271E of the Act, dt.29.12.2014, Ld. AR submitted that Addl. CIT had levied penalty u/s.271E of

the Act. Thus according to him the reason mentioned by the CIT for attempting the revision had no legs to stand.

11. Per contra, Ld. DR strongly supported the order of the Pr. CIT.

12. We have perused the orders and heard the rival contentions. It is true that in the computation of income filed by the assessee for the impugned assessment year, it had shown short-term capital gains of Rs.7,23,97,463/- from sale of property. It is also true that assessee had shown loss on sale of inventory of Rs.5,30,46,848/- under the head 'income from business or profession'. Records also show that assessee had given an explanation vis-à-vis computation of short-term capital gains vide its letter dt.11.01.2013, addressed to the AO which read as under :

The total cost incurred for development of 1,70,868 (including the share of the Owner) upto 32st March 2007 was Rs.24,24,17,179. Thus the cost of construction was Rs.1,418/- per Sq Ft.

Further. as can be seen from the sale deeds (submitted to you in the earlier hearings), this cost of construction also includes fully centralised Air Conditioning and Diesel Generators for 100 power backup (including Air Conditioning)

The costs claimed in computing short term capital gains are as per the books of account and supported by vouchers and bills. In this connection, we would also like to bring to your kind notice that a portion of the Building was sold during the financial year 2008-09 and the remaining portion was sold during the financial year under scrutiny now. The assessment for the year 2008-09 (AY 2009-10) has been completed.

13. Another explanation was also provided on 23.01.2013, vis-a-vis the sale consideration, which read as under :

Note on why the sale consideration of property sold is only around Rs.3000/-per sq ft while the FMV as at 31st March 2007 was Rs.3500/-

Even though, construction of the Building was completed and obtained Occupancy Certificate in July 2005, the same could not be readily leased out by the Company in spite of best efforts. This could be done in parcels over some time.

Since we could not lease out the building in full, a business decision was taken to sell the property at best possible terms. Accordingly, during the year 2008-09, building measuring 46,962 Sq. ft was sold to SPML Keerthihole Power Company Limited @ Rs.2,000 per Sq. ft even-though the property was valued by the valuer at Rs.3500 during March 2007. After this, the balance of the building was sold to different parties in small parcels to realize better price.

The details of sale of property in 2009-10 have already been submitted to you. The sale price comes to an average of around Rs.3000/- per sq ft. The sale consideration obtained was higher than the guidance value at the time of sale which was only Rs.11 00/- per square feet. The guidance value rate is attached for your ready reference. Hence, this was the best price that we could get for the property at that point of time considering the market situations.

The Sale consideration per sq ft in case of sale done in FY 2008-09 along with copies of sale deeds :

As explained earlier, sale of property to SPML and LIDPL was at Rs.2,000/- per square feet during the FY 2008-09. Copies of sale deeds are attached herewith for your ready reference (Annexure 2)

Sale deed for sale of property to Sushil Kalra & Surendra Paul :

This is attached as Annexure 3. Rest of the sale deed copies have already been furnished to you.

14. Submission of the assessee before the CIT was that the method of computation adopted by it on sale of the property was one mandated u/s.45(2) of the Act. Section 45(2) of the Act is reproduced hereunder :

(2) Notwithstanding anything contained in sub-section (1), the profits or gains arising from the transfer by way of conversion by the owner of a capital asset into, or its treatment by him as stock-in-trade of a business carried on by him shall be chargeable to income-tax as his income of the previous year in which such stock-in-trade is sold or otherwise transferred by him and, for the purposes of section 48, the fair market value of the asset on the date of such conversion or treatment shall be

deemed to be the full value of the consideration received or accruing as a result of the transfer of the capital asset.

15. A careful look at the assessment order passed by the AO, show that there is not even a whisper with regard to the computation of short-term capital gains or the business loss or the section under which these were considered. AO in the operative part of the assessment order dt.27.03.2013 held as under :

3 .The assessee company is engaged in business of Holdings & leasing of Properties and Consultancy services. During the course of hearing, vide order sheet noting on 31/12/12 & 11/01/13, the assessee was asked to furnish the details of exempted income along with the disallowances if any to be made u/s.14 as per provisions of section 14A of the I T Act. However, the assessee has not furnished the details of expenditure to be disallowed as per Rule 8D of IT Rules(rule 80 had been introduced with effect from 24-3-2008). The onus is on the assessee to show the expenditure incurred in relation to the exempted income, which was not discharged. The assessee has shown dividend income of Rs21,653/- which was claimed as exempt u/s. 10(35) of the I T Act. The investments made by the assessee in Mutual funds was Rs 55,07,727/-. The assessee has also made investments in Companies The dividend income is exempted from income tax. To make such investments, lot of expenditure in the form of application of mind by the Directors who were paid remuneration, other related expenditure has been incurred which relate to exempted income. The assessee had incurred expenditure in relation to income not includible

In total income but has not furnished any details in this regard. Therefore, having regard to the accounts of the assessee of the previous year, the undersigned is not satisfied with the correctness of the claim of expenditure made in relation to income which does not form part of the total income under the Act. Accordingly, the disallowance as per Rule 80 of I T Rules, 1962 is calculated as follows :-

The investments made by the assessee as on 31/3/2009 is Rs.1,92,22,217/-

The investments made by the assessee as on 31/3/2010 is Rs 5,37,14,490/-

The average of opening & Closing investments Rs 7,29,36,707/2 = Rs 3,64,68,353/-

One ha If percent of the average value of investment of 3,64,68 353 =Rs 1,82,342/-

Thus, the amount of Rs.1,82,342/- determined as per Rule 8D is assessed to tax.

16. What we find is that the AO considered the assessee to be engaged in the business of holdings and leasing of property and consultancy services and not as a real estate dealer. In the audit report filed by the assessee along with the return of income at para 2 of Annexure, it is stated as under :

2. The company does not have any inventory other than capital assets held for sale classified as inventory and accordingly the requirements of this clause are not reported upon.

Audit report thus clearly say that what was classified as inventory was nothing but capital assets of the assessee.

17. Income from operations for the relevant previous year as per Schedule - 12 and other income shown by the assessee at schedule 13, read as under :

	2010
SCHEDULE 12 INCOME FROM OPERATIONS	
Rent Received	11,124,210
Maintenance Chgs Recvd	4,393,155
Consultancy charges	-
TOTAL	15,517,365
SCHEDULE 13 OTHER INCOME	
Profit on Extinguishment of Liability	21,784,735
Profit on Sale of Property	31,752,845
Other Interest Income	1,967,006
Income from sub-letting	840,420
Dividend Received from mutual funds	21,653
Other Miscellaneous Income	5,100
Excess provision written back	56,695
Premium Written Back	-
TOTAL	56,428,454

18. Operational income of the assessee was rent and maintenance charges. Profit on sale of property fell under other income. Thus neither the assessee nor its auditor considered it to be in real estate business. The two explanations given by the assessee before the AO reproduced by us above did not mention anything regarding conversion of the property to stock-in-trade. As per the assessee in its audited accounts for FY 31.03.2007 such conversion was clearly mentioned. What is mentioned in the audited final accounts in FY 31.03.2007 appears at schedule 6 thereof which reads as under :

INVENTORY

Building pending Completion of Construction [Refer Note No.2(ii)] -242,417,179

19. Note No.2(ii) of Schedule 16 reads as under :

ii) Subsequent to the previous Balance sheet, the company was successful in rectifying the defects relating to MSTP property. It has also entered into an agreement for sale of this property and has received an advance. Hence the building which is yet to be fully finished has been reclassified from Investment to Inventory. The additional costs incurred on the dedicated diesel generator and air conditioner and other facilities during the year have been added to the carrying value of this property.

20. In our opinion, the above statements and entries in the audited final accounts for 31.03.2007 did not give a clear picture on the method of treatment nor the fair market value which was adopted while transferring such investment to inventory. AO had not applied his mind to the fact that assessee was not doing real estate business nor did he apply his mind to the reported transactions as a prudent man should have done. Assessee had at no point of time stated

before the AO that the method in which it had shown the profits / losses arising from the sale of such property was computed in accordance with Section 45(2) of the Act. Any person with ordinary prudence would have been prodded to make enquiries about what assessee had stated. Assessee's contention that it had given all the details called for by the AO, falls flat since there is no mention at any place as to what were the details called for by the AO. Assessee could not produce any letter or communication in which the AO sought explanation on this particular aspect. Thus there is nothing to show that the AO had considered the issue. In our opinion there was clear absence of enquiry by the AO which he ought to have done. Just because in the preceding year no action u/s.263 of the Act was initiated would not be a reason to hold that Revenue ought not have done this for the impugned assessment year also.

21. Vis-a-vis payments made in cash and repayments, what we find is that assessee had not mentioned before the CIT, details of the proceedings taken by the Addl.CIT levying penalty u/s.271E of the Act. Even the said order u/s.271E of the Act, placed at paper book Annexure –A, is confined to Section 271E only and does not say anything on Section 271D. During the course of assessment proceedings the AO had never examined this issue at all.

22. In the above circumstances, we are therefore of the opinion that the assessment order was erroneous and prejudicial to the interests of Revenue for want of enquiry and for non-application of mind. We find that Pr. CIT was

justified in invoking the powers vested on him u/s.263 of the Act. We do not find any reason to interfere.

23. In the result, appeal of the assessee is dismissed.

Order pronounced in the open court on 14th day of August, 2015.

Sd/-

Sd/-

(N. V. VASUDEVAN)
JUDICIAL MEMBER

(ABRAHAM P GEORGE)
ACCOUNTANT MEMBER

MCN

Copy to:

1. The assessee
2. The Assessing Officer
3. The Commissioner of Income-tax
4. Commissioner of Income-tax(A)
5. DR
6. GF, ITAT, Bangalore

By Order

Assistant Registrar