

**IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCH ' B '**

**BEFORE SHRI VIJAY PAL RAO, JUDICIAL MEMBER AND
SHRI INTURI RAMA RAO, ACCOUNTANT MEMBER**

I.T. A. No.193/Bang/2014
(Assessment Year : 2005-06)

M/s. Canara Housing Development Company,
No.10/1, Lakshminarayana Complex,
Palace Road, Bangalore-560 052.

.... Appellant.

Vs.

Joint Commissioner of Income Tax (OSD),
Central Range, Bangalore.

..... Respondent.

Appellant By : Shri Vijay Mehta & Shri R. Ramakrishnan, CAs

Respondent By : Ms. Neera Malhotra, CIT (DR) (ITAT)-2, Bengaluru.

Date of Hearing : 28.03.2017.

Date of Pronouncement : 12.05.2017.

O R D E R

Per Shri Vijay Pal Rao, J.M. :

This appeal by the assessee is directed against the order dt.28.11.2013 of Commissioner of Income Tax (Appeals) for the Assessment Year 2005-06.

2. Though the assessee has raised various grounds in this appeal however at the time of hearing the learned Authorised Representative of

the assessee has stated at Bar that the effective ground of appeal is only

Ground No.1 which reads as under :

“ 1. The learned CIT (Appeals) is not justified in dismissing the appeal – claim of deduction of Rs.64 Crores paid to M/s. Caraka Academy of Life Long Learning.”

We find that the other grounds are only in the nature of argument in support of Ground No.1.

3. Brief facts leading to the controversy are that the assessee is a partnership firm and engaged in the business of real estate including purchases, procurement, acquisition of right in the land and real estate properties, integrated development of properties, etc. The assessee entered into an Agreement to Sale dt.2.4.2002 in respect of four properties referred to therein. As per the terms of the Agreement dt.2.4.2002, the assessee agreed to sell / transfer the constructed area to **M/s. Manipal Infocom Pvt. Ltd. (MIPL)** against the total consideration of Rs.22 Crores which was received by the assessee in advance at the time of agreement. It is pertinent to mention that in the meantime the name of M/s. MIPL was changed to **M/s. Manipal Universal Learning Pvt. Ltd. (MULPL)**. Further due to the legal restriction of acquiring the real estate interest by MIPL, the right/interest in said four properties was assigned

to **M/s. Caraka Academy of Lifelong Learning Pvt. Ltd. (CALL)** vide Agreement dt.5.4.2005. Since the assessee failed to deliver the property within time frame as stipulated in the Agreement and revised Agreement a dispute arose in respect of the quantum of compensation to be paid by the assessee to the other party. The matter was referred to the arbitration for resolution of dispute. The Learned Arbitrator had given its award on 30.8.2005 based on the consent terms arrived by the parties to the dispute. Accordingly, the assessee paid Rs.64 Crores as compensation / damages to CALL. The assessee claimed deduction of the said amount however the Assessing Officer disallowed the claim of deduction for compensation paid to CALL while completing the assessment under Section 143(3) of the Income Tax Act, 1961 (in short 'the Act') on 28.12.2007. The assessee challenged the action of the Assessing Officer before the CIT (Appeals) but could not succeed. The matter was carried to the Tribunal in the first round of appeal and vide order dt.10.11.2010 in ITA No.406/Bang/2010, this Tribunal set aside the matter to the file of the Assessing Officer with the direction to examine the parties to the agreement and also to the Joint Development Agreement (JDA) and then decide the issue as per law. In the set aside

proceedings, the Assessing Officer repeated the disallowance of claim of Rs.64 Crores on account of compensation paid. The matter has again reached the Tribunal for adjudication.

4. Before us, the learned Authorised Representative of the assessee has submitted that the Assessing Officer has denied the claim particularly on three grounds viz.

(i) Agreements are entered into by **Shri P. Dayananda Pai** in his individual capacity and not on behalf of the assessee firm.

(ii) The property agreed to be sold did not belonging to the assessee and

(iii) The liability had not crystallised in the previous year relevant to the Assessment Year 2005-06.

5. As regards the first objection of the Assessing Officer that the Agreements were entered into by Shri P. Dayananda Pai in his individual capacity, the learned Authorised Representative of the assessee has submitted that all transactions of the assessee are entered in the name of Shri P. Dayananda Pai who is Managing Partner of the assessee-firm. The learned Authorised Representative has referred to an Agreement dt.15.05.2006 for sale of property for Rs.18.75 Crores entered into on the name of Shri P. Dayananda Pai and submitted that it is a routine

business practice of the assessee-firm to acquire and sale the properties through the agreement in the name of Shri P. Dayananda Pai. Thus the learned Authorised Representative of the assessee has submitted that the income arising from such transaction done through Shri P. Dayananda Pai in the earlier year i.e. Assessment Year 2004-05 has been offered to tax and accepted by the Assessing Officer while completing the assessment under Section 143(3) on 16.03.2005. He has also referred to the details of various transactions entered into in the name of Shri P. Dayananda Pai which has been recorded in the books of accounts of the assessee and the income from those transactions were offered to tax and accepted by the Assessing Officer. Thus the learned Authorised Representative has submitted that Shri P. Dayananda Pai and other partners as per prevailing business practice entered into agreements in their own names with the intention to acquire the properties for and on behalf of the assessee firm. The acts of Shri P. Dayananda Pai and other partners are with consent of all other partners and duly recorded in the books of accounts of the assessee. The learned Authorised Representative has referred to the balance sheet as on 31.3.2005 and Schedule showing property advances paid and submitted that profit

arising from these transactions are consistently shown in the accounts, return of income and Assessing Officer has been consistently accepted the same in the earlier assessment years as well as in the subsequent assessment years. He has referred to the assessment order passed under Section 143(3) for the Assessment Year 2004-05 as well as for the Assessment Year 2008-09 and submitted that the Assessing Officer has accepted the income offered to tax from such transaction of purchase and sale of the property in the name of Shri P. Dayananda Pai as well as other partners on behalf of the assessee. The Assessing Officer has recognized this practice in the assessment order passed for Assessment Year 2008-09. Thus the evidences accepted by the Assessing Officer clearly show that Shri P. Dayananda Pai had acquired rights in the properties and entered into formal agreement for and on behalf of the assessee although the documents pertaining to the properties are entered by Shri P. Dayananda Pai in his individual name. Thus the learned Authorised Representative has contended that the Assessing Officer having accepted the income arising from similar transactions in the hands of the assessee in the earlier and subsequent assessment years cannot treat the transaction entered into under identical manner

differently merely because the assessee had incurred loss therein.

Further the learned Authorised Representative has pointed out that the Tribunal in the set aside order had specifically directed the Assessing Officer to examine the parties to the agreement as well as to the JDA to find out the real nature of the transaction however the Assessing Officer did not carry out direction of the Tribunal to examine the parties. Therefore without examining the parties to the agreements the Assessing Officer cannot arrive at this conclusion regarding entity who had entered into the transaction merely based on surmises.

6. Qua the second objection of the Assessing Officer that properties did not belong to the assessee, the learned Authorised Representative of the assessee has submitted that the assessee identifies the land in and around Bangalore city belonging to various persons and acquire interest, rights and title over the properties without actually registering the title in its name. The assessee offered to tax the income arising from sale of such interest, rights and title over the properties. The assessee negotiates with the potential buyers and gets land / property directly to the buyers from the original land owners. For rendering of such service the assessee received substantial consideration as aggregator of land and

as a consenting party in the transfer and title deed. The assessee also acts as a venture capitalist contributes towards cost of the projects and creates rights, interest and title over the property. The advances paid to the property owners are shown as asset and advances received against the properties are shown as liability in the balance sheet. Thus the assessee need not to be the owner of the property and still enter into a contract with promoters to sell such property to deliver in future to the buyer of the property. The learned Authorised Representative of the assessee has pointed out that this nature of business of the assessee has been accepted by the department and particularly by the Assessing Officer for the Assessment Year 2008-09. It is clear from the Agreement dt.2.4.2002 that the assessee agreed to sale part of its rights and entitlement in the properties being developed by other developers. The financials of the assessee disclosed various properties owned by the assessee however these properties are not registered in the name of the assessee. He has referred to the balance sheet and other Schedules of assets and liabilities and submitted that the assessee has been showing rights in the properties in the accounts though the same are not registered in the name of the assessee. The income arising on the

transfer of these properties/rights therein has been consistently offered to tax by the assessee and the same has been assessed by the Assessing Officer. The acts done by Shri P. Dayananda Pai are for and on behalf of the assessee firm even as per the provisions of Sections 4, 14,18,19,20 and 22 of the Partnership Act. The payment of damages has been made during the course of business and to protect its goodwill by doing so the assessee has maintained its goodwill that it honours and maintains commitment in the property related matter which spill over several years and therefore inspires and enhance the customers of the assessee which is necessary for the purpose of business. In support of his contention he has relied upon the decision of Hon'ble Supreme Court in the case of **CIT Vs. Nainital Bank Limited** 62 ITR 638.

7. As regards the third objection of the Assessing Officer that the liability has not crystallized in the previous year relevant to the assessment year under consideration, the learned Authorised Representative has asserted that the claim of deduction is based on the principle of prudence and conservatism. He has contended that the assessee failed to deliver the property as on 31.3.2005. Therefore the default / failure occurred and consequently liability stood crystallized on

31.3.2005. Accordingly, the assessee claimed deduction in the Assessment Year 2005-06. The learned Authorised Representative has referred to the para 8.2 of the Accounting Standard 4 (AS-4) regarding contingencies and events occurring after the date of balance sheet and submitted that it provides need of adjustment to the assets and liabilities on account of the events occurring after the balance sheet date that provide additional information materially affecting the determination of amounts relating to condition existing at the balance sheet date. The assessee had liability of Rs.22 Crores prevailing as on the date of balance sheet i.e. 31.3.2005 which was insufficient. The assessee failed to deliver the property and it occurred liability to pay compensation of higher amount which stand corroborated by the award given subsequently to the date of balance sheet. Thus the learned Authorised Representative of the assessee has argued that as per AS-4, the assessee has correctly valued its liability based on the event occurred after the date of balance sheet. He has relied upon the following decisions :

(i) ACIT Vs. Allied Gems Corporation (Bombay) 163 ITR 56 (Bom)

(ii) Bharat Earth Movers Vs. CIT 245 ITR 428 (SC)

8. Alternatively the learned Authorised Representative of the assessee has submitted that in case the liability has not crystallized in the Assessment Year 2005-06 then the Assessing Officer may be directed to allow the deduction in Assessment Year 2006-07. The learned Authorised Representative has further pointed out that the amount of compensation received by the other party has been accepted by the Assessing Officer. In support of his contention, he has relied upon the following decisions :

- (i) Perfect Equipments Vs. DCIT 85 ITD 50 (AHD).
- (ii) Ajay Devagan Vs. Addl. CIT in ITA No.514/Mum/2007 dt.9.10.2009.
- (iii) JCIT Vs. Mukund Limited 291 ITR (AT) 249 (Mum) (SB)

9. As regards the other reasons assigned by the Assessing Officer in disallowing the claim of the assessee, the learned Authorised Representative of the assessee has submitted that for claiming the deduction as a business expenditure it need not be necessary there is yield of income from the project. The assessee was not developed any of the properties in question by itself and therefore yield of income from the projects is irrelevant in deciding the issue of allowing of deduction for compensation paid on account of breach of contract. The compensation paid for failure to transfer does not amount to buy back of such property

as observed by the Assessing Officer. The compensation is paid for relinquishment of right and not for purchase of constructed property. The transaction has been entered into with a third party at arm's length and therefore the same cannot be treated as a colourable transaction. The recipient of the compensation offered the amount to tax. The assessee has also offered income to tax arising from these projects. There is not even an allegation that the money has come back to the assessee. There is no evasion of tax and as such the transaction cannot be termed as colourable device. Even otherwise when the Assessing Officer has not given effect to the directions of the Tribunal then the order passed by the Assessing Officer is liable to be quashed/set aside on this ground alone. He has relied upon the following decisions :

I. Deepak Diwan Vs ITO 54 TTJ 567 (Del)

II. Ushdev International Limited Vs. JCIT (ITA No.1905/Mum/2013)

Thus it was prayed that disallowance made by the Assessing Officer of Rs.64.74 Crores be deleted.

10. On the other hand, the learned Departmental Representative has referred to the Agreement Dt.2.4.2002 and submitted that the second party invested a sum of Rs.22 Crores for the purchase of various

properties belonging to first party Shri P. Dayananda Pai but the fact remains that as on the date of agreement the first party was not having any ownership or right in the properties in question. In the year 2002, neither the assessee nor Shri P. Dayananda Pai was the owner of these properties or had any right in the properties in question. He has referred to revised agreement dt.10.3.2004 and submitted that the time period of handing over of the constructed portion to the second party was extended upto 10.3.2006 and prior to the expiry of the said extended time limit no damages can be claimed. Therefore the liabilities to pay any damages or compensation would not arise or crystallize before 10.03.2006 as extended time limit vide agreement dt.10.03.2004. The Assessing Officer has given an opportunity to the assessee and also considered the submissions of the assessee however the assessee failed to establish that it was the owner of the property or any right in the properties in question. The learned Departmental Representative has further contended that the Tribunal has clearly left the matter open to the Assessing Officer to complete the assessment as per law. The assessee has not brought any record to suggest that there was some information which the Assessing Officer has missed taking into account.

He has contended that liability was not crystallized during the year under consideration. He has relied upon the orders of the authorities below.

11. In rejoinder the learned Authorised Representative of the assessee has submitted that the payment to acquire the property was admittedly made by the assessee. One of the property was belonging to the sister concern and the assessee was having right in the built up area in the property. The time period to transfer the built up area was spread over to two years and not at the end of two years. The assessee has agreed to pay compensation because it was not possible for the assessee to honour the obligation of handing over the built up area by the end of the time period allowed.

12. We have considered the rival submissions as well as the relevant material on record. This is second round of appeal. In the first round, the Tribunal vide order dt.10.11.2010 remanded the matter to the file of the Assessing Officer for conduct of further enquiry / examination and reconsideration of the issue as directed in para 8 of the Tribunal as under :

“ 8. The other findings of the CIT (Appeals) was that the agreements were entered into by Shri Dayand Pai in his individual capacity and his name is mentioned as representative of the assessee firm only in the arbitration

award. On perusal of the copies of the said agreement dt.2.4.2002 and 4.6.2005, we find that the status of Shri Dayanand Pai, is in his capacity as individual and not in the capacity of the Managing Partner of the assessee firm. But, another point worth taking note of and cannot be ignored is that the assessee firm had received the sale consideration of Rs.22.00 Crores as reflected in its accounts and therefore, it is the case of the assessee that it is the beneficiary of the said agreement and therefore, will have to fulfill the liability of paying the compensation. The assessee firm has shown it as an advance in its books of accounts. This gives credence to the argument of the assessee that Shri Dayanand Pai being the sheet anchor of the group had entered into the agreement on behalf of the firm. We feel that some more factual findings are necessary in this regard. According to us, the Assessing Officer should have examined the other parties to the agreement i.e. M/s. MIPL and also M/s. Caraka Academy of Life Long Learning Pvt. Ltd., to find out the pith and substance of the agreements and not go by mere recitals in the agreements. Therefore, in the interest of justice, we deem it fit and proper to remand the issues to the file of the Assessing Officer with a direction to examine the parties to the agreements and also to examine the joint development agreements and to reconsider the issue in accordance with law. Needless to mention that the assessee shall be given a fair opportunity of hearing and the assessee also shall co-operate with the revenue authorities in speedy disposal of the case."

Thus it is clear that in the remand proceedings, the Assessing Officer was required to examine the parties to the agreement and also to examine the JDA. The Assessing Officer while passing the order dt.30.12.2011 in pursuant to the directions of the Tribunal has observed and held in paras 1.1, 2, 3 to 6 as under :

1.1 The AO disallowed the claim of the assessee to the extent of Rs.64.74 crores being compensation paid. The matter was confirmed by the CIT(A) and the assessee preferred further appeal before the ITAT. The ITAT, in its order dated 10.11.2010, in ITA No.406(BNG)/2010 has remanded the matter back to the file of the AO to decide it afresh with a direction to examine the other parties to the agreements (M/s. MIPL and also M/s. Caraka Academy of Lifelong Learning P.Ltd), to examine the joint development agreements to find out the pith and substance of the agreements.

2. During the course of remand proceedings, the assessee was called upon to submit the joint development agreement entered into by it with the four developers and builders viz. HM Constructions (two JDAs), M/s. Ittina / Sterling Developers and M/s. IBC Knowledge Park in support of its claim for acquisition of built up areas at various places, which in turn are the subject matter of the agreement dated 2.4.2002, between Sri P.Dayananda Pai and M/s. Manipal Infocom P.Ltd. (MIPL). In response, the assessee vide its letter dated 23.11.2011 submitted as follows with regard to each of the property :

..... The assessee represented by his partners, P.Dayananda Pai for its benefits entered into an agreement with Manipal Infocom Pvt. Ltd. on 2.4.2002 and copy of the agreement has already been filed. In terms of the same agreement, the assessee has offered built up area of the first party entitlement on the following four valuable properties being developed by various builders as shown below :

(i) JP Nagar Property :

In this regard, the assessee has submitted as under :

"In the land admeasuring 28 acres under group housing scheme in 8th Phase, JP Nagar, Bangalore where the First party in the agreement P. Dayananda Pai was entitled to get 6,00,000 sq. ft built up area along with undivided share in the land by way of residential apartments. P. Dayanada Pai had earlier entered into an agreement orally with Shivanis for the development of residential accommodation in Raghuvanpalya. Property which is evidence by written document executed between them on 19.3.2004, copy is enclosed as ANNEXURE-1. Before entering into a written agreement it was as early as orally agreed in January 2002 itself between the parties to develop the residential apartments as a venture "Global Associates" and to name the residential complex as "H.M. World City" although formal written agreement was entered in 2004. P.

Dayananda Pai based on this oral agreement entered into "Agree to sell" for the benefit of the firm portion of the built up area to Manipal Infocom Pvt. Ltd. ie. 1,00,000 sq. ft for a total consideration of Rs.7 Crores. Because of abnormal delay in M/s. HM Constructions giving the assessee's firm share of built up areas, P. Dayananda Pai could not deliver 1,00,000 sq.ft of built up areas in time to M/s. Manipal Infocom Pvt. Ltd. as they are not agreeable to wait for a longer time."

In support of the above claim, the assessee has produced two documents viz.

- (a) Deed of sale executed on 10.1.2005 between Mrs. K. Jeenabai and 10 others represented by their Attorney Holders, Mr.K.B.Lakshman and Mr. Ashwin Pai under registered Power of Attorney dated 6.10.2003 and three confirming parties (including Sri P.Dayananda Pai and Mr. K.B. Lakshman) in favour of M/s. Global Associates.
- (b) An agreement of venture executed on 19.3.2004 between Mr. P.Dayananda Pai on the first part and Mr. H.J.Siwani and Mr. M.J.Siwani on the second part.

The sale deed mentioned at (a) above, at para XXI at page 10, it is mentioned that the confirming party No.2, Mr. K.B.Lakshman not being desirous of taking conveyance of the said property agreed to assign his rights to the property to the confirming Party No.3 ie. Mr. P.Dayananda Pai, who has agreed to purchase the same property and paid to the confirming party No.2 the entire sale consideration which is inclusive of reimbursement of the amount paid by confirming party No.2 to confirming party no.1 and the vendors. Further, para XXII at page 11 of the sale deed mentions that "Whereas confirming party No.3 (Sri P.Dayananda Pai), who thus became entitled to take conveyance of the same property has contributed the same as his share of capital in the AOP together carrying on business under the name and style M/s. Global Associates (the purchaser herein)."

From the above narration in the sale deed, which is produced by the assessee in support of its claim for sale of built up area of 1,00,000 sq.ft to M/s. MIPL vide agreement dated 2.4.2002, it is seen that neither the assessee, M/s. CHDC nor its Managing Partner Mr.P.Dayananda Pai were the owners of the property on the date of the agreement dated 2.4.2002. To elaborate it further, as per the sale deed mentioned at (a) above, the confirming party No.2, Sri K.B.Lakshman came to be Attorney Holder for the vendors only on 6.10.2003 and confirming party no.3, Sri P.Dayananda Pai became entitled to take conveyance of the said property only on 10.1.2005 (ie. the date of the sale deed). This proves that the assessee was not the owner of the JP Nagar property of about 28 acres on the date of agreement dated 2.4.2002 offering to sell 1,00,000

sq.ft of built up area to M/s.MIPL. Further, as mentioned in the agreement dated 2.4.2002 at page-2, 3 and 4, there is no Joint Development Agreement with M/s. H.M. Constructions for delivery of 6,00,000 sq.ft of built up area to the assessee (M/s. CHDC or Sri P.Dayananda Pai) out of which assessee has offered 1,00,000 sq.ft to M/s. MIPL. Hence, no credibility can be given to the agreement dated 2.4.2002 which the assessee is claiming to be the base/ foundation for making the payment of compensation of Rs.64 crores in pursuance of the Arbitration Award dated 30.8.2005.

(ii) Airport Road Property (Pattandur Agrahara Property) :

In this regard, the assessee has submitted as under :

"The assessee firm had purchased properties through agreement in village called Pattandur Agrahara Village, KR Puram Hobli, Bangalore East Taluk, Bangalore District as early as 1995 when making initial payment of Rs.10 lakhs on 5.5.1995 and further payments were also made till August 1995 to the extent of Rs. 45 lakhs and the same is reflected in the books of the Assessee firm as property advances. In view of the certain acquisition proceedings P.Dayanada Pai approached KIADB to acquire the said land on mutual consent and allot the same to one of the group companies called Pai Electronic Systems Pvt. Ltd. wherein he is one of the Founder Directors or Director of the Company. As per his request and good office KIADB allotted the land for industrial use which was

confirmed later by handing over the possession to the said company vide possession certificate bearing No. KIADB/SUC-14586/815/2003-04 dated 24.6.2003. P.Dayanada Pai representing the firm had entered into agreement orally with HM Constructions for development of commercial space in the schedule property within the period of 24 months from the sanction of plans and shall be completed in all respect as per the specification agreed between the parties. After the allotment of the land by KIADB a formal joint development agreement dated 29.4.2005 ANNEXURE 11 was entered into against which the assessee firm through his group concern was entitled for 75,000 sq. ft of commercial space and the same was agreed to be sold for a consideration of Rs. 7.5 crores to Manipal group of companies.

M/s. HM Constructions were not able to get plan sanction for commercial building because the zoning regulations under the new CDP promulgated by BDA. Hence, the project is delayed and as on date also M/s. HM Constructions have not been able to obtain sanction of plans for commercial building. Hence the assessee firm are not able to give 75,000 sq.ft of commercial space in the project to Manipal Infocom Pvt. Ltd."

From the above submissions of the assessee it is clear that the property in question never belonged to the assessee or to Sri P.Dayananda Pai. From the Joint Development Agreement dated 29.4.2005, it is revealed that the property admeasuring 1 acre 39 guntas of industrial land was allotted to M/s. Pai Electronic Systems Pvt. Ltd. vide possession certificate dated 24/26/06/2003. It is astonishing to know from the said so called Joint Development Agreement dated 29.4.2005 that it nowhere mentions about the built up area to be handed over to M/s. Pai Electronic Systems Pvt. Ltd., except for the fact that the developer is entitled to 72% of the built up area and M/s. PESPL is entitled to 28%. It is revealed from the above facts that even M/s.PESPL was given possession of the property of 1.39 acres only on 24.6.2003, which is almost one and half years subsequent to the date of agreement offering the built up area to M/s. MIPL. Since this particular property was in the possession of KIADB, a Government Organization, till 24.6.2003, by no stretch of imagination, the assessee can say that they (although through another group concern) had authentic right over the property so that it can offer to sell the built up area to M/s. MIPL. Hence, these facts also support the view that the agreement dated 2.4.2002 is unbelievable.

(iii) **Brooke Fields Property :**

With regard to transaction in respect of this property, the assessee has submitted as follows :

" The assessee has one property about 5 Acres of land at Brooke Fields Road which was earlier given for joint development to M/s. Itina Developers wherein the assessee was to get 2,00,000 sq. ft of residential built up area along with undivided share in land cost in somewhere 2001 and 2002. Later the understanding reached with Itina Developers was canceled and the property later came to be given to Ms. Sterling Developers Pvt. Ltd. copy of the agreement entered into with them by our group concern called "Surya Builders and Developers" is enclosed herewith ANNEXURE-III to show that our group concern was having 5 acres 6 guntas of land in survey No. 9/2 and 10/1 at Kundanahalli, KR Puram, Bangalore Taluk near Brooke Fields compound. Thus, Surya Builders and Developers is a group company and investment in the said property is reflected in the balance sheet of Canara Housing Development Company. Out of the entitlement of 2,00,000 sq. ft P. Dyananda Pai agreed to sell area of 50,000 sq. ft at the rate of Rs.700 per sq. ft for a total consideration of Rs. 3.50 crores.

Manipal Inforcom Pvt. Ltd could not wait for the delay and hence withdrew the offer of assessee firm of buying 50,000 sq.ft of residential apartment."

The assessee has produced an agreement dated 17.2.2005 between Sri Ravindra Pai, son of Sri P.Dayananda Pai, Sri P.Ashwin Pai and Sri Dev S.Patel, partners representing M/s. Surya Builders and Developers and M/s. Sterling Developers Pvt. Ltd. for development of property situated at Kundanahalli Village, KR Puram Hobli, Bangalore East Taluk. M/s. Surya Builders and Developers is entitled to 34% of the built up area. It is pertinent to note here that

from the land records obtained from the Revenue Authorities, Sub-Registrar, KR Puram, it is observed that M/s. Surya Builders and Developers acquired this land only on 17.2.2004 which is almost two years subsequent to the agreement dated 2.4.2002 offering to sell the built up area to MIPL by the assessee. In the light of the above facts, it is noticed that the assessee or Mr. Dayananda Pai had no right of ownership on the above property at any point of time either before or after the agreement with M/s. Sterling. The assessee could not have made any sale agreement to sell a property over which it never had ownership at any point of time. Though, M/s. Surya Builders and Developers is one of the group concern

of the assessee, that itself acquired the land only on 17.2.2004 which is much later than the assessee's agreement dated 2.4.2002 with M/s. MIPL.

(iv) Bannerghatta Road Property (IBC Knowledge Park) :

In this regard, assessee's submission is as under :

"Similarly he had agreed to give 50,000 sq. ft built up area in IT Park being developed by IBC Knowledge Park on the joint development agreement entered into on 2002 by one of the group firms Bangalore Housing Development and Investments (M/s. BHD). The said firm had to receive minimum 4,00,000 sq. ft built up area from the developers IBC Knowledge Park. 2,00,000 sq. ft has been delivered by the developers and leased by them directly to Accenture on behalf of the owner of the land and out of the balance 2,00,000 sq. ft to be received by the firm, 50,000 sq. ft was traded for a total consideration of Rs. 4 crores ie. By P. Dayananda Pai on behalf of the Assessee firm as per the agreement dated 2002 ANNEXURE-IV. Since the developer did not give the possession of 2,00,000 sq.ft. The assessee firm could not honour its commitment of 50,000 sq. ft to Manipal Infocom Pvt.Ltd.

Further, the matter is in dispute even now before Tribunal for adjudication for delivery of 2,00,000 sq. ft of commercial built up area."

From the assessee's submission, the first and the foremost thing that is noticed is that the property in question is not owned by the assessee M/s. CHDC or Sri P. Dayananda Pai. The property is owned by M/s. BHDl, where, of course, Mr. P. Dayananda Pai is a partner along with others. Further, the Joint Development Agreement was entered only on 1.7.2002 ie. after the date of agreement between the assessee and M/s. MIPL. Here again, the assessee being not the owner, cannot agree to sell property belonging to some other entity, although it may be a group concern. It may also be mentioned that the assessee has not produced any kind of agreement or contract indicating any assignment of the right of M/s. BHDl in the property developed by M/s. IBC Knowledge Park in favour of the assessee or Mr. P. Dayananda Pai. Hence, it is clear that the

now settled the dispute and want an award on the basis of a compromise, it was not necessary to go into the question of nature of disputes between the parties. Hon'ble Arbitrator, by referring to Sections 30 & 31 of Arbitration and Conciliation Act, 1966, has accepted the compromise and Award is passed in terms of the compromise petition. The date of appointment of the Arbitrator is 27.6.2005, the date of filing of Claim Petition before the Arbitrator was on 11.7.2005, Compromise Settlement Petition was filed on 5.8.2005 and the final Arbitrator's Award based on the compromise was passed on 30.8.2005. From the sequence of events, it appears that the assessee along with M/s. MIPL have approached the Hon'ble Arbitrator with a predetermined purpose of getting the stamp of arbitration to their mutually agreed transaction and it is an act of colourable device to claim the expenditure by the assessee.

- (vi) This expenditure on account of compensation paid is not an expenditure for the purpose of the business of the assessee because it is connected with the properties which never formed part of the assessee's business transactions and the assessee was never the owner of the subject property.
- (vii) The expenditure on compensation payment can be claimed by the entity which owns the property and not by somebody else.

- (viii) In view of the fact that Arbitration Award between M/s. M/s Canara Housing Development Company. and Usha Beltron Ltd., Usha Martin Power Co. Ltd. and Mysore Cements was issued on 5.3.2001 ie. during F.Y.2000-01, relevant to the A.Y.2001-02, the same is not an allowable expenditure during the A.Y.2005-06. Hence, claim made by the assessee on account of compensation payment to these parties is not allowable.
- (ix) Without prejudice to the discussions and inferences drawn as above, it is also pertinent to mention here that the assessee is not entitled to claim this expenditure on account of payment of compensation in this assessment year, because of the following reasons :
- (a) The assessee was issued with a show-cause notice mentioning therein the chronology of events leading to the Arbitration Award. Basically, the Arbitration Award is dated 30.8.2005 and as such the claim of M/s. MIPL, if any, gets crystallized and becomes an ascertained liability for the assessee only in the F.Y.2005-06 relevant to A.Y.2006-07. The following sequence of events support this view.

assessee or Sri Dayananda Pai never had any right of ownership over the property which they can agree to transfer to M/s. MIPL.

3. From the facts narrated and discussed above, it is clear that the assessee's claim for expenditure incurred on payment of compensation to M/s. MIPL is not allowable, because of the following reasons :

- (i) The assessee was not the owner of or had any right of ownership over the properties as on the date of agreement ie. 2.4.2002 with M/s. MIPL.
- (ii) The assessee has not produced the original of the agreement dated 2.4.2002, though asked for. As per Sec.64 of Indian Evidence Act, documents must be proved by primary evidence.
- (iii) As per Sec.7 of the Transfer of Property Act, only a person competent to contract and entitled to the transferable property or authorized to dispose off the transferable property not his own, is competent to transfer such property In the case before us, the assessee was not the owner of the property which is the subject matter of transfer on the date when assessee entered into an agreement to sell them to M/s. MIPL.

- (iv) No person can transfer or agree to transfer a property which is neither owned by him nor has any right of ownership over that property enabling him to sell the same.
- (v) In the Arbitration Award, Hon'ble Arbitrator mentions that a claim petition was filed by the claimant claiming refund of amount and compensation and interest and the total claim is Rs.95 crores. It is also mentioned that respondent Sri P.Dayananda Pai, representing M/s. CHDC and M/s. BHDl has not yet filed the statement of defense and in the meantime, the parties to the petition reported that they have settled the dispute and a compromise petition duly signed by both the parties has been filed before him. In paragraph 2 of the Award, it is also mentioned that since the parties have

The Arbitrator was appointed on 27.6.2005, the claim petition by MIPL / CALL was filed on 11.7.2005 before the Arbitrator making a claim for Rs.95 crores, the Compromise Petition for settling the claim at Rs.86 crores was filed on 5.8.2005 and final Arbitration Award came on 30.8.2005.

In this regard, the assessee was asked to justify his why its claim should be allowed in the financial year ending 31.3.2005 relevant to A.Y.2005-06. In response, the assessee submitted as under :

"Though the period for completion and delivery of the constructed four properties was extended to 31.3.2006 (as stated in brief, but it is two years from 17.1.2004) since the project did not at all take off on one or other grounds as stated in para 7 above there was no reasonable prospect of the seller complying with the terms of the contract by 31.3.2006 having regard to the large size and the number of properties which were agreed to be delivered viz. (i) Property A 100,000 sq.ft in HM World City, (ii) Property B 75,000 sq.ft commercial space (iii) property C 50,000 sq.ft for residential apartments and (iv) Property D 50,000 sq. ft in IBC Knowledge Park. Furtehr Caraka Academy of Lifelong Learning P.Ltd. could not wait and has to seek alternate sources and therefore THE

REPAYMENT OF DEPOSIT AND THE COMPENSATION HAS BECOME INEVITABLE LIABILITY AS ON 31.3.2005. Since by quick turn of events the dispute arose and was referred to Arbitrator and the entire matter was settled within a short span of 5 months, the assessee, as a prudent business person had to provide for the compensation as awarded by the sole arbitrator on 30.8.2005. Under the Accounting Standard 29 para 36 any additional evidence provided by events after balance sheet could be taken into account."

4. The assessee has relied on the following decisions in support of its claim :
- (i) 299 ITR 1 : CIT Vs. Bilahari Investment P. Limited :

This case law is on the issue of contract method followed by the assessees and substituted by percentage of completion method by the AO and has no relevance with respect to the facts of this case.

- (ii) 297 ITR 176 (SC) in the case of Union Bank of India : This case law is on the issues of "deferred taxation" and is not applicable considering the facts of the case which is under consideration.
- (iii) 37 ITR 1 (SC) : Culcutta Co.Ltd. vs. CIT : This is on the issue of deciding the liability that had already accrued on the dates of the deeds of sale, though that liability was to be discharged at a future date. This is not relevant considering the facts of the present case.
- (iv) 73 ITR 53 : Metal Box Co. of India Ltd. Vs. Their workmen : This is on the issue of deciding the proof of correctness of depreciation. This is not relevant considering the facts of the present case.
- (v) 245 ITR 428 : Bharath Earth Movers Vs. CIT : This is on the issue of deciding the provision for encashment of accrued leave. It was claimed as a deduction. This is not relevant considering the facts of the present case.

5. In this connection, decision of the Kerala High Court in 182 ITR 175 in the case of Ashumá Cashew Company Vs Commissioner of Income Tax the Lordships have held that Liability to pay damages arises only on passing award by arbitrator and not on the date of breach of contract and further it has been held that Liability can be said to have crystallized only when the damages is determined and accepted by both the parties either by private negotiation or determined by an arbitrator or court. Finally, the Honourable High Court has further held that that enforceable liability can be deemed to come into existence only when it was determined and fixed by the arbitrators and not when the breach has occurred. This has been further confirmed by the Hon'ble Supreme Court.

5.1 The above referred decision clearly supports the fact that the liability of compensation payment has not come into existence and is not an allowable expenditure for the F.Y.2004-05 relevant to the A.Y.2005-06.

5.2 In view of the fact that in this case, Justice Sri G. Vidyathan has passed his arbitration award vide order dated 30.8.2005, which was subsequently modified on 10.10.2005 for correcting certain clerical mistakes during the financial year 2005-06 relevant to the assessment year 2006-07, without prejudice to the discussion on the issue of allowability of the compensation payment as an expenditure, this can not be allowed for the A.Y.2005-06 in view of the Rulings of the Court.

6. In view of the above discussions, claim of assessee on the issue of compensation payment amounting to Rs. 64,74,05,370/- is disallowed and added to the total taxable income of the assessee for the year relevant to the A.Y.2005-06.

(Addition made : Rs.64,74,05,370/-)

Loss declared by assessee		(-)61,11,28,165
Add: Compensation disallowed		64,74,05,370
Total Taxable Income		3,62,77,205
Tax thereon	1,26,97,020	
Add: S.C.@ 2.5%	3,17,426	
Education Cess @ 2%	2,60,289	
Total Tax		1,32,74,735
Add: Int. u/s.234B		91,59,543
Total Tax & Interest payable		2,24,34,278

It is manifest from the order of the Assessing Officer that he did not even take any step to examine the parties to the agreement. Thus it is a case of gross violation of directions of the Tribunal to examine parties to the agreement. It is pertinent to mention that the jurisdiction of the Assessing Officer and scope of remand proceedings cannot go beyond the directions of the remand order. It was not a open remand of the matter as contended by the learned Departmental Representative but the matter was remanded by the Tribunal with specific directions. Therefore the scope of the remand proceedings and the jurisdiction of the Assessing Officer was determined in the remand order itself. The Assessing Officer chose not to give effect to the specific directions of the Tribunal and therefore the order passed by the Assessing Officer is contrary to the directions of the Tribunal and also against the judicial discipline. Therefore the impugned order passed by the Assessing Officer

is liable to be quashed being not sustainable on this ground alone. A

similar view is taken by in the case of Deepak Deewan Vs. ITO (supra),

Delhi Bench of the Tribunal while dealing with an issue arising from the

order passed by the Assessing Officer in pursuant to the remand order by

the CIT (Appeals) has held in paras 5 to 7 as under :

“ 5. After recording these findings the Commissioner (Appeals) restored the matter to the file of the Assessing Officer on the limited point for making necessary investigation after giving the assessee due opportunity of being heard in the matter.

6. Whereas the Commissioner (Appeals) did ask the Assessing Officer to make further enquiry and investigation and record a finding, certain aspects of the matter as have been highlighted above had been decided by him. Revenue did not challenge the order of the Commissioner (Appeals). Therefore, these findings have become final. When we see the order of the Assessing Officer and that of the appellate authority in the second round, we do not find any fresh material having been collected by the Assessing Officer for taking a different view. The only enquiry made by the Assessing Officer after the matter was set aside was regarding Shri Sachdeva. As is clear from the records, the Assessing Officer has not been able to enforce the attendance of Shri Sachdeva. No other material against the assessee has been collected in the second round of the proceedings. As such the addition of Rs. 10 lakhs made by the Assessing Officer is unwarranted.

7. We do not know what would have been the fate of the findings of the Commissioner (Appeals) in his appellate order dated 3rd January, 1989 if these were challenged before the Tribunal. However once these findings have not been challenged, the Assessing Officer while making the fresh assessment cannot ignore those findings as these have become final. We are, therefore, making ourselves very clear that we are not subscribing to the view of the Commissioner (Appeals) in his appellate order dated 3rd January, 1989 but since the present appeal arises out of order of the Assessing Officer passed as a result of the first appellate order, we are bound to hold that the Assessing Officer was legally bound to act upon the findings of the first appellate authority. The Revenue not having established the case as perceived by the Commissioner (Appeals) vide order dated 3rd January, 1989, the addition of Rs. 10 lakhs, in our view, could not be repeated. The addition is accordingly deleted.ò

Accordingly, in view of the above discussion, we set aside the impugned order dt.30.12.2011 passed by the Assessing Officer qua this issue being not sustainable.

ON MERITS

13. One of the objections of the Assessing Officer to deny the claim of deduction on account of compensation paid is that the assessee was not the owner of the property in question at the time of Agreement dt.2.4.2002. This objection of the Assessing Officer is based on the fact that the JDA in respect of the properties in question were on subsequent dates and not prior to the Agreement dt.2.4.2002. It is pertinent to note that the particulars of the properties to be developed and constructed area to be given to **M/s. Manipal Infocom Pvt. Ltd. (MIPL)** have been specifically mentioned in the said agreement dt.2.4.2002. At this stage the relevant part of the recital as well as terms & conditions of the Agreement dt.2.4.2002 are reproduced below :

AND WHEREAS the Second Party is desirous of acquiring residential and commercial buildings in view of contemplated business expansions in various parts of the City and Second party having come to know that the First party is having rich experience in acquisition of land and developing them through Joint agreement activity and relying upon such experience is entering into agreement depositing huge amounts.

AND WHEREAS the Second party has decided to invest a sum of Rs.22.00 Crores (Rupees Twenty Two Crores only) with the First party for the purchase of various properties belonging to the First party.

AND WHEREAS the First Party being in control of vast valuable Real Estate in Bangalore City and has entered into arrangements to jointly develop some of the properties with various reputed Builders.

AND WHEREAS the First party has now offered to the Second party portions of the builtup areas out of the First party's entitlement in following four valuable properties being developed by various Builders and considered to be good investment.

- a) In the land admeasuring 28 Acres for a Group Housing Scheme in 8th Phase, J.P.Nagar, Bangalore, wherein as per the Joint Development Arrangement, the First party is entitled to get free of cost about 6,00,000 sq.ft. of builtup area together with proportionate undivided share in the land by way of Residential Apartments.
- b) The First party has entered into an arrangement to jointly develop 16 Acres of prime commercial land situated on the present Airport Road with M/s.H.M.Constructions under which the First Party is entitled to get builtup area of 3,25,000 sq.ft. of commercial space together with proportionate undivided share in the land in the proposed I.T. Park.

- c) The First Party has given a property with an extent of about 5 Acres on Brooke Field Road near the present Airport Road to one of the leading Apartment Builders namely M/s. Ittina Land Developers for jointly developing the property and under this Arrangement, the First is entitled to get approximately 2,00,000 sq.ft. of residential builtup area together with proportionate undivided share in the land free of cost.

AND WHEREAS the First Party has now offered to the Second Party the following builtup areas in three of the above mentioned properties at the selling rates for the respective items.

- a) 1,00,000 sq. ft. of residential builtup apartments at 8th Phase, J.P.Nagar, BANGALORE, at the rate of Rs.700/- psf amounting o Rs.7.00 Crores.
- b) An area of 75,000 sq.ft. of commercial space in the proposed I.T. Park on the present main Airport Road at rate of Rs.1,000/- psf amount to Rs.7.50 Crores.
- c) An area of 50,000 sq.ft. by way of Residential Apartment on Brooke Field Road at the rate of Rs.700/- psf amount to Rs.3.50 Crores.

AND WHEREAS the First Party is a partner along with his brother in M/s. Bangalore Housing Development and Investments, which owns the property bearing Corporation No.4/1, Bannerghatta Road, BANGALORE. M/s India Builders Corporation is setting up an I.T. Park in this property and the First party is entitled for 31% of builtup area out of which the First Party is offering to sell to the Second Party 50,000 sq.ft. of builtup area for a lumpsum amount of Rs.4.00 Crores.

AND WHEREAS the Second party has accepted the offer of the First Party to purchase the builtup Areas in the four above mentioned properties that are being developed at the rate offered by the First Party and has agreed to invest Rs.22.00 Crores (Rupees Twenty Two Crores only) with the First Party.

AND WHEREAS the First party having understood the necessity of the Second party possessing the completed building at the earliest and the time being the essence of the agreement and the First party having assured the Second party that it will complete the construction and hand over the possession on or before 31st March 2005 failing which the First party will

refund the deposit with additional compensation to enable the Second party to acquire similar buildings.

- 1) The First Party has offered to sell the following builtup areas in 4 of the properties owned by the First Party at the rate mentioned hereunder in consideration of the investment made by the Second Party.

- a) Property in 8th Phase, J.P.Nagar, Bangalore to be developed by M/s.H.M.Constructions, the builtup area being offered is 1,00,000 sq.ft. at the rate of Rs.700/- psf amounting to Rs.7.00 Crores.
- b) An area of 75,000 sq.ft. of commercial space in the property situated on the main Airport Road to be jointly developed by M/s H.M.Constructions at the rate of Rs.1,000/- psf amounting to Rs.7.50 Crores.
- c) An area of 50,000 sq.ft. of residential Apartments to be developed by M/s Ettina Land Developers, situated on Brooke Field Road, near the Airport Road at the rate of Rs.700/- psf amounting to Rs.3.50 Crores.
- d) 50,000 sq.ft. of commercial builtup area in the land bearing Corporation No.4/1, owned by the First Party and development made by M/s India Builders Corporation, known as M/s IBC Knowledge Park at a lumpsum amount of Rs.4.00 Crores.

Thus the total sale consideration amount for all the above 4 properties comes to Rs.22.00 Crores. And the Second Party considering these investments as attractive has agreed to purchase the above 4 properties for a total sale consideration amount of Rs.22.00 Crores.

- 2) The Second Party has paid a sum of Rs.22.00 Crores (Rupees Twenty Two Crores only) through cheque No.761986, dated 01/04/2002, drawn on ICICI Bank, to the First Party, drawn in favour of the First party, the receipt of this the First Party acknowledges herewith at the time of signing this Sale agreement in quittance of full and final agreed sale consideration amount.
- 3) The First party undertakes to give all the connected Title Deeds, Legal Opinions, Sanctioned plan etc., in respect of each of the property within 30 days from now.
- 4) The First Party undertakes to get a confirmation letter from all the Builders confirming and agreeing to deliver this builtup areas directly to Second party on completion of the respective projects.

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9) The First party agrees that if the Second party comes to the decision that it will be impossible to complete the building before the due date based on the status of the project found on inspection undertaken by the Second party then it can terminate the agreement and claim for the refund of consideration and compensation.

10) For any of the breaches committed by either party, the party in default shall make good for all the losses and consequential damages suffered by the other without prejudice to the right of each party to sue the other for specific performance of this contract.

11) The First party agrees hereby that in case the project is not completed before the due date the Second party can terminate the agreement. If the First party communicates its inability to complete due to reasons beyond its control then the Second Party can at its sole discretion grant further time or can terminate the agreement and the First party shall repay the consideration together with interest calculated at the rate of 20% per annum from the date of payment by the Second party to the date of return. The First party shall indemnify the Second party the cost and expenses to be incurred in acquiring similar property.

12) That all disputes and differences which shall arise between the parties hereto, in any matter shall be referred to arbitration by a sole Arbitrator to be appointed by mutual consent and shall be decided in accordance with the prevailing Arbitration Act.

14. Thus the properties to be developed and built up area in those properties to be transferred by the assessee to the other party were duly identified in the said agreement dt.2.4.2002. The assessee agreed to deliver the constructed area in the projects in future and within the time period as provided in the agreement. The parties to the agreement had no doubt and ambiguity about the properties to be developed under JDA

and therefore the question of having the ownership of the property at the time of agreement does not arise. The assessee produced all the JDAs in respect of the properties in question and therefore the assessee acquired rights in these properties and particularly in the constructed area of the properties through the JDAs and part of which was to be transferred to MIPL / MULPL / CALL. Therefore the properties which are particularly lands were identified by the assessee for development through the other developers under the JDAs then the registration of the ownership of the property is not a pre-requisite condition for acquiring interest, right and title in the constructed area of the property is being developed under JDAs. There is no embargo for entering into a contract for performance of one part in future. The properties were very much in existent at the time of agreement as specified in the agreement itself and it was the intention of the parties to the agreement to have share in the constructed area of the properties to be developed in future. The assessee being in the business of real estate for several decades and derived income from various land deals, including selling of rights over certain properties as well as interest and share over the land which were created by way of agreement, token receipts, Memorandum of

Understanding without actually registering the property in its name, had entered into the agreement which is part of the normal business activity of the assessee. The validity and enforceability of agreement dt.2.4.2002 as well as the revised agreement dt.10.3.2004 cannot be questioned on the basis that the assessee was not the registered owner of the property when it was clear to the parties to the agreement that these properties would be developed in future under JDA and therefore they will receive the constructed area as per the agreement. Accordingly we do not find any substance or merit in this object of the A.O./CIT (Appeals).

15. As regards the agreement was entered into by Shri P. Dayananda Pai and not by the assessee firm or for or on behalf of the assessee firm it is worth noting that the transaction of receipt of Rs.22 Crores being advance from MIPL / MULPL was duly recorded in the books of accounts of the assessee partnership firm. The amount of advance was shown in the balance sheet as on 31.3.2003 as well as in subsequent balance sheets which have been placed at pages 113 to 159 of the paper book. Further this is not an isolated transaction carried out through Shri P. Dayananda Pai but it is a regular practice of the assessee to purchase and sell the property through Shri P. Dayananda Pai. All other

transactions of purchase and sale have been accepted by the Assessing Officer. For the Assessment Years 2004-05 and 2008-09, the Assessing Officer has accepted the income from the transaction of purchase and sale of property through Shri P. Dayananda Pai and therefore this practice of the assessee partnership firm of doing the transaction through Shri P. Dayananda Pai was very well recognized and accepted by the Assessing Officer except this particular transaction where the assessee paid the compensation to the other party. Once the transactions are recorded in the books of accounts of the assessee partnership firm and the receipt and payment in respect of the purchase and sale of the properties are made by the assessee firm then it is a clear case of mutual understanding and consent between the partners of the assessee firm as well as the parties to the transaction that Shri P. Dayananda Pai acted on behalf of the assessee partnership firm and not in his personal individual capacity. Section 14 of the Partnership Act deal with the property belong to the partnership firm if rights and interests in the property originally brought into the stock of the firm. For ready reference, we quote Section 14 of the Partnership Act, 1932 as under :

“14. The property of the firm. --- Subject to contract between the partners, the property of the firm includes all property and rights and interests in property originally brought into the stock of the firm, or acquired, by purchase or otherwise, by or for the firm, or for the purposes and in the course of the business of the firm, and includes also the goodwill of the business.”

Therefore the provisions of Partnership Act also permits the property to be recognized as of the firm if brought into the stock of the firm. In the case on hand when the transaction is recorded in the books of accounts of the firm and the right and interest in the properties was included in the stock of the firm then, the question of ownership in respect of the said property does not arise. Similar transaction of purchase of rights in the property and sale of the same through the agreement entered into by Shri P. Dayananda Pai has been accepted by the Assessing Officer as the income arising from the similar transaction has been accepted in the hand of the partnership firm in the earlier year i.e. Assessment Year 2004-05 as well as in the subsequent year i.e. Assessment Year 2008-09. We find that in the books of accounts the assessee used to disclose various properties owned by the assessee though these properties are not registered in the name of the assessee firm. The Assessing Officer has not questioned all these transactions as shown in the books of

accounts for the Assessment Years 2003-04, 2004-05 and 2005-06 except for the year under consideration and particularly one transaction in respect of the assessee paid compensation to the other party. The income arising on sale / transfer of the property / rights have been regularly offered to tax and the same has been assessed by the Assessing Officer. Therefore acquiring the rights, interest and title over the property without registering to its name is the normal and regular business activity of the assessee. This fact has been acknowledged by the Assessing Officer in the assessment order dt.30.12.2010 for the Assessment Year 2008-09 as under :

4. Nature of business transactions:

The assessee is into the real estate business for several decades and this is one of the flagship concerns of Shri.Dayanand Pai group, popularly called as "Century Group". The assessee firm derives income from various land deals including the selling of rights over certain properties. The assessee sells land as well

as the rights, interest and share over the lands which were created by way of agreements, token receipts, Memorandum of understandings, etc.,

The assessee identifies agricultural/converted lands in and around Bangalore City, which are located as contiguous parcels belonging to various persons, and gets the land transferred either to its name or to its nominees. Further, the assessee identifies potential buyers and enters into Memorandum of Understanding and sells them directly. The assessee enters into agreements with land owners and creates interest, right and title over the properties without getting it actually registered to its name/nominees. After acquiring the rights over the properties, the assessee negotiates with potential buyers and gets the land transferred directly to the buyers from the original land owners. For this service the assessee receives substantial consideration as an aggregator of land and as a consenting party in the transfer and title deeds. In this process, the buyers are either identified by the assessee or by the land owners.

The assessee further acts as a venture capitalist in real estate transactions. He contributes towards the initial cost of the real estate project done by other real estate agents. This is usually a property advance to be paid to the land owners in the initial stage; by contributing towards the cost of the project, the assessee creates rights, interest and title over such properties. When the property is sold by the concerned persons, the assessee gets substantial share of profit from such projects. Literally, the assessee acts as a venture capitalist with substantial margin of profit.

The assessee received huge property advances and the same are reflected as a liability in the Balance Sheet. At the same time, the assessee pays huge property advances to the owners of the land and the same are reflected as assets in the Balance Sheet. A few of such liabilities are shown as long standing liabilities for several years. A detailed analysis of the above liabilities has been made during the course of scrutiny assessment proceedings. This is described in detail in the following paras. Before giving the description of the findings, related to each such liability, it is worthwhile to mention the nature of accounting treatment given by the assessee for the transactions entered into by him, since it has a bearing on the taxability or otherwise of the receipts.

The assessee enters into various projects with one party and the receipts and payments made to the concerned party are not classified project-wise. There is no distinction between the projects and from records it was observed that the project-

wise entries were not maintained. The transactions have been accounted party-wise/entity-wise whereas the project-wise entries of receipts and payments were not maintained. When the advance receipts for a particular project accrue as a sale, on completion of the transaction and on transfer of the title deeds from the seller to the buyer, instead of reflecting sales and purchases in the P & L account, the assessee reflects the same as liabilities and assets in the Balance sheet indefinitely. The assessee is consistently following the mercantile system of accounting, as seen from the 3CD report annexed to the return of income.

Thus the advance paid to the property owners are shown as assets in the balance sheet and advance received from purchaser of the property / rights are shown as liabilities in the balance sheet. On completion of the actual transfer the said advances converted to income or expenditure as the case may be. Therefore in view of the facts and circumstances of the case as well as above discussion, we are of the considered opinion that the transactions in question under the Agreement dt.2.4.2002 are in the normal course of business of the assessee through its Principal Partner by Shri P. Dayananda Pai and therefore all these transactions were duly recorded in the books of accounts of the assessee then the genuineness of the transaction cannot be questioned merely on the ground that the properties were not registered in the name of the assessee or the Agreements were executed by Shri P. Dayananda Pai.

CRYSTALLISATION OF LIABILITY

16. The Assessing Officer has held that as per the Revised Agreement dt.10.03.2004 the assessee was to deliver the constructed area within two years and therefore the liability to pay the compensation would not arise prior to 10.03.2006. Hence the Assessing Officer was of the view that the liability has not been crystallized during the year under consideration. As per the terms of the Revised Agreement dt.10.03.2004, the assessee was required to deliver the property during the extended period of two years. The relevant part of recital and clauses of the Agreement dt.10.03.2004 are reproduced as under :

.....

AND WHEREAS the First Party has now offered to the Second Party the following builtup areas in three of the above Joint Development Agreement at the selling rates for the respective items.

a) 1,00,000 sq.ft. of residential builtup Apartments at 8th Phase, J.P.Nagar, Bangalore, at the rate of Rs.700/- psf amounting to Rs.7.00 Crores.

b) An area of 75,000 sq.ft. of commercial space in the proposed I.T. Park on the present main Airport Road at rate of Rs.1,000/- psf amounting to Rs.7.50 Crores.

c) An area of 50,000 sq.ft. by way of Residential Apartment on Brooke Field Road at the rate of Rs.700/- psf amounting to Rs.3.50 Crores.

AND WHEREAS the First Party is a Partner along with his brother in M/s.Bangalore Housing Development and Investments, which owns the property bearing Corporation No.4/1, Bannerghatta Road, Bangalore. M/s.India Builders Corporation is setting up an I.T. Park in this property and the First Party is entitled for 50,000 sq.ft. of builtup area, which the First Party is offering to sell to the Second Party for a lumpsum amount of Rs.4.00 Crores.

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3) The First Party undertakes to give all the connected Title Deeds, Legal Opinions, Santioned plan etc., in respect of each of the property within 30 days from now.

4) The First Party undertakes to get a confirmation letter from all the Builders confirming and agreeing to deliver this builtup areas directly to Second Party on completion of the respective projects.

5) The First Party assures that all the completed builtup areas with Occupany Certificate for all the above 4 properteis within a spread over period of 2 years from now.

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12. For any of the breaches committed by either party, the party in default shall make good for all the losses and consequential damages suffered by the other without prejudice to the right of each party to sue the other for specific performance of this contract.

The assessee agreed to give the other party specified area in four properties for a consideration of Rs.22 Crores already received in advance by the assessee at the time of original Agreement dt.2.4.2002.

As per Clause 5 of the revised agreement the assessee undertook to provide built up area with occupancy certificate within a spread over period of two years from the date of agreement. Failing which the assessee would be liable to make good for all losses and damages to the other party as provided in Clause 12 of the Agreement.

16. The objection of the department is that the time period for delivery of the constructed area was to expire on 10.03.2006 and therefore liability was not crystallized as on 31.3.2005. It is pertinent to note that it is not a case of sale of good but it is an agreement for transfer of constructed area in the project to be constructed under JDAs. Therefore it depends on the progress of the work of construction and very well be judged in advance whether the assessee would be able to fulfill its commitment / obligation within the time limit as provided in the agreement. Thus when the assessee realized that the status of the construction of the project under JDA has not reached to the stage as expected and therefore it was not at all possible to deliver the completed property to the other party within the time limit then the assessee is free to take a decision to protect its business interest and minimize the losses which would be suffered by it in future. Though the event of final amount of compensation happened after closing of Financial Year under consideration however, as per the prudent and conservative accounting principle such contingencies are to be taken into account even after the date of balance sheet. As per para 8.2 of AS-4, the adjustment to the

assets and liability are required for the events occurring after the balance sheet date. Such events have been defined in para 3.2 of AS-4 as under :

“3.2 Events occurring after the balance sheet date are those significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statements are approved by the Board of Directors in the case of a company, and, by the corresponding approving authority in the case of any other entity.”

Therefore the loss due to the event took place after the date of balance sheet could be allowed while computing the income for the relevant assessment year. Section 145(2) provides that the Central Govt. may notify in the official Gazette from time to time the accounting standards to be followed by any class of assessee or in respect of any class of income. The amended provisions of section 145(2) elaborate the requirement of accounting standards to be followed for computation of taxable income. Therefore, the accounting standards notified under section 145(2) of IT Act are to be followed for computation of income and disclosure of information by any class of assessee or any class of income. The standards for income computation and disclosure of information as notified under section 145(2) of the Act are not meant for maintenance of books of accounts but are to be followed for

computation of income and disclosure of information for the purpose of assessment to tax. Events occurring after balance sheet date might confirm the state of affairs on the balance sheet date and therefore to deal with such situation AS4 permits adjustment of assets and liabilities at the balance sheet date if events occurring after the balance sheet date confirm the conditions existing on balance sheet date. The concept/rule of taxing the real income and not merely on the basis of book entries has been laid down by Hon'ble Supreme Court in the following decisions:

- i) CIT v. Shoorji Vallabhdas & Co. (1962) 46 ITR 144 (SC)
- ii) CIT v. Birla Gwalior (P) Ltd. (1973) 89 ITR 266 (SC)
- iii) Godhra Electricity Co. Ltd. V. CIT (1998) 225 ITR 746 (SC)

The Hon'ble Supreme Court again in case of **Sutlej Cotton Mills v. CIT** 116 ITR 1 held that the entries in the books of accounts are not conclusive of matter if the same are not in conformity with the accounting principles. What is required is the true nature of the transaction and whether it has resulted in profit or loss to the assessee. Therefore, it is settled proposition that regardless of entries in the books of accounts taxability of income or transaction is always based on the provisions of Act, substance which brings the true state of affairs and financial results. If a

transaction, treatment and claim of the assessee is legal, valid and Bona

Fide then the same has to be accepted. The Mumbai Bench of the

Tribunal in the case of **ACIT Vs. Applied Gems Corporation (Bombay)**

163 ITD 56 (Bom) while dealing with an identical issue has held in para

4.4 as under :

“ **4.4** We have carefully considered the rival submissions. It is quite well understood that section 4 of the Act, charges income tax in respect of the total income of a previous year relevant to the concerned assessment year. Section -5 of the Act, prescribes the scope of total income and so far as we are concerned, the dispute relates to the income chargeable under the head 'profits and gains of business or profession'; which is liable to be computed in accordance with the methodology prescribed in section 145(1) of the Act i.e. either in terms of cash or mercantile system of accounting regularly employed by the assessee. Sub-section (2) of section 145 empowers the Central Government to notify Accounting Standards for any class of assessee or in respect of any class of income. In the present case, assessee firm has maintained its accounts on mercantile system and while computing income for the year under consideration, it claimed deduction for a sum of Rs. 49,64,937/- representing loss on short realization of export proceeds, which were outstanding as on 31/3/2009, of course, short realization having taken place in the subsequent period. The claim of the assessee is that the mercantile system of accounting adopted by the assessee justifies such adjustment and for that matter, reference is made to the principle of prudence, which has been emphasized in the Accounting Standard -1 notified under section 145(2) of the Act also. The principle of prudence seeks to ensure that provision ought to be made for all known liabilities and losses even though there may remain some uncertainty with its determination. So however, it has to be appreciated that what the principle of prudence signifies is that the probable losses should be immediately recognized. In the present context, the stand of the assessee is that though realization of export receivables took place in the subsequent period, but the loss could be accounted for in the instant year itself as it would be prudent in order to reflect the correct financial results. Factually speaking, Revenue does not dispute the short realization from debtors to the extent of Rs. 49,64,937/- and, therefore, insofar as the quantification of the loss is concerned, the claim of the assessee cannot be assailed on grounds of uncertainty. Therefore, assessee is justified in determination of such loss on the basis of actual figures which were available while assessing its income in the instant assessment year. In the case of *U.B.S. Publishers and Distributors (supra)*, which has been relied upon before us, the issue relates to the assessment year 1967-68 (previous year ending on 31/05/1966). In the assessment proceedings, it was found that

assessee therein had claimed an expenditure by way of purchases of a sum of Rs. 6,39,124/- representing additional liability towards foreign suppliers in respect of books imported on credit up to the end of 31/05/1966. The said additional claim was based on account of devaluation of Indian currency, which had taken place on 06/06/1966 i.e. after the close of the accounting year. Such a claim was disallowed on the ground that it did not pertain to the previous year ending 31/5/1966 and that the event of devaluation had taken place only on 06/06/1966, which was after the close of the accounting period. The claim of the Assessing Officer was that since assessee was maintaining its accounts on mercantile system, the liability on account of devaluation of the Indian currency could not be said to have accrued during the accounting period ending on 31/5/1966 as devaluation took place after the end of the accounting period. The Tribunal allowed the claim of the assessee holding that though devaluation of Indian currency took place after the end of the previous year, but assessee was justified in determining his liability on the basis of the actual figures available when accounts for that year were yet not finalized. The Hon'ble Allahabad High Court affirmed the decision of the Tribunal and noted that liability to pay in foreign exchange accrued with the import of books and was not as a result of devaluation. According to the High Court, since the actual figure of loss on account of devaluation was available when the accounts for 31/5/1966 ending were finalized, the same was an allowable deduction in assessment year 1967-68 itself. The parity of reasoning laid down by the Hon'ble Allahabad High Court is squarely applicable in the present case also. In the present case, short realization of export proceeds to the extent of Rs. 49,64,937/-, took place in next year but it related to export receivable for the instant year, and at the time of finalization of accounts for the instant year, the actual figure was available, and therefore, assessee made no mistake in considering it for the purposes of arriving at the taxable income."

Thus it is held that the principle of prudence seeks to ensure that provision ought to be made for all known liability and losses even though may remain some uncertainty with its determination. The claim of damages and compensation was made by the other party to the agreement vide claim statement dt.11.07.2005. The dispute was referred to the sole arbitrator. The basis of the claim was the Fair Market Price of the area to be delivered by the assessee to the other party. The assessee never disputed the liability but only the quantum

was to be determined through the arbitration. Therefore the liability was already in existence in terms of the agreement between the parties that in the event of failure to deliver the completed constructed area, the assessee would be liable to make good of the losses and damages to the other party. Even otherwise right from beginning the advance received by the assessee has been shown as liability in the books of accounts. The liability to pay the compensation and damages is also a certain liability as per the terms and conditions of the agreement between the parties though the quantum was to be determined through arbitration. In the case on hand, the failure of the assessee to fulfill its obligation is in the nature of default of business obligation and therefore the compensation payable / paid by the assessee would become an allowable claim being the business loss / expenses in order to carry out their business / obligation and therefore the said claim of deduction is in the revenue field.

18. Though the Assessing Officer has questioned the manner in which the Arbitration Award has been passed on the basis of mutual consent of the parties however, it is pertinent to note that when the compensation is determined between the parties as per the fair market price as on the

date then merely because the assessee agreed to settle the dispute by mutual compromised terms cannot be a reason of doubting the genuineness of the claim. Further the actual payment of the compensation has not been disputed therefore, when the assessee has realized in definite terms that it would not be possible for it to honour the commitment and obligation under the agreement then the liability arises under the agreement is a certain liability though the quantum of the same could have been determined subsequently. The Assessing Officer has relied upon the decision of Hon'ble Kerala High Court in the case of **Asuma Cashew Company Vs. CIT** 162 ITR 175 however, we find that the dispute in the said case was liability to pay damages as determined by the Arbitration was held to be crystallized on the date of Award because in that case the assessee denied its liability to pay the damages and it was only because of the arbitration award the assessee recognize the same. Whereas in the case on hand, the assessee did not dispute the liability to pay the compensation in the event of failure on the part of assessee to honour its obligation. Therefore the liability to pay the compensation was never disputed by the assessee, only the quantum was settled through Arbitration. Accordingly in view of the

above discussion, we hold that the liability to pay the compensation was crystallized when the assessee accepted its failure to perform its part under the agreement within the stipulated time period and thus determination of compensation after the balance sheet date has to be taken into account in view of the principle of prudence and conservatism accounting as provided under AS-4. Hence we decide this issue in favour of the assessee and allow the claim.

19. The Assessing Officer has raised certain other objections regarding the property has not started yielding income and the transaction is a colourable device however we find that yielding of income is not a pre-condition for allowance of deduction when this particular transaction is only a part of a regular business activities of the assessee. It is not the case of the Assessing Officer that the business of the assessee has not established or commenced but the objection of the Assessing Officer is restricted to the point that this particular transaction has not started yielding income. We are of the view that the business activity of assessee comprises all the transactions and therefore a particular transaction or deal which is only a part of the regular business activity need not start yielding income for allowing the claim in question.

Further when the transaction is not between the related parties and it is not the case of the Assessing Officer that the money has come back to the assessee then the said transaction of payment of compensation as per the outcome of the Arbitration Award cannot be held as a colourable device. The recipient of the compensation has considered this amount for the purpose of income chargeable to tax. Hence the objections of the Assessing Officer are without any legal material or basis. The assessee has offered the income arising from the project in question to tax and therefore the transaction of development of properties in question cannot be held as a bogus or colourable device.

20. To conclude the orders of the authorities below are set aside qua this issue and the claim of the assessee is allowed. Since we have allowed the claim of the assessee for the assessment year under consideration therefore the alternate plea raised by the assessee becomes infructuous.

21. In the result, the appeal of the assessee is allowed.
Order pronounced in the open court on the 12th day of May, 2017.

Sd/-
(INTURI RAMA RAO)
Accountant Member

Sd/-
(VIJAY PAL RAO)
Judicial Member

Bangalore, Dt.12.05.2017.

*Reddy gp