IN THE INCOME TAX APPELLATE TRIBUNAL
PUNE BENCH "B", PUNE

BEFORE SHRI R. K. PANDA, VICE PRESIDENT
AND
MS ASTHA CHANDRA, JUDICIAL MEMBER

ITA No.691/PUN/2024
Assessment Year : 2017-18

Rajkamal Stone Metal Works Survey No.57, Ambegaon Khurd, Tal. Haveli, Dist. Pune – 411046	**Vs.**	ACIT, Circle – 5, Pune
PAN: AABFR4460Q		
(Appellant)		**(Respondent)**

Assessee by	**:**	Shri Nikhil S Pathak
Department by	**:**	Shri Arvind Desai, Addl. CIT DR
Date of hearing	**:**	22-10-2024
Date of pronouncement	**:**	25-10-2024

O R D E R

PER R.K. PANDA, VP :

This appeal filed by the assessee is directed against the order dated 12.02.2024 of the CIT(A) / NFAC, Delhi relating to assessment year 2017-18.

2. Facts of the case in brief, are that the assessee is a firm engaged in the business of manufacturing of crushed sand, aggregate and stone metals under the name and style M/s. Rajkamal Stone Metal Works. It filed its return of income on 29.10.2018 declaring total income of Rs.2,64,97,800/-. The case of the assessee was selected for manual scrutiny as per para 1(vi) of CBDT's Instruction No.04/2018 dated 20.08.2018 for the following reasons:

> *"5. This case was selected for Manual scrutiny. The reasons for selection are: To verify the sources and mode of payment made of Rs.17,50,000/- in old demonetized currency to M/s. Shaheed Lt. Col Prakash Patil Petroleum."*

3. Accordingly, statutory notices u/s 142(1) of the Income Tax Act, 1961 (hereinafter referred to as 'the Act') were issued and served on the assessee to which, the AR of the assessee appeared before the Assessing Officer from time to time and filed the requisite details.

4. During the course of assessment proceedings the Assessing Officer noted from the capital account of the partner that an amount has been debited to the extent of Rs.62,70,540/- under the head 'lands' during the year under consideration. On being questioned by the Assessing Officer, it was submitted that the said lands were purchased by the assessee firm for its business use but the purchase deeds were made in the name of the partners who had contributed the capital for purchase of the properties and the amount for purchase of the lands was paid by the firm. As no business was carried out on this land, the partners decided to transfer the said land to both the partners at cost price by passing necessary journal entries.

5. However, the Assessing Officer was not satisfied with the arguments of the assessee. He noted that the assessee firm and the sister concern has purchased the lands for business purpose. However, as no business was carried on in these lands, the same was transferred to the partners which amounts to a transfer resulting into a capital gain. Further, the valuation report of the said land was not filed by the

assessee. In absence of any documentary evidence, the capital gain could not be calculated, he, therefore, made addition of Rs.62,70,540/- in the hands of the assessee firm on account of transfer of land from the firm to the partners.

6. In appeal, the CIT(A) / NFAC confirmed the action of the Assessing Officer by observing as under:

> *"5 I have carefully considered materials available and facts involved in the case. Coming to the Grounds of Appeal the first and the last one are general in nature and, therefore, do not need any adjudication.*
>
> *5.1. Ground of Appeal at 2 is the main grievance of the appellant. Ground at 3 is only supportive in nature in the present case, the contention of the appellant is that mere book entry through capital account of the partners cannot lead to any transfer of asset. As a sequitur, the appellant claimed that there could be no capital gains. He also relied on the judgment in the case of JM. Mehta and Sons, 214 ITR Page 716.*
>
> *6. Section 47 of the Act, deals with transaction not recorded as transfer. Section 47 (ii) of the Act, prior to its deletion, it provided:*
>
> > *1. Nothing contained in Section 45 shall apply to the following provisions*
> >
> > *2. In distribution of the capital assets on the dissolution of the firm, the body of individuals or without associations of persons.*
>
> *6.1. This provision is omitted by Finance Act, 1997 with effect from 01.4.1998. In other words, prior to this omission, distribution of capital assets of the dissolution of the firm was not treated as a transfer. Section 2(47) of the Act defines asset as transfer in relation to a capital asset. It is inclusive definition. Simultaneously, on the deletion of the aforesaid provision. Section 45 of the Act was amended by insertion of Sub-section (3) and (4) which exclusively dealt with transfer of a capital asset by a person to a firm, by way of distribution of the capital assets of the firm. Section 45 (4) of the Act reads as under:-*
>
> > *"Section 45 (4) The profits or gains arising from the transfer of a capital asset by way of distribution of capital assets on the-dissolution of a firm or other association of persons or body of individuals (not being a company or a co-operative society) or otherwise, shall be chargeable to tax as the income of the firm, association or body, of the previous year in which the said transfer takes place and, for the purposes of section 48, the fair market value of the asset on the date of such transfer shall be deemed to be the full value of the consideration received or accruing as a result of the transfer."*

6.2. Here, the key word is "or otherwise". Thus, the provision was inserted to plug loophole in the Act. It now included distribution of assets of a firm among partners, on dissolution and otherwise, as transfer. That is, the expression 'otherwise has to be read with the words transfer of the capital assets. If so read, it becomes clear that even when a firm is in existence and there is a transfer of capital assets, it comes within expression 'otherwise'. The word 'otherwise' takes into sweep not only cases of dissolution but also cases of transferring of assets by existing partnership firms.

7. This view was finally upheld by the Hon'ble Supreme court in the case of Mansukh Dyeing and Printing Mills, [2022] 145 taxmann.com 151 (SC), wherein it held,

> *"7.2 The object and purpose of introduction of section 45(4) was to pluck the loophole by insertion of section 45(4) and omission of section 2(47)(ii) While introduction to section 45(4), clause (ii) of section 2(47) came to be omitted. Earlier, omission of clause (ii) of section 2(47) and Section 47(ii) exempted the transform by way of distribution of capital assets from the ambit of the definition of "transfer" The same helped the assessee in avoiding the levy of capital gains tax by revaluing the assets and then transferring and distributing the same at the time of dissolution. The said loophole came to be plucked by insertion of section 45(4) and omission of section 2(47)(ii) At this stage, it is required to be noted that the word used "OR OTHERWISE in section 45(4) is very important."*

8 In the present case also, a subsisting firm had transferred its asset to its partners at Rs.62,70,540/-. This tantamount to transfer, within the meaning of section 2(47) of the Act. Details of purchase of the asset were not available with the AO. Same has not been produced even at this stage. However, in the interest of justice and fair play, the AO is directed to re-compute capital gains on the basis of factual details, in case those are provided by the appellant.

9. In fine, Grounds of Appeal are partially answered in favour of the appellant.”

7. Aggrieved with such order of CIT(A) / NFAC, the assessee is in appeal before the Tribunal by raising the following grounds of appeal:

1 In the facts and circumstances of the case and in law, the learned CIT(Appeals) has erred in confirming the action of the learned Assessing Officer of taxing the amount of Rs.62,70,540.00 on account of transfer of capital assets owned by the appellant firm to its partners resulting into Capital Gains. The said finding/action of the learned Assessing Officer is patently illegal, bad in law, arbitrary, perverse and devoid of merits, the same may please be deleted.

2 The learned CIT (Appeals) failed to appreciate that the appellant firm has transferred only the amounts pertaining to the immovable properties sitting in the Balance Sheet of the assessee firm to its partners capital accounts without execution of any instruments in writing and hence there was no legal transfer of the impugned properties to the partners giving rise to the Capital gains. Hence the impugned addition of Rs.62,70,540.00 may please be deleted.

3 The learned CIT(Appeals) has erred in not deleting the impugned addition of Rs.62,70,540.00 made by the learned Assessing Officer which is contrary to the well settled principles of law explained by the Hon. Bombay High Court in the case of CIT v/s J.M. Mehta and Sons reported in 214 ITR Page 716 the same may please be deleted.

4 The appellant craves the permission to add, amend, modify, alter, revise, substitute, delete any or all grounds of appeal, if deemed necessary at the time of hearing of the appeal.

8. The Ld. Counsel for the assessee strongly challenged the order of the CIT(A) / NFAC in confirming the addition of Rs.62,70,540/-. Referring to the copy of the Balance Sheet placed at page 3 of the paper book, the Ld. Counsel for the assessee drew the attention of the Bench to the partners capital account and submitted that an amount of Rs.62,70,540/- was shown as withdrawal from the capital account of Sameer A Pimple and Rs.1,65,58,640/- as withdrawal from the capital account of Shirish K Sankhe. He submitted that the assessee firm had purchased four pieces of lands during the assessment year 2006-07 which were registered in the name of the partners but the money was given out of the funds of the partnership firm and were shown in the Balance Sheet of the partnership firm in the asset side for the year ending 31.03.2016. The capital accounts of the partners were debited with cost of the lands at book value and those lands were not re-valued. Referring to the fixed assets schedule as on 31.03.2017, he submitted that such lands appearing in the Balance Sheet at Rs.2,28,29,180/- was shown as

reduction and the value has been shown as zero in the Balance Sheet as on 31.03.2017. The Ld. Counsel for the assessee submitted that although the Assessing Officer has not brought to tax the cost of the lands reduced from the capital account of the partner Mr. Shirish K Sankhe at Rs.1,65,58,640/-, however, he has taxed an amount of Rs.62,70,540/- shown as withdrawal in the hands of Shirish K Sankhe towards the cost of the land. He submitted that since the lands were not revalued and such excess amount due to revaluation has not been credited to the capital account of the partners and since they have not withdrawn any amount as such from that valuation reserve, therefore, the decision of the Hon'ble Supreme Court in the case of CIT vs. Mansukh Dyeing and Printing Mills (2002) 145 taxmann.com 151 (SC) relied on by the CIT(A) / NFAC is not applicable. Referring to the said decision, the Ld. Counsel for the assessee submitted that the Hon'ble Supreme Court in the said decision has held that where pursuant to reconstitution of assessee-partnership firm, assets of assessee were revalued and the excess amount due to such reduction was credited to partners accounts in their profit sharing ratio, said credit was in effect distribution of increased value of assets to partners, and as said credits were available to partners for withdrawal, assets so revalued and credited into capital accounts could be said to be 'transfer' which would fall in category of 'otherwise' under section 45(4) and said amount would be chargeable to short term capital gain. He submitted that since the assessee in the instant case has not revalued such value of lands and no excess amount has been credited to the capital account of the partners, therefore, the said decision is not applicable. He submitted that since the assessee has transferred the

lands to the partners on book value only, therefore, no capital gain is attracted. Further, the lands were transferred to the respective partners by passing a journal entry and neither there was a sale deed nor any agreement, therefore, in view of the decision of the Hon'ble Bombay High Court in the case of CIT vs. M.J. Mehta and Bros. (1995) 214 ITR 716 (Bom), it is not a valid transaction. He submitted that the Hon'ble Bombay High Court in the said decision has held that the transfer of immovable property belonging to the firm to its partners by means of book entry was not valid. He accordingly submitted that the CIT(A) / NFAC was not justified in confirming the addition made by the Assessing Officer.

9. The Ld. DR on the other hand heavily relied on the orders of the Assessing Officer and the CIT(A) / NFAC. He submitted that the provisions of section 45(4) are clearly applicable to the present case.

10. We have heard the rival arguments made by both the sides, perused the orders of the Assessing Officer and the Ld. CIT(A) and the paper book filed on behalf of the assessee. We have also considered the various decisions cited before us. We find the Assessing Officer made addition of Rs.62,70,540/- in the hands of the assessee firm on the ground that when the assessee firm had purchased the lands for business purpose and due to no business activity carried on in these lands, the same were transferred to the partners, therefore it amounts to transfer resulting into capital gain. Since the assessee has not filed valuation report of the same and in absence of any documentary evidence the capital gain could not be calculated,

he, made addition of Rs.62,70,540/- which was shown as withdrawal of the land from the capital account of the partner Sameer A Pimple. We find the CIT(A) / NFAC sustained the addition made by the Assessing Officer, the reasons of which have already been reproduced in the preceding paragraphs. It is the submission of the Ld. Counsel for the assessee that four pieces of lands were purchased in the name of two partners, the funds were given out of the funds of the firm and the assets were shown in the Balance Sheet of the assessee firm and since no business activity was carried out on the said lands, these were transferred to the capital accounts of the two partners at book value only by passing a journal voucher entry and therefore, no capital gain is chargeable.

11. We find some force in the arguments of the Ld. Counsel for the assessee. A perusal of the Balance Sheet of the assessee firm shows that the opening value of such land as on 01.04.2016 was shown as Rs.2,28,29,180/- which was transferred to the two partners namely Sameer A Pimple at Rs.62,70,540/- and Shirish K Sankhe at Rs.1,65,58,640/- on the ground that the lands were registered in their name originally. It is an admitted fact that there was no revaluation of such lands and no excess amount other than the cost of the lands has been credited to the capital accounts of the partners which is otherwise eligible for withdrawal by the partners. It is also an admitted fact that the lands were transferred to the capital accounts of the partners at book value only and therefore, no capital gain has arisen.

12. So far as the decision of the Hon'ble Supreme Court in the case of CIT vs. Mansukh Dyeing and Printing Mills (supra) relied on by the CIT(A) / NFAC is concerned, the same in our opinion, is not applicable to the facts of the present case. In that case, pursuant to reconstitution of assessee-partnership firm, assets of assessee were revalued and such revalued amount was credited to partners accounts in their profit sharing ratio, said credit was in effect distribution of increased value of assets to partners, and as said credits were available to partners for withdrawal, assets so revalued and credited into capital accounts could be said to be 'transfer' which would fall in category of 'otherwise' under section 45(4) and accordingly it was held that the said lands were chargeable to short term capital gain. The relevant observations of the Hon'ble Supreme Court read as under:

> *"7.5 In the present case, the assets of the partnership firm were revalued to increase the value by an amount of Rs. 17.34 crores on 01.01.1993 (relevant to A.Y. 1993-1994) and the revalued amount was credited to the accounts of the partners in their profit-sharing ratio and the credit of the assets' revaluation amount to the capital accounts of the partners can be said to be in effect distribution of the assets valued at Rs. 17.34 crores to the partners and that during the years, some new partners came to be inducted by introduction of small amounts of capital ranging between Rs. 2.5 to 4.5 lakhs and the said newly inducted partners had huge credits to their capital accounts immediately after joining the partnership, which amount was available to the partners for withdrawal and in fact some of the partners withdrew the amount credited in their capital accounts. Therefore, the assets so revalued and the credit into the capital accounts of the respective partners can be said to be "transfer" and which fall in the category of "OTHERWISE" and therefore, the provision of Section 45(4) inserted by Finance Act, 1987 w.e.f. 01.04.1988 shall be applicable.*
>
> *7.6 Now, so far as the reliance placed upon the decision of this Court in the case of Hind Construction Ltd. (supra) is concerned, at the outset, it is required to be noted that the said decision was pre-insertion of Section 45(4) of the Income Tax Act inserted by Finance Act, 1987 and in the earlier regime – pre-insertion of Section 45(4), the word "OTHERWISE" was absent. Therefore, in the case of Hind Construction Ltd. (supra), this Court had no occasion to consider the amended / inserted Section 45(4) of the Income Tax Act and the word used "OTHERWISE". Under the circumstances, for the purpose of interpretation of newly inserted Section 45(4), the decision of this Court in the case of Hind*

> *Construction Ltd. (supra) shall not be applicable and/or the same shall not be of any assistance to the assessee. As such, we are in complete agreement with the view taken by the Bombay High Court in the case of A.N. Naik Associates and Ors., (supra). We affirm the view taken by the Bombay High Court in the above decision."*

13. However, in the instant case, since there was no revaluation of any asset and the assets were transferred at cost price to the partners, therefore, the decision of the Hon'ble Supreme Court in the case of CIT vs. Mansukh Dyeing and Printing Mills (supra) is not applicable to the facts of the present case.

14. Further, the assets in question were transferred to the two partners by passing a journal entry only. The Hon'ble Bombay High Court in the case of CIT vs. M.J. Mehta and Bros. (supra) has held that the transfer of immovable property belonging to the firm to its partners by means of book entry was not valid. Once the transfer is treated as not valid because of mere passing of book entry, therefore, in our opinion, there cannot be any capital gain.

15. We further find that while the Assessing Officer has brought the amount of Rs.62,70,540/- being transfer of land to Sameer A Pimple, however, the amount of Rs.1,65,58,640/- transferred to Shirish K Sankhe towards the land has not been brought to tax and no action either u/s 263 or 147 of the Act has been initiated. In other words, the Assessing Officer has partly accepted a transaction and partly rejected the same. Therefore, the CIT(A) / NFAC in our opinion is not justified in sustaining the addition of Rs.62,70,540/- made by the Assessing Officer. In view of the above discussion, we set aside the order of the CIT(A) / NFAC and direct

the Assessing Officer to delete the addition. The grounds raised by the assessee are accordingly allowed.

16. In the result, the appeal filed by the assessee is allowed.

Order pronounced in the open Court on 25th October, 2024.

Sd/-	**Sd/-**
(ASTHA CHANDRA)	(R. K. PANDA)
JUDICIAL MEMBER	VICE PRESIDENT

पुणे Pune; दिनांक Dated : 25th October, 2024

GCVSR

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order is forwarded to:

1. अपीलार्थी / The Appellant;
2. प्रत्यर्थी / The Respondent
3. The concerned Pr.CIT
4. DR, ITAT, 'B' Bench, Pune
5. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

// True Copy //

Senior Private Secretary
आयकर अपीलीय अधिकरण ,पुणे
/ ITAT, Pune

S.No.	Details	Date	Initials	Designation
1	Draft dictated on	22.10.2024		Sr. PS/PS
2	Draft placed before author	24.10.2024		Sr. PS/PS
3	Draft proposed & placed before the Second Member			JM/AM
4	Draft discussed/approved by Second Member			AM/AM
5	Approved Draft comes to the Sr. PS/PS			Sr. PS/PS
6	Kept for pronouncement on			Sr. PS/PS
7	Date of uploading of Order			Sr. PS/PS
8	File sent to Bench Clerk			Sr. PS/PS
9	Date on which the file goes to the Head Clerk			
10	Date on which file goes to the A.R.			
11	Date of Dispatch of order			