IN THE INCOME TAX APPELLATE TRIBUNAL
"A" BENCH : BANGALORE

BEFORE SHRI N.V. VASUDEVAN, JUDICIAL MEMBER
AND SHRI JASON P. BOAZ, ACCOUNTANT MEMBER

S.P. No.204/Bang/2014 & ITA No.1125/Bang/2014
Assessment year : 2007-08

M/s. Apco Concrete Blocks & Allied Products, No.805, 14th Cross, I Phase, J.P. Nagar, Bangalore – 560 078. **PAN: AABFA 9128J**	Vs.	The Deputy Commissioner of Income Tax, Circle 4(1), Bangalore.
APPELLANT		RESPONDENT

Appellant by	:	Shri Sarangan, Sr. Counsel
Respondent by	:	Shri P. Dhivahar, Jt. CIT(DR)

Date of hearing	:	23.02.2015
Date of Pronouncement	:	27.02.2015

O R D E R

Per N.V. Vasudevan, Judicial Member

This is an appeal by the Assessee against the order dated 12.6.2014 of the CIT(Appeals)-II, Bangalore relating to AY 07-08.

2. One Mr.Abraham Mathew acquired an extent of 2 Acres and 3 guntas of land in S.No.46/2A, Kanakapura Road, Bangalore (hereinafter referred to as "the property") under a registered sale deed dated 30.7.1971. He was running the business of trading in concrete blocks as Sole Proprietor. The property at the time of acquisition in the year 1971 was agricultural land and, subsequently, converted for industrial purpose. The property was shown as business asset from the year 1973. On 1.4.1981 the sole proprietor business was converted into a Partnership firm under a deed of partnership dated 1.4.1981 whereby the sons and daughters of Mr.Abraham Mathew were inducted as partners. All the assets and liabilities of the sole proprietor business became the assets and liabilities of the partnership firm, except capital contribution by the partners. As far as the Mr.Abraham Mathew's capital contribution to the firm is concerned, it included a value of Rs.2,70,975/- which was taken in the books of accounts on 1.4.1981 when the property was introduced as an asset of the partnership firm. The partnership firm so formed is the Assessee in the present appeal.

3. The property was sold by the Assessee on 31.5.2006 for a sale consideration of Rs.6 Crores. The dispute before the AO in the assessment proceedings was with regard to computation of Long Term capital gain on sale of the property. The cost of acquisition to be adopted for the purpose of computing long term capital gain was the dispute before

the AO. While computing the capital gains, the assessee estimated the market value of the property as on 1.4.1981 on the basis of the valuation report obtained from the Government Registered Valuer at Rs.30 lakhs. After providing indexation, the value was determined at Rs.1,55,70,000/- and reducing the same from the net consideration of Rs.6 crores, offered a sum of Rs.4.44 crores for the purpose of computation of capital gains. However, according to the AO, the cost of acquisition should be the actual cost to the assessee firm and the actual cost is nothing but the cost shown as per the books of account as on 1.4.1981 and not the fair market value (FMV) as on 1.4.1981 as contended by the assessee. Therefore, the AO adopted the value of Rs.2,70,975/- as taken in the books of accounts on 1.4.1981 when this asset was introduced as an asset of the assessee firm. Accordingly, the AO worked out the index cost of the acquisition at Rs.14,06,360/- and reducing the same from the net consideration arrived at the LTCG at Rs.5.83,95,652/- instead of Rs.4.44 crores disclosed by the assessee. The Assessee had worked indexed cost of acquisition at Rs.1,55,70,000/-. The CIT(A) confirmed the order of the AO.

4. The Assessee filed appeal before the Tribunal against the order of the CIT(A) in ITA No.1024/Bang/2010. The main contentions of the assessee before the Tribunal were that :-

(i) The property was acquired by the Assessee by one of the modes specified in s. 49 of the Act i.e., by succession and NOT by purchasing the same by paying any money; that the assets and liabilities of the firm by succession of the proprietary concern by inducting others into the firm. Thus, there was a succession of the proprietary concern by the partnership firm and, therefore, it was argued, the capital asset became the property of the Assessee only by succession which did fall within the ambit (modes) prescribed in s.49(1) (iii)(a) of the Act. The said section implicitly denotes that the cost of acquisition of the asset shall be deemed to be the cost for which, the previous owner of the property acquired it i.e., the proprietor of the erstwhile proprietary concern. The above contention was based on an additional ground of appeal raised by the Assessee before the ITAT seeking to plead that the case of the Assessee will be a case of succession falling within section 49(1)(iii)(a) of the Act;

(ii) the ruling of the Hon'ble Apex Court in the case of Sunil Siddharthbhai v. CIT reported in (1985) 156 ITR 509 (SC) is directly applicable to the facts of the issue under consideration whereby it was held that when an individual brings his individual property as capital contribution of the firm there is no transfer resulting in chargeable capital gain;

(iii) the Ld. CIT (A) ought to have held that the immovable property having been acquired in the year 1971, the market value of the property as in 1971 as increased by the cost of inflation index and other expenses for the conversion of the land for industrial use should have been allowed as a deduction u/s 48 of the Act while computing the Capital Gains;

(iv) the CIT (A) had, further, failed to recognize that the value taken was supported by a Registered Valuer's report as on the date of the formation of the firm and as increased by the cost of inflation index, if any, as the cost of acquisition for computation of Capital Gains; and

(v) there was no cost of acquisition for the firm since the asset was already in the books of account of the proprietary concern which was, subsequently, converted into a partnership firm by an agreement of partnership entered into between the erstwhile proprietor and the new partners without change in the book value of the asset and, therefore, the book value of the asset as on the date of conversion of the proprietary concern into a partnership firm cannot be taken as the cost of acquisition of the asset.

5. The Assessee filed a paper book containing 1–55 pages which consist of, inter alia, copies of (i) partnership deed dated 1.4.1981; (ii) cost inflation index,; (iii) conversion sanctioned certificate; (iv) Valuation report etc.

6. The Tribunal vide its order dated 6.1.2012 in ITA No. 1024/Bang/2010 adjudicated the issue holding as follows:-

(1) It is an undisputed fact that there was no cost of acquisition for the Assessee since the asset was already in the books of account of the proprietary concern which was subsequently converted into a partnership firm by an agreement of partnership entered into between the erstwhile proprietor of the proprietary concern and his family members - the new

partners. However, there was no partition among the family members of the proprietor of the proprietary concern. There were salient distinguishing features, as highlighted by the Ld. Counsel that the subject property was not valued as on the date of formation of partnership firm. Moreover, the balance sheet of the proprietary concern had become the balance sheet of the partnership firm without any change subject to capital contribution. The property not having been revalued at the time of converting the proprietary concern into a partnership firm without any change subjected to capital contribution and that the property not having been revalued, the value taken in the balance sheet of the partnership firm was, evidently, notional.

(2) The Hon'ble Supreme Court in the case of Sunil Siddharthbhai Vs. CIT 156 ITR 509 (SC) had ruled that introduction of property owned individually by a partner as capital of the partnership firm does not give raise to a transfer which can be brought to tax as capital gain in the hands of the individual.

(3) Sec.45(3) of the Act was brought into the statute book only from 1.4.1988 and will have no bearing on the transfer of capital asset by the individual to the Assessee firm on 1.4.1981.

(4) The contention raised by the Assessee in the additional ground was that there was a succession in business and therefore provisions of Sec.49(1)(iii)(a) would apply and therefore the cost of acquisition of the property has to be determined with reference to the cost to the previous owner i.e., Mr. Abraham Mathew who acquired the property individually in his name in the year 1971 and brought in the property as business asset in the year 1973. In para 7.2.5 of

the Tribunal's order the Tribunal while dealing with the above contention wrongly referred to Sec.55(2)b(i) instead of Sec.55(2)(b)(ii) nevertheless held that the FMV as on 1.4.1981 has to be adopted.

7. The Tribunal finally concluded as follows in para 7.28 of it's order:-

> "7.2.8. In an overall consideration of the facts and circumstances of the issue as discussed in the foregoing paragraphs, we are of the considered view that the Ld. AO had not examined as to whether the cost value given by the assessee firm is correct or otherwise, in stead, he had adopted the book value as on 1.4.1981. In view of the above, the issue is remitted back to the file of the AO with a specific direction to examine as to whether the value [FMV] shown by the assessee firm is correct as on 1.4.1981 and to take appropriate action in accordance with the provisions of the Act at that relevant period., The Ld. AO shall, however, keep in view the ruling of the Hon'ble Supreme Court [156 ITR 509] as well as the finding of this Bench cited supra while deciding the issue. It is ordered accordingly."

8. The AO while giving effect to the order of the Tribunal, held that as per the decision of the Hon'ble Supreme Court in the case of *Sunil Siddharthbhai (supra)*, when a partner brings his asset as capital contribution of the firm there was a transfer but such transfer cannot give raise to computation of capital gain because no consideration passes from the firm to the partner and therefore the computation machinery provided under the Act fails and hence there cannot be any determination of capital gain. According to the AO, there was a transfer of the property on 1.4.1981 when the individual brought in the property as property of the firm and

therefore the property was acquired by the Assessee on 1.4.1981 only and not earlier to that date and that the mode of acquisition is not by way of succession. The relevant observations of the AO were as follows:-

> "4. Having become the owner on 1.4.1981 the assessee firm sold the said land in the year in discussion and accordingly capital gains arose in this year on which there is no dispute by the assessee. The only dispute is the cost of acquisition that needs to be adopted for computing these capital gains. As per the definition provided in sec. 55(2)(b)(i), in relation to any capital asset which became the property of the assessee **before first day of Apri1 1981**, the cost of acquisition means the cost of acquisition of the asset to the assessee or the F.M.V of the asset on first day of April, 1981 at the option of the assessee. It has also been provided in 55(2)(b)(ii) that where the capital asset became the property of the assessee by any of the modes specified in sec. 49(1) and capital asset became property of the previous owner before 1.4.1981, cost of acquisition means cost of the capital asset to the previous owner or the F.M.V of the asset on 1.4.1981 at the option of the assessee. One of the modes specified in sec. 49(1) is the succession and the assessee is taking a stand that the partnership firm acquired the asset by succession. This argument of the assessee is not acceptable because in a case of a succession, no consideration is paid by the successor to the orignа1 owner. Here the assessee is claiming the successor status in so far as the asset is concerned but the original owner continues as a partner in the assessee firm with a truncated right over this asset and his capital account has been credited with an amount equivalent to the value of the said asset. The capital so credited represents the deemed consideration paid by the assessee firm to the partner who introduced this asset and that introduction has been held as a transfer even by the Hon'ble Supreme Court in the above judgment. In view of the above, the contention that introduction of this asset by the partner in the firm is a mode of acquisition falling under sec. 49(1) cannot be accepted. Therefore, the provisions of sec. 55(2)(b)(i) shall apply for determining the cost of acquisition. As per this provisions, **the option of the assessee to adopt the F.M.V. of the asset as on 1.4.1981 as the cost of acquisition can only be exercised when the assessee became the owner before 1.4.1981**. Since the

assessee became the owner not before 1.4.1981 but only on 1.4.1981, this option of adopting the F.M.V. as on 1.4.1981 for cost of acquisition is not available to the assessee. **The Hon'ble ITAT directed to examine whether the F.M.V shown by the assessee firm is correct as on 1.4.1981. However, in view of the above discussions, since FMV is not relevant, with due regards to the Hon'ble ITAT, the correctness of the F.M.V. as on 1.4.1981 is also considered as not relevant and therefore not looked into.** (underlining by us for emphasis)

In these circumstances, only the cost recorded in the books of the firm is the cost of acquisition for the purpose of computing capital gains. Accordingly, the cost as adopted in the original assessment is adopted and LTCG is computed as under."

LTCG arrived now as discussed above: Net consideration received from & execution of sale deed dated 31.05.2006	Rs. 6,00,00,000
Less : Book value of the land & building as on 1.4.1981 1. Indexation on land & building Rs.270975 x 519 =Rs. 14,06,360 2. Cost of borewell Rs. 1,97,988	Rs.16,04,348
Total Long Term Capital Gain	**Rs.5,83,95,652**
Less : LTCO as declared by the assessee	Rs.4,44,09,562
Excess LTCG now assessed	Rs. 1,39,86,090

9. On appeal by the Assessee, the CIT(A) confirmed the order of the AO. It was pointed out before CIT(A) that the direction of the tribunal have not been followed by the Tribunal, in as much as the direction of the tribunal was to ascertain the FMV as on 1.4.1981 of the property, whereas the AO refused to follow the said direction on his conclusion that the direction of the tribunal was not correct. The CIT(A), however, held that the Tribunal had only remanded to the AO the determination of valuation of the

property and therefore the approach of the AO in adopting the value of Rs.2,70,975/- which was recorded as capital value of the property on formation of the partnership firm was correct.

10. Aggrieved by the order of the CIT(A), the Assessee has filed the present appeal before the Tribunal.

11. The ld. counsel for the assessee submitted before us that the AO, while giving effect to the directions of the Tribunal, has clearly violated the directions of the Tribunal. It was submitted by him that the Tribunal in para 7.2.8 of its order clearly directed the AO to examine the FMV shown by the assessee as on 1.4.1981 is correct. According to him, a reading of the entire order of the Tribunal would show that the Tribunal accepted the contention of the assessee that the assessee was entitled to adopt the FMV as on 1.4.1981 and that the value as shown in the books of account of the property at the time of the formation of the partnership was only notional and it cannot be regarded as FMV of the property as on 1.4.1981. It was further pointed out by him that the AO in the impugned order giving effect to the directions of the Tribunal, has held that the decision of the Tribunal as stated above was not correct and therefore is not being looked into. According to him, doing so was a complete violation of the order of a superior forum. In this regard, the ld. counsel for the assessee drew our attention to the decision of the Hon'ble Supreme Court in the case of *Bhopal Sugar Industries Ltd. Vs. ITO 40 ITR 618 (SC)*.

12. In *Bhopal Sugar Industries Ltd. (supra)*, the scope of remand and duty of ITO were explained by the Hon'ble Supreme Court. In the said decision, the facts were that the Tribunal directed the ITO "*to ascertain the average transport charges per maund from the centres to the factory and add to it the rate of Rs. 1-4-6 per maund of sugarcane*". The Direction was clear and unambiguous. The ITO instead of ascertaining the average transport charges per maund from the centres to the factory, referred to the transport charges from the farms to the factory and on that footing disregarded the directions of the Tribunal. The Hon'ble Supreme Court held that if a subordinate Tribunal refuses to carry out directions given to it by a superior Tribunal in the exercise of its appellate powers, the result will be chaos in the administration of justice. That by the impugned order, the ITO failed to carry out a legal duty imposed on him and such failure being destructive of a basic principle of justice, a writ of mandamus should issue ex debito justitiae to compel the respondent to carry out the directions given to him by the Tribunal. The following were the relevant observations of the Hon'ble Supreme Court (at page 622) :-

> **"5.** It is worthy of note here that while the Tribunal had directed the respondent to ascertain the average transport charges from the centres to the factory, the respondent referred to the cost of transportation from the farms to the factory. Clearly enough, the respondent misread the direction of the Tribunal and failed to carry it out. He proceeded on a basis which was in contravention of the direction of the Tribunal.

6. In these circumstances, the appellant-company moved the Judicial Commissioner, Bhopal, then exercising the powers of a High Court for that area, for the issue of a writ to compel the respondent to carry out the directions given by the Tribunal. The learned Judicial Commissioner found in express terms that the respondent had acted arbitrarily and in clear violation of the directions given by the Tribunal; in other words, he found that the respondent had disregarded the order of the Tribunal, failed to carry out his duty according to law and had acted illegally. Having found this, the learned Judicial Commissioner went on to examine the correctness or otherwise of the order of the Tribunal and found that the Tribunal went wrong in not treating the centres as "markets" within the meaning of r. 23 of the Income-tax Rules. He then came to the conclusion that in view of the error committed by the Tribunal, there was no manifest injustice as a result of the order of the respondent; accordingly, he dismissed the application for the issue of a writ made by the appellant-company.

7. We think that the learned Judicial Commissioner was clearly in error in holding that no manifest injustice resulted from the order of the respondent conveyed in his letter dt. 24th March, 1955. By that order the respondent virtually refused to carry out the directions which a superior Tribunal had given to him in exercise of its appellate powers in respect of an order of assessment made by him. Such refusal is in effect a denial of justice, and is further more destructive of one of the basic principles in the administration of justice based as it is in this country on a hierarchy of Courts. If a subordinate Tribunal refuses to carry out directions given to it by a superior Tribunal in the exercise of its appellate powers, the result will be chaos in the administration of justice and we have indeed found it very difficult to appreciate the process of reasoning by which the learned Judicial Commissioner while roundly condemning the respondent for refusing to carry out the directions of the superior Tribunal, yet held that no manifest injustice resulted from such refusal.

8. It must be remembered that the order of the Tribunal dt. 22nd April, 1954, was not under challenge before the Judicial Commissioner. That order had become final and binding on the parties, and the respondent could not question it in any way. As a

> matter of fact the CIT had made an application for a reference, which application was subsequently withdrawn. The Judicial Commissioner was not sitting in appeal over the Tribunal and we do not think that, in the circumstances of this case, it was open to him to say that the order of the Tribunal was wrong and, therefore, there was no injustice in disregarding that order. As we have said earlier, such a view is destructive of one of the basic principles of the administration of justice."

13. It was the submission of the ld. counsel for the assessee that two options are now open before the Tribunal. The first option, according to him, was that since the AO has not carried out the directions of the Tribunal, uphold the determination of long term capital gains as done by the assessee. The second option would be to direct the AO to carry out the directions given by the Tribunal.

14. The ld. DR submitted that in para 7.2.8 of the order of Tribunal, the Tribunal has directed the AO to take appropriate action in accordance with the provisions of the Act. According to him, the AO therefore has reappreciated the claim of assessee with regard to FMV as on 1.4.1981. The Bench pointed out that in the order of AO, he has not given this reason for not following the directions of the Tribunal, but has held that the directions of the Tribunal are not correct. The ld. DR relied on the order of AO/CIT(Appeals).

15. We have considered the rival submissions. In our view, on an overall reading of the order of the Tribunal, it is clear that the Tribunal has directed the AO to look into the FMV as on 1.4.1981 shown by the assessee. The indexed cost of acquisition as per assessee was Rs.1,55,70,000. It is also clear from the order of Tribunal that the value of Rs.2,70,975 taken as value of the property in the books of account of the assessee as on 1.4.1981 is only notional and should not be considered for the purpose of working out the FMV as on 1-4-1981 while working out the cost of acquisition of the property. In our view, the proper way to construe the directions of the Tribunal in para 7.2.8 of its order is to verify whether the indexed cost of acquisition of Rs.1,55,70,000 arrived at by the assessee is correct or not, on the presumption that the assessee was entitled to adopt the FMV as on 1.4.1981 as its cost of acquisition and ignoring the value as on 1.4.1981 as recorded in the books of account of the assessee at the time of formation of the partnership. We may also add that the order of Tribunal has become final and not challenged by the Revenue. In the given circumstances, the AO was precluded from questioning the correctness of the order of Tribunal in the order giving effect to the order of Tribunal and refusing to follow the same. We are of the view that it would be just and appropriate to set aside the order of the AO and remand the issue to the AO for consideration of the issue afresh after giving opportunity of being heard to the Assessee. We order accordingly.

16. In the result, the appeal of the assessee is allowed for statistical purposes.

17. **SP No.204/Bang/2014** : In view of the decision rendered on the main appeal, the stay petition has become infructuous and the same is dismissed as infructuous.

Pronounced in the open court on this 27th day of February, 2015.

Sd/-	Sd/-
(JASON P. BOAZ)	(N.V. VASUDEVAN)
Accountant Member	Judicial Member

Bangalore,
Dated, the 27th February, 2015.

/D S/

Copy to:

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR, ITAT, Bangalore.
6. Guard file

By order

Assistant Registrar/
Senior Private Secretary
ITAT, Bangalore.