

**IN THE INCOME TAX APPELLATE TRIBUNAL  
MUMBAI BENCH "A", MUMBAI**

**BEFORE SHRI S. RIFAUH RAHMAN, HON'BLE ACCOUNTANT MEMBER AND  
SHRI SANDEEP SINGH KARHAIL, HON'BLE JUDICIAL MEMBER**

**ITA NO.707/MUM/2022 (A.Y: 2017-18)**

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| Siddharth Developers<br>205 Commerce House<br>140 N.M. Road, Fort<br>Mumbai - 400023<br><br><b>PAN: ABFFS4068J</b> | v. | ACIT – Central Circle – 5(3)<br>Room No. 1906, 19 <sup>th</sup> Floor<br>Air India Building<br>Nariman Point, Mumbai – 400 021 |
| <b>(Appellant)</b>   |    | <b>(Respondent)</b>  |

|                                  |          |                           |
|----------------------------------|----------|---------------------------|
| <b>Assessee Represented by</b>   | <b>:</b> | <b>Shri Nishit Gandhi</b> |
| <b>Department Represented by</b> | <b>:</b> | <b>Shri Salil Mishra</b>  |
|                                  |          |                           |
| <b>Date of Hearing</b>           | <b>:</b> | <b>06.10.2022</b>         |
| <b>Date of Pronouncement</b>     | <b>:</b> | <b>03.01.2023</b>         |

**ORDER**

**PER S. RIFAUH RAHMAN (AM)**

1. This appeal is filed by the assessee against order of the Learned Commissioner of Income Tax (Appeals)-53 [hereinafter in short "Ld.CIT(A)"] dated 22.02.2022 for the A.Y.2017-18.

2. Brief facts of the case are, assessee filed return of income on 31.10.2017, declaring Total Loss of ₹.13,63,38,473/-. The case was selected for scrutiny and notice u/s. 143(2) and 142(1) of Income-tax Act,

1961 (in short "Act") were issued and served on the assessee. In response AR of the assessee attended and submitted the information as called for.

**3.** Assessee firm is a builder and is engaged in the business of real estate and allied activities and derived income from house property. Assessing Officer noticed from the submission that during the year under consideration sales have been booked in the 'Chhotani Chawl Project. The cost for the project has been debited to the Work-in-Progress from A.Y.2011-12 onwards: The opening value of the property at Chhotani Chawl was ₹.93.65 crores. During the year the addition to the value of the property was of about ₹.10.34 crores mainly on account of interest payments which is to the extent of ₹.5.13 crores. Sales recorded during the year was of ₹.44.32 Crores whereas cost of ₹.76.87 Crores had been booked against the same. This resulted in loss of ₹.32.55 crores. It is also seen that some of the sales were also made at less than the stamp duty value of the property.

**4.** Assessing Officer issued notice u/s. 142(1) of the Act and assessee was asked to explain as to why the sales have been booked at such a loss. Assessee vide letter dated 12.12.2019 submitted that the sales were

booked at loss because of the sluggish market conditions. Assessee also furnished the details of the cost that were debited to the project over the years and further stated that the same have been examined in the assessment proceedings of the earlier years and hence are allowable in A.Y. 2016-17 when the corresponding sales have been made.

**5.** Assessing Officer further observed from the submission that even if finance and tenant compensation cost were removed, the cost of construction was Rs. 18,000/sqft which was much more than the average rates observed in the residential real estate of ₹.3500/sqft or even ₹.5000/sqft. seen in luxury residential flats. Vide notice dated 17.12.2019 assessee was asked to provide the details including the architect certificates, FSI calculation, details of the advances received and also to explain as to how the cost of construction/sqft. is so high

**6.** In response, vide letter dated 20.12.2019 assessee submitted that construction cost includes not only the saleable area but also the rehab area. Assessee submitted that though the saleable area is only 25,587 Sqft but the construction area is much more than that at 1.24,753 Sqft. Assessee also made the contention that construction area pertaining to rehab portion was 69.815 Sqft and the total proposed built up area is

76.739.35 Sqft. Assessing Officer observed that assessee has claimed that after reducing the interest cost and considering the whole construction area instead of only built-up area the construction cost comes to only ₹.5,660/-. Assessing Officer observed following problems in the computation made by the assessee: -

*a) Only built up area needs to be considered and not the whole construction area.*

*b) It has been assumed that both the rehab and the saleable area are similarly constructed at the same costs.*

**7.** After considering all the submission, Assessing Officer observed that following points emerge: -

*a) Total area sold till the end of F.Y. 2016-17 was 18,913 sqft at a value of about Rs 44.32 crore which translates to average selling price of Rs. 23,400/sqft. This sale value is much less than the cost incurred by the assessee.*

*b) Though the assessee claims that the market conditions were sluggish and hence sales were made at such a loss when the claim is checked against data obtained from various real estate sites which provide data for the movement in prices of real estate the same was not found to be correct. As against the average rate of sales of Rs. 23,400/sqft of the assessee it is noticed that the market rates were in the vicinity of Rs 34000/sqft for the Lower Parel area as can be seen from the following screenshot.*

.....

*Also it is seen from the submissions made that sales agreement have been booked at different rates ranging from Rs 32,000/sqft to even Rs. 19,000/sqft. Such levels of variation are possible only if books of account don't record the correct state of affairs."*

8. In view of the above observations, Assessing Officer is of the opinion that with this background it becomes clear that the loss claimed to have been booked by the assessee are not correct. As far as the sales considerations are concerned assessee added an amount of ₹.8,93,57,550/- u/s 43CA. However even if the stamp duty value is taken as the sales consideration still there is a loss of more than ₹.23 crores against sale of units from Chhotani Chawl. Considering the real estate is sellers market, no prudent businessman would incur such losses. There was no pressing requirement for booking sales at such a heavy loss. Interest costs of the assessee were on an average only ₹.5 crores per year, so even assuming the sales were booked to reduce interest liability still booking a loss of ₹.33 crores only to avoid comparatively much smaller interest cost is not tenable. Accordingly, show cause notice was issued to the notice and after considering submissions Assessing Officer noticed as under: -

*"In the submission it has been stated that the construction area is of 1,24,753 Sq. Ft The same has been used to arrive at a cost of Rs. 8,336/sqft. After reduction of finance cost, the figure works out to Rs. 5,660/sqft.*

*In the above calculation there are however two problems, to arrive at cost of construction per sq. Ft.: total constructed area is taken into account whereas largely only built up area needs to taken into account. When built up area of 7131.91 Sqmt. is taken into account then cost works out to Rs. 9200/-*

*Further, to say that in both the rehab building and saleable building similar cost was incurred is also Incorrect. It is only logical to assume that the rehab building would not have cost of construction of more than Rs. 3500/sqft. In that case considering that the saleable area is only 44% of the total sale and rehabilitation combined, the cost of construction for the saleable area works out to Rs. 16.4701 (9200-3500\*0.56)/0.44]*

*Even if out of Rs. 16,470; approximately Rs. 5000/sqft is taken for the cost of construction in non-built-up area, tenant compensation and other sundry costs, then also there is a huge overstatement of the cost of construction over and above the average rates of construction observed in the real estate industry ie. Rs. 5000/sqft. The excess expenditure even after such huge offsets and estimations on conservative basis. is of the tune of Rs. 16,55,47,243/- [25586.90"( 16470-5000-5000)]*

*Taking into account the above computation, I am not satisfied with the correctness and completeness of the cost of construction arrived at in books of account maintained. hence please explain as to why the books of account maintained by the assessee company be not rejected as the costs of the project have been greatly inflated by booking non- genuine expenses.*

*Accordingly, as per working above, please explain as to why the excess expenditure booked of Rs 16,55,47,243/- as estimated above be not disallowed."*

**9.** In response assessee vide letter dated 24/12/2019 made the following submissions, for the sake of clarity it is reproduced below: -

*"i. While estimating the cost of production, you have taken into account only the constructed area, which is part of the FSI. There are large portions of the constructed area which is around 40% of the constructed area, like staircase, lift area etc. that are not included in the FSI. Cost is involved in the construction of those area also. In this regard you are requested to refer to our submission dated 20.12.2019. As per this submission the total constructed area of the two buildings is 1,24,753 Sqft. Out of this 76,739.35 Sqft is the FSI portion and the balance 48,014 sqft. pertains to Nich, Dry Balcony, Flower Bed, Staircase, Lift, Lift Lobby and Passage. This 48,014 sqft. pertains to both Rehab building and as well as sale building. Out of this 29,341.1 sqft. (Total constructed saleable are 54,928 sqft. less total saleable carpet area 25,586 sqft.) pertains to sale building. To that extent there is difference is layout comfort offered in the sale*

*building. But we do not agree with your general statement, that projects have a huge difference between construction costs of Rehab Building and Sale building.*

*ii. The work-in-progress in the year ending 31.03.2016 is Rs. 93.65 Crore. The WIP as on 31.03.2017 is Rs. 103.99 crores. Therefore, the increase in WIP during the year is of Rs. 10.34 Crore. This includes interest of Rs. 5.14 crores. Therefore, the actual construction cost incurred is only Rs. 5.20 crores during the FY 2016-17. There were scrutiny assessments in A. Yr's 2013-14, 2014-15, 2015-16 and the return of A.Y 2016-17 was accepted u/s 143(1). Copies of assessment orders are enclosed herewith. While framing the assessment order of AY. 2017-18, the AO cannot disturb the accepted WIP of earlier years. The scope assessment is restricted to verify the expenditure claimed in the Profit and Loss of the current year which is Rs. 5.14 crore interest cost and construction expense of Rs. 5.20 crores*

*iii. A total income of Rs. 2.93 crores has already been offered to tax upto A.Y. 2014- 15. This income was computed on estimated profit, spread over A. Ys. 2012-13 to 2014-15. Copy of the balance sheet as on 31.03.2016 and its relevant schedule is enclosed herewith wherein profit estimated for earlier years is shown in schedule 'L' for your ready reference*

*iv. In view of the above the assessee firm firmly believes that there is no overstatement of expenditure and the book results of the firm needs to be accepted."*

**10.** After considering the submissions of the assessee, Assessing Officer rejected the submissions with the following grounds: -

*"i. The consideration that there are costs to even developing non-FSI area has already been taken into account. Against the construction cost of Rs. 16.470/sqft.. a set-off of Rs. 5000 has been provided to for expenditure on this account which is more than sufficient to such incidences of expenditure.*

*ii. In the submission it has been stated that a large portion of non-FSI construction has gone to the sale building. The submission states that 29,341.1 sqft of area pertains to saleable are of merely 25,586.90 sqft. This implies that there is more non-FSI construction area for every unit of saleable carpet area. If such were the project parameters, then the fact that sales have been made at even less than the Stamp Duty value is very untenable.*

*iii. The contention that WIP of earlier years cannot be disturbed if the returns for all those years have been scrutinised and the closing stock have been accepted for those years is also not acceptable. The cost that were debited in those years are being claimed in the F.Y. 2016-17 based on matching principle which effects the profit. Further when the books of account of the assessee are themselves being rejected there is little merit in the argument that cost of earlier years should be allowed."*

**11.** Assessing Officer observed that it is evident, the assessee took large portion of sale proceeds in cash which remained unaccounted and has also booked bogus expenditure. So the books of assessee are not reliable and it does not give true, correct and complete picture of business affairs. The guiding principles regarding maintenance of proper and acceptable books of accounts are envisaged by section 145 of the Act. Section 145 of the Act, casts triple onus on the assessee to maintain books of account in such manner as to meet the following the three criteria:

- i) Satisfaction about the correctness of the accounts.*
- ii) Satisfaction about the completeness of the accounts.*
- (iii) Regularity in following the method of accounting provided in sub-section (1) of section 145 or accounting standards as notified under sub-section (2) of section 145.*

**12.** Thus, Section 145 of the Act puts triple onus on the assessee to provide for and maintain the correctness, completeness and regularity of the method of accounting strictly to the satisfaction of the Assessing Officer; in order to meet the rigours of the section 145. The failure to meet even one of the requirements of section 145 of the Act, 1961 renders

the books maintained by the assessee liable to rejection on account of incorrectness or incompleteness or irregularity. Accordingly, the books of assessee is rejected as per Section 145 of the Act. In this regard, he relied on the following case laws:

- (i). *CIT v. MC Millan & Co. [1958] 33 ITR 182*
- (ii). *Kachwala Gems V. JCit [2007] 288 irt 10 (SC)*
- (iii). *Seth Nathuram Munalal v. CIT [1954] 25 otr 216 (NAG.)*

**13.** With the above observations, and relying on various case law Assessing Officer made addition of ₹.16,55,47,243/-.

**14.** Aggrieved assessee, preferred an appeal before the Ld.CIT(A) and filed detailed submissions before the Ld.CIT(A). After considering the submissions Ld.CIT(A) sustained the addition made by the Assessing Officer.

**15.** Aggrieved assessee is in appeal before us raising following grounds in its appeal: -

*"ON NATURAL JUSTICE:*

1. *In the facts and circumstances of the case and in law, the order passed by the Learned Commissioner of Income Tax (Appeals) 53-Mumbai ["the CIT (A)" for short] u/s 250 of the Income Tax Act, 1961 ["the Act" for short] is bad in law and deserves to be quashed since the same is passed in violation of principles of natural justice*

*based on extraneous and irrelevant considerations while ignoring the relevant and material considerations more specifically, the submissions, details and evidences furnished by the Assessee.*

**ON MERITS:**

2. *In the facts and circumstances of the case and in law the Ld. CIT(A) erred in confirming the action of the Learned Assessing Officer ["the AO" for short] in rejecting the books of accounts of the Assessee invoking section 145(3) of the Act.*

2.1. *While doing so, the Ld. CIT(A) failed to appreciate that the necessary conditions for invocation of section 145(3) were not fulfilled in the present case.*

3. *In the facts and circumstances of the case and in law, the Ld. CIT(A) erred in confirming the action of the AO in adjusting the Work in Progress (WIP) of the Chhotani Chawl Project of the Appellant by disallowing an amount of Rs. 16,55,47,243/- from the opening WIP of the project and thereby disallowing the loss in the current year of Rs. 13,63,38,473/- and assessing the total income at Rs. 2,92,08,770/-.*

3.1 *While doing so, the Ld. CIT(A) failed to appreciate that:*

*(a) The adjustments so made are not within the purview of section 145(3) of the Act as the AO is not empowered to re-work the costs already forming part of the opening WIP:*

*(b) The Opening WIP has been accepted in the scrutiny assessment for earlier years and the same cannot be disturbed in a subsequent year.*

*(c) The Ld. AO has reworked the WIP on mere assumptions, presumptions,*

*surmises and conjectures which is impermissible under the provisions of the Act;*

*(d) The Books of accounts of the Appellant are audited under the Act and the same were accepted in earlier years by the Department when the cost was actually incurred and hence the same cannot be brushed aside in the impugned assessment year as is done in the present case;*

*(e) There is absolutely no basis to apply an assumed average rate of cost of construction when the entire details of the actual cost of construction were furnished before the Ld. AO as well as the CIT(A); and;*

*(f) In any case, the reworking of the WIP is not in accordance with the extant law and therefore deserves to be reversed.*

4. *In the facts and circumstances of the case and in law, the action of the Ld. AO as affirmed by the Ld. CIT(A) deserves to be reversed and it is prayed accordingly.*

5. *Each of the above grounds are without prejudice to one another and the Appellant craves leave to add, amend, alter, delete or modify all or any of the above grounds of appeal."*

**16.** At the time of hearing, Ld. AR of the assessee submitted and filed his written submissions, for the sake of clarity it is reproduced below: -

*"The Appellant is engaged in the business of Real Estate Builders and developers since the past many years. In Assessment Year (AY) 2011-12 the Appellant had started construction and development of a project called Chhotani Chawl Project The total area for construction on the said project was 124753 square feet (sq.ft.) [Ref Architect's Certificate at pgs. 191 & 192 of PB approved plan at pg. 193 of PB) As such the total area to be constructed by the Assessee was 1,24,753 sq ft. A further break-up of the said total area segregated into FSI and Non-FSI area and further segregated into Sale Area Building and Rehabilitation / Tenant Area Building is annexed herewith [Ref Area bifurcation chart attached as Exhibit A hereto] On the said project, the Assessee [the Appellant herein] incurred costs for buying the land and existing structure, construction cost, compensation to tenants, interest expenses, BMC expenses, administrative costs and various other costs over the years. A detailed breakup of the year wise costs is already furnished before the Assessing Officer. The same is also being furnished before this Hon'ble Tribunal [Ref: Letter dated 12.12.2019 at pgs.164, 166 & 167 reproduced at pgs.247 to 248C of PBJ The total cost incurred on the project till 31.03.2017 is Rs. 1,03,99,88,964/- [Approx. Rs.103.99 Crores]. As such for a total constructed area of 1,24,753 sq.ft the total cost incurred by the Assessee is Rs 103.99 Cr which works out to an average of Rs 8336 per sq ft In fact the project ran into losses due to delay in the project by 4 years which led to increased cost of interests, costs of transit accommodation/rent for alternate accommodation to tenants, increased litigation expenses, increased administrative expenses. So if these expenses (which had to be incurred because of the delay in project) are excluded the total cost per square feet works out to Rs. 5,183 psf even if the per square feet rate is taken of only Floor Space Index (FSI) area. However, while framing the assessment, the Ld. Assessing Officer (Ed. AO) has*

*made certain assumptions and based on that held that it is only the built up area (and not the total constructed area) that needs to be considered for calculating cost of construction and as a result arrived at some ridiculous figure of construction cost per sq.ft. [Ref. Para 3.4 at pg. 2, para 3.5, 3.6 at pg.4, paras 3.8 and 3.9 at pg. 6 of the 40 In the understanding of the Ld. AO no cost is required to be incurred in respect of the area other than the Built up Area of 7131.91 sq. metres (mtrs) [76,739.65 sq ft despite the fact that the total constructed area 1,24,753 sq ft. i.e. 11590 sq mtrs. In the opinion of the Ld AO an area of more than 40% of the total constructed area did not need any cost [Ref pg. 2 of 401 Further the Appellant is also unable to understand as to how the cost of construction for saleable area has been arrived at by the Ld. AO in respect of the saleable area (solely based on assumption) that the total cost of saleable area works out to 16470 per sq. ft. In the humble submission of the Assessee the whole basis of arriving at the calculation is totally wrong and contrary to the facts on record in as much as the total cost incurred by the Assessee is in respect of the entire project and not just the saleable area or the built up area. The cost is incurred on the total constructed area of 1,24,753 sq ft. However, the Ld. AO has firstly assumed that whole construction area is not to be considered for calculating cost [Ref. para 3,4, pg.2 of 40] Secondly he has assumed that the rehabilitation/tenant building and sale building have different costs of construction. Thirdly, he has assumed that the saleable area is 44% whereas the total saleable area is 25586 sq.ft. which is 2377 sq. meters out of a total built up area of 7131.91 sq.mtrs. and out of the total constructed area of 11,590 sq.mtrs. [1,24,753 sq.ft.] which comes to around 33%. However, the AO has gone on his assumptions and estimated a total cost of 16470 per sq.ft. in respect of saleable area as per his calculation which is about 44%. The Assessee is unable to understand the calculation made by the Ld. AO and as such unable to comment on the same. However, the correct figures in respect of the project in the form of a Chart are annexed hereto and marked as Exhibits A to A2. In this background, the Appellant submits its propositions as follows:*

### **PROPOSITIONS**

1. *At the outset, the Appellant humbly submits that based on the very same yardstick adopted by the Ld. AO the total cost of construction incurred by the assessee is Rs.8336 per sq ft. [Ref page 190 of PB & Ex. A] whereas that as per the AO the same is to be taken at Rs. 10,000 per sq.ft. As such there is no question of incurring any excess cost of construction as alleged by the Ld. AO. In that view of the matter the entire addition made by the Ld. AO deserves to be deleted on this preliminary ground itself.*

2. Further, admittedly the project ran into losses due to delay in execution and completion of the same by 4 years. The details of the excess cost incurred due to the same is also explained to the Ld. AO and which remains undisputed [Ref.pg. 192D attached to letter dated 20.12.2019 pg. 189 of PB). Now, the actual total cost incurred on the project is Rs. 1,03,99,88,964/-. A detailed break up of cost is given at pg. 247 of PB and is further elaborated at pages 248 to 248C of PB stating year wise cost incurred. If from this total cost, the cost overruns due to interest, compensation for transit and alternate accommodation, excess payment to BMC for revalidation, compensation against cancellation, etc. are excluded, the average total cost would reduce substantially. In this regard refer Exhibit A1 annexed herewith. Based on that it is quite evident that the total cost incurred by the Appellant is in fact lesser than the cost estimated by the Ld. AO and it is only due to the extra-ordinary circumstance of the project getting delayed by 4 years that excess cost had to be incurred by the Appellant.

3. The Appellant further submits that the entire addition made by the Ld. AO springs out of presumption, assumptions and surmises. This is evident on a bare perusal of the assessment order where the AO has simply taken some random figures based on assumptions and thereafter concluded that the Appellant's cost of construction is overstated [Ref: para 3.4, 3.5, 3.6 and 3.8 of AO]. On a bare perusal of the said paragraphs it is quite evident that the disallowance is sought to be made merely on the basis of assumptions and nothing more which is impermissible [Ref: Dheeraj Lal Girdhari Lal v/s CIT - (1954) 26 ITR 736 (SC), Dhakeshwari Cotton Mills Ltd. v/s CIT - (1954) 26 ITR 775 (SC), Omar Salay Md. Sheikh v/s CIT (1959) 37 ITR 151 (SC), Lal Chand Bhagat Ambika v/s CIT-(1959) 37 ITR 288 (SC), et. al.]

4. The Appellant further submits that in this case the Assessing Officer has not even raised a slightest doubt on the expenditure actually incurred. All the details of expenses, WIP, etc were furnished to the Ld. AO during the course of assessment [Ref. Letter dated 12.12.2019 at pgs 164 to 167, letter dated 20.12.2019 at pgs. 189, 190 to 192D, letter dated 24.12.2019 at pgs 198 to 199 of PB) However, without even raising a slightest dispute on the said details and evidences, the Ld. AO has made the disallowance on his own assumptions. This, in the humble submission of the Appellant is grossly unfair and in any case impermissible in law.

5. The Ld. AO while making the said disallowance has also assumed that the cost of construction in general would be only Rs 5,000/- per sq ft and that of the flats given to the tenants would be only Rs 3500 per sq ft. First of all, it is grossly unfair on the part of

*the Ld. AO to assume that the tenants/original residents of chawl would have been given sub-standard / lower quality homes as compared to sale area. This assumption is seriously objectionable apart from being incorrect in as much as the explanation in this regard was also furnished to the Ld. AO during the course of assessment. In any case, such an assumption of maximum cost per sq ft of Rs.5,000/- or Rs.3,500/- and a total cost of Rs.10,000/- per sq. ft. is nowhere to be found in law or even on facts. Further, the Ld. AO has not even stated as to on the basis of what evidences, details, analyses, etc. has he arrived at these figures.*

*6. As far as the Appellant is concerned, it is one project and on that project the Appellant has incurred cost of construction. Obviously such project cannot be completed in an year and particularly this project ran into cost overruns as it got delayed by around 4 years due to various disputes and clearances [Ref. pg. 192D of PB annexed to letter dated 20.12.2019 at pg. 189 of PB] This fact is not even disputed by the Ld. AO. The said costs incurred over the years on the project have been carried forward to the Work in Progress (WIP) Account and all those years have been assessed under section 143 (3) of the Income Tax Act, 1961 ["the Act" for short] in scrutiny assessment. Further, the very same method of accounting is regularly followed by the Assessee and the accounts are maintained in the very same manner year after year and the same have been accepted by the Department [Ref: Assessment orders at pgs. 250 to 266 of PB). The WIP has been carried over year after year and the closing WIP as on 31.03.2016 (AY 2016-17) was Rs. 93.65 crores [Ref. Balance Sheet as on 31.03.2016 annexed hereto as Exhibit B]. As such, when the expenditure is actually incurred and in fact allowed in the earlier years to be carried forward by the Revenue itself, the Appellant fails to understand as to how the said fact can be substituted with assumed costs based on assumptions. As such the disallowance is uncalled for, grossly unfair and in any case unsustainable.*

*7. For the relevant assessment years the only addition made to the opening WIP of Chhotani Chawl Project is Rs.10.34 Crores [Ref. pg.47 & 48 of PB]. Out of this around Rs.5.13 crores is on account of interest. However, the total disallowance in the current year, Rs.16.55 Crores is more than the expenditure actually incurred. Such an approach is impermissible in law and in any case unheard of.*

*8. The Ld. AO has while invoking Section 145(3) in effect disallowed expenditure incurred in earlier year forming a part of WIP and allowed by the AO himself in earlier years in assessment u/s 143(3) of the Act. In effect, the Ld. AO has rejected the books of accounts of earlier years by making adjustments therein as per the*

*assessment order. As per Section 145(3) the same is not permissible since the rejection of books can be only of the relevant assessment year and that power too cannot be exercised on mere assumptions. In the present case, no fault/defect has been found with the books of accounts of the Appellant for the relevant year. Not only that, the said books are duly audited every year under the Act and the same are stated to be reflecting a true and fair state of affairs by the Auditor. Further, it is not even the AO's case that the method of accounting is not regularly followed by the Assessee and the accounts are maintained in the very same manner year after year and even accepted by the Department in scrutiny assessments u/s 143(3) of the Act each year. As such, the very invocation of section 145(3) is bad in law and deserves to be set aside.*

9. *In any case, the Appellant most humbly submits that, the Ld. AO is not permitted to decide on how the Assessee should run its business. The AO cannot sit in the armchair of businessman and decide what is the appropriate quantum of expenditure or dictate the terms or circumstances for incurring the same [Ref.CIT vs Dhanrajgirji Raja Narsingirji - (1973) 91 ITR 544 (SC), et. al.]. In fact it has been held that the AO cannot disallow any expenditure merely because in his opinion the Assessee could have managed by incurring a lesser expenditure [Ref. Jamshedpur Motor Accessories Stores v/s CIT-(1974) 95 Taxman 664 (Patna), et. al.]. The AO also cannot decide the commercial expediency in incurring the said expenditure and it is the Assessee's prerogative to decide the same [Ref. S.A. Builders Ltd. v/s CIT-(2007) 288 ITR 1(SC), CIT v/s Escorts Heart Institute & Research Centre Ltd. -(2012) 349 ITR 8 (Delhi), et al.]. In fact it has been held that the AO can only decide if the expenditure is real and whether the same is incurred for the purpose of business and nothing more. In the present case no such dispute as regards the actual incurrence or the purpose of the expenditure has been raised at all. The action of the AO in the impugned assessment order clearly manifests that the AO has in fact decided that the Assessee is entitled to incur only the expenditure as assumed by the Ld. AO and nothing further. Such an approach is in clear contravention of the law as laid down by the Hon'ble Supreme Court and other Hon'ble Courts and hence the same is unsustainable.*

10. *As stated earlier, the Ld. AO is not entitled to make a disallowance based on mere assumptions. Further, the impugned assessment order is passed under section 143(3) of the Act and not under section 144 of the Act [Ref: pg.1 & pg.8 of the AO]. As such, in the humble submission of the Appellant, the reliance on the case law pertaining to section 144 is misplaced.*

11. *Without prejudice to the above even while framing an assessment u/s 144 after rejecting the books of the Assessee, the AO is merely entitled to estimate the profit for the relevant year [Ref. Sandeep Suri vs DCIT-ITA 1842/M/10, et. al.]. There is no power to deny expenditure/disallow loss / alter WIP of earlier by making a best judgment assessment under section 144 of the Act. As such the action of the Ld AO as affirmed by the CIT (A) is bad in law even on this count*

12. *In any case, the Ld. AO has not even stated as to under which section of the Act such a disallowance as made by him is permissible. In fact it is a settled law that the income-tax law seeks to put in the net certain class of income, and can only successfully do so, if it frames a provision appropriate to that end [Ref. CIT v/s Jalgaon Electric Supply Co. Ltd-(1960) 40 ITR 184 (SC), et. al.]. As such, the disallowance made by the Ld. AO is unsustainable even on this count.*

13. *It also needs mention that the very same Assessing Officer [Ref pg. 8 of 40 & PR-266 of PB) has accepted the accounts and passed the assessment order for the immediately succeeding year i.e. A. Y.2018-19 accepting the returned loss of Rs 4.30 crores which also included the loss on sale of flats from the Chhotani Chawl projects. A copy of the computation and audited accounts for AY 2018. 19 is annexed hereto and marked as Exhibit C. This clearly manifests that the approach of Ld. AO is inconsistent and smacks of biased/prejudiced mindset. In any case the said action is also contrary even to the principle of consistency [Ref. CIT Vs Excel industries Ltd.- (2013) 258 ITR 295 (SC)] and therefore the same deserves to be reversed. It is therefore humbly prayed that the returned income for AY 2017-18 be accepted and the action of the Ld. AO as affirmed by the CIT(A) be reversed.*

14. *The Appellant further submits that it has already offered a total income of Rs.2.93 crores upto A. Y.2014-15. This fact is not even denied by the Ld. AO [Ref: page 3.7 (iii), Page 5 of 40]. However, admittedly the project has run into losses due to cost over runs, etc. The loss is an actual loss on account of the actual expenditure on construction, interest, compensation to tenants, etc. This is sought to be substituted by the Ld. AO converting the loss into profit try making a disallowance from the opening WIP. This is not just grossly unfair but also against the settled principle that only Real Income can be brought to tax and not any hypothetical income [Ref. Godhra Electricity Cows CIT-(1997) 225 ITR 746 (SC), CIT us Shoorji Vallabhdas & Ca-(1962) 46 ITR 144 (SC), Morvi Industries vs CIT-(1971) 82 ITR 835 (SC), et. al.] In the present case the AO is seeking to tax the hypothetical income which has never been earned. In fact even after adding the amount of Rs.8,93,57,550/- being*

*consideration as per stamp duty value in terms of section 43CA of the Act [Ref pg.38 of PH) there is still a huge loss in the project. As such, the disallowance of loss based on assumptions is grossly unjust apart from being totally contrary to law.*

*15. Without prejudice to the above it is humbly prayed that such profit already declared at Rs.2.93 Crores must be deducted from the profit computed by the AO for the relevant Assessment year since ultimately there is huge loss in the project which is not even denied by the Ld. AO himself and is also evident from the assessment order for the subsequent year i.e. AY 2018-19.*

*16. The Appellant further submits that the rejection of books is also grossly unfair the assessment order for the subsequent year i.e., AY 2018-19. because no specific reason has been attributed by the Ld. AO before rejecting the books of the Assessee. The conditions as stipulated in section 145(3) are not at all fulfilled in the present case. As stated earlier, the said books are audited and cannot be simply brushed aside. Further the method of accounting is regularly followed by the Assessee and the same is also accepted year after year. The very invocation of section 145(3) is bad in law in this case since neither the AO has raised doubt about the correctness or completeness of the books nor a doubt is raised regarding the method accounting being regularly followed by the Assessee. The only basis of rejecting the books is the assumption that the expenditure / cost of construction must be only the AO's assumed rate of Rs. 5000/- per sq. ft. and that too only on the built up area instead of the actual expenditure as incurred by the Assessee on the total constructed area and which is also accepted by the Department over all these years. Such an approach is nowhere provided in the Act. As such, the rejection of books u/s 145(3) by the AO as affirmed by the CIT(A) is bad in law and such action deserves to be set aside.*

*17. To summaries, the Appellant submits that, the very rejection of books and disallowance of loss is bad in law because:*

*(i) The Ld. AO has found no fault with the books of accounts of the Appellant and the conditions for invoking section 145(3) are not fulfilled in the present case;*

*(ii) The books of accounts of the Appellant are audited under the Act and the same were accepted earlier years by the Department when the cost was actually incurred and hence the same cannot be brushed aside in the impugned assessment year as is done in the present case;*

*(iii) The adjustments so made are not within the purview of section 145(3) of the Act as the AO is not empowered to re-work the costs already forming part of the opening WIP,*

*(iv) The Opening WIP has been accepted in the scrutiny assessment for earlier years and the same cannot be disturbed in a subsequent year,*

*(v) The Ld. AO has reworked the WIP on mere assumptions, presumptions, surmises and conjectures which is impermissible under the provisions of the Act,*

*(vi) There is absolutely no basis to apply an assumed average rate of cost of construction when the entire details of the actual cost of construction were furnished before the Ld. AO as well as the CIT(A) and have not even been disputed; and,*

*(vii) In any case, the reworking of the WIP is not in accordance with the extant law.*

*18. In any case, the detailed working of cost which led to higher average per sq. ft. cost along with year wise break up thereof was furnished to the Ld. AO which has been conveniently ignored by him [Ref. pg. 192D annexed to letter dated 20.12.2019]. As could be seen the action of the Ld. AO is upheld on mere presumptions. The same is therefore unsustainable in law.*

*19. The Appellant further submits that the order passed by the Ld. CIT (A) is bad in law also because he has not taken into consideration the most primary argument of the Assessee that the average cost per sq.ft. of the project (Rs.8336 per sq.ft.) is less than the assumed estimated cost per sq.ft. as per the AO (Rs. 10000/- per sq ft) The working of the Ld. AO is itself erroneous in as much as at least the following three errors are evident on the face of the order [Ref para 3.6 of AO, Pg4]*

*(i) The AO has assumed that only built up area needs to be considered for working out the cost and thereafter gone on to hold that as per his working the average cost is Rs 9200 psf. The Appellant is not aware as to how this figure is arrived at. However, if this figure of cost Rs.9200 psf is considered against the total cost incurred of Rs. 103,99,88,964/- then the total constructed area comes to 113042 sq ft. [103.99 Cr/9200 psf - 113,042 sq ft] This is grossly incorrect.*

*(ii) The AO has further assumed that the cost of the Rehab building will be only Rs.3500 psf. This is totally without any factual basis. However even assuming that the same is the cost for Rehab Building, still the AO has grossly erred in working out the cost of sale building*

*by reducing further 56% from the said Rs.3,500/- and thereafter arrived at 16,470 psf as follows  $19200 - (3500 \times 0.56) / 0.441$  This comes to roughly Rs 16,455/- [AO has taken Rs. 16470/-] Factually, the cost of Rs.9200/- includes the assumed figure of Rs.3500 psf as well and the AO has made a further wrong calculation and assumption in as much as 3500 psf is again reduced by 56%*

*(iii) In any case, this calculation of the AO is not understandable. However, it could be seen that (a) first it is assumed that built up area is only to be considered and not the entire constructed area; (b) Then it is assumed that out of the total built up area for 56% of the Area [Rehabilitation Building] the cost incurred is at Rs.3500 psf, (c) Then it is assumed that the total per sq. ft. cost cannot go beyond the limit of Rs. 10,000/- [Rs.5,000/- + Rs.5,000/-] set by the AO; (d) Then after doing some mathematical working (which is also erroneous and incomprehensible) the AO arrives at a psf rate of Rs. 16,470/- for sale building; (e) Then based on the assumed psf cost of sale building the AO reduces Rs.10,000/- as stated above and makes an addition at Rs.16,55,47,243/- based on the assumption that for 25,586.90 carpet area excess cost of Rs.6,470/- psf is incurred. All this exercise is done since as per the AO his assumed cost of Rs.10,000/- per sq. ft. on an average is to be applied across the board for the entire construction. This assumed figure is sought to be substituted for the actual expenditure incurred by the Appellant. In the humble submission of the Appellant this cannot be sustained since no such provision under law permits substitution of assumptions for facts.*

*20. As such the addition made by the Ld.AO and affirmed by the Ld. CIT (A) is unsustainable in law. It is, therefore, prayed that the addition made by the Ld. AO be deleted.*

*21. The Appellant further submits that the disallowance has been sustained by the Ld. CIT (A) on gross assumptions of non-furnishing of working of costs, non- furnishing of details as to whether sale consideration was inclusive of built up area as well as non FSI area, etc. while it is common knowledge that sale agreements are always made based on carpet area, which fact has not even been denied by the Ld. AO. Further, it is a statement totally contrary to the facts on record that the working of cost has not been provided by the Appellant. In any case for the sake of completeness the working of cost bifurcated into FSI, non FSI area is annexed hereto as [Ex.AI & A21. In fact, the Ld. CIT(A) has not even given due consideration to the submissions made by the Assessee and confirmed the disallowance. This is grossly unfair. As such it is prayed that the disallowance be deleted.*

22. *As far as the observation as regards sale value as per Sale Deed is concerned, as stated earlier and for the sake of completeness the Appellant would like to point out that the difference between reckoner rate and agreement value is already added to the income of the Appellant in terms of section 43CA of the Act [Ref.Pg. 38 of PB) and the details of sales as per the agreements were even furnished to the Ld. AO [Ref Letter dated 18.11.2019 at pg.159, 161 & 162 of PB) as well as the Ld. CIT(A) [Ref: Submissions at pg.204 to 246 of PB). As such there is no basis to even assume that there is any loss to the revenue.*

23. *in view of the above it is humbly prayed that the disallowance made by the AO is unsustainable in law and deserves to be deleted and further the invocation of Section 145 (3) be reversed*

**17.** On the other hand, Ld. DR relied on the order of the lower authorities and submitted the written submissions, for the sake of clarity it is reproduced below: -

*"BRIEF FACTS EMERGING FROM ORDERS OF LOWER AUTHORITIES*

*The appellant firm is a builder engaged in the business of real estate and allied activities. The appellant filed return of income for A.Y.2017-18 on 31.10.2017 declaring loss at Rs 13,63,38,373/-.*

*During the year, the appellant has recognized revenue from sale of flats amounting Rs. 44.32 Crore from the "Chhotani Chawl" project (in Lower Parel area), against which the appellant has booked cost of Rs 76.87 Crore, thus resulting in loss of Rs 32.55 Crore.*

*AO noted following discrepancy in the said transaction as recorded in books of accounts, -*

*i. Some of the sales were made at value lesser than the stamp duty value.*

*ii. Cost of construction was Rs 18,000/- per square feet which was much higher than the average cost of construction of Rs 3,500/- prevailing in residential real estate segment, or even Rs. 5,000/- prevalent in luxury residential segment.*

*iii. The average selling price of flats worked out to Rs 23,400/- per square feet, which was much lower than the market rate of Rs 34,000/- per square feet prevailing in the Lower Parel area.*

*iv. The sale agreements were made at rates varying from Rs. 19,000/- per square feet to Rs 32,000/- per square feet. Such large variation in rates clearly indicated that the books of accounts did not reflect the correct state of affairs.*

*The total constructed area of the project was 1,24,753 square feet out of which 76,739 square feet was FSI portion, and 48,014 square feet was non- FSI portion. AO has worked out the cost of construction at Rs 9,200/- per square feet for the total built-up area.*

*Further, the project comprised of both saleable building and rehabilitation building, out of which the saleable area was only 44% of the total area. Accordingly, AO has worked out the cost of construction for the saleable area at Rs 16,470/- per square feet.*

*AO has estimated the excess cost of construction at Rs.16,55,47,243/- after allowing the set-off towards the following.*

*i. Rs. 5,000/- per square feet for the average cost of construction observed in residential real estate, and*

*ii. Rs 5000/-per square feet for the cost of construction of non-built up area, tenancy compensation and other sundry costs.*

*Thus AO has worked out the excess cost of construction by applying the rate of Rs. 6,470/- per square feet (Rs16,470/- less Rs 5,000/- less Rs 5000/-) to the total saleable area of 25,586.90 Square feet.*

*On these facts, AO has rejected the book of accounts under section 145(3) and disallowed the bogus expenditure of Rs 16,55.47 243/, being excess cost of construction. It is pertinent to note that this disallowance has been made by the AO out of total expenditure of Rs. 1,03,99,88,964/- relating to construction of Chhotani Chawl project, recognized and claimed in the Profit and Loss account for the year under consideration. This amount comprises of opening balance of Rs 93.65 Crore transferred from the construction Work-In-Progress account and expenses of Rs 10.34 Crore incurred and claimed during the current year. Thus, the opening balance of Rs 93.65 Crore has also been claimed as a revenue expenditure, for the first time, during the year under consideration only. Therefore, the allowability, or otherwise, of the total claim of expenditure of Rs. 103,99 Crore, including the amount of Rs 93.65 Crore, which has been transferred from Work-In- Progress to the Profit and Loss*

*account, is required to be considered in the current year only, as per the applicable provisions of the Act.*

*In appeal, CIT (Appeals) has noted that the detailed working of cost of saleable area and rehabilitation area was not provided by the appellant during the assessment proceedings of the appellate proceedings. The appellant had not bifurcated the cost of construction of FSI and non-FSI area. The appellant had also not brought on record the fact that the sale consideration as per the sale deed was inclusive of the built up area as well as non-FSI area. On these facts, CIT (appeal) has upheld the view taken by AO that the books of account were not complete and correct, and the profits from the project could not be correctly arrived at relying from the books. Accordingly, CIT(Appeals) has upheld the action of AO in rejecting the books of accounts and estimating the cost of project.*

### **Legal Position**

*1) Hon'ble Supreme Court in the case of CIT Vs British Paints India Ltd (1991) (188 ITR 44) (SC) has held that it is not only the right but the duty of the Assessing Officer to consider whether or not the books disclose the true state of accounts and the correct income can be deducted therefrom. It is incorrect to say that the officer is bound to accept the system of accounting regularly employed by the assessee, the correctness of which has not been questioned in the past. There is no estoppel in these matters, and the officer is not bound by the method followed in the earlier years.*

*2) Hon'ble Bombay High Court in the case of Paras Organics Pvt. Ltd. Vs Addl. CIT (2019) (104 taxmann.com 405) (Bombay) has upheld the action of Assessing Officer in rejecting the books of accounts, based on detailed factual findings which revealed discrepancy in consumption of raw material and production of finished goods, and making addition on account of suppressed production.*

*SLP preferred against the said HC order has also been dismissed by Supreme Court in (2020) (118 taxmann.com 93) (SC).*

*3) Hon'ble Bombay High Court in the case of National Plastics Industries Vs ITO (2009) (309 ITR 191) (Bombay) has upheld the action of Assessing Officer in rejecting the books of accounts where besides noticing deficiencies in books of account of assessee, he also noticed that there were instances of various leakages of revenue in books of account, and that method of accounting applied was not proper, and accordingly proceeded to compute income by applying Gross Profit rate."*

**18.** Considered the rival submissions and material placed on record. We observe that Assessing Officer observed from the record that the assessee has sold flats during the year for ₹.44.32 crores and claimed costs against the above sales of ₹.76.87 crores. He observed that the assessee entered a contract to built total area of 124,753 sft, out of which 69815 sft towards rehab portion and total built up area is 76,739.35 sft. He assumed that both rehab and saleable area are similarly constructed at the same costs. He also observed that assessee had sold 18913 sft during this year at a value of ₹.44.32 crores, on conversion, the average selling price per sft is ₹.23,400/-. Further he observed that the prevailing market rate in the vicinity is ₹.34000/-.

**19.** Assessing Officer observed from the record that assessee had incurred total cost of ₹.103,99,88,964/- and observed that the above cost has to be apportioned based on the basis of built up area, he accordingly calculated the cost of per sft of built up area at the cost of ₹. 9200/- sft by eliminating the finance cost. After considering the agreement for building rehab area of construction, he factored the whole cost of construction on the saleable area i.e., the assessee will get 44% of the saleable area out of total built up area, he calculated the cost of construction by applying formula  $((9200-3500)$  (presumed cost of

construction of rehab units) \* 0.56)/0.44)) at ₹.16470/-. He presumed the maximum cost of construction at the rate of ₹.10,000/-, hence he disallowed the difference of ₹.6470/- excess cost of construction to the extent of ₹.16,55,47,243/-. Ld CIT(A) also sustained the additions made by the Assessing Officer.

**20.** After considering the facts on record, we are of the opinion that the Assessing Officer merely referring the financial data, by applying his own understanding and presumption, disallowed the huge cost of construction. Assessing Officer should have properly analysed the information on record, he should have applied the proper accounting concepts in the field of construction industry. We have analysed the same in the following discussions:

**21.** First we have to determine the cost of construction embedded in the sale price:

The average selling price determined by the Assessing Officer is ₹.23,400/-. We will consider the above selling price as actual selling price to determine the other cost in the above said selling price. The main cost are, cost of additional investment in the land, rehabilitation costs, admin

and finance cost and reasonable profit. Since the assessee has not shared any information on this aspect, we proceed to determine the same as per standard practice as under:

| <b>Particulars</b>  |                  | <b>Amount<br/>(per sft)<br/>Rs.</b> |
|---|------------------|-------------------------------------|
| Selling price   |                  | 23,400/-                            |
| Less: Payment towards cost of land and rehab arrangements | Estimated at 20% | 4,680/-                             |
| Finance cost and administration cost                      | Estimated at 10% | 2,340/-                             |
| Expected profit   | Estimated at 10% | 2,340/-                             |
| Net construction cost                                     | Balance          | 14,040/-                            |

**22.** From the above, cost of construction of saleable area is determined as above, the argument of the assessee that the cost of construction should be calculated on total constructed area or built up area cannot be accepted. The assessee has entered in the agreement to construct the houses for the existing land and house owners by acquiring rights on the land and in return getting a portion of saleable area from them, what is the relevant income and expenditure for the assessee is, the saleable area available for them and total construction cost. Therefore, we have to determine what is the total cost of construction incurred by the assessee from the total cost details submitted by the assessee. In the given case, assessee has submitted total cost incurred by them over the period of Financial years 2010-11 to 2016-17. The total cost includes various cost

including finance, administration, payment towards land and extra ordinary cost due to delay in execution of the project, the assessee submitted that there is a delay of 4 years, however it has not submitted any papers. It is fact on record that there is extra-ordinary delay in execution of project i.e., 6 years. There is merit in the claim of the assessee. Therefore, we will eliminate all other costs not relating to construction cost from the total cost, which will take care of the extraordinary cost of delay in execution. We noticed that assessee has submitted a detailed break up of various expenses in the paper book at Page No. 248 of the paper book. Hence, the cost of construction is calculated as under:

| <b>Particulars</b>   | <b>Amount (Rs.)</b> |
|--|---------------------|
| Total cost declared by the assessee  | 103,99,88,964       |
| Less: Payments towards land and registration                                       | 16,37,91,520        |
| Rehabilitation expenses for tenant   | 1,065,58,500        |
| Administrative expenses (includes architect fees, legal expenses and BMC expenses) | 5,66,86,988         |
| Selling Expenses   | 32,44,018           |
| Finance Expenses   | 33,37,88,389        |
| Total Other cost   | 66,40,69,415        |
| Net Construction cost  | 37,59,19,549        |

**23.** From the above, the total construction expenses incurred by the assessee is ₹.37,59,19,549/- and the cost of construction cost per saleable area is ₹.14,692/- [ $₹.37,59,19,549 \div ₹.25586.90$ ]. We have already determined the cost of construction based on the standard market

practice without there being any assistance from the assessee. This cost of construction calculated are within the standard rate of construction as determined above, i.e., ₹.14,040/-.

**24.** We have observed from the Assessing Officer that the assessee has declared excess cost of construction without analysing the information submitted by the assessee, he proceeded to presume and applied some unscientific method to determine the excess cost of construction. Further, we are of the opinion that no businessman will book additional expenses without there being proper reason. In the given case, the project was taken up and had to face the litigation and had to complete the project under distress. The Assessing Officer has to verify the expenses whether assessee has booked any extra ordinary expenses to claim the additional expenses, these are expected when the project was very successful and assessee intended to do some tax planning. In this case, no such things are possible since the project was completed under distress. Without there being any cogent material in the control of the Assessing Officer against the assessee, it is not proper to presume events and merely observing huge cost, proceeded disallow the expenditure as excessive. We are not inclined to accept the presumptions applied by the Assessing Officer. It is a venture in the area of construction, there is possibility of up and downs

in executing the project particularly when there are projects involving rehabilitation similar to the project undertaken by the assessee. Therefore, we are incline to direct the Assessing Officer to delete the additions made by applying unscientific method and presumptions.

**25.** In the result, the appeal filed by the assessee is allowed.

Order pronounced in the open court on 3<sup>rd</sup> January, 2023

Sd/-  
**(SANDEEP SINGH KARHAIL)**  
**JUDICIAL MEMBER**

Mumbai / Dated 03/01/2023  
Giridhar, Sr.PS

Sd/-  
**(S. RIFAUR RAHMAN)**  
**ACCOUNTANT MEMBER**

**Copy of the Order forwarded to:**

1. The Assessee
2. The Respondent.
3. The CIT(A), Mumbai.
4. CIT
5. DR, ITAT, Mumbai
6. Guard file.

//True Copy//

BY ORDER

(Asstt. Registrar)  
**ITAT, Mum**