

IN THE INCOME TAX APPELLATE TRIBUNAL  
“F” BENCH, MUMBAI

**BEFORE SHRI OM PRAKASH KANT (ACCOUNTANT MEMBER)**  
**AND**  
**SHRI PAVAN KUMAR GADALE (JUDICIAL MEMBER)**

I.T.A. No.478/Mum/2020  
(Assessment year 2016-17)

M/s Fortune R PJ Developers 1 <sup>st</sup> Floor, Rathod Bhavan Opp Jain Mandir, Tembhi Naka Thane (W) – 400 601 <b>PAN : AADFF5410E</b>	vs	ACIT, Circle-1, Thane
<b>APPELLANT</b>		<b>RESPONDENT</b>

Assessee represented by	Shri Devendra Jain
Revenue represented by	Shri S.N. Kabra, Sr.DR

Date of hearing	06-01-2022
Date of pronouncement	31-01-2022

**ORDER**

**Per O.P. Kant (AM) :**

This appeal by the assessee is directed against order dated 01/11/2019 passed by the learned Commissioner of Income tax (Appeals)-1, Thane [in short, the Ld. CIT(A)] for assessment year 2016-17 raising following ground:

*“In the facts and circumstances of the case and in law, the learned Commissioner of Income Tax (Appeals) - 1, Thane has erred in confirming the disallowance of proportionate interest expenditure of Rs. 70,00,371/- (worked out on the basis of closing stock of Project A and Project B) made by the learned Assessing Officer in respect of Project "B" holding it to be capital expenditure.”*

2. Briefly stated facts of the case are that during relevant period, the assessee was engaged in construction and development of real estate i.e. flats, shops etc. For the assessment year under consideration, the assessee filed return of income on 22/09/2016 declaring total income of ₹ 31, 54, 040/-. The return of income filed by the assessee was selected for scrutiny assessment and statutory notices under the Income-tax Act, 1961 ( in short 'the Act') were issued and complied with. The assessment under section 143(3) of the Act was completed by the Assessing Officer on 28/12/2018, wherein the interest claimed by the assessee in the profit and loss account as expenditure was disallowed to the extent of ₹ 70, 00, 370/-. On appeal, the Ld. CIT(A) upheld the disallowance made by the Assessing Officer. Aggrieved by the finding of the Ld. CIT(A), the assessee is in appeal before the Tribunal, raising the sole ground reproduced above.

3. Before us the learned counsel of the assessee filed a paper book containing pages 1 to 11.

4. We have heard rival submissions of the parties on the issue in dispute and perused the relevant material on record.

5. Briefly stated, facts relevant to issue in dispute, are that the assessee had undertaken to construct a real estate project namely " Fortune Avenue" , which consisted of project 'A' and project 'B', located at Thane ( Maharashtra). During assessment proceeding, it was observed that as per the certificates issued by the Architect and Consultant, the building No. one (project 'A') was completed on 17/12/2016 and the assessee had offered certain amount of the sales on said project on the basis of booking and payment received. However, in respect of building No. two (project 'B') the assessee neither furnished certificate of

percentage of construction completed nor any sales were offered as income (revenue) in the profit and loss account. But on the other hand , the Assessing Officer observed, interest expenses debited in the profit and loss account for the year under consideration amounting to ₹ 1, 50, 56, 800/-which consisted of interest on capital of ₹ 85, 58, 950/-and interest paid on loans of ₹ 64, 91, 850/-. The Assessing Officer found that substantial amount of newly acquired unsecured loans and capital was used for the purchase of plot of land for project 'B', however no income or revenue from said project has been credited, and therefore, he was of the view that interest on borrowings by way of capital and unsecured loans was required to be allocated project –wise. The Id. Assessing Officer held that interest part on borrowing as well as partners capital attributable to project 'B' i.e. unfinished project , cannot be allowed as an expense in respect of the profits derived from project 'A' and same should be allowed to be capitalized to the work in progress (WIP) of project 'B'. The Assessing Officer, accordingly worked out the proportionate interest of ₹ 70, 00, 370/-in respect of project 'B' and added the same to the income of the assessee. For ready reference, the disallowance computed by the Assessing Officer is extracted as under:

S.No.	Particulars	Project A	Project B
1	Sales	Rs.3,20,73,825/-	Nil
2	Closing Stock (WIP)	Rs.9,17,53,736/-	Rs.7,97,41,831/-
3	Interest on capital (Partner)	Rs.85,58,950/-	
4	Interest paid (Others)	Rs.64,91,850/-	
5	Ratio of Closing Stock of Project A : Project B	1.15 : 1	
6	Interest on Capital Project A : Project B (on the basis of closing	Rs.45,78,044/-.	Rs.39,80,906/-

	stock)		
7	Interest Paid (Others) Project A: Project B (on the basis of Closing Stock)	Rs.34,72,385/-	Rs.30,19,465/-
8	<b>TOTAL</b>	Rs.80,50,429/-	Rs.70,00,371/-

6. Before the Ld. CIT(A), the assessee did not explain whether it was following project completion method or percentage completion method for offering profit from the said projects for the purpose of the Income-tax. The Ld. CIT(A) after analysing the facts and submissions including the decisions relied upon by the assessee, upheld the disallowance, observing as under:

5. I have carefully considered the facts of the case, findings of the AO in the assessment order, submissions of the appellant and material placed on record. From the facts of the case it is noticed that the appellant undertook to construct a project 'Fortune Avenue' on plot bearing survey No. 120, H. No. 15 at village Kolshet, Thane. The said project consists of Project 'A' and Project 'B'. It was certified, by the Architects and Consultants that Building No. 1 (project A) was completed on 17.12.2016 and the appellant had offered certain amount of Sales on the Project A on the basis of payments received and the bookings. However, in respect of Building No. 2 (project B) neither the certificate of percentage of construction work was submitted nor any Sales/Profit were declared. In respect of project 'B' the appellant had furnished two registered agreements, dated 21.05.2015 for Rs. 5,15,00,000/- and Rs. 1,50,00,000/-. These two registered properties are situated at Survey No 120, Hissa No. 14, Kolshet, Thane and payments were made from January 2015 to March 2015. The appellant had shown WIP (Closing Stock) of Rs. 6,90,86,200/- for AY 2015-16 and Rs. 7,97,41,831/- for AY 2016-17 in respect of Project B, out of which major expense was related to purchase of land of Rs. 7,04,02,880/- (Rs. 6,65,00,000/-, which was paid during the period of January 2015 to March 2015 + Stamp duty of Rs. 38,40,000/- & Registration charges of Rs. 62,880/-). It was noted that the appellant had shown sales of Rs. 3,25,22,825/- (Project A) and Closing Rs. 16,11,32,597/- (Project A & B) as on 31.03,2016 for AY 2016-17. Similarly for AY 2015-16 (he appellant had shown sales of Rs, 33,63,000/- and Closing S of Rs. 13,08,35,565/- as on 31.03.2015. However the appellant had had debited interest expenses for AY 2015-16 and 2016-17 as under:

S.No.	Particular	Amount in (Rs.)
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1	Interest on Capital	63,78,115/-	85,58,950/-
2	Interest Paid	6,48,920/-	64,91,850/-
<b>TOTAL</b>		<b>70,27,035/-</b>	<b>1,50,56,800/-</b>

5.1 The appellant had submitted the project wise bifurcation of the Valuation of the Closing Stock and details of Capital and Unsecured loans in respect of Project A and Project B as under :

**Details of Capital and Unsecured Loans:-**

S.No.	AY	Unsecured Loans (B/S)	Capital as per Balance Sheet	Unsecured Loans (newly introduced)	Capital (Newly introduced)	Investments in Plots	
						Project 'A'	Project 'B'
1	14-15	0	3,02,83,500	0	3,02,83,500	2,80,00,000	NIL
2	15-16	4,97,04,306	6,26,34,695	4,97,04,306	3,23,51,195	5,01,63,000	6,65,00,000
3	16-17	7,05,30,958	8,22,71,230	2,08,26,652	1,96,36,535	5,01,63,000	7,04,02,800

**Valuation of Closing Stock:-**

S.No.	Particular	Amount in (Rs.)	
1	Opening Balance	6,217,49,365/-	6,90,86,200/-
2	Cost / Expenses	3,00,04,371/-	1,06,55,631/-
3	Total Stock	9,17,53,736/-	7,97,41,831/-
4	Sales	3,20,73,825/-	NIL

From the above charts it is seen that out of total stock of Rs. 7,97,41,831/- in respect of Project 'B', Rs. 7,04,02,800/- pertains to investment in plots. This fact clearly establishes that majority of newly established unsecured loans and Capital was used for the purchase of the plot for Project 'B' and interest expenses were claimed against the same, thereby decreasing the Net Profit. It is pertinent to mention here that till AY 2016-17 no major work had been done in respect of Project 'B', hence the interest incurred on the unsecured loans and partner's capital for the purchase of land in respect of Project 'B' cannot be allowed as revenue expenses for AY 2016-17 and the same will be allowed to be capitalized in the WIP. The AO, therefore, disallowed the interest expenses claimed in respect of Project 'B' by calculating the same on proportionate basis as under:-

S.No.	Particulars	Project A	Project B
1	Sales	Rs.3,20,73,825/-	Nil
2	Closing Stock (WIP)	Rs.9,17,53,736/-	Rs.7,97,41,831/-

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4	Interest paid (Others)	Rs.64,91,850/-	
5	Ratio of Closing Stock of Project A : Project B	1.15 : 1	
6	Interest on Capital Project A : Project B (on the basis of closing stock)	Rs.45,78,044/-.	Rs.39,80,906/-
7	Interest Paid (Others) Project A: Project B (on the basis of Closing Stock)	Rs.34,72,385/-	Rs.30,19,465/-
8	<b>TOTAL</b>	Rs.80,50,429/-	Rs.70,00,371/-

The AO. accordingly disallowed interest expenses of Rs. 70,00,371/-, claimed in respect of Project 'B' and added the same to the income of the appellant.

5.2 During the course of appellate proceedings the AR stated that the AO accepted the fact that the expenses by way of interest which are debited to the P&L A/c are "for the purpose of business" and does not restrict its application to "for the purpose of earning income." Provisions of section 36(1)(iii) are distinctly clear, it covers wider aspect "for the purpose of business" and does not restrict its application to "for the purpose of earning income." It is further stated that the AO formed his opinions considering that no business activity is carried on subsequent land purchase which contradicts with his findings that appellant had incurred of Rs, 93,38,951/- (Rs. 7,97,41,331/- less Rs. 7,04,02,800/- after land).

5.3 It is reiterated that Project 'A' commenced during AY 2014-15 and the profit for the first time was declared in AY 2016-17. Where as in respect of Project 'B' only land has been purchased and no profit has been declared there from. A building project takes a substantial period of time to get ready for is intended use or sales, therefore, would come under the definition of 'a qualifying asset'<sup>1</sup>. Hence, in the present case in respect of acquisition of land in respect of the Project 'B' should be capitalised.

5.4 During the course of appellate proceedings the AR, vide order sheet noting dated 25.07.2019 was specifically asked to give the method of accounting followed by the appellant. In compliance the AR, vide its submission dated 21.08.2019, stated that:

*"Method of Accounting adopted by the Appellant date of commencement and •^ completion of both projects.*

*The commencement of business is in the financial year 2013-14. For first time in F. Y 2014-15 the appellant shown sales revenue of Rs 33,63,000/-. Further in F. Y 15-16 revenue recorded is Rs 3,25,22,825/-*

*In December 2016 project of first land purchased has been completed. All sales revenue is related to construction of this project.*

*Meanwhile in the financial year 2014-15 the appellant purchased land for second phase of its construction business which is adjacent to earlier building under construction. It is to note that in the financial year 2015-16, the appellant has incurred expenditure on this second phase of about Rs One crore on construction activity.*

*Now the construction of second phase is going on. It is a 20 storey project.*

*Cognizance of above all fact i.e. Revenue recorded on commencement, completion and profit declared is being considered by the Assessing officer. I may request and invite your attention to Para 10 and 11 of the Assessment order."*

*From the above submission it is evident that the AR has abstained from clearly submitting whether the appellant is following the Project Completion method or Percentage Completion method. Hence I am constrained to analyse the material placed on record. It is seen that the appellant had purchased the land pertaining to Project 'A' during the AY 2014-15 and started the construction in AY 2014-15. However, the profit in respect of Project 'A' for the first time was declared in AY 2016-17 and no profit was declared during AY 2014-15 & 2015-16. From the above facts inference can be drawn that the appellant is declaring profits once the flats are constructed. The AR has placed his reliance on the ratio of decision in the case of M/s Lokhandwala Construction Industries Ltd. (Bombay High Court). However the facts of this case cannot be applied to that of the appellant as in the case of M/s Lokhandwala Construction Industries Ltd. the Hon'ble Bombay High Court was concerned with the question as to whether the interest expenditure is a capital expenditure or revenue expenditure. In similar set of circumstance the Hon'ble ITAT, Mumbai in the case of Wall Street Construction Ltd vs Jt. Commissioner of Income Tax, vide order dated 22.09.2005 has held that: - "where an assessee is following project-completion method of accounting, the interest identifiable with that project should be allowed only in the year when the project is completed and the income from that project is offered for taxation."*

*5.5 In view of above facts and following the decision of Hon'ble ITAT (supra) it is held that the interest expenses of Capital and Unsecured loans, pertaining to Project 'B', cannot be allowed as an expense in respect of the profits derived from Project 'A' and the same will be allowed as a Capital expenditure and allowed to be capitalized to the Work in Progress (Closing Stock) of Project B. Therefore, the addition of Rs. 70,00,371/- made by the AO is hereby sustained and this ground of appeal is dismissed."*

7. Thus, the issue in dispute before us, is whether the interest expenditure pertaining to project 'B' is allowable to the assessee in the year under consideration or not. According to the lower authorities, the interest corresponding to project 'B' cannot be allowed in the year under consideration

and it should be allowed in the year in which assessee will declare profit from said project according to the method of accounting employed by the assessee for declaring profit for the purpose of Income-tax. Whereas, according to the assessee, it is carrying on business operation and therefore in terms of section 36(1)(iii) of the Act, interest should be allowed on borrowings taken for the purpose of the business. The learned counsel of the assessee has relied on the decision of the Hon'ble Bombay High Court in the case of **Lokhandwala Construction Industries Ltd 260 ITR 579**, which was also relied before the Ld. CIT(A). The Hon'ble High Court in the said case summed up their decision as under:

*“31. For the reasons discussed above, we hold that where an assessee is following project-completion method of accounting, the interest identifiable with that project should be allowed only in the year when the project is completed and the income from that project is offered for taxation.”*

8. Thus according to the Hon'ble High Court , where the assessee is following project completion method for crediting income, then the interest expenditure pertaining to a particular project is eligible for deduction only in the year in which the project is completed and income from the project is offered for taxation.

9. In the instant case before us, the assessee has not clarified before the lower authorities that whether it was following project completion method or percentage completion method for crediting income to profit and loss account. Before us, the assessee has filed a copy of submission dated 23/12/2019 before the Assessing Officer in respect of assessment year 2017-18 i.e. subsequent assessment year. In the said submission, the authorised representative of the assessee has clearly mentioned that the assessee is following percentage

completion method. It is also mentioned that in the earlier year also the revenue was recognized following the percentage completion method. The learned authorised representative has also mentioned that interest expense was not claimed in computation of taxable income for A.Y.2017-18 . The relevant part of said submission is reproduced as under:

*Ref.: M/s Fortune RPJ Developers. AY 2017*

*In the matter of assessment before you, it is respectfully submitted in response to your questionnaire as under:*

**Method of accounting employed:** *It is Percentage Completion basis.*

*Sir, it can be noticed from earlier years of Profit & Loss A/cs, that year wise revenue has been recognized in the books. In fact O.C. for the project is received on 07.12.2016. However as and when worked progressed coupled with reasonable volume of earning expected out of effective sale agreements entered viz-a-viz WIP, the revenue has been recognized.*

*After this year in which O.C. has been obtained, in subsequent years no construction cost has been debited. Although part of Administrative expenses and provisions for completion and external work (Legal requirement as per RERA law) could have been provided for completion compliance as per Project Summary separately mentioned in my letter of even date and annexed as 'A' . The Assessee could not correctly measure quantum of expense required then. However, at this stage, prudently the Assessee has worked on such qualification and prepared revised computation of Income for your kind consideration.*

*Further, it is clarified that in respect of on going project i.e. Project B; after purchase of land, settlement with claimants till March 2019, excavation work is carried because there was hard rock underlying (which was not anticipated). There is neither any booking nor any agreement to sale being entered into for and in respect of project to come. It can be noted that interest expense is not claimed in computation of taxable income."*

10. We find that under percentage completion of method the revenue from booking or sales is credited to the profit and loss account in proportion to the expenditure incurred on the project as compared to the total cost of the project. In the assessment year under consideration, the assessee has not credited any amount of revenue on the ground that no substantial construction work was executed in the year under consideration. In such circumstances, even under the percentage completion method also the interest expenditure which is specifically related to project 'B' cannot be allowed and it shall be eligible for deduction in

percentage terms of cost of construction debited following the percentage completion method. The decisions of Hon'ble Supreme Court in the case of **Taparia Tools Ltd (2015) 55 taxmann.com 361 (SC)** relied upon by the assessee, is also not applicable in the facts of the case being the facts of the said case different from the instant case . In the said case there were two options as regards payment of interest to the subscribers/debentures holders. They could either receive interest periodically over a period of five years, or else, the debenture holders could offer for one time upfront payment of ₹ 55 per debenture. In the second alternative, ₹ 55 per debenture was to be immediately paid as upfront on account of interest. The assessee was following mercantile system of accounting and this amount became payable to the debenture holder in accordance with terms and condition of nonconvertible debentures issue floated by the assessee, on the exercise of the option by the aforesaid debenture holder, which occurred in the respective assessment year in which deduction of the said expenditure was claimed. The Hon'ble Supreme Court rejecting the 'matching concept' applied by the Hon'ble High Court, allowed the interest in the year of the claim observing as under:

*"15. Mr. Dastur next contended that on the contrary in this case if the assessee had adopted the said amortization, the Department would have told the assessee that it was not entitled to deduction in the second year as no liability accrued in the second year and as no payment was made in the second year.*

*16. Mr. Dastur next contended that under the contract, option was given to the Lenders but, the Department has denied the option which amounted to re-writing of contract, which was not permissible to the Assessing Officer. In this case, he relied upon the judgment in the case of CIT v. Sri Bibhuti Bhusan Dun [1963] 48 ITR 233 (Cal.). Mr. Dastur contended that deduction under the Income-tax Act does not depend on the status of the assessee nor does it depend on the profit/loss of the assessee. He, therefore, submitted that the judgment of the Supreme Court in MIIC Ltd. 's case (supra) did not apply. Mr. Dastur, therefore, contended that the judgment of the Tribunal was wrong and in the circumstances, liable to be set aside."*

11. We find that in the instant case interest which was specifically related to project B and neither expenditure on said project was claimed nor any revenue from said project was offered in the profit and loss account. The interest corresponding to the project 'A' has already been allowed by the Assessing Officer and only part pertaining to project B has been disallowed. This interest expenditure disallowed was not related to borrowing for maintaining business infrastructure but it was related to specific real estate project. As no significant risks and rewards of ownership of the project 'B' were transferred by the assessee to prospective buyer, no revenue from said buyer was recognized following principle of percentage completion method. Thus, no liability in respect of interest expenses pertaining to project 'B' was accrued, hence it is not allowable in the year under consideration.

12. In view of the above, we do not find any infirmity in the order of the Ld. CIT(A) on the issue disputed and accordingly uphold the same. The sole ground raised by the assessee is dismissed.

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

Order pronounced on 31/01/2022.

Sd/-

Sd/-

<b>(PAVAN KUMAR GADALE)</b>	<b>(OM PRAKASH KANT)</b>
<b>JUDICIAL MEMBER</b>	<b>ACCOUNTANT MEMBER</b>

Mumbai, Dt : 31/01/2022

Pavanan

Copy to :

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

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By Order

Asstt. Registrar, ITAT, Mumbai