

**IN THE INCOME TAX APPELLATE TRIBUNAL
COCHIN BENCH**

**BEFORE SHRI INTURI RAMA RAO, AM
AND SHRI SOUNDARARAJAN K., JM**

**ITA No. 428/Coch/2015
Assessment Year: 2012-13**

ACIT, Circle-1, Non-Corporate Appellant
IInd Floor, C.R. Building, I.S. Press Road
Ernakulam 682018

vs.

PVR Tourist Home Respondent
Palarivattom, Kochi 682025
[PAN: AADFP3442Q]

Appellant by: Shri Suresh Sivanandan, CIT-DR
Respondent by: Shri Mohan Pulickal, Advocate

Date of Hearing: 10.03.2025
Date of Pronouncement: 21.03.2025

ORDER

Per: Inturi Rama Rao, AM

This is an appeal restored by the Hon'ble High Court vide order dated 01.07.2024 in ITA No. 203 of 2019 with the following directions: -

“9. Thus, while we uphold the finding of the Tribunal that the charge of Short Term Capital Gains, in the instant case, has to be as mandated in Section 45(4) of the Income Tax Act, we remand the matter back to the Tribunal for computing the extent of short-term capital gains, if any, that would be brought to tax in relation to the appellant herein. The Appellate Tribunal would have to do the said exercise by

taking into account the totality of transactions effected during the previous year relevant to the assessment year in question.

10. Thus, this appeal is allowed by answering question Nos. 1 and 2 against the assessee and in favour of the revenue and by not answering question Nos. 3 and 4, in the light of the discussions in this judgment and the remand necessitated to the Tribunal for a specific finding on the extent of short term capital gains, if any, that would accrue to the appellant firm during the assessment year in question. The Appellate Tribunal shall examine the provisions of Section 48, as modified by Section 50(1) of the Income Tax Act, and determine whether or not any short-term gains had accrued to the appellant firm for the assessment year in question. Taking note of the time that has elapsed since the filing of this appeal before this Court, we direct that the above computation exercise be completed by the Appellate Tribunal within an outer time limit of six months from the date of receipt of a copy of this judgment, after hearing the appellant firm.”

2. The factual ground of the case is that the appellant is a partnership firm engaged in the business of running hotel. The return of income for AY 2012-13 was filed on 31.10.2013 declaring income of Rs. 67,59,352/-. Against the said return of income, the assessment was completed by the Asst. Commissioner of Income Tax, Circle -1(1), Non-corporate, Kochi (hereinafter called "the AO") vide order dated 23.03.2015 passed u/s. 143(3) of the Income Tax Act, 1961 (the Act) at a total income of Rs. 9,77,46,777/-. While doing so, the AO made addition on short term capital gains in respect of building of Rs. 6,50,7,334.

3. The factual background leading the above addition is that originally the partnership firm was consisted of two partners, namely,

Shri P.A. Francis and Smt. Etty Francis as per the partnership deed dated 01.04.1996. This partnership was reconstituted w.e.f. 07.07.2011 by induction of 3 new partners, viz., Shri Poonghat Srinivas, Smt. Anita Patel and Smt. Sherita D'Souza. A building was constructed on a plot of land admeasuring 3.5 acres owned by Shri P.A. Francis and Smt. Etty Francis. The partners of the firm sold it for a consideration of Rs. 8.4 cores of which Rs. 7.4 crores was appropriated towards sale consideration of the building and balance one crore was towards sale consideration of land. This property was sold to one Mr. Poonghat Srinivas vide sale deed dated 03.05.2011, who latter on was inducted into the partnership firm and brought this asset into the partnership firm at the same value, i.e. Rs. 8.4 crores. The appellant firm had not shown any capital gain or profit on account of this transaction, as it was of the opinion that there was no change in the written down value (WDV) of the building. However, the AO was of the opinion that for the purpose of computing the capital gain u/s. 50 of the Act the cost of acquisition as provided under the provisions of section 50A, alone should be considered, by which the value of the asset brought back by the incoming partner was adopted at WDV and cost of the asset sold. Thus, he computed the short term capital gain at Rs. 6,50,77,334/-.

4. Being aggrieved, an appeal was filed before the CIT(A), who vide order dated 08.06.2015 in ITA No. 62/NC-R-1/VC-CP1/CIT(A)-II/2014-15 directed the AO to delete the addition on account of short term capital gain in respect of building by holding that the

value of any block of asset is to be taken at the end of the previous year after taking into consideration the addition, if any, made in the block of assets during the year.

5. Being aggrieved by the decision of the CIT(A), the Revenue preferred appeal before this Tribunal. The Tribunal has allowed the appeal filed by the Revenue applying the provisions of section 45(4) of the Act. The relevant portion of the order reads as under: -

“9.9 Now the question is whether section 45(4) covers transfer only transfer on dissolution or also a transfer during the subsistence of a firm or "distribution" and/ "or otherwise" is to be understood in the true spirit of the legislation. "Distribution" is akin to final settlement. Every transfer is not a "distribution" because the latter involves division, realization, encashment of assets and appropriation after settling the liabilities. Reconstitution of the firm should not come within the expression "or otherwise" because it will render the word "distribution of capital assets" otiose. In fact, it runs contrary to legislative intent which was simply to tax the transfers in the course of final settlement between the partners which is the reason section 47(ii) was deleted by the amendment that introduced section 45(4). Thus, the purpose and object of the Finance Act, 1987 was to charge tax arising on distribution of capital assets of the firm which otherwise was not subject to tax. Therefore, the language of section 45(4) should be construed to mean that the expression "or otherwise" is not to be read ejusdem generis with the expression "dissolution of the firm or Body or AOP". The expression "or otherwise" is to be read with the words "transfer of the capital assets" by way of distribution of capital assets. The distribution of capital asset does not mean only physical distribution. It also covers constructive distribution or distribution of sales consideration among partners, by passing necessary entries in the firm's

books of accounts. If so read, it becomes clear that even when the firm is in existence and there is transfer of capital assets, it comes within the expression "otherwise" as the object of the amending Act was to remove the loopholes which existed, whereby capital gain was not chargeable. In the present case, the sale deed dated 03/05/2011 was executed by Shri P.A. Francis and PVR Industries as the vendors and in favour of Shri Poonghat Shrinivas for a total consideration of Rs. 7.4 crores for building and Rs. 1.00 crore for land, the total amount being Rs.8.4 crores and out of this, Rs.7.4 crores has been paid to the present assessee and Rs. 1.00 crore to the partner Shri P.A. Francis. Therefore, there is transfer of capital asset within the scope of section 45(4) of the Act by the firm to Shri Poonghat Shrinivas who acquired the absolute right over the building. However, there is no question of reference u/s. 55A on the reason that the fair market value is the actual sales consideration received by the assessee which is already determined between the partners.”

6. The Tribunal also rejected the contention of the appellant that in WDV there was no change in the capital gain by holding as under: -

10. At this stage, it is appropriate to mention the plea of the Ld. AR that even if there was transfer, section 50 of the Act is applicable and the gains cannot be charged to tax as written down value of the property at the end of the year is more than the written down value of the property at the beginning of the year. We are not in agreement with this contention of the assessee in view of the judgment of the Jurisdictional High Court in the case of CIT vs. Kumbazha Tourist Home (Dissolved) cited supra;. The facts of this case are that a firm was constituted with the object of running a lodge house on July 1, 1979. At the time of constitution of the firm the partners brought the land and the respective portion of the building thereon towards their share capital and the firm for several

years claimed ownership of the building and based on the same, depreciation was claimed in respect of the building for all the assessment years until 1993-94 which was the last year of assessment of the firm. Admittedly, on dissolution the property reverted back to the partners in the same way it was brought by them to the firm as their capital. The Assessing Officer initiated proceedings for assessment for capital gains under section 45(4). The Assessing Officer limited the levy of capital gains to the extent of 14.25 cents of land involved. Since the building was sold at the book value, i.e., depreciated value, the Assessing Officer accepted the transaction as one falling u/s. 50(1) of the Act not attracting any capital gains tax because the transfer was at the book value. The Commissioner acting under section 263 held that the entire transaction attracted tax on capital gains u/s. 45(4) of the Act. The assessee's appeal on the levy of capital gains tax on land value was allowed by the Commissioner (Appeals). The Tribunal held that the reference to the valuer was not justified and therefore, the assessment of capital gains did not arise. On appeal to the High Court:

"Held, that the clear finding was that the land and building was brought to the firm as capital by the partners and based on the ownership claimed by the firm, it claimed depreciation for all the years it was carrying on the lodging business using the land and building. Admittedly, on dissolution the land and building were distributed among the partners of the dissolved firm. This was a clear case falling under section 45(4) attracting liability for capital gains. The reference of the asset for valuation under section 55A was within the powers of the officer. Matter remanded to decide the valuation issue"

7. Being aggrieved by the order passed by this Tribunal the appellant firm preferred an appeal u/s. 260 of the Act before the Hon'ble Jurisdictional High Court by framing the following questions of law: -

“ (i) Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in allowing the additional ground raised by the Revenue before the second appellate forum, which were not raised either by the Assessing Officer or the Commissioner of Income Tax (appeals) nor considered by them?

(ii) Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in holding that the transfer of the depreciable capital assets attracted capital gains tax under Sec.45(4) of the Act, in the absence of distribution of any capital asset among the partners following a dissolution of the appellant firm?

(iii) Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in upsetting the conclusion reached by the CIT (Appeals) that under Sec.50 of the Act, the transfer in question was not exigible to capital gains tax?

(iv) Are not the provisions of Sections 50A and 45(4) of the Act inapplicable to the facts and circumstances of the case and is not Sec.50 of the Act the correct provision of law applicable to the transfer of the depreciable asset in issue?”

8. The Hon'ble High Court finally remanded the matter back to the file of this Tribunal with a direction contained in paras 9 & 10, which are extracted supra.

9. That is how the matter had come up before this Tribunal.

10. The learned CIT-DR submits that the issue of applicability of provisions of section 45(4) to the said transaction is upheld by the Hon'ble High Court and, therefore, the sale consideration received on sale of the building to Shri Poonghat Srinivas is to be brought to

tax. Further he submits that since the same asset, which was bought into the books of the partnership as capital contribution of Shri Poongaht Srinivas for the purpose of computing capital u/s. 50 of the Act the depreciable value of the asset alone is to be considered.

11. On the other hand, the learned A.R. of the assessee submits that for the purpose of computing capital gains as per section 45(4) of the Act the computation is to be done in the manner prescribed u/s. 48 r.w.s. 50 of the Act. He further submits that for the purpose computing capital gain u/s. 50 of the Act the value at which it was brought back into the books of the firm by the incoming partner Shri Poonghat Srinivas should be considered as addition to the block of assets as specified under sub-clause (1) of section 50 of the Act. If such method is adopted, it would not result in short term capital gain.

12. We have heard the rival contentions of both the parties and perused the material available on record. The matter was remanded to this Tribunal by the Hon'ble High Court with a specific finding upholding the applicability of section 45(4) of the Act, however directed this Tribunal to examine the applicability of provisions of section 50 r.w.s. 48 of the Act and compute the short term capital gains, if any. A perusal of section 45(4) clearly shows that distribution of capital asset as a result of dissolution of a firm or otherwise the fair market value of the asset on the date of such transfer shall be deemed to be the full value of consideration

received. In this case there is no dispute about the amount of fair market value of consideration, i.e. Rs. 7.4 crores. Therefore, the AO shall compute the capital gain u/s. 45(4) of the Act. Hence, we remit the matter back to the file of the AO to compute the amount of capital gain u/s. 45(4) of the Act by adopting the sale consideration received from Shri Poonghat Srinivas of Rs. 7.4 crores as sale consideration by reducing the WDV of the asset as per the provisions of the Income Tax Act.

13. Next question that is required to be determined by us is applicability of section 48 and section 50 of the Act. The provisions of section 48 provides for the method of computation of income chargeable under the head capital gains. Provisions of section 48 stipulates that the income chargeable under the head 'capital gains' shall be computed by deducting from the full value of the consideration received or accruing as a result of the transfer of the capital asset the following amounts, viz. expenditure incurred wholly and exclusively in such transfer and the cost of acquisition of asset and cost of any improvement thereto, whereas the provisions of section 45 are charging provision and section 48 provided for basis of computation. It is also settled law that the provisions of section 45 must be read with section 48 of the Act. If the computation cannot be effected for any reason the, charging provision u/s. 45 fails. In the present case, in the paragraph (supra) by virtue of the dictum laid down by the Hon'ble High Court that provisions of section 45(4) are applicable and capital gains u/s. 48

r.w.s. 45(4) are computed. As applicability of section 50, on mere perusal of section 50 it is clear that the object behind enacting the provisions of section 50 is to compute the short term capital loss or the gains on sale of depreciable assets, sale of an asset when the asset is sold on which depreciation has been allowed in the earlier years as per the Income Tax Act and Rules. The actual amount of depreciation in fact becomes known, which would call for an adjustment to be made to the depreciation which had been earlier allowed as per the provisions of Income Tax Act and Rules made thereunder. This adjustment is called for in the year of sale by way of short term capital gains or loss. If the realisation of sale proceeds is more than the opening WD value of the asset as increased by the value of addition made in the asset during the year, it would result in short term capital gains under the provisions of section 50 of the Act. Of course, the amount of value of addition should be adjusted in terms of the provisions of section 50 of the Act. However, these provisions of section 50 have no application to the facts of the present case as the same amount was assessed to capital gain u/s. 45(4) of the Act. In other words, provisions of both section 45(4) and section 50 cannot be applied to the same amount. In this regard reliance is placed on the decision of the Hon'ble Supreme Court in the case of Commissioner of Income Tax v. Urmila Ramesh [1998] 230 ITR 422 (SC) rendered in the context of provisions of section 41(2) read with provisions of section 2(22)(c) of the Act.

14. In the above terms, the appeal filed by Revenue stands partly allowed.

Order pronounced in the open court on 21st March, 2025.

Sd/-

**(SUNDARARAJAN K.)
JUDICIAL MEMBER**

Sd/-

**(INTURI RAMA RAO)
ACCOUNTANT MEMBER**

Cochin, Dated: 21st March, 2025

n.p.

Copy to:

1. The Appellant
2. The Respondent
3. The Pr. CIT concerned
4. The Sr. DR, ITAT, Cochin
5. Guard File

Assistant Registrar
ITAT, Cochin