

ITA Nos. 3622/D/95, 2546/D/01, 3233/D/01, 267/D/03, 4986/D/03

**IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCHES: “B”: “SPECIAL BENCH” NEW DELHI**

**BEFORE SHRI I.P. BANSAL, JUDICIAL MEMBER
AND
SHRI C.L. SETHI, JUDICIAL MEMBER
AND
SHRI DEEPAK R. SHAH, ACCOUNTANT MEMBER**

ITA No. 3622/Del/1995
Assessment Year: 1992-93

ITA No. 2546/Del/2001
Assessment Year: 1997-98

ITA No. 3233/Del/2001
Assessment Year: 1998-99

ITA no. 267/Del/2003
Assessment Year: 1999-2000
and
ITA No. 4986/Del/2003
Assessment Year: 2000-01

**DLF Universal Limited,
DLF Centre, 9th Floor,
Sansad Marg, New Delhi**

**Dy. Commissioner of Income Tax,
Vs. Special Range (Cent.) – I,
Mayur Bhawan, New Delhi**

(Appellant)

(Respondent)

**Assessee By: Shri Pradeep Dinodia, FCA
Shri R.K. Kapoor and
Shri S.K. Sharma, ARs**

**Respondent By: Shri N.P. Swahney, Sr. Standing Counsel
and Shri Prakash Yadav, Jr. Standing Counsel**

ORDER

PER C. L. SETHI, JUDICIAL MEMBER

The Hon'ble President, ITAT, vide order dated 15.06.2008 as modified by his order dated 06.03.2009 has constituted the Special Bench in the above referred appeals to dispose of all the appeals in entirety, on the facts and circumstances of the case, and in accordance with law (including directions of Hon'ble High Court in the matter).

ITA no. 3622/Del/1995

2. Firstly, we take up the appeal pertaining to the assessment year 1992-93.

3. In the appeal filed by the assessee for the assessment year 1992-93, ground No. 1 divided into sub-ground No. 1.1 to 1.7 read as under:-

1.1 That the learned CIT(A) has erred on the facts and circumstances of the case and in accordance with the provisions of law and past history of the case in confirming the addition of Rs. 6,01,78,261/- being the surplus arising on land brought into the common stock of the partnership firm M/s. DLF Commercial Developers.

1.2 That the learned CIT(A) has erred on the facts and circumstances of the case and in accordance with the

provisions of law in holding that the stock in hand brought into the common stock of the partnership by the company by credit, at an agreed value, to the company's capital account amounted to a transfer of the asset to the partnership giving rise to a taxable profit.

- 1.3 That the learned CIT(A) has erred on the facts and circumstances of the case and in accordance with the provisions of law in holding that the amount of Rs. 6,01,78,261/- determined for credit to the capital account is a consideration and a profit derived from the business and in any case a benefit arising to the appellant from such business.*
- 1.4 That the learned CIT(A) has erred on the facts and circumstances of the case and in accordance with the provisions of law in holding that the bringing of the individual assets into the common stock of partnership gives rise to a profit in the commercial sense without appreciating that in 156 ITR 509, it has been clearly held that such a transaction does not amount to a sale and that whatever is brought into the partnership ceases to be the exclusive property of the person who brought it in, that is, an exclusive interest is reduced to a shared interest.*
- 1.5 Without prejudice to the above, it is respectfully prayed that the CIT(A) is clearly in error in holding that the entire surplus is assessable in the year under appeal.*
- 1.6 That the learned CIT(A) has erred on the facts and circumstances of the case and in accordance with the provisions of law in holding that in case of stock in trade there is no difficulty in computation of the profit u/s 28 without appreciating that in 156 ITR 509, it has been specifically held by the Hon'ble Supreme Court that "notwithstanding the transfer, there would be no consideration in such cases available to the partner during the subsistence of the partnership and his rights are limited to getting his share of profit".*

1.7 That the learned CIT(A) has erred on the facts and circumstances of the case and in accordance with the provisions of law and without raising the issue, in holding that the firm is not genuine in as much as it is formed with the sole objective of evading payment of taxes.”

4. Briefly stated, apropos the issue involved in ground No. 1.2 to 1.7 of the appeal of the assessee, the facts are that the assessee, a company, is engaged in the business of real estate development, and hold certain lands as stock in trade. By a Memorandum of the partnership executed on 23rd day of March, 1992, made effective from 16th day of March, 1992, the assessee company entered into partnership with four of its subsidiaries companies and one individual. The assessee contributed all its right in the five plots of land admeasuring about 16.98 acres including the area of land owned but it, situated in DLF Qutab Enclave Complex, hereinafter referred to as “said land”, valued at Rs. 11.50 crores as capital contribution to a newly constituted partnership firm viz., M/s. DLF Commercial Developers, in which the assessee became a partner with share of 76%. All the right in the said plot of land became the property of the partnership firm with effect from 16th day of March, 1992. The assessee’s contribution of capital in the newly constituted firm represented

the market value of the said plot of land. The market value was determined at Rs. 11.50 crore. In the assessee's books of account, the said land contributed towards capital in the partnership firm was shown at a cost of Rs. 4,40,62,419/-. The said newly constituted partnership firm credited the capital account of the assessee company by Rs. 11.50 crores being the value of the land contributed by the assessee as capital. The assessee also recorded the value of said land contributed as capital in the firm at Rs. 11.50 crores in its books, and the surplus amounting to Rs. 6.01 crore was credited to the profit and loss account, but, was claimed as not exigible to tax in the return of income filed by the assessee. The assessee claimed the surplus being difference between the value at which the land was credited in assessee's capital account in the firm in which assessee became a partner and the book-value, credited in its profit and loss account to be exempted from tax relying upon the decision of Hon'ble Apex Court in the case of CIT vs. Hind Construction Ltd. 83 ITR 211 (SC). According to the assessee, the surplus of Rs. 6.01 crores was not its income liable to tax as there was no sale or transfer of land in law as there could be no sale to self. The assessee also submitted before the

A.O. that identical controversy has been decided in favour of the assessee in the assessment year 1985-86. However, the A.O., after considering the facts that in its books, the assessee has credited the surplus in the profit and loss account and utilized this income for declaring dividend, has treated this surplus amounting to Rs. 6.01 crore as profit derived from the transfer of lands to the firm by the relying upon the judgment of the Hon'ble Apex Court in the case of Sunil Sidhharth Bhai vs. CIT reported in 156 ITR 509. The A.O. while treating this amount of Rs. 6.01 crore as profit chargeable to tax also relied upon the provision of sub-section (3) of section 45 of the Income-tax Act, which was inserted in the Income-tax Act with effect from 01.04.1988. The A.O. had also taken a view that the new partnership firm constituted in the name and style M/s. DLF Commercial Developers was a bogus partnership or a sham partnership and the transaction was not genuine. In this connection, the A.O. placed reliance on the decision of Apex court in the case of McDowell and Company reported in 154 ITR 148 (SC). The A.O. further held that he was not following the decision of Id. CIT(A) for the assessment year

1985-86, because that decision has not become final as the order of the Id. CIT(A) was pending before the ITAT.

5. On an appeal, the Id. CIT(A) upheld the order of the A.O., firstly, on the reasoning that the assessee company had shown the surplus as its income in its profit and loss account by making appropriate credits to the profit and loss account, and on commercial principles, the surplus represents the business profit as has been treated as such by the assessee; secondly, on the reasoning that the ratio of the decision in the case of Hind Construction Company (supra) was not applicable to the facts of the assessee's case as there were vital distinguishing features as detailed by the A.O. in his order; thirdly, on the reasoning that after the decision of Hon'ble Supreme Court in the case of Sunil Sidharth Bhai (supra), the decision of the Hind Construction Ltd. (supra) stands modified to that extent; fourthly, on the reasoning that since the land so transferred represented the stock in trade of the assessee, the profits were chargeable to tax u/s 28 of the Act, which stands on different footing with the gains arising from the transfer of capital or fixed assets, and lastly, on the reasoning that the present partnership firm newly constituted is not

genuine in as much as it has been constituted or formed with the sole object of evading payment of taxes and, therefore, the assessee's reliance on the ratio in the case of Hind Construction Company (supra) was totally out of context and irrelevant.

6. Being aggrieved, the assessee has preferred this appeal before the Tribunal, and the Tribunal vide order dated 30.03.2007 dismissed this ground raised by the assessee and upheld the order of the Id. CIT(A) by deciding the issue against the assessee. The Tribunal vide order dated 30.03.2007, decided the issue against the assessee on merits in the light of detailed reasoning given in para No. 6 to 29 of that order. The Tribunal declined to accept the contention of the assessee, in the light of insertion of section 45(3) of the Act with effect from 1.04.1988, and further that some of the decisions cited before the Tribunal in the assessment year 1992-93 were not considered in the earlier assessment year 1985-86 and the issue was not much deliberated upon by the Tribunal in that earlier year.

7. Against the order of the Tribunal dated 30.03.2007, the assessee preferred an appeal before the Hon'ble High Court, and their Lordship

vide order dated 11.01.2008 set aside the order of the Tribunal and remitted the matter to the Tribunal for a fresh consideration in accordance with law by observing as under:-

“The question that arose on the merits of the case before the Tribunal was whether on revaluation of the stock in trade of the Assessee, the Assessing Officer was justified in making an addition of Rs. 6.01 crores.

An identical issue had arisen in the case of the Assessee, though in respect of a different amount for the assessment year 1985-86. In respect of that assessment year, the Assessing Officer made an addition, but that was set aside by the Commissioner of Income Tax (Appeals) by a detailed order dated 29th October, 1990.

Aggrieved by the order passed by the Commissioner of Income Tax (Appeals), the Revenue preferred an appeal which was heard and dismissed by the Tribunal on 31st January, 2001 being Appeal no. 873/Del/1991 relevant for the assessment year 1985-86.

The Tribunal did not give its own reasons while disposing of the appeal of the Revenue but relied upon the basis and reasons given by the Commissioner, which it found to be sound and convincing, so as not to warrant any interference with the order passed by the Commissioner.

When the same issue arose in the present assessment year 1992-93, the Assessing Officer again took a view which was not favourable to the Assessee with the result that the Assessee preferred an appeal before the Commissioner, but by an order dated 10th

March, 1995 the Commissioner dismissed the appeal of the Assessee.

Being aggrieved, the assessee preferred an appeal before the Tribunal and one of the points urged by the Assessee was that since the issue raised in 1985-86 was identical, the order passed by the Tribunal in respect of that year should be followed by the Tribunal in this year also. The Tribunal considered that contention in paragraphs 30 to 32 of its order and rejected it on three grounds; firstly, that on the earlier occasion the Commissioner had not taken into consideration an amendment to Section 45(3) of the Act which came into force from 1st April, 1988 which was, therefore, not applicable in respect of the assessment year 1985-86; secondly, that some of the decisions cited before the Tribunal in the present matter were not cited on the earlier occasion; thirdly, that the issue raised was “sensitive” and was not deliberated upon by the Tribunal on the earlier occasion. ON this basis, the Tribunal declined to follow the order passed in respect of the assessment year 1985-86.

It is now well settled that when one Bench of the Tribunal takes a view, then another Bench of the Tribunal cannot pass a contrary order but must, if it disagrees with that view, have the conflict resolved by referring the matter to a larger Bench. This is not only a matter of judicial propriety but also a matter of judicial discipline.

In Union of India vs. Shri P.D. Sharma & Ors., 2004 III AD (Delhi) 131, a Division Bench of this Court observed as follows:-

“It is now trite law that a Coordinate Bench of the Tribunal cannot take a view contrary to a view expressed by earlier Bench rendered earlier. In

case it differs from the decision of the earlier Bench, the only course open to it is to refer the matter to a Larger Bench.”

In Sundarjas Kanyalal Bhatia & Ors. Vs. Collector, Thane, (1989) 3 SCC 396, the Supreme Court held as follows:

“The judicial decorum and legal propriety demand that where a learned Single Judge or a Division Bench does not agree with the decision of bench of co-ordinate jurisdiction, the matter shall be referred to a larger bench. It is subversion of judicial process not to follow this procedure.” (emphasis supplied)

In arriving at this conclusion, the Supreme Court relied upon two of its earlier decisions, namely, Mahadeolal Kanodia vs. Administrator General of West Bengal, AIR 1960 SC 936 and Lala Shri Bhagwan vs. Ram Chand, AIR 1965 SC 1767.

Under these circumstances, we answer the question in the negative and remit the matter to the Tribunal for a fresh consideration in accordance with law.”

8. In pursuance to the aforesaid order of the Hon’ble High Court, the matter come up again before the Tribunal for its fresh consideration and decision.

9. When the appeal again came up before the Division Bench in pursuance to the aforesaid High Court’s order, the Division Bench

observed that since the Tribunal for the reasons recorded in the order passed for the assessment year 1992-93 had taken a view contrary to the view taken by the Tribunal in the assessment year 1985-86, the matter needs to be resolved by a larger bench. The Division Bench then recommended the Hon'ble President to constitute a special bench to decide the following question as well as to decide the whole appeal:-

“Whether in the facts and circumstances of the case of the assessee the surplus arising from land brought into the common stock of the partnership firm, M/s. DLF Commercial Developers, by credit, at an agreed value, to the company's capital account amounted to a transfer of the asset to the partnership give rise to a taxable profit?”

10. It is in the above circumstances that Hon'ble President constituted the Special Bench to dispose off the entire appeal for A.Y. 1992-93, and also appeals for other assessment years referred to in the cause title hereto, and while disposing off the appeals in entirety, the Special Bench was directed to consider the following question also:-

“Whether on the facts and in the circumstances of the case, the surplus

arising on revaluation of the land, held by the assessee as stock-in-trade and brought into the common stock of the partnership firm M/s DLF Commercial Developers, and by credit, at an agreed value, to the assessee's capital account, amounted to a transfer of the asset to the partnership firm and can be assessed as the business profits of the assessee?"

11. The matter was then heard at length by the Special Bench on various dates i.e. 14.10.2008, 20.10.2008, 11.11.2008, 17.11.2008 and lastly on 18.11.2008. However, in the course of dictating the order, it was felt that the question framed as above was restricting powers of the Bench to consider all aspects of the matter involved in ground no. 1.1 to 1.7 in as much as, in the question, a limited issue was framed to decide as to whether surplus from the contribution of land to a firm can be assessed as business profits of the assessee, though, in the course of hearing of the appeal, reliance was placed by the department upon the applicability of section 45(3) of the Act, as so referred to and relied upon by the authorities below in their orders, and also referred to by the Tribunal in its order dated 30.03.2007 passed in first round of this appeal. The matter

was again put up before the Hon'ble President, and the President after hearing both the parties passed the order as under:-

“06.03.2009:

Present Shri Dinodia for the assessee and Shri NP Sawhney for the Deptt. Both the parties agree that the Special Bench should dispose of the appeals without considering the question in accordance with law and facts of the case (including the directions of Hon'ble High Court). Directions u/s. 255(3) be issued accordingly.”

12. The matter was then again heard by the Special bench to dispose of the entire appeals in accordance with law, and the facts of the case (including directions of the Hon'ble High Court), but without restricting ourselves to the question framed earlier.

Submissions of the Assessee

13. Shri Pradeep Denodia, CA, appearing for and on behalf of the assessee has submitted that the said plot of land contributed as capital by the assessee to a newly constituted partnership firm in which the assessee became a partner holding 76% of shares, were held by assessee as its stock in trade of its business of real estate development, and the said land

was also held by the newly constituted partnership firm as stock in trade. He further submitted that the said land was contributed to the firm as capital contribution by the assessee in the capacity of a partner. The newly constituted partnership firm credited the capital account of the assessee company at a market value of Rs. 11.50 crores, which was more than the cost price to the assessee. The surplus of Rs. 6.01 crores determined after considering cost to the assessee was shown in the profit and loss account of the assessee company, but, was claimed to be exempted from tax, in view of the decision of the Hon'ble Supreme Court in the case of CIT vs. Hind Construction Ltd. reported in (1972) 83 ITR 211 (SC). He further submitted that there was no sale of stock in trade by the assessee to a partnership firm when the same was contributed towards capital of the assessee as a partner. He pointed out that the law is well settled that no one can earn profit from himself by over valuing the stock as it is not a commercial transaction in the business sense, and as such, in the light of this well settled principle of taxation, the stand of the department in charging the surplus amount to tax must fail. He further contended that when the assessee revalues its stock in trade at an amount

more than cost price to it, the surplus does not result in the taxable amount as there was no sale at that time. Likewise, there was no sale of stock in trade at time when the new partnership firm was created and the land was contributed by the assessee to a firm as its capital contribution. He further submitted that without prejudice, even if the transaction of contributing land stock as its capital is treated as transfer, no gain arises to the assessee on the transaction in question as the biggest difference lies in the fact of the present case is that the assessee transferred its stock in trade and not any capital asset. In this respect, the decision of Apex Court in the case of Hind Construction Co. (supra) was relied upon by the learned counsel for the assessee by saying that the facts of the case of Hind Construction Co. (supra) were identical to the facts of the instant case of the assessee. In support of his contentions, the ld. counsel for the assessee has also relied upon the following decisions:-

- i. Chainrup Sampatram v. Commissioner of Income-tax [1953] 24 ITR 481 (SC)
- ii. Sir Kikabhai Premchand v. Commissioner of Income-tax [1953] 24 ITR 506 (SC)
- iii. Sanjeev Woollen Mills v. Commissioner of Income-tax [2005] 279 ITR 434 (SC)

13.1 The ld. counsel for the assessee then submitted that the present case is a case where stock in trade and not any capital asset was contributed by

the assessee to a partnership firm towards its capital. He, therefore, submitted that the definition of “capital asset” and “transfer” defined u/s. 2(14) and 2(47) respectively cannot be imported into the present case in as much as no capital asset is involved in the instant case of the assessee. He, further, pointed out that the stock in trade is specifically excluded from the ambit of a “capital asset” as defined u/s. 2(14) of the Act, and as such the definition of “transfer” in relation to a capital asset defined u/s. 2(47) is not applicable to the stock in trade. He, thus, submitted that contribution of stock in trade to a firm by a partner as capital contribution is neither sale nor a transfer, and as such, no income or profit did accrue or arise to the assessee on account of any surplus, resulted out of such contribution of stock in trade to a firm, at the amount more than the book value. At this stage, he placed heavy reliance on the decision of Hon’ble Calcutta High Court in the case of CIT vs. Hind Construction Ltd., 78 ITR 664, which has been affirmed by the Hon’ble Supreme Court in the case of CIT vs. Hind Construction Ltd. 83 ITR 211 (SC). Reliance was also placed upon the judgment of Hon’ble Madras High Court in the case Commissioner of Income-tax v. Janab N. Hyath Batcha Sahib [1969] 72

ITR 528 (MAD.) to contend that when a person hands over its property to a firm of partners consisting of himself and others, there is no transfer of property so as to constitute a sale of goods as defined under “Sales of Goods Act”, and the partner cannot be said to have sold his property to the partnership firm. To the similar effect, reliance was placed upon the decision of Hon’ble Allahabad High Court in the case of Dr. M.C. Kackkar v. Commissioner of Income-tax[1973] 92 ITR 87 (ALL.). He further submitted that the aforesaid decisions of Hon’ble Madras High Court in the case of Commissioner of Income-tax v. Janab N. Hyath Batcha Sahib and Hon’ble Allahabad High Court in the case of Dr. M.C. Kackkar v. Commissioner of Income-tax, have been approved by the Hon’ble Supreme Court in the case of Malabar Fisheries Co. v. Commissioner of Income-tax 120 ITR 49 (SC). According to the learned counsel for the assessee, the view that the surplus arising on revaluation of its stock in trade at the time of contributing the same to a partnership firm is profit or gain chargeable to tax as the transaction amounts to a transfer of stock in trade from a partner to the firm is completely misleading and against the settled legal positions on the matter involved.

13.2 Having contended as above, the ld. counsel for the assessee proceeded to argue that there is no charging provision in Income Tax Act to tax this nature of transaction of making over a stock in trade as capital contribution to a firm in which the assessee is or becomes a partner. He further contended that if any transaction does not fall within the ambit of taxation, the tax cannot be imposed on the grounds of morality or equity. Similarly, in the converse situation, tax imposed by the statute must be levied inspite of its causing hardship to a tax payer. In this connection, reliance were placed upon the following decisions:-

- i Commissioner of Income-tax v. Keshavlal Lallubhai Patel [1965] 55 ITR 637 (SC)
- ii. Smt. Mohini Thapar v. Commissioner of Income-tax [1972] 83 ITR 208 (SC)
- iii. Commissioner of Income-tax v. C. P. Sarathy Mudaliar [1972] 83 ITR 170 (SC)
- iv Manish Maheshwari v. Assistant Commissioner of Income-tax (2007) 289 ITR 341 (SC) = [2007] 159 taxman 258 (SC)

13.3 It was further submitted by the learned counsel for the assessee that the law has been amended many times pursuant to judicial pronouncements in order to bring within the tax net certain transactions which the courts otherwise found to be outside the purview of tax provisions, and some of such instances pointed out by the learned counsel for the assessee, are the amendment by way of insertion of section 45(2) w.e.f. 001.04.1964 (omitted in 1966 and reintroduced in 1984 in its present form) to tax the conversion of capital assets into stock in trade, section 45(3) and 45(4) inserted w.e.f. 01.04.1988 to bring to tax certain situations which were otherwise held to be non-taxable by the courts. But, he submitted, no such amendment has been brought to tax the surplus arising from revaluation of the stock in trade at the time when the same is contributed as capital by a partner to a firm, and, thus, there being no charging provisions in the Act, the surplus arising from revaluation of stock in trade at the time when the same is contributed as capital by a partner to a firm cannot be brought to tax.

13.4 With regard to the reliance placed by the AO upon the sub-section (3) of section 45 and upon the judgment of the Hon'ble Supreme Court in

the case of Sunil Siddharthbhai v. Commissioner of Income-tax [1985] 156 ITR 509 (SC), he submitted that provisions of section 45(3) and decision of Hon'ble Supreme Court in the case of Sunil Siddharthbhai cannot be applied to the present case in as much as the said provision and the decision are made in connection with a capital asset being contributed by the partner to a firm towards its capital, and not applicable to the case where stock in trade belonging to a partner is contributed by that partner to a firm towards its capital. He vehemently urged that a legal fiction created in section 45(3) in relation to a capital asset cannot be extended beyond its terms and intent and thus cannot be applied in cases where stock in trade is contributed by a partner as its capital to a firm in which he is or becomes a partner. He, therefore, contended that the contribution of stock in trade by a partner to a firm cannot be considered to be a transfer and/or sale under the general law for the purpose of taxing the surplus arising from such contribution at an amount more than the cost to a partner. He submitted that the case of contribution of stock in trade by a partner to a firm is fully covered by the decision of Hon'ble Supreme Court in the case of CIT vs. Hind Construction Ltd., (supra) and not by

propositions laid down by the Hon'ble Supreme Court in the case of Sunil Siddharthbhai vs. CIT read with section 45(3) inserted in the statute w.e.f. 01.04.1988. He urged that even the application of the provisions of section 45(3) of the Act inserted w.e.f. 01.04.1988 has not brought any change for bringing to tax the surplus arising from contribution of stock in trade by a partner to a firm at an amount more than the cost to the assessee because in the newly inserted section 45(3) of the Act, the words "transfer of capital asset" is used though in the instant case of the assessee, it was a contribution of land which was held as stock in trade by the assessee. Thus, according to the learned counsel for the assessee, the decision of Apex Court in the case of Sunil Siddharthbhai (supra) is of no help to the revenue as their Lordships in that case were concerned with the situation where transfer of capital asset and not stock in trade was involved.

13.5 With regard to the CIT(A)'s observations that since the assessee company has shown the surplus as its income in its audited account by making appropriate credit to the profit and loss account, the surplus represents the business profit on commercial principles, the ld. counsel for the assessee submitted that it is well settled that entries in the books of

accounts representing profit and loss account and balance-sheet are not sacrosanct and not binding either on the assessee or on the revenue as so held and observed in the following decisions:-

- i Kedarnath Jute Mfg. Co. Ltd. v. Commissioner of Income-tax [1971] 82 ITR 363 (SC)
- ii Sutlej Cotton Mills Ltd. vs. CIT (1979) 116 ITR 1 (SC)
- iii United Commercial Bank v. Commissioner of Income-tax [1999] 106 Taxman 601 (SC) = 240 ITR 355 (SC)
- iv Karnataka Small Scale Industries Development Corpn. Ltd. v. Commissioner of Income-tax [2003] 126 Taxman 121 (SC) = 258 ITR 770 (SC)

13.6 He further submitted that the identical issue has been decided in favour of the assessee by this Tribunal in A.Y. 1985-86, after following the decision of Hon'ble Supreme Court in the case of Hind Construction Ltd. (supra), and that decision still holds the field in the case of contribution of stock in trade by a partner to a firm towards its capital contribution.

Submissions of the Revenue

14. Shri N.P. Sahni, Sr. Standing Counsel for the department assisted by Shri P. Yadav, Jr. Standing Counsel for the department, has submitted that the present case is a case where the assessee has shown the profit of Rs. 6.01 crores in respect of the portion of land transferred to a partnership firm in which the assessee became a partner, and has credited same in the profit and loss account prepared by the assessee, and a corresponding amount has been credited by the firm in the assessee's capital account, which goes to show and establish that it is a case of sale of stock in trade on credit by the partner to a firm, as there being no bar on sale of stock in trade by a partner to a partnership firm in which he is a partner. He further submitted that instead of contributing capital by payment of money, the assessee has contributed its capital by adjusting the sale value of the land transferred or sold by it to partnership firm. It was further contended by the Id. Standing Counsel for the revenue that when the assessee claims that he contributed its stock in trade to a firm, and treated the sale value as its capital credited in its capital account in the books of a firm, the transaction is nothing but is, in reality and substance, a transaction by way of sale at a given value, which was to be paid by the

firm to the assessee partner. If it is the case of the assessee that stock in trade is given as stock in trade to a partnership firm for business, it is a case of trading or commercial transaction and is to be considered as sale at a given value at which assessee's capital account is credited in the books of a partnership firm, and thus the surplus arising there from is to be charged to tax as a business profit.

14.1 He further submitted that the intention of the assessee with regard to the transaction in question is to be gathered or judged from over all conduct of the assessee and the entries made by it in its books of accounts. From perusal of entries made in the books of accounts by the assessee, it is clear that the assessee has treated the transaction as sale of stock in trade by it to a firm in as much as, the assessee has itself credited the amount of sales and resultant profit in its profit and loss account, and the profit resultant there from was also utilized for the purpose of distribution of dividend to the share holders. He further contended that if the contention of the assessee, which are contrary to the entries made in the accounts and narration made in partnership deed, is looked dispassionately and in all fairness, it would termed as nothing but a collusive arrangement

between the parties to evade payment of correct taxes in respect of surplus amount credited in assessee's capital account.

14.2 With reference to the assessee's stand relying upon the decision of Hon'ble Supreme Court in the case of Hind Construction Ltd., the ld. Standing Counsel for the revenue has submitted that the present case is not the case where value of stock in trade has been merely over-valued in the books of the assessee, but, it is the case where a credit on account of sale of land in question has been made in the profit and loss account and the corresponding entry has been made by the firm in its books, which indicates and points out that the transaction was in the nature of a sale of stock in trade by the assessee partner to the firm. He, therefore, submitted that the facts of the present case are on quite different footing than that of in the case of Hind Construction Ltd. (supra).

14.3 According to the learned Standing Counsel for the revenue, the decision of Hind Construction Co. Ltd. cannot be applied in the changed scenario, the facts of the instant case after insertion of provision of Section 45(3) of the Act w.e.f. 01.04.1988. He further submitted that the extended definition of "transfer" defined u/s. 2(47) of the Act can be

applied to the transaction of contribution of land by the assessee to a firm as capital contribution even if the land was held by the assessee company as stock in trade before it was so contributed. In this respect, he placed reliance upon the decision in case of *Sunil Siddharthbhai vs. CIT* 156 ITR 509 (SC), *CIT vs. Suresh Chand Jain* 178 ITR 241 (AP) and *A.L.A. Firm vs. CIT* 189 ITR 285 (SC).

14.4 The ld. Standing counsel for the revenue made an attempt to distinguish the decision of Hon'ble Supreme Court in the case of *Hind Construction Ltd.* by contending that the case of a partner bringing his personal assets into the firm should be distinguished from the cases where a partner sales his assets including stock in trade to the firm, where tax consequences would be the same as in the case of sale to an outsider. He then submitted that the present case is a case where stock in trade has been in reality sold by the assessee to a firm in which it became a partner as would be clear from the treatment given by the assessee to the transaction in its books of accounts, by crediting the amount as sales, and by crediting the resultant profit in its profit and loss account.

14.5 It was further submitted by the Standing counsel for the department that in the case of CIT vs. Hind Construction (supra) the Apex Court examined the question only from the point of view of sale, and not from the point of view whether there was any transfer of asset from a partner to a firm, which question has been considered and answered by the Hon'ble Apex Court in the case of Sunil Siddharthbhai (supra) holding that when any asset is contributed by a partner to a firm as its capital, it amounts to a transfer even under the general law. Sr. Standing counsel for revenue has also placed reliance upon the following decisions:-

- i. Addl. Commissioner of Income-tax v. M.A.J. Vasanaik [1979] 116 ITR 110 (KAR.)
- ii. A. Abdul Rahim, Travancore Confectionery Works v. Commissioner of Income-tax [1977] 110 ITR 595 (Ker.)
- iii. Baldevji v. Commissioner of Income-tax [1985] 156 ITR 776 (MAD.)

14.6 He then submitted that the dictum “one cannot make profit out of himself”, is not attracted in the present case, in as much as, in the present case, the assessee being a separate taxable entity has transferred its stock in trade to a partnership firm, another taxable entity, and the surplus arising there from has been credited in the profit and loss account. He

then pointed out that if it is case of the assessee that stock in trade was contributed to a firm, and the value of stock in trade at the amount more than the cost to the assessee is credited in its capital account by a firm, the transaction in that event would be only a business or trading transaction as is clear from the treatment given by the assessee to the transaction in its books of accounts. He, therefore, submitted that the AO as well as the CIT (A) has rightly taken a view that the surplus arising from transfer of stock in trade by the assessee to a firm is a profit assessable u/s. 28 of the Act. In support of the contention that a partner can sale its stock in trade to a firm and there is no bar in making trading or commercial transaction in respect of the stock in trade between a firm and its partner, and, an individual partner is distinguished and separate taxable entity as against the partnership firm in which he may be a partner, the ld. Sanding Counsel for the revenue has placed heavy reliance on the decision of Hon'ble Supreme Court in the case of Commissioner of Income-tax v. A. W. Figgies & Co. [1953] 24 ITR 405 (SC). He then submitted that in the light of the position of law that the firm is a separate taxable entity from its partner, it is abduntly

clear that the transaction of contributing stock in trade by a partner to a firm as its capital would be a transaction between two persons, and the concept that no person can make profit out of himself would not be applicable in that case. A reference was made to the decision of Hon'ble Madras High in the case of Baldevji v. Commissioner of Income-tax [1985] 156 ITR 776 (MAD.).

14.7 The ld. Sr. Standing Counsel for the revenue further submitted that if it is a case of capital contribution of a capital asset, a capital gain is chargeable to tax under the amended provision of section 45(3) of the Act, inserted in statute w.e.f. 01.04.1998

14.8 To sum-up, the ld. standing counsel for the revenue submitted that the revenue's arguments are twofold as under:-

- i. If it is a assessee's case that it is case of capital contribution in the form of stock in trade, there is a change of ownership or extinguishment of right in that stock in trade of the assessee partner against the consideration credited in the assessee's capital account, and the surplus arising there from would be taxable as business profit.

- ii. If it is case of assessee that it is a case of capital contribution in the form of capital asset, the amount credited in the assessee's capital account shall be deemed to be consideration received by the assessee on transfer of capital asset to a firm, and capital gain arising there from would be chargeable under the head "capital gain" under the newly inserted provisions of section 45(3) of the Act, inserted from 01.04.1988.

14.9 As against the contention of the ld. counsel for the assessee that there is no provision in the Act to bring to tax the surplus arising from revaluation of stock in trade at the time when same is contributed as capital to a firm by a partner and the partner's account is credited by the amount more than the cost of stock in trade to the assessee partner, and no amendment like insertion of section 45(2), 45(3) and 45(4) has been made in the Income Tax Act, the ld. Sr. Standing counsel for the revenue has submitted that if it is the case of the assessee that stock in trade has been given to a firm by the partner towards its capital at a value more than the cost to the assessee, there is a transfer of stock in trade from partner's

hand to the firm's hands and the resultant surplus shall be considered as business profit, which is duly covered by section 28 itself. He further submitted that insertion of section 45(3) in the Act was necessitated only because of the position taken in cases of transfer of capital asset by way of contribution to a firm by certain assesseees to avoid payment of correct taxes, but so far as cases of transfer of stock in trade from partner to a firm are concerned, there was no problem and there was no necessity of making any amendment either in section 28 or some other section. In such like cases where stock in trade is contributed by the partner to a firm, the rights or interest in stock in trade were passed on from one person to another, and the transaction would be amounted to either sale or transfer in the general law if not within the meaning of section 2(47), and liability to taxation on the surplus amount would arise on the date of such transaction. He further contended that if we look to the meaning of "person" as defined in section 2(31) of the Act, it is clear that an individual partner is distinct and separate taxable entity as against a partnership firm, in which he may be a partner, and there being no bar of making any commercial or trading transaction between the firm and its

partner, the transfer of stock in trade by a partner to a firm shall be considered as a transaction of sale or otherwise of transfer of stock in trade, and the transaction would be taxed accordingly. In support of this submission, he placed reliance upon the judgment of Apex Court in the case of Commissioner of Income-tax v. A.W. Figgies & Co. [1953] 24 ITR 405 (SC), with a submission that this decision was rendered by a bench of three judges of Hon'ble Supreme Court, and still hold the ground with binding force.

14.10 The ld. Standing counsel for the revenue further submitted that if it is a case of capital contribution or extinguishment of rights in the land of the assessee partner, and the surplus arising from change of ownership or extinguishment of right of the assessee would thus, be taxable as business profit, and is to be taxed accordingly. On question where there is change of ownership or extinguishment of right of the assessee in the land in question, a reliance was also placed upon the decision of Hon'ble Apex Court in the case of Commissioner of Income-tax v. Grace Collis [2001] 115 Taxman 326 (SC).

14.11 He further submitted that position of Apex in the case of Hind Construction Ltd. would be of no help to the assessee in as much as the transaction of constituting firm by contributing land held by the assessee at higher value than the cost to the assessee is nothing but a colourable and calculated device to evade payment of correct taxes in respect of the surplus amount credited in the assessee's capital account by the firm when the resulted profit has been credited by the assessee in its profit and loss account, but has not offered it to tax. He, therefore, submitted that the transaction of contribution of capital of land in a partnership firm by the assessee partner is to be considered as transfer or sale of stock in trade by the assessee to a partnership firm i.e. from one taxable entity to another.

14.12 On the applicability of the provisions contained u/s. 45(3) of the Act to the facts of the present case, the ld. Standing counsel for the department has submitted that the said land contributed by the assessee partner to a partnership firm in which the assessee became a partner is otherwise to be considered as capital asset in as much as when stock in trade in the form of land held by the assessee was introduced by the way

of capital contribution in a firm, the same stands converted to capital asset at that material point of contribution for the reason that the partnership firm was newly constituted and the land was contributed towards its capital, and, hence, the land has changed its character from stock in trade to capital asset. He further pointed out that in the partnership deed, it is nowhere stated that the capital contribution brought by the assessee was stock in trade even at the time it was contributed as capital in a firm in which assessee became a partner. In the deed of partnership, it is clearly stated that with effect from 16th day of March, 1992 all the rights of the assessee partner in the said plots of land (including the asset of land owned by the assessee) became the property of the partnership firm. The land was on account of capital contribution of the assessee in a firm, and it was upon to the firm to use it in any manner either as trading item or capital asset or as investment or in any other manner. The transaction of making over a land by the assessee to a partnership firm has been claimed by the assessee not to be in the nature of commercial or trading transaction and hence, the asset employed in the said transaction cannot be considered to be stock in trade in as much as stock in trade is always

employed in the course of business or trading transaction. Stock in trades are the goods which are held for the purpose of trading in the course of carrying on business activities. When assessee accepted the position that the transaction in question is not a trading or commercial transaction, the question of treating the asset employed in that transaction as stock in trade cannot by any stretch of imagination, arise. He, therefore, concluded that the land, which was contributed by the assessee to partnership firm towards its capital, is nothing but is a contribution on capital account, and, thus, it has to be treated as capital asset. Therefore, even on this analogy, the surplus arising from the transaction in question by way of contribution of land as capital in a firm in which the assessee became partner at an amount more than the cost to the assessee, which has been credited in the capital account of the assessee in the books of the firm, is to be assessed u/s. 45(3) of the Act if not found to be assessable u/s. 28 of the Act.

REJOINDER BY THE ASSESSEE

15. In the rejoinder, the learned counsel for the assessee reiterated that the main argument of the revenue that the assessee has reflected the surplus in its profit and loss account and has shown the sales

of land in the books, and, therefore, the treatment given by the assessee in its books of accounts clearly proves that it was a transaction of sale and it is only in the income tax return that the assessee was claiming the surplus to be exempted from tax, is not tenable and acceptable in as much as it is well settled that the entries in the books of account are not conclusive or determinative in deciding the taxability or otherwise of a given item, and, thus, merely on the basis of entry in the books of account, it cannot be said that the any income or gain arises or accrues to the assessee in the true commercial sense which a businessman would understand as real income or gain.

15.1 With regard to the revenue's reliance on the decision in the case of *Baldevji v. Commissioner of Income-tax* [1985] 156 ITR 776 (MAD.) in support of the contention that there was a transfer of land in question when the land was contributed towards capital by a partner to a firm in which he is or becomes a partner, the ld. counsel for the assessee has pointed out that in this decision, the Hon'ble Court was concerned with the term "sold or otherwise transferred" for the purpose of withdrawal of benefit of development rebate under section 155 (5) of the

Act in relation to a capital asset and not in relation to stock in trade, and hence placing reliance upon this decision is out of context.

15.2 The ld. counsel for the assessee further contended that once the proposition laid down by the Hon'ble Supreme Court in the case of Sunil Siddharthbhai (supra) that when a partner hands over a business asset to a partnership firm as his contribution to its capital, he cannot be said to have effected a sale is settled, there is no need to travel beyond this, and thus, contention of the revenue that it was a case of sale of stock in trade must be rejected. He further reiterated that in the light of decision of Hon'ble Supreme Court in the case of Sunil Siddharthbhai v. Commissioner of Income-tax (supra), which has been followed by Hon'ble Madras High Court in the case of CIT vs. Padma Narasimhan and other [2002] 255 ITR 441 (Mad.), it is well settled that although that was a case of transfer of capital asset, no income or gain accrues to a partner. He, therefore, urged that the issue arising in the instant case of the present assessee is fully covered by the judgment of Hon'ble Supreme Court in the Hind Construction Ltd. (83 ITR 211), Sunil Siddharthbhai (156 ITR 509), and Sanjeev Woollen Mills (279 ITR 434) and as also supported by other relevant judgments given in the synopsis of the assessee to the similar effect.

DECISION

16. We have considered rival contentions of parties in the light of the facts of the present case, provisions of law contained in that behalf and

decision cited at the bar. We have carefully gone through the orders of the authorities below and as well the material on record.

16.1 The question that arises for our consideration is whether, having regard to the facts and circumstances of the case, the surplus of Rs. 6.01 crores arising from the transaction of contributing the said land as capital by the assessee in a newly constituted partnership firm in which assessee became a partner, is liable to be taxed in the hands of the assessee as its income under Income Tax Act, 1961.

16.2 In the light of the treatment given by the assessee to the transaction in its books of accounts, the main case made out by the revenue is of sale or transfer of stock in trade by the assessee to a firm as against the assessee's claim that it is the case of capital contribution of stock in trade by a partner to a firm and not the case of any commercial or trading transaction in the business sense, and thus no sale or transfer of stock in trade had taken place. The answer to the controversy, in our opinion, rests mainly and primarily upon the determination of the nature of transaction made by the assessee as a partner with the firm in which assessee became a partner. We, therefore, find it necessary and proper on

our part to first ascertain and determine the true nature and character of the transaction and the asset employed in the transaction.

Tests to determine the nature of transaction and asset employed therein

16.3 It is well settled that name or label which is given to any transaction by any party is irrelevant in assessing the exigibility of receipt arising from the transaction to tax. The true character or nature of any transaction is to be decided in each case on its facts. Various rules have been enunciated as furnishing a key to the solution of the question, but as often observed by the courts times and again, it is not possible to lay down any single test as infallible or single criterion as decisive in the determination of the question, which must ultimately depend on the facts of the particular case, and the authorities bearing on the question are valuable only as indicating the matters that have to be taken into account in reaching a decision. It is also impossible to evolve any single formula or criterion, which can be applied in determining the character of transaction, which comes before the courts in tax proceedings. It would besides be inexpedient to make any attempt to evolve such a rule or formula. No single test of universal application can be discovered for a

solution of the question. The answer to the question must necessarily depend in each case on the impression and effect of all the relevant factors and circumstances provided therein, and which determine the character of the transaction. The court has to look not only into the documents but also at the surroundings circumstances so as to arrive at a decision as to what was the real nature of the transaction in a given case. The question whether any asset is capital asset or otherwise can be determined with regard to the nature of the transaction in which such asset is employed and intention of the party, which would be gathered from surrounding circumstances after giving combined effect to all the factors and circumstances of any given case. It is also well settled that the character of asset at the time of its transfer alone is relevant, and what was the nature at the time of its acquisition, is altogether irrelevant. The character of the asset is thus to be judged at the time when it is either sold or transferred or employed in any transaction. The material time with reference to which the question whether a particular asset which have been sold or transferred or otherwise transferred or employed in any transaction is a capital asset or not is to be decided, is the date of such sale

or transfer, and not the time when it was acquired. We have to consider the changes in circumstances under which the asset is subsequently employed, from the circumstances prevailing on the date of its acquisition. It is also to be considered whether the case is a case of conversion of asset from one nature to another. In other words, it is also to be seen whether any capital asset has been converted into a stock in trade or vice-versa, which can be determined with reference to the combined effect of all the factors appearing in any given case including the nature of the transaction in which it is employed and the intention of the party.

16.4 As held by various courts times and again, for determining the real nature of income, the entries in the books of account are not decisive or conclusive. Whether the assessee is entitled to a particular deduction or not will depend on the provisions of law relating there to, and not on the view, which the assessee may take on his rights nor can the existence of entries in the books of accounts be decisive or conclusive in the matter. In other words, it is settled law that the manner in which entries are made in the books of account is not determinative of the question whether the assessee has earned any profit or suffered any losses.

It is the true nature and quality of the receipt and not the head under which it is entered in the account books, which would be proved decisive. The name which the parties may give to the transaction, which is the source of the receipt, and the characterization of the receipt by them are of little consequence. What is relevant is the true and legal effect of the transaction, and the entries in the books are not relevant.

16.5 In this view of the matter, it is, therefore, necessary for us to examine, analysis and appreciate all the relevant factors and circumstances of the present case to determine the true nature and character of the transaction of making over of assessee's personal asset as capital contribution towards its capital to a partnership firm in which the assessee became a partner and to determine the nature and character of asset employed in that transaction.

16.6 With regard to the controversy existing between "capital" and "revenue" receipts, the courts have found it difficult to lay down any general considerations which would conclusively determine whether a certain receipt falls under one or the other category. Whether a particular receipt or transaction is on capital account or revenue account has

frequently engaged the attention of the courts. It may be broadly stated that what is received for loss of capital is a capital receipt: and what is received as profit in a trading transaction is taxable income. But the difficulty arises in ascertaining whether what is received in a given case is on account of loss of capital or profit in trading transaction. Cases on the border line give rise to vexing problems. It need hardly be said that the form in which the transaction, which give rise to income, is clothed and the name which is given to it are irrelevant in determining the true and correct nature of the transaction. There is material distinction between commercial and trading transaction and transaction on capital field. The assessee may by making entries in the books, which are not in conformity with the facts of the case and proper accountancy principles, conceal real nature of the asset or the receipt or the transaction, as the case may be. In that event as already observed above, true nature and character of the transaction or receipt or asset in a given case is to be determined on a consideration of the totality of the circumstances of the case.

Nature and character of transaction of making over personal assets of whatever character by a partner to a firm as capital contribution, in

which he is or becomes a partner, and the nature of asset at time when it is employed therein.

16.7 In the instant case before us, we are called upon to determine the true and correct nature of the transaction of contribution of partners' personal asset as capital contribution in the firm in which he became a partner. The facts of the present case reveals that the assessee company was carrying on a business of real estate, besides others. In the course of carrying on business of developing and dealing in real estates, the assessee held certain lands and right in lands as stock in trade of its business. The assessee company entered into a partnership with four of its subsidiaries companies and one individual as evidenced by the memorandum of partnership executed at New Delhi on 23rd day of March, 1992, with a object to start and carry on the business of developing and dealing in real estate, construction of buildings and letting them out or selling them. The assessee company had 76% share, while the four subsidiary company held 5% share each and the individual 4% in the profits or loss of the firm. In pursuant to their intention to enter into partnership with the object to start and carry on the real estate business, the assessee had agreed to bring all its right in five plots of land measuring about 199.99 acres into the

common stock of partnership, so that all the partners, who had agreed to entered into said partnership, may participate jointly in the development and construction of building there upon, which were to be let out for earning rental income there from or sale of individual units comprised in such buildings. In pursuance to the aforesaid mutual agreement, the assessee had brought all its right in the said plot of land into a common stock of partnership w.e.f. 16.03.1992, and all the rights of the assessee upon the said plot became the property of the partnership firm w.e.f. 16.03.1992. The assessee got the said plot of land brought into common stock of partnership valued by experts determining the value thereof at Rs. 1150 lacs. In consideration of the assessee having brought in all its right in the said plots of land into common stock of the partnership firm, the assessee's capital account was credited by Rs. 1150 lacs in the accounts of the partnership firm. The assessee also credited its books by said sum of Rs. 1150 lacs, and the difference between the cost reflecting in the assessee's account and the amount of Rs. 1150 lacs at which the assessee's capital account was credited, after considering all expenses incurred in respect of said land by the assessee has been credited to the

profit and loss account of the assessee company. In the books of the assessee company, the transaction resulted into the surplus of Rs.6.01 crores, which was credited to the profit and loss account, but claimed as not exigible to tax in the return of income filed by the assessee for the assessment year in question. According to the assessee, the readjustment on account of the revaluation of stock in trade resulting in surplus of Rs. 6.01 crores was not its income as there was no transfer or sale of lands to any other person as in law, there could be no sale to itself, and the readjustment of the value of its lands held by the assessee as its stock-in-trade could not in law result in to any profit chargeable to tax. The assessee placed reliance upon the decision of Hon'ble Supreme Court in the case reported as CIT vs. Hind Construction Ltd. 83 ITR 211 (SC).

16.8 For ready reference, the relevant portion of recitals made in the deed of partnership executed on 23.03.1992 between the assessee and five other persons, and made effective from 16.03.1992, are being reproduced here as under:-

“PARTNERSHIP DEED

This Memorandum of partnership made at New Delhi the 23rd day of March, 1992 between

1. M/s. DLF Universal Limited, a public Limited company incorporated under the Companies Act, 1956 and having its registered office at Model Town, Faridabad in the state of Haryana of the ONE PART;

2. M/s. Apollo Land & Housing Co Ltd. also a Company incorporated under the Companies Act, 1956 and having its registered office at 1-E, Jhandewalan Extension, New Delhi of the SECOND PART;

3. M/s. Moonlight Builder & Developers Ltd. also a Company incorporated under the Companies Act, 1956 and having its registered office at 1-E, Jhandewalan Extension, New Delhi of the THIRD PART;

4. M/s. Sunrise Land & Housing Co Ltd. also a Company incorporated under the Companies Act, 1956 and having its registered office at 1-MM, Jhandewalan Extension, New Delhi of the FOURTH PART;

5. M/s. DLF Builders & Developers Ltd. also a Company incorporated under the Companies Act, 1956 and having its registered office at 1-E, Jhandewalan Extension, New Delhi of the FIFTH PART;

6. Mr. Rajinder Singh son of Late Sri Kartar Singh Lamba resident of C-36, Fateh Nagar, New Delhi 110 018 of the SIXTH PART;

WHEREAS the parties of the first to second parts are carrying on the business of developing and dealing in real estate and are engaged in the development of a Project known as “DLF QUTAB ENCLAVE COMPLEX” in Gurgaon, District of Haryana State which is hereinafter referred to as ‘the said project’ and

WHEREAS it was agreed between the parties hereto that out of aforesaid land, five plots of land admeasuring about 16.98 acres and morefully described in the Schedule written hereunder (and hereinafter referred to as “the said plots”) may be brought into the common stock of a partnership so that all the parties hereto participate jointly their further development and construction of buildings to be let out for earning rental income therefrom or sale of individual units comprised in such buildings; AND

WHEREAS the parties of the Third to Sixth part also agreed to participate in the further development of the said plots and the construction of buildings thereon as aforesaid; AND

WHEREAS in accordance with the aforesaid agreement the party of the first part brought all its right in the said plots into the common stock of partnership; AND

WHEREAS with the effect from the 16th day of March, 1992 all the rights of the party of the first part in the said plots (including the area of land owned by it) became the property of the partnership firm; AND

WHEREAS the parties hereto agreed that on the basis of expert valuation, the current value of the rights in the said plots is Rs.1150 lacs; AND

WHEREAS the amount of Rs.1150 lacs was accordingly credited to the account of the party of the first part in the account books of the partnership firm on account of its having brought its right in the said plots into common stock of partnership to be treated as its contribution towards the capital of the partnership; AND

WHEREAS the party of the first part has already paid an amount of Rs.1,27,90,215/- as advance towards purchase of land to its subsidiary companies from whom the land hereby brought into the common stock of partnership has been

agreed to be purchased but whatever further amount becomes payable to the subsidiaries, the same will be payable by the firm; AND

WHEREAS all the other parties hereto have agreed to contribute such amounts towards the capital of the partnership firm as are mentioned hereinafter and which may be varied from time to time; AND

WHEREAS it was agreed that further amounts required for the business of the partnership will be contributed by the parties hereto as may be mutually agreed upon from time to time; AND

WHEREAS the Board of Directors of the parties of the first to fifth parts approved the proposal for their respective Companies entering into partnership at their respective meetings.

WHEREAS the business of the partnership has already commenced with effect from 16th day of March, 1992.

WHEREAS the parties hereto are now desirous of recording the terms and conditions on which they have entered into partnership on the 16th day of March, 1992.

NOW THIS MEMORANDUM WITNESSETH and it is hereby recorded and confirmed as under:-

- 1. That the parties hereto have entered into partnership with effect from the 16th day of March, 1992 with the object of starting and carrying on the business of developing and dealing in real estate, constructing buildings and letting them out or selling them.*
- 2. That the business is being and shall continue to be carried on under the name and style of DLF Commercial Developers.*
- 3. That the party of the first part has brought all its right in the said plots of land admeasuring about 16.98 acre*

situated in DLF Qutub Enclave Complex and which are morefully described in the Schedule written hereunder into the common stock of partnership and all its right in the said plots became the property of the partnership firm with effect from 16th day of March, 1992.

4. That on account of the party of the first part having brought its right in the said plots into the common stock of the partnership, an amount of Rs.1150 lacs has been credited to the Capital Account of the party of the first part in the account books of the partnership firm.

5. That the party of the first part has already advanced an amount of Rs.1,27,90,215/- to the aforesaid subsidiary companies but whatever further amounts become payable to them, the same shall be paid and borne by the partnership firm.

6. That the party of the second to fifth part have agreed to bring by way of capital contribution an amount of Rs. One lac each and party of the sixth part agreed to bring in Rs. Fifty thousand. The parties hereto may decide to contribute such further amounts of capital as may be required form time to time.

7. That regular books of account shall be maintained in respect of the business of the partnership and on a day to be mutually agreed upon, the account books shall be closed annually and a statement of all the assets and liabilities and the profit and loss account shall be prepared and signed on behalf of each partner and got audited by Chartered Accountants approved by the parties by mutual consent from time to time. The parties hereto shall be entitled to received the net profit or bear the net loss (including profit or loss of a capital nature) in the following proportion:-

<i>1</i>	<i>M/s DLF Universal Ltd</i>	<i>76%</i>
<i>2</i>	<i>M/s Apollo Land & Housing Co Ltd.</i>	<i>5%</i>
<i>3</i>	<i>M/s Moonlight Builders & Developers</i>	<i>5%</i>

	<i>Ltd.</i>	
4	<i>M/s Sunrise Land & Housing Co Ltd.</i>	5%
5	<i>M/s DLF Builders & Developers Ltd.</i>	5%
6	<i>Mr. Rajinder Singh</i>	4%

7. *That the retirement, death, insolvency or liquidation of any of the parties hereto shall not lead to the dissolution of the partnership as between the surviving or continuing parties.”*

16.9 From the submission of the assessee made before the authorities below as well as before us, we see that the learned counsel for the assessee has tried to make out the nature and character of the transaction in question as under:

- i. That the said land contributed as capital contribution by the assessee to the firm was held as stock in trade by the assessee.
- ii. That the stock in trade was contributed to the firm as capital contribution by the assessee in the capacity of a partner.
- iii. That the stock in trade contributed to the firm as capital contribution by the assessee in the capacity of a partner was also held as stock in trade by the firm.

- iv. That the surplus arises to the assessee on account of revaluation of stock in trade at higher value than the cost to the assessee and from contributing the same to a firm as its capital is not a profit or gain from business as contribution of stock in trade by a partner as its capital to a firm at higher value is not a commercial or trading transaction in a business sense, and it does not amount to a “sale” or “transfer”.

16.10 The Revenue, on the other hand, has drawn inference/conclusion on the facts of the present case as under:

- i. That as per entries in the books of the assessee where the assessee has shown sale, reduction of stock in trade, crediting of sale account, crediting surplus in the P&L account, utilizing the surplus by way of distribution of dividend and carrying the surplus to balance-sheet, and as per entry in the books of the partnership firm where the assessee partner's account was credited and purchase account was debited, and even otherwise as per general law, there leaves no doubt that ownership in stock in trade has been passed over by way of

transfer or sale as understood in general law from assessee partner to a firm, and the transaction in question was a transaction of the sale between two different and distinct assessable entities.

- ii. That from the fact that the assessee company has entered into partnerships year after year with its subsidiaries and employees in a calculated manner, it is clear that the assessee has indulged in a colourable device to evade payment of correct taxes on transfer of stock in trade at an enhanced price, giving the transaction a colour of capital contribution by a partner to a firm as against real transaction of sale of stock in trade from one assessable entity to another.
- iii. Even otherwise, it is a case of capital asset brought in by partner to a partnership towards its capital contribution, and the profit or gains arising there from is chargeable to tax under the head “capital gains” as per provisions contained in section 45(3) of the Act inserted w.e.f. 01.04.1988

16.11 In so far as the fact that the land contributed by the assessee partner to a firm towards its capital was held as stock in trade by the assessee for its business of real estate before the same was so contributed as capital to a firm is concerned, there is no dispute between the parties.

16.12 Now, the question arises as to whether the personal asset being said land contributed by assessee towards its capital in a partnership firm at the time the assessee became a partner is to be treated as capital asset or continued to be treated as stock in trade of the assessee, or whether it is a case of sale or transfer of stock in trade or capital asset, as the case may be, from a partner to a firm. Undoubtedly, a dispute in this regard does indeed lie between the assessee and the department, which is to be decided in this case

16.13 As already observed above herein, the book-entries do not fix or regulate the liability of the assessee to tax. Moreover, the way in which entries are made by parties in their books of account or documents or papers is not determinative of the true and correct nature of the transaction. What is to be considered in the true and correct nature of the transaction with regards to the totality of the facts and circumstances of a

given case. Therefore, the entries in the books of accounts of the assessee and the partnership firm alone are not decisive or conclusive to decide the question whether the assessee has transferred its personal assets to a partnership firm by way of capital contribution or it is a normal sale in the ordinary course of its business or trading transaction. We have carefully gone through the terms of the deed of partnership entered into between the assessee and five other partners, four are subsidiary of the assessee company and one is an employee of the group company. There is no prohibition in law in entering into a partnership by a company with its subsidiaries. Further, under the law, a partner is permitted to bring his personal assets into a partnership by way of his capital contribution. The Hon'ble Supreme Court in the case of Sunil Siddharthbhai v. Commissioner of Income-tax (1985) 156 ITR 509 (SC) was dealing with the situation where an individual makes over his capital asset to a partnership as his contribution towards capital and the asset was valued for that purposes at the market value, and in that event, it was held by the Hon'ble Supreme Court that there was a transfer of capital asset within the meaning of section 45 of the Income Tax Act, 1961. Thus, there is no bar

in making over of personal asset belonging to a partner to a firm at a revalued market price as his contribution towards capital. Therefore, mere because, in the present case, the assessee has contributed land at revalued price, which is more than the cost price to the assessee, it cannot be said that the asset in question was not contributed to a firm by partner towards its capital. Even, such a transaction now takes care of by Section 45(3) of the Income Tax Act, 1961, inserted from the assessment year 1988-89. Sub-section (3) of Section 45 of the Act, effective from assessment year 1988-89, enacts that the profits and gains arising from the transfer of a capital asset by a person to a firm, in which he is or becomes a partner, by way of capital contribution or otherwise, shall be chargeable to tax as his income of the previous year in which such transfer takes place and, for the purposes of Section 48, the amount recorded in the books of account of the firm as the value of the capital asset shall be deemed to be the full value of the consideration received or accruing as a result of the transfer of the capital asset.

Whether the transaction is a colourable device or ruse to evade payment of correct taxes

16.14 In the case of Sunil Siddharthbhai v. Commissioner of Income-tax (supra), the Hon'ble Supreme Court issued a word of caution by stating that the principles laid down by them in that case will hold good if the firm or the transaction is a genuine one, and thus observed as follows:-

“If the transfer of the personal asset by the assessee to a partnership in which he is or becomes a partner is merely a device or ruse for converting the asset into money which would substantially remain available for his benefit without liability to income-tax on a capital gain, it will be open to the income-tax authorities to go behind the transaction and examine whether the transaction of creating the partnership is a genuine or a sham transaction and, even where the partnership is genuine, the transaction of transferring the personal asset to the partnership firm represents a real attempt to contribute to the share capital of the partnership firm for the purpose of carrying on the partnership business or is nothing but a device or ruse to convert the personal asset into money substantially for the benefit of the assessee while evading tax on a capital gain. The ITO will be entitled to consider all the relevant indicia in this regard, whether the partnership is formed between the assessee and his wife and children or substantially limited to them, whether the personal asset is sold by the partnership firm soon after it is transferred by the assessee to it, whether the partnership firm has no substantial or real business or the record shows that there was no real need of the partnership firm for such capital contribution from the assessee. All these and other

pertinent considerations may be taken into regard when the ITO enters upon a scrutiny of the transaction for in the task of determining whether a transaction is a sham or illusory transaction or a device or ruse he is entitled to penetrate the veil covering it and ascertain the truth.”

16.15 In the light of aforesaid word of caution emphasized by the Hon’ble Supreme Court, we proceed to examine whether the transaction of creating the partnership firm in the present case before us is a genuine or a sham transaction, or even where the partnership is genuine, whether the transfer of land in question as capital contribution by the assessee to a partnership firm in which the assessee became a partner was merely a devise or ruse for converting the land into money which would substantially remain available for assessee’s benefit without liability to income tax.

16.16 The AO doubted the genuineness of the firm and also the transaction, and he held that it was a sham transaction with colourable device to avoid tax. The AO stated that the new partnership firm constituted w.e.f. 16.03.1992 did not file any return of income for assessment year 1992-93 nor applied for registration of firm u/s. 185 as it

then stood. The AO had taken a note of the above-stated words of caution emphasized by Hon'ble Supreme Court in the case of Sunil Siddharthbhai v. Commissioner of Income-tax [1985] 156 ITR509 (SC). The AO also made a reference to the decision of Hon'ble Supreme Court in the MacDowell's reported in 154 ITR 148 (S.C.). The CIT(A) almost concurred with the findings of the AO on this aspect of the matter. The CIT(A) had highlighted a fact that the partnership firm was formed between the assessee and its 100% subsidiaries and one employee of the group, and he then hold that the transaction was made between interested and related persons as a colourable device to evade payment of taxes on surplus arising from the transaction.

16.17 On this aspect of the matter, the learned counsel for the assessee has submitted that the firm started filing of its return of income from next assessment year 1993-94 and compliance of provisions of section 184 of the Act as applicable from assessment year 1993-94 and subsequent years was duly made, and the AO has also assessed the firm as such till dates as is evident from assessment orders for assessment year 1993-94 to 1998-99, which are placed in the paper book filed by the

assessee. He, therefore, contended that the genuineness of the new firm cannot be doubted. In its comments against AO's observations (placed at page 10-21 of the paper books dated 01.04.2006 filed by the assessee on 10.04.2006/12.04.2006), the assessee stated that *"if the transaction of contribution of stock in trade, as capital to the new firm is sham, no transfer under (Sic) law take place as the transaction was not intended to be given effect to. In any case, the alleged surplus for enhancing the value of the land by book entries does not tantamount to sale as no one can sale to himself, in view of the law laid down by the Supreme Court in the case of Hind Construction Ltd. 83 ITR 211 (SC) and considered in Sunil Siddharthbhai v. Commissioner of Income-tax [1985] 156 ITR509 (SC) upholding the decision of Hind Construction Ltd."* Against CIT(A)'s observation, the assessee submitted his comments (placed at pages 22 to 23 of paper books filed by the assessee on 10.04.2006/12.04.2006) stating that since it was initial year of consisting of less than a month, no commercial activities were started during the year under consideration, but in subsequent assessment years from assessment year 1993-94, the firm has been duly assessed u/s. 143(3) of the Act by the AO, and all the

partners whether they are companies or individuals being separate entities, were being assessed to tax separately. It was further stated that the funds for carrying out business of the firm were raised by the firm. Before us, the learned counsel for the assessee has reiterated the comments of the assessee against the observations of the AO and the CIT(A) and pointed out that the Hon'ble Supreme Court in the case of Sunil Siddharthbhai (supra) issued a word of caution by stating that the principles laid down by their Lordship will hold good if the firm is a genuine one. The observation of Hon'ble Supreme Court at page 523 of the report was referred to, and with regard to the said observation, the learned counsel for the assessee submitted that these are very important observations of the Hon'ble Supreme Court and they wish to submit that in all the cases before the Hon'ble Bench, no money whatsoever has been withdrawn by the assessee from the firms against the contribution of stock in trade made towards the capital (see the written synopsis filed by the assessee's A/R before us)

16.18 Contra, the Id. Sr. Standing Counsel for the revenue has submitted that it is pertinent to note that the assessee company has entered

into partnerships year after year with its subsidiaries and employees in a calculated manner to evade payment of correct taxes, and it is a clear-cut case of colourable device, and the decisions of the Apex Court in the cases of Sunil Siddharthbhai (supra) and McDowell and Company (supra) support the finding of the AO. He further submitted that the AO doubted not only the genuineness of the firm but also the very transaction of contributing land held by the assessee as stock in trade to a partnership firm towards its capital at an enhanced value credited in the assessee's account as the assessee did not offer the surplus arising from the said transaction to tax on the ground that no gain or benefit had accrued to the assessee either by way of sale or transfer though the surplus was recognized in the profit and loss account prepared by the assessee.

16.19 We have considered this aspect of the matter touching the words of caution emphasized by the Hon'ble Supreme Court in the judgment in the case of Sunil Siddharthbhai (supra). The learned counsel for the assessee has rightly submitted that these are very important observations of the Hon'ble Supreme Court. However, he submitted that in all the cases before us, no money whatsoever has been withdrawn by

the assessee from the firms against the contribution of stock in trade made towards capital. In the light of the decision of Hon'ble Supreme Court in the case of Sunil Siddharthbhai (supra), it is clear that it is open to the Income Tax Authority to go behind the transaction and examine whether the transaction of creating the partnership is a genuine or sham transaction and, even where the partnership is a genuine, the transaction of transferring the personal asset to the partnership firm represents a real attempt to contribute to the share capital of the partnership firm for the purpose of carrying on the partnership business or is nothing but a device or ruse to convert the personal asset into money substantially for the benefit of the assessee while evading tax on a capital gain. To examine and decide this aspect of the matter, certain factors or indicia as mentioned in the said decision including some other pertinent consideration may be taken into regard, and the AO shall be entitled to penetrate the veil covering it and ascertain the truth. The relevant passage of this decision has been set out above in para 16.14 of this order.

16.20 From the material placed on record, we find that the partnership firm so constituted has been assessed to tax as such from year

to year by the department, and the department has not considered the firm as bogus or sham. Thus, we do not find any material to hold that the very transaction of creating the partnership itself is not genuine but a sham transaction. Having said so, we have to examine further even if the partnership is genuine, whether the transaction of transferring the assessee's personal asset in the form of land to the partnership firm represents a real attempt to contribute to the share capital of the partnership firm for the purpose of carrying on the partnership business or is nothing but a device or ruse to convert the personal asset into money substantially for the benefit of the assessee while evading tax on the surplus arising from the transaction. We find that the assessee's company has entered into partnership year after year with its subsidiaries and employees by contributing part of total land held by it to these firms. The year-wise details about constituting various firms is as under:-

DETAILS OF PARTNERSHIP FIRMS			
S. NO.	Name of Partnership Firm	Date of Partnership	Relevant Asst. Year
1	DLF Commercial Developers	16.03.1992	1999-1993
2	Real Estate Builders	31.01.1997	1997-1998
3	DLF Office Developers	24.02.1998	1998-1999
4	DLF Property Developers	24.02.1998	1998-1999

5	DLF City Centre	04.03.1999	1999-2000
6	DLF Holdings (now know as: DLF Residential Builders)	21.12.1998	1999-2000
7	DLF Home Builders	02.09.1998	1999-2000
8	DLF Residential Developers	30.06.1998	1999-2000
9	DLF Residential Partners	02.09.1998	1999-2000
10	DLF Phase – IV Commercial Developers	10.06.1999	2000-2001

16.21 In the present case, the assessee's capital account was credited by the amount of Rs. 11.50 crores being the market value of the land contributed by the assessee as valued by the expert. On a plot of land contributed by the assessee to a firm, the firm has developed/constructed three commercial complexes namely, "Super Mart 1", "Galleria" and "Plaza Tower" since 1997 and 2000 onwards, and some portion of "Galleria" and "Super Mart 1" have been sold, but no portion of "Plaza Tower" has been sold till date. The first sale of 20 units out of total 272 units of Super Mart 1 were made in A.Y. 1997-98, and the first sale of some units out of total 566 units of Galleria is stated to be made in the year of 2000. No business activities were carried out by the firm in the year of its constitution. The assessee's capital account in the books of a firm was credited by an amount of Rs. 11.50 crores on 16.03.1992 and it

remained as closing balance as on 31.03.1992. The capital so credited in assessee's account remained the same till 31.03.1998. However, on perusal of statement of accounts of a firm, viz., M/s. DLF Commercial Developers, for the year ended on 31.03.1993 to 31.03.1998, filed by the assessee before us, we find that besides partner's capital accounts, current accounts of each partner in the books of a firm have been created. These statement of accounts are placed at pages 39 to 64 of a paper book dated 01.04.2006 filed by the assessee on 10.04.2006/20.04.2006 before us in this appeal. On perusal of partner's current account as on 31.03.1993, it is seen that assessee's share in loss of Rs. 57191.16 for the year ended on 31.03.1993 has been debited in the assessee partner's current account. In the year ended on 31.03.1994, an amount of Rs. 4,46,75,888/- (i.e. 446.75 lacs) has been withdrawn by the assessee from the firm though the firm had incurred a loss of Rs.14,92,448/-, and the share in loss fallen in assessee's share was Rs. 11,34,260/-. It is thus seen that the assessee had received the sum of Rs. 4,46,75,888/- for its benefit in the year ended on 31.03.1994. The year wise withdrawal made by the assessee from the

firm vis-à-vis its share in profit or loss of a firm upto 31.03.1998 are detailed as under:-

<u>Year ended</u>	<u>Withdrawal (in Rs.) (Receipt)</u>	<u>Profit/(loss)</u>
31.03.1993	NIL	(57,191/-) Loss
31.03.1994	4,46,75,888/-	(11,34,260/-) Loss
31.03.1995	2,64,45,376/-	(5,25,877/-) Loss
31.03.1996	(2,08,99,797/-)	(3,24,237/-) Loss
31.03.1997	31,77,26,485/-	2,25,02,835/- Profit
31.03.1998	22,51,74,769/-	3,29,60,839/- Profit
<u>Total</u>	<u>59,31,22,721/-</u>	<u>5,34,22,109/-</u>

The year-wise debit balance in the current account of assessee in the books of firm are determined in the balance-sheet as under:-

<u>Year Ended</u>	<u>Debit balance in partners current account</u>
31.03.1993	87,191/-
31.03.1994	4,58,67,341/-
31.03.1995	7,28,38,594/-
31.03.1996	5,22,63,034/-
31.03.1997	34,74,86,684/-
31.03.1998	53,97,00,614/-

16.22 From the above details, it is thus established that the assessee has been regularly withdrawing money from the firm to substantial extent more than the aggregate amount of capital contributed by the assessee and share of profit fallen in assessee's share, and even within the initial period of three years from the date of constitution of firm, the assessee had withdrawn the sum of Rs. 4,46,75,888/- in the year ended on 31.03.1994 and sum of Rs. 2,64,45,376/- in the year ended on 31.03.1995, and thereafter it continued to withdraw the money in each year with the net debit balance of Rs. 53.97 crores as on 31.03.1998 as against capital of Rs. 11.50 crores. The aggregate amount of money withdrawn by the assessee comes to Rs. 59,31,22,721/- (i.e. Rs. 59.31 crores) as against aggregate amount of profit fallen in assessee's share amounting to Rs. 5,34,22,109/- (i.e. Rs. 6.34 crores) till 31.03.1998, and thus the amount over-withdrawn by the assessee comes to Rs. 53,97,00,612/- (i.e. 53.97 crores) as against capital of Rs. 11.50 crores standing in the name of the assessee as on 31.03.1998.

16.23 In the light of the aforesaid facts establishing that the assessee had over withdrawn net money to the extent of Rs. 53.97 crore

till 31.03.1998, the submission of the assessee that no money whatsoever has been withdrawn by assessee from the firm against contribution of stock in trade made towards the capital is totally misleading and false. The assessee has tried to give a totally wrong picture about the huge money withdrawn by it by debiting the same in a separate current account of partners and that too without making a whisper about it in its submissions made in this case either before the authorities below or before us. There is no dispute as to the proposition that an act which is otherwise valid in law cannot be treated as non est merely on the basis of some under lying motive supposedly resulting in some economic detriment of prejudice to the national interest as so observed by the Hon'ble Supreme Court in Union of India vs. Azadi Bachao Andolan (2003) 263 ITR 763. But this proposition is applicable in so far as the act of assessee in constituting partnership firm by contributing its personal assets to a firm as capital contribution as concerned. However, with regard to assessee's conduct in converting land into money by withdrawing huge and substantial money from the firm is to be viewed from the words of caution emphasized by Hon'ble Supreme Court in the case of Sunil Siddharthbhai

v. Commissioner of Income-tax (supra) and also in view of the following observation of Constitution Bench of Hon'ble Supreme Court in the case of *Mc Dowell & Co. Ltd. v. Commercial tax Officer* [1985] 154 ITR 148(SC), which has been referred to in the case of *Union of India vs. Azadi Bachao Andolan* and was quoted with approval:-

“Tax planning may be legitimate provided it is within the framework of law. Colourable devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honourable to avoidable the payment of tax by resorting the dubious methods. It is the obligation of every citizen to pay the taxes honestly without resorting to subterfuges.”

16.24 From this calculated device adopted, by the assessee, by withdrawing substantial amount of money for its benefit and debiting the same in its current account, it becomes clear that though the partnership firm as such is genuine, the transfer or contribution by the assessee of its personal land to the share capital of the firm represent a device or ruse for converting the land into money substantially withdrawn by the assessee from the firm for its benefit. Thus, the entry of Rs. 11.50 crores being value of land credited in assessee's capital account cannot be considered to be imaginary or notional one with no benefit or gain to the assessee.

Therefore, the assessee's contention that the amount of Rs. 11.50 crores credited in assessee's capital account cannot be made a basis to work out any gain or profit arising to the assessee from the transaction of transferring its personal asset as capital contribution to a firm in which the assessee became a partner is not acceptable and is thus rejected. Therefore, even the partnership firm is considered to be genuine, the transaction of transferring assessee's land by way of capital contribution to the partnership at a market value more than the cost to the assessee represents a devise or ruse to convert the personal land of the assessee into money substantially for the benefit of the assessee while evading tax on a surplus amount arising to the assessee from the said transaction. In this view of the matter, which we have taken in the light of word of caution mentioned by the Hon'ble Supreme Court in the case of Sunil Siddharthbhai (supra), the amount representing the value of land contributed by the assessee as its capital in a firm in which the assessee became a partner and which has been credited in the assessee's capital account, is to be considered as a consideration received by the assessee on the transfer of its personal asset to a partnership firm. We, therefore, hold

that the surplus arising from making over assessee's personal asset, i.e. said plot of land in question, to the firm as his contribution to its capital account is a profit or gain accrued to the assessee and is chargeable to tax.

Whether transaction is on capital field or the revenue

16.25 Now, we have to examine whether the transaction in question is on capital field or the revenue, and the surplus so arising to the assessee is assessable to tax as profits from business or capital gain. It is an admitted position that the land in question has been transferred to a firm towards capital contribution by the assessee in the capacity of a partner. The firm so constituted is considered to be genuine one. The transaction cannot, therefore, be considered to be made in the nature of any normal and ordinary transaction of sale in course of any commercial or trading activity. The land has been contributed to firm as capital by the assessee partner in its capacity as a partner and not as a trader in any trading transaction. We are, therefore, in agreement with the contentions of the learned counsel for the assessee that the land in question belonging to the assessee was contributed to a partnership firm as assessee partner's contribution towards capital in the partnership when the assessee entered

into a partnership with five other partners, and so, the transaction cannot be regarded as a trading or commercial transaction in the business sense. Resultantly, the transaction of making over of any personal assets of a partner to a firm as his contribution towards capital is, therefore, to be regarded as made on a capital field.

Nature and character of the asset contributed by a partner to a firm as capital contribution at the time when the asset is employed in the transaction of contributing capital by a partner to a firm as his capital contribution

16.26 This now leaves us to determine the nature and character of the asset contributed by assessee partner to a firm as its capital contribution, at the time when he became a partner. The case of the assessee advanced before us is that the land contributed by assessee to the firm as its capital contribution at the time when the assessee became a partner in a firm, was nothing but stock in trade in as much as the same was held by the assessee as stock in trade of its business of real estate. On the contrary, the department has advanced an alternative argument that in case the transaction is regarded as a case of capital contribution of asset by a partner, and not a sale of asset by a partner to a firm, the asset

contributed by partner to a firm as its capital contribution should be regarded as capital asset brought in by the partner to the firm in which he became a partner.

16.27 To resolve this controversy, we think that it is appropriate for us to find out what right arises or accrues to a partner from the transaction of contributing his personal asset as its capital in the partnership firm in which he becomes a partner. In this respect, making a gainful reference to the judgment of three judges of the Hon'ble Supreme Court in the case of Sunil Siddharthbhai v. Commissioner of Income-tax (1985) 156 ITR 509 (SC) would suffice as, in this decision, the Hon'ble Supreme Court has analyzed and considered number of decisions decided times and again by the various High Courts and also by Supreme Court including its own decision in the case of Hindi Construction Co. (supra) and Malabar Fisheries (supra), which have been heavily relied upon by the ld counsel for the assessee to support his contention advanced before us.

16.28 In the said decision of Hon'ble Supreme Court in the case of Sunil Sidharthabhai (supra), it has been held that the consideration for the making over of the personal asset by the partner to a firm is the right,

which arises or accrues to the partner, during the subsistence of the partnership, is to get his share of the profit from time to time, and after the dissolution of the partnership or with his retirement from the partnership, to get the value of his share in the net partnership assets as on the date of the dissolution or retirement after deduction of liabilities and prior charges. In other words, in consideration for the transfer of the personal asset by a partner to a partnership firm towards his capital contribution, in which he becomes a partner, the following rights arises or accrues to a partner:-

- i. Right to get his share of profit from time to time during the subsistence of the partnership; and
- ii. On the dissolution of partnership or with his retirement from the partnership, the right to get the value of his shares in the net partnership asset as on the date of dissolution or retirement after deduction of liabilities and prior charges.

16.29 In the aforesaid decision in the case of Sunil Siddharthbhai v. Commissioner of Income-tax (Supra), Hon'ble Supreme Court further observed that at the time when the partner transfers his personal asset to

the partnership firm, there can be no reckoning of the liabilities and losses which the firm may suffer in the years to come. All that lies within the womb of the future. It is impossible to conceive of evaluating the consideration accrued by the partner when he brings personal asset in the partnership firm, when neither can the date of dissolution or retirement be envisaged nor can there be any ascertainment of liability and prior charges which may not have even arisen yet. It was further observed that when partner's personal asset merge into the capital of partnership firm, the corresponding credit entry is made in the partner's account in the books of the partnership, but that entry is made merely for the purpose of the adjusting the rights of the partner's inter-se, when the partnership is dissolved or partner retires. From this, it is, thus, clear that by bringing his personal asset towards capital in the partnership firm, the partner acquires rights to get share of the profits from time to time, and to get the value of his share in the net partnership asset as on the date of dissolution or retirement after deduction of liabilities and prior charges, and the credit entry in the partner's account on account of personal assets brought in into the partnership firm towards capital contribution is made merely for the

purpose of the adjusting the rights of the partners inter-se when the firm is dissolved or any partner retires. In this case, it has also been held that whatever is brought into the partnership ceases to be exclusive property of the person who brought it in, that is, and exclusive interest is reduced to a shared interest, as so contended by the assessee also vide contentions raised into ground no. 1.4 by the assessee.

16.30 The Hon'ble Supreme Court in the case of Sunil Siddharthbhai (surpa) has noted the observation made in its own judgment in the case of Addanki Narayanapa vs. Bhaskara Krishanappa AIR (1966) (SC) 1300; (1966) 3 SCR 400 (SC), where the Hon'ble Supreme Court explained the identical proposition as laid down in the case of Sunil Siddharthbhai v. Commissioner of Income-tax (supra), by observing as under:-

".....Whatever may be the character of the property which is brought in by the partners when the partnership is formed or which may be acquired in the course of the business of the partnership it becomes the property of the firm and what a partner is entitled to is his share of profits, if any, accruing, to the partnership from the realisation of this property, and upon dissolution of the partnership to a share in the money representing the value of the property. No doubt, since a firm has no legal existence, the

partnership property will vest in all the partners and in that sense every partner has an interest in the property of the partnership. During the subsistence of the partnership, however, no partner can deal with any portion of the property as his own. Nor can he assign his interest in a specific item of the partnership property to anyone. His right is to obtain such profits, if any, as fall to his share from time to time and upon the dissolution of the firm to a share in the assets of the firm which remain after satisfying the liabilities set out in clause (a) and sub-clauses (i), (ii) and (iii) of clause (b) of section 48....."

16.31 In the aforesaid case of Addanki Narayanapa vs. Bhaskara Krishanappa (SC) (supra) the position has been elaborated by Hon'ble Supreme Court, which has been noted by the Hon'ble Supreme Court in the case of Sunil Sidharthbhai (supra), as under:-

"...The whole concept of partnership is to embark upon a joint venture and for that purpose to bring in as capital money or even property including immovable property. Once that is done whatever is brought in would cease to be the exclusive property of the person who brought it in. It would be the trading asset of the partnership in which all the partners would have interest in proportion to their share in the joint venture of the business of partnership. The person who brought it in would, therefore, not be able to claim or exercise any exclusive right over any property which he has brought in, much less over any other partnership property. He would not be able to exercise his right even to the extent of his share in the business

of the partnership. As already stated, his right during the subsistence of the partnership is to get his share of profits from time to time as may be agreed upon among the partners and after the dissolution of the partnership or with his retirement from partnership of the value of his share in the net partnership assets as on the date of dissolution or retirement after a deduction of liabilities and prior charges..."

16.32 In the case of Sunil Siddharthbhai (supra), the Apex Court further observed as under:-

It is apparent, therefore, that when a partner brings in his personal asset into a partnership firm as his contribution to its capital, an asset which originally was subject to the entire ownership of the partner becomes now subject to the rights of other partners in it. It is not an interest which can be evaluated immediately, it is an interest which is subject to the operation of future transactions of the partnership, and it may diminish in value depending on accumulating liabilities and losses with a fall in the prosperity of the partnership firm. The evaluation of a partner's interest takes place only when there is a dissolution of the firm or upon his retirement from it. It has sometimes been said, and we think erroneously, that the right of a partner to a share in the assets of the partnership firm arises upon dissolution of the firm or upon the partner retiring from the firm. We think it necessary to state that what is envisaged here is merely the right to realise the interest and receive its value. What is realised is the interest which the partner enjoys in the assets during the subsistence of the partnership firm by virtue of his status as a partner

and in accordance with the terms of the partnership agreement. It is because that interest exists already before dissolution, as was held by this Court in Malabar Fisheries Co. v. CIT [1979] 120 ITR 49, the distribution of the assets on dissolution does not amount to a transfer to the erstwhile partners. What the partner gets upon dissolution or upon retirement is the realisation of a pre-existing right or interest. It is nothing strange in law that a right or interest should exist in praesenti but its realisation or exercise should be postponed. Therefore, what was the exclusive interest of a partner in his personal asset is, upon its introduction into the partnership firm as his share to the partnership capital, transformed into a shared interest with the other partners in that asset. Qua that asset, there is a shared interest. During the subsistence of the partnership the value of the interest of each partner qua that asset cannot be isolated or carved out from the value of the partner's interest in the totality of the partnership assets. And in regard to the latter, the value will be represented by his share in the net assets on the dissolution of the firm or upon the partner's retirement.”

16.33 The Hon’ble Supreme Court in the aforesaid case of Sunil Siddharthbhai v. Commissioner of Income-tax (Supra) proceeded further to observe as under:-

The learned counsel for the assessee has attempted to draw an analogy between the position arising when a personal asset is brought by a partner into a partnership as his contribution to the partnership capital and that which arises when on

dissolution of the firm or on retirement, a share in the partnership assets passes to the erstwhile partner. It has been held by this Court in CIT v. Dewas Cine Corporation [1968] 68 ITR 240, CIT v. Bankey Lal Vaidya [1971] 79 ITR 594 and recently in Malabar Fisheries Co. v. CIT [1979] 120 ITR 49 as well as by the Punjab and Haryana High Court in Key Engg. Co. v. CIT [1971] 82 ITR 950, the Kerala High Court in CIT v. Nataraj Motor Service [1972] 86 ITR 109 and the Gujarat High Court in CIT v. Mohanbhai Pamabhai [1973] 91 ITR 393 that when a partner retires or the partnership is dissolved, what the partner receives is his share in the partnership. What is contemplated here is a share of the partner qua the net assets of the partnership firm. On evaluation, that share in a particular case may be realised by the receipt of only one of all the assets. What happens here is that a shared interest in all the assets of the firm is replaced by an exclusive interest in an asset of equal value. That is why it has been held that there is no transfer. It is the realisation of a pre-existing right. The position is different, it seems to us, when a partner brings his personal asset into the partnership firm as his contribution to its capital. An individual asset is the sole subject of consideration. An exclusive interest in it before it enters the partnership is reduced on such entry into a shared interest.

16.34 In this decisions, the Hon'ble Supreme Court further observed that there is no difficulty in accepting proposition that when a partner hands over a business asset to a partnership firm as his contribution to its capital, he cannot be said to have effected a sale. But

while the transaction may not amount to a sale, can it be described as a transfer of some other kind?

16.35 In the said case the Hon'ble Supreme Court then observed and held as under:-

“ In its general sense, the expression 'transfer of property' connotes the passing of rights in the property from one person to another. In one case there may be a passing of the entire bundle of rights from the transferor to the transferee. In another case, the transfer may consist of one of the estates only out of all the estates comprising the totality of rights in the property. In a third case, there may be a reduction of the exclusive interest in the totality of rights of the original owner into a joint or shared interest with other persons. An exclusive interest in property is a larger interest than a share in that property. To the extent to which the exclusive interest is reduced to a shared interest it would seem that there is a transfer of interest. Therefore, when a partner brings in his personal asset into the capital of the partnership firm as his contribution to its capital, he reduces his exclusive rights in the asset to shared rights in it with the other partners of the firm. While he does not lose his rights in the asset altogether, what he enjoys now is an abridged right which cannot be identified with the fullness of the right which he enjoyed in the asset before it entered the partnership capital

16.36 With reference to the provisions contained in section 17(1)(b) of the Registration Act, whether there is transfer when

partner's exclusive interest, on its introduction as capital in the firm is reduced into a shared interest, the Court observed as under:-

“Our attention has also been invited to clause (b) of sub-section (1) of section 17 of the Indian Registration Act, 1908, which requires the registration of non-testamentary instruments which purport or operate to create, declare, assign, limit or extinguish, whether in present or in future, any right, title or interest, whether vested or contingent, of the value of one hundred rupees and upwards, to or in immovable property; and to the view taken by the Courts in this country that when a person brings in even his immovable property as his contribution to the capital of the firm no written document or registration is required under that clause. That view was expressed in Firm Ram Sahay Mall Rameshwar Dayal v. Bishwanath Prasad AIR 1963 Pat. 221. The learned Judges relied on the English law that the personal assets introduced by a partner into the firm as his contribution to its capital becomes the property of the firm by reason of the intention and agreement of the parties. The view does not spring from the consideration that there is no transfer, the view is that no document of transfer is required and that, therefore, registration is unnecessary. The Patna High Court reiterated that view in Sudhansu Kanta v. Manindra Nath AIR 1965 Pat. 144.”

16.37 Thereafter, with reference to shares brought in by the partner into the firm, the Hon'ble Supreme Court has held as under:-

“Accordingly, we hold that when the assessee brought the shares of the limited companies into the

partnership firm as his contribution to its capital, there was a transfer of a capital asset within the terms of section 45. In this view of the matter, we agree with the conclusion reached by the Kerala High Court in A. Abdul Rahim, Travancore Confectionery Works v. CIT [1911] 110 ITR 595 (FB), the Karnataka High Court in Addl. CIT v. M.A.J. Vasanaik [1979] 116 ITR 110 and by the Gujarat High Court, in the judgment under appeal.”

Various propositions of law laid down by the Hon’ble Supreme Court in the case of Sunil Siddharthbhai v. Commissioner of Income-tax 156 ITR 509

16.38 From the aforesaid decision of three judges of the Hon’ble Supreme Court in the case of Sunil Siddharthbhai (supra), the position of law that emerging is summarized as under:

- i. The whole concept of partnership is to embark upon a joint venture and for that purpose to bring in as capital money or even property including immovable property. Once that is done whatsoever is brought in would cease to be the exclusive property of the person who brought it in. It would be the asset of the partnership in which all the partners would have interest in proportion to their share in the joint venture of the business of partnership.

- ii. The person who brought in his personal asset into a firm would not be able to claim or exercise any exclusive right over any asset which he has brought in, much less over any other partnership asset. He would not be able to exercise his right even to the extent of his share in the business of the partnership during the subsistence of the partnership, no partner can deal with any portion of the partnership asset as his own.
- iii. Where a partner of a firm makes over his personal assets to a firm as his contribution towards capital, and whatever may be the character of the property which is brought in by the partners when the partnership is formed, what a partner, is entitled to or what right, which accrues or arises to a partner, is, during subsistence of partnership, to get his shares of the profits from time to time, and upon dissolution of the firm or with his retirement from the partnership, to get the value of his shares in the net profit from assets as on the date of the dissolution or retirement after deduction of liabilities and prior charges.

- iv. When a partner brings in his personal asset into the partnership firm as his contribution to capital, asset which originally was subject to the entire ownership of the partner becomes now the subject to the rights of other partners in it. In other words, what was the exclusive interest of a partner in his personal asset is upon its introduction into the partnership firm as his share to the partnership capital, transformed into a shared interest shared with the other partners in that asset. Qua that asset, there is a shared interest. It is not an interest which can be evaluated immediately. It is an interest which is subject to the operation of future transaction of the partnership.
- v. The evaluation of a partner's interest takes place only when there is dissolution of the firm or upon his retirement from it, and what is realized is the interest which the partner enjoys in the asset during the subsistence of the partnership firm by virtue of his status as a partner, and in accordance with the terms of the partnership agreement. It is because that interest exists already before dissolution, as was held by Hon'ble Supreme Court in the case of *Malabar Fisheries Co. v. Commissioner of Income-tax* [1979] 120

ITR 49 (SC), that the distribution of the assets on dissolution or upon the retirement is the realization of a pre-existing right or an interest, which does not amount to a transfer to the erstwhile partners. What the partner gets upon dissolution or upon retirement is the realization of a pre-existing right or interest. That is why it has been held that there is no transfer.

- vi. When a partner hands over its business asset to a partnership firm as his contribution to its capital, he cannot be said to have effected the sale.
- vii. In its general sense, the expression “transfer of property” connotes the passing of right in property from one person to another. In one case there may be a passing of the entire bundle of rights from the transferor to the transferee. In another case, the transfer may consist of one of the estates only out of all the estates comprising the totality of the rights in the property. In a third case, there may be a reduction of the exclusive interest in the totality of rights of the original owner into a joint or shared interest with other persons, and an exclusive interest in property is larger than the share in that

property. To the extent to which the exclusive interest is reduced to a shared interest, there is a transfer of interest. Therefore, when a partner brings in his personal asset into the capital of the partnership as his contribution to its capital, he reduces his exclusive rights in the asset to shared rights in it with the other partners of the firm. While he does not lose his right in the asset altogether, what he enjoys now is an abridged right which cannot be identified with the fullness of the right which he enjoyed in the asset before it entered the partnership capital.

- viii. When a partner retires or partnership is dissolved, what the partner received is his shares in the partnership, i.e. the net asset of the partnership firm. What happens here is that a shared interest in all the assets of the firm is replaced by an exclusive interest in an asset of equal value. That is why it has been held that there is no transfer. It is the realization of a pre-existing right. The position is different when a partner brings his personal asset into the partnership firm as his contribution to its capital. An individual asset is the sole subject of consideration. An exclusive interest in it before it

enters the partnership is reduced on such entry into a shared interest.

- ix. When a partner of a firm makes over his personal asset, which are held by him, to a firm as his contribution towards capital, there is a transfer of a asset in its general sense because the exclusive interest of the partner in personal asset is reduced, on their entry into the firm, into a shared interest. In other words, to the extent to which the exclusive interest is reduced to a shared interest it would seem that there is a transfer of interest. In other words, to the extent to which the exclusive interest is reduced to a shared interest, it would seem that there is a transfer of interest.
- x. At the time when the partner transfers his personal asset to partnership firm there can be no reckoning of the liabilities and losses which the firm may suffers in years to come. It is impossible to conceive of evaluating the consideration acquired by the partner when he brings his personal asset into the partnership firm when neither can the date of dissolution or retirement be envisaged nor can there be any ascertainment of liabilities and prior charges which

may not have even arisen yet. Therefore, the consideration which a partner acquires on making over his personal asset to the firm as his contribution as its capital cannot fall within the terms of section 48 of the Act.

- xi. The view that when a person brings in even his immovable property as his contribution to the capital of the firm, no document or registration is required under section 17(1)(b) of the Registration Act does not spring from the consideration that there is no transfer.
- xii. On introducing his personal asset into the partnership firm as his contribution to its capital, it cannot be said that any income or gain arises or accrues to the assessee in a true commercial sense which a businessman would understand as real income or gain.
- xiii. However, the situation would be different if it transpires that either partnership firm in question is not genuine or if the partnership firm is genuine, the transaction of transferring the personal asset to the partnership firm represents a device or ruse to convert the personal asset into money substantially for the benefit of the assessee while evading tax on capital gain, and in that respect the AO is entitled to

consider all the relevant indicia and other pertinent consideration in this regards, and he is entitled to penetrate a veil covering and ascertain the truth.

Nature of right accrues or arises to a partner on his capital contribution of his personal assets to af firm in which he is or becomes a partner.

16.39 From the said decision of the Hon'ble Supreme Court in the case of Sunil Siddharthbhai v. Commissioner of Income-tax (Supra), it is settled that when the partner brings personal asset into the partnership firm as his contribution to its capital, and whatever may be the character of the property which is brought in by the partner when the partnership firm is formed or which may be acquired in the course of the business of the partnership it becomes the property of the firm and what right the partner acquired is to get his shares of profit during the subsistence of partnership, and upon dissolution of the partnership or on retirement, to share in the asset of the firm which remain after satisfying the liabilities. Thus, the nature of the right acquired by the assessee by contributing his personal asset of whatever character in to a partnership firm towards its

capital is a right of capital in nature to claim share of profit in the partnership firm, and upon the dissolution of the firm or his retirement, the share in the asset of the firm after satisfying the liabilities. It makes it clear that the transaction of becoming a partner and contribution of asset of whatever character as capital in the firm in which one becomes a partner is undoubtedly on a capital field, and not in the nature of any commercial or trading transaction. It is also not the case of the assessee that contribution of assessee's asset being land in question to a partnership firm towards its capital when assessee became a partner was a commercial or trading transaction. When it is accepted that the transaction is not in the nature of trading or commercial transaction, the question of treating the asset involved in that transaction as stock in trade does not arise. It is altogether a different matter that before contributing any personal asset by the partner to a firm, it might have a character of stock in trade or capital asset or any other asset in the hands of a partner, but at the time when the same is contributed as capital contribution in a firm in which the assessee becomes a partner, it would certainly have a character of capital asset only having regard to the capital nature of the transaction and nature of rights

acquired by a partner in the firm on his becoming a partner. In other words, whatever may be the character of the property in the partner's hand before the same is brought in by the partner as capital contribution when a partnership is formed and he becomes a partner, the property brought in partakes the character of a capital asset, and in consideration of it being contributed to a partnership towards its capital, the partner acquires a right to get his share of profit in the firm, and upon dissolution of the partnership firm or his retirement, a partner is entitled to get share in the asset of the firm which remain after satisfying the liabilities of the firm.

Whether a partner hands over his business asset to a firm as his capital contribution, he can be said to have effected a sale.

16.40 The Id. counsel for the assessee has rightly contended that when a partner hands over his business asset to a partnership firm as his contribution to its capital, he cannot be said to have effected a sale within the meaning of Sales of Goods Act, meaning thereby that the transfer of partner's personal asset to a partnership firm as his contribution to its capital is not a commercial or trading transaction. We find no difficulty in accepting this proposition in the light of the decision of Hon'ble Supreme

Court in the case of Commissioner of Income-tax v. Hind Construction Ltd [1972] 83 ITR 211 (SC), which has been accepted and approved in the case of Sunil Siddharthbhai v. Commissioner of Income-tax (Supra). When a view that when a partner hands over his personal asset of whatever character to a partnership firm as his contribution to its capital, the partner cannot be said to have effected a sale of that item is accepted, the question of treating that personal asset as stock in trade in the course of transaction when the same was contributed to a partnership firm as its capital, cannot arise irrespective of whatever may be the character while remaining in the hands of a partner before the same was contributed by him to a firm as its capital. In order to decide the character of an asset at the time when it transferred to a firm by a partner by way of capital contribution, one has to determine the nature of the asset that attaches to it at the time when the transaction of contributing the capital by a partner to a firm takes place, and such quality or character of an asset cannot be altered or affected by any previous or subsequent act or conduct of a partner or a firm in relation to that asset which has been contributed as capital in partnership firm by that partner. The treatment given or the

entry made in the books of accounts by the partner in his books of accounts or by the partnership firm in their books with regard to any asset contributed by a partner as its capital to a firm is no more than a previous or subsequent act or conduct, which shall have no effect upon the very character attached to the asset at the time of transaction under which the asset is transferred by the partner to a partnership firm towards its capital contribution. In this view of the matter and in the light of the fact that when partner hands over its personal asset of whatever character to a partnership firm as his contribution to its capital, the transaction cannot be said to be in the nature of trading or commercial one so as to treat the asset involved in such transaction as stock in trade. The logical and rational view or conclusion that one could arrive is that at the time when any asset is transferred by a partner to a partnership firm as his contribution to its capital, the asset cannot retain the character of stock in trade at that material point of time and in the course of such contribution of capital as the same is not employed in any commercial or trading transaction carried out in the course of any business activity of the partner. There is no quarrel as to the contention of the assessee that as per

definition of “capital asset” defined u/s. 2(14) of the Act, any stock in trade, consumable stores or raw materials held for the purpose of the business or profession of the assessee are excluded from the ambit of “capital asset”. In other words, an exception has been provided in the definition of “capital asset” under section 2(14) of the Act to exclude “stock in trade or consumable stores or raw material held by the assessee for the purposes of his business or profession” from the purview of a capital asset. The phrase “stock in trade” would mean all those goods or commodities in which the particular individual deals in the sense of buying or selling in the course of its business activity. The stock in trade held by the assessee for the purpose of his business or profession would retain its same character only if it continues to be employed for the purpose of any business or commercial activity carried out by the assessee. This would mean that when a businessman withdraws his stock in trade held by him for the purpose of business or profession from his business for some purpose or purposes other than the purpose of dealing with it in the course of any trading or commercial transaction, it would lose its character of being “stock in trade”, and will acquire such character with regard to the

purpose for which same has been employed. In other words, the stock in trade held by the assessee for the purpose of his business or profession shall get converted into such other nature of asset having regard to the purpose for which it has been withdrawn from the business. In business, it does happen that capital asset is converted into stock in trade, and stock in trade into capital asset or asset ceases to be stock in trade. For example, where a dealer in jewellery brings in his personal jewellery to business, there is a conversion of capital asset to stock in trade. Similarly, a stock in trade is converted into a capital asset, when the dealer in jewellery withdraws jewellery from his business for his personal use or for holding the same as investment. Where a grocer draws a part of his stock for his personal consumption, there is a conversion from stock in trade to personal investment on withdrawal of stock in trade. In the case of a grocer, when he withdraws part of his stock for his personal consumption, stock in trade so withdrawn would not retain the character of stock in trade at the time when a grocer consumes that item withdrawn from his business; it is not a loss to business but it is regarded as a personal expenses or drawing. In a situation where a grocer withdraws a

part of his stock for his personal consumption, he would debit his business by the cost at which stock in trade was acquired, and no notional value can be attached thereto. The grocer would debit the cost of the stock withdrawn by him for his personal consumption which would negative the cost of purchase debited in the trading account, and the item shall be considered to be out of the purview of stock in trade at the time the grocer withdraws his stock for his personal consumption. In the case of *Sir Kikabhai Premchand v. Commissioner of Income-tax* (1953) 24 ITR 506 (SC), the Hon'ble Supreme Court has decided that it is only a cost that should be the basis for computing the business income on conversion of stock withdrawn from business. In this case, the Hon'ble Supreme Court has taken up an illustration of a dealer in rice held as stock, drawing a small part of it for his home consumption. If he had debited the purchase to personal account, even initially, there would have been no profit element reckoned on such purchases. It should, therefore, make no difference merely because such stock is merely routed through business books. In the decision in the case of *Sir Kikabhai Premchand v. Commissioner of Income-tax* (supra), the Hon'ble Supreme Court further

observed that withdrawing stock in trade by a businessman is not a business transaction and by act of withdrawal no profit can be said to accrue to him and, accordingly it is sufficient if said businessman has credited it business with cost price of stock so withdrawn. It is well settled that profits from sale of stock in trade in the course of trading operation is business profit. As a natural corollary, when any asset is not employed in the course of any trading or commercial operation, the same cannot be considered to be stock in trade held for the purpose of business. Further, in the light of the ratio of decision of Hon'ble Supreme Court in the case of Sir Kikabhai Premchand vs. CIT (surpa), we may say that when stock in trade by a businessman is withdrawn from his business, its nature and character gets converted into a different character, and the act of withdrawing the stock in trade by a businessman cannot be held to be a business or commercial or trading transaction in the sense a businessman would understand. In Sir Kikabhai Premchand v. Commissioner of Income - tax (supra), where a part of the stock in trade was withdrawn by the assessee and endowed them on certain trusts of which the assessee was a trustee, the Hon'ble Supreme Court held that there being no commercial

or trading transaction, it was not a case of sale of stock in trade and the withdrawal of stock in trade should be taken at cost . The Supreme Court further held that no man can be supposed to be trading with himself. From the said decision, it thus transpires that withdrawal of stock in trade from business is not a trading or commercial transaction in the course of carrying on business, and the withdrawal of stock in trade should be taken at cost. In the present case, when the assessee withdraws some plot of land being part of stock in trade for making contribution to a partnership firm as its capital at the time when he became a partner, there is a conversion on withdrawal of stock in trade into capital asset in as much as, as already discussed above, the act of contributing personal asset into a partnership firm as its capital when assessee becomes a partner in a firm is a transaction on capital field.

16.41 With regard to the proposition that one may convert a capital asset into stock in trade or vice-versa, a useful reference may be made to one more decision of Hon'ble Supreme Court in the case of Commissioner of Income-tax v. Bai Shirinbai K. Kooka [1962] 46 ITR 86 (SC), where the assessee held certain shares by way of investment,

converted those shares into stock in trade of his business dealing in shares, and later on sold the shares, it was held that the profits on sale of shares sold by the assessee must be computed at the difference between sale price and the market price of the shares on the date of their conversion as stock in trade of the business of the assessee. As already observed above, whether there is any such conversion of stock in trade to capital asset or capital asset into stock in trade can only be decided in the light of the facts and circumstances of a given case. The taxability of the amount being the difference between the cost of asset originally acquired as investment and the market price of the asset on the date of its conversion from capital asset to stock in trade, now takes care of by the provisions contained in sub-section (2) of section 45 of the Act, which has been inserted w.e.f. 01.04.1985 with a view to bring the aforesaid difference to tax as capital gain on conversion of investment into stock in trade. Since market value was adopted on conversion of investment into stock in trade in the aforesaid decision of Hon'ble Supreme Court in the case of Commissioner of Income-tax v. Bai Shirinbai K. Kooka (supra), it was considered fair by the legislature that the assessee should pay tax on such capital gains with

reference to the market value adopted when computing the business income arising to the assessee from investment or personal asset converted into stock in trade. Conversely, a stock in trade can be converted into capital asset, and the tax on transfer of a such capital asset will be imposed in the year in which such capital asset is sold or otherwise transferred after deducting there from the cost of acquisition, and other deductions as provided under the law.

16.42 In the instant case of the assessee, it is not in dispute that the said land in question, amongst others, was acquired as stock in trade of the assessee's business. However, later on in the year under consideration, the said land in question being a part of the total stock in trade of the business got revalued by the assessee, and was contributed as capital contribution to a partnership firm in which assessee became a partner with a view to carry on business in partnership. At the cost of repetition, it is emphasized that the transaction of making over assessee's personal asset i.e. land in question, to a firm as its capital contribution in the capacity of a partner is not a commercial or trading transaction as so admitted by the assessee also. To say it differently, the land in question contributed by the

assessee to a firm as its capital contribution has not been transferred or sold to a firm in the course any trading or commercial activity or transaction carried out by the assessee. We fail to understand that when land in question has not been sold or transferred to a firm in the course of any trading or business activity, but has been transferred by way of capital contribution to a firm, on what basis or criteria the land in question should be considered as stock in trade, when the same was contributed to a firm towards capital, when it is admitted position of law that the asset, which are held for sale in the ordinary course of business; in the process of production for such sale or in the form of materials or supplies to be consumed in the production process are only be considered as stock in trade or inventories. In the course of hearing of this appeal, a reliance was placed by the Id. Standing Counsel for the Revenue on the Accounting Standards viz., Accounting Standard - 1, Accounting Standard -2, and Accounting Standard - 10 (AS - 1, AS -2, and AS - 10 respectively) in reply to the query raised by the Bench about the meaning of words “capital asset” and “stock in trade”. It was pointed out to the Bench by both the parties that AS -2 deals with the valuation of inventories. The

meaning of inventories as defined in AS –2 is that the inventories are assets held for sale in ordinary course of business; in the process of production for such sales; or in the form of materials or supplies to be consumed in the production process or in the rendering of services. Above meaning given to the inventories is an accepted proposition. From this definition of stock in trade or inventory, it is clear that in order to consider any asset as stock in trade or inventory, it is to be established that it was held for sale in the ordinary course of business; in the process of production of such sales; or in the form of materials or supplies to be consumed in the production process or in rendering of services. Under section 2(14) of the Act, any stock in trade, consumable stores, or raw materials held for the purpose of his business or profession are excluded from the ambit of “capital asset”. The expression used in section 2(14) of the Act is “any stock in trade, consumable stores or materials held for the purposes of his business or profession”. Thus, the emphasis has been given to the criteria that any stock in trade, consumable stores, or raw materials must be held for the purpose of his business or profession in order to treat the same as such. As a natural corollary, if one claims that

any asset is are either acquired or disposed of or otherwise dealt with as stock in trade, or consumable stores or raw materials, he must prove that the transaction of that asset effected by him is in the course of his business or profession, so as to treat the asset in question as stock in trade, consumable stores or raw materials, at the time when the transaction was made. The aforesaid definition of inventories mentioned in AS – 2 has also been taken note of by the Hon’ble Supreme Court in the recent decision of Liberty India vs, CIT (2009) 317 ITR 218 (SC) by observing as under:

“19. Since reliance was placed on behalf of the assessee(s) on AS – 2 we need to analyse the said Standard.

20. AS – 2 deals with valuation of inventories. Inventories are assets held for sale in the ordinary course of business; in the process of production for such sale; or in the form of materials or supplies to be consumed in the production.

“Inventory” should be valued at the lower of cost and net realizable value (NRV). The cost of “inventory” should comprise all costs of purchase, cost of conversion and other costs including costs incurred in bringing the “inventory” to their present location and condition.

16.43. In this view of the matter, we, therefore, hold that in order to treat any asset as stock in trade, it must be established and proved that the asset was involved in the course of any commercial or trading transaction of a business carried out by the assessee, and that is to be considered and decided with reference to the transaction in which such asset is employed and not with reference to any past or subsequent act of the assessee, qua that asset.

16.44 Having regard to the nature of right acquired by a partner of a firm when he becomes a partner, his share in firm undoubtedly constitutes “property”, and “share of a partner” in a partnership firm would certainly be a capital asset within the meaning of section 2(14) of the Act. Such an asset being a share of a partner in a partnership firm can be transferred, like any other property, and, on transfer being completed, the charge on capital gain tax would be attracted. As already observed above, when a partner of a firm makes over his personal asset to a firm as its contribution towards capital, the partner acquires a right to receive share in profit of the firm during the subsistence of the partnership and upon its dissolution or on his retirement, a right to share in the net asset of the firm. It thus,

makes it clear that the partner has acquired a capital asset in the nature of his share in the partnership firm in consideration of his making over his personal asset to a firm. The transaction of making over personal assets to a firm, or receiving or realization of his share in assets on dissolution of the firm or on retirement of the partner, is undoubtedly to be held on a capital field.

16.45 Therefore, having regard to the nature of the transaction of contributing asset by a partner to a partnership firm towards his capital, the nature of the right that the partner acquires when he contributes his personal asset to a partnership firm as its capital, and such transactions being not in the nature of any commercial or trading transaction, notwithstanding the fact that the said land contributed by the assessee to a partnership firm as its capital was held as stock in trade for the purpose of assessee's business before the same was so contributed as capital in a firm, it ceases to be stock in trade at the time when the same was contributed into a partnership firm by the assessee partner towards its capital, and it gets converted from stock in trade into capital asset at that material point of time. Therefore, the question as to whether any income

or gain has arisen or accrued to the assessee in the course of contributing the said land as capital contribution into a partnership firm at the time when assessee becomes a partner, is to be decided in the light of the premises that assessee has transferred or contributed a capital asset as capital contribution to a partnership firm in which he became a partner, and not in the light of the premises that there was a sale or transfer or contribution of stock in trade by a partner to a firm by way of capital contribution when the assessee became a partner.

16.46 The question whether, on facts of the present case, the land in question held by the assessee as stock in trade has been converted into capital asset and it partook the character of capital asset at the time when the assessee contributed it as its capital to a firm when he became a partner, can also be judged from one more point of view about the conduct, motive and intention of the assessee while making over the land in question as capital contribution to a firm in which he became a partner. The intention and motive of the assessee to treat any asset whether as stock in trade of its business or capital asset at any given point of time can be judged or inferred from the conduct of the assessee coupled with all

surrounding circumstances and materials of any given case, having regard to the nature of transaction in which such asset is employed. In the present case, it is not in dispute that the assessee was following method of valuation of closing stock of its business at cost or market price, whichever is lower, as per settled and accepted principles of accountancy. Accordingly, the land in question as well all other plots of lands held by the assessee as stock in trade were used to be valued as per the said method of valuation at the end of the year when accounts of the assessee were made out. However, on 16.03.1992 in the middle of the current year under consideration, the assessee got only the land in question revalued by the experts determining the market value as on 16.03.1992 at Rs. 11.50 crores, which is more than the cost to the assessee, and the land was then contributed to the newly constituted partnership firm as capital contribution, and the surplus of Rs. 6.01 crores arising from the said transaction, was credited in the profit and loss account of the assessee firm and the value of the land was credited in the capital account of the assessee partner in the books of the firm. In this respect, and at this stage, we must keep in our mind that all other plots of lands and right inland

held by the assessee as stock in trade, except the land in question, were neither valued nor any entry of any revaluation in respect there to was made in the accounts of the assessee company. The conduct of the assessee in valuing only a part of stock in trade at market value as on 16.03.1992 for the purpose of contributing the same as capital contribution in to the partnership firm in which he became a partner on and from 16.03.1992, clearly indicates the intention and motive of the assessee that the assessee did not have any intention to treat the land in question as stock in trade anymore, but the intention was to treat the same as capital asset for the purpose of contributing the same as capital contribution to a firm for becoming a partner. It is an accepted system of accountancy that stock in trade of business at the end of the year are valued at cost or market price, whichever is lower, to determine the profit or loss, as the case may be of any business. Thus, the question of valuating the stock in trade at market value higher than the cost price in the middle of the year before the year ends, and then passing corresponding entries in the books of accounts, is totally unwarranted and is not usually associated with the stock in trade, unless the assessee

intended to withdraw the stock in trade from his business and convert the same into capital asset for the purpose of contributing the same as capital in a partnership firm in which assessee became a partner. There is no mandatory accounting standard, which mandates the assessee to revalue its inventory upward as so admitted by the learned counsel for the assessee in reply to the query raised by the Bench. In the present case, we, therefore, find that there were material changes in circumstances under which the land was valued at market price higher than the cost price, the land was then contributed by the assessee partner to a partnership firm as capital contribution and the surplus arising from the said transaction was credited in the profit and loss account of the assessee, from the circumstances prevailing either on the date of its acquisition as stock in trade or just before the same was decided to be contributed as capital in a firm at a market price. At this stage, we find it necessary to point out one proposition that though accounting practices may not be the best guide in determining the nature of any asset held by the assessee, they are indicative of what the assessee itself thought of its nature or what treatment the assessee itself intended to give to the same. The intention of

the assessee to hold any asset whether as stock in trade or capital asset can be gathered from the conduct of the assessee and the treatment given to it by the assessee in its records and books, though the same may not be conclusive but are undoubtedly a relevant factors coupled with some other factors or circumstances appearing in any given case. From all the factors as discussed above, if taken together, alongwith the position of law as to the nature of the transaction and rights acquires by the assessee on becoming a partner in a firm, it is clearly established and proved that the land held by the assessee as stock in trade before the same was contributed to a firm as capital has been converted into a capital asset at the time when the same was contributed as capital contribution to a firm in which the assessee became a partner. In this view of the matter, we, therefore, hold that the land in question contributed by the assessee as capital to a firm in which assessee became a partner was a capital asset in nature at that relevant point of time, and all the incidence of taxation would thus follow accordingly.

16.47 Before proceeding further, at this juncture, we have to deal with one more aspect of the matter flowing from the contentions of the

learned counsel for the assessee to the effect that the AO as well as the CIT has not controverted or disputed the fact that the land in question was a stock in trade both before and after the same was contributed by the assessee partner as its capital contribution to the partnership firm in which the assessee became a partner, and this finding of fact cannot now be changed at this stage. We have given our serious consideration to this contention raised by the learned counsel for the assessee. On perusal of orders of the authorities below, it becomes clear that both the authorities below have recorded a finding of fact that the land, which was contributed by the assessee company to a the firm, was its stock in trade, and it became the partners' capital in the firm being the asset received in lieu of capital of the partner. Both the authorities below have also accepted the position that the land, which was contributed by assessee company as its capital, was held as stock in trade by the partnership firm in which the assessee became a partner. We have also accepted this position that the land in question contributed by assessee partner to a partnership firm as its capital contribution when the assessee become a partner, was held by the assessee as stock in trade before the same was contributed as its capital

contribution to a firm. There is no dispute as to the fact that after receiving the land in question as capital contribution by the assessee partner, the firm treated the same as stock in trade of its business of real estate and started making construction thereupon for its business of real estate development in subsequent years. At the same time, the fact that the land in question was contributed to a firm as capital contribution by the assessee in the capacity of a partner is also not in dispute. In our opinion, the real controversy, in the present case, is not with regard to the nature of asset before or after the same was contributed to the partnership firm as capital contribution by the assessee partner when the assessee became a partner, but is with regard to the nature of the asset at the material point of time when the same was contributed to a partnership firm by the assessee partner as its capital contribution when he became a partner in the firm. While the AO has claimed that it is a case of sale of stock in trade from one entity to another and the surplus resulted out there from is a profit from business chargeable to tax, the assessee has contended that it is a case where stock in trade has been contributed to a partnership firm by the assessee as its capital contribution and no

commercial or trading transaction has taken place so as to give a rise to a sale or transfer of stock in trade by a partner to a firm. In the light of the controversy set out above, we have addressed ourselves to determine the true and correct nature of the transaction and/or the asset employed in the transaction under which the assessee partner contributed towards its capital its personal asset held by it as stock in trade before the same was contributed as its capital to a firm, in which the assessee became a partner. This question whether the land in question was a capital asset or stock in trade in nature at the time when the same was contributed by the assessee to a partnership firm as its capital contribution when the assessee became a partner in that firm, is not one of fact: though it is dependent on the facts and the circumstances of the present case, the question does involve conclusions of law to be drawn from those facts. We, therefore, do not find any force or merit in the contention of the learned counsel for the assessee that the fact admitted by the revenue authorities below are now being changed.

Whether particular income assessed by the AO under one head can be brought to tax under another head by the Tribunal.

16.48 The learned counsel for the assessee has also contended before us that the revenue has changed its stand when an alternative

argument was advanced by the learned special counsel for the revenue that in the event the Tribunal comes to the conclusion that the transaction of making over personal assets by a partner to a partnership firm as its capital contribution is a case of capital asset brought in by a partner as its capital contribution in a firm in which it became a partner, the Tribunal may adjudicate the question whether the profit or gain arising to the assessee as a result of the said transaction is chargeable to tax under the provisions of Section 45(3) of the Act effective from 01.04.1988 even if not under section 28 of the Act. Both the parties have been heard on this aspect of the matter and also on the merits whether the surplus arising from the transaction involved in this case could indeed be assessed as capital gain.

16.48.1 There is no dispute to the position that the profits or gains or benefits arising to the assessee from said transaction in question has been assessed under the head “business” by the AO in the light of the view that stock in trade was sold or transferred by the assessee company to a firm at an appreciated price. It was the claim of the assessee itself that the stock in trade held by it was contributed to a firm in which the assessee became

a partner, and in the light of the stand so taken by the assessee, the AO brought the surplus to tax under the head “business”. In the light of the stand taken by the assessee that the land transferred to a partnership firm was stock in trade at the time when the same was contributed to a firm, the AO has treated the transaction of making over the land of the assessee to a firm to be in the nature of trading or commercial transaction rejecting the assessee’s claim that it was not liable to be taxed as no sales had taken place. However, when an argument has been advanced supported by various decisions when a partner contributes its personal assets of whatever character to a firm towards its capital contribution when he becomes a partner, the asset involved in the transaction would partake the character of capital asset at that material point of time. The learned standing counsel for the revenue advanced an alternative argument based on same set of facts but on different conclusions of law drawn from those facts that in case the contribution of land by assessee partner to a firm is accepted to have been made towards its capital contribution in a firm and the land involved in the said transaction of capital contribution to a firm is held to be of a “capital asset in nature” at the time when the same was

contributed as capital contribution, the profit or gain arising from the transfer of a land by the assessee to a firm may be taxed under section 45(3) of the Act inserted with effect from A.Y. 1988-89. This alternative argument is, in our view, undoubtedly arising from the same set of facts, and in respect of same item of income arising from the same transaction, which have been considered in the assessment made by the AO. Further, the provisions of section 2(14), 2(47) and 45(3) of the Act were very much relied upon by the AO while assessing the item to tax as is clear from the respective orders of the authorities below and from the submissions of the assessee made before the authorities below as well as before us. It is not the new source of income or new item of income that is sought to be taxed by the revenue at this stage. It is the same income assessed by the AO that is now sought to be taxed under section 45(3) of the Act in the light of the legal inferences drawn from same of set of facts, as against the business profit assessed in the assessment made by the AO. The subject matter of appeal has not been really changed. The change is only with regard to the correct head of income under which it is to be assessed under the Income Tax Act. Thus, the contention of the assessee

in this regard that the department has no right to take an alternative plea to tax the profits or gains arising from transfer of land by assessee to a firm by way of capital contribution as per provisions of section 45(3) of the Act is not found convincing.

16.48.2 Further, the answer to a question that whether the land in question had a character of capital asset or stock in trade at the time when the same was contributed as capital to a firm in which the assessee became a partner is based on a legal conclusion to be drawn from same set of facts. The relevant provisions of law contained in section 2(14), 2(47) and 45(3) were very much relied upon by the department authorities below to bring the item to tax though the tax has been imposed by the AO and the CIT(A) under the head “business profit”. This makes it clear that the department has not made out a new claim for the first time before the Tribunal by way of an alternative argument made before us.

16.48.3 It is not the case where any enhancement of income is sought for by the Revenue. It is also not the case where any benefit already granted to the assessee is sought to be taken back by the department. The only point raised by the Sr. Standing Counsel for the revenue is that in

case the surplus arising from the transaction is not found to be assessable under the head “business”, the same may be taxed under the head “capital gain”, and in that situation the tax liabilities of the assessee would not increase. All the facts to decide the question as to whether the surplus in question is assessable under the head “business” or “capital gain” are available on record, which has been considered by the authorities below and which has been referred to by the assessee. The AO as well the assessee both have admitted the fact that the land was contributed as capital contribution by the assessee in the capacity of a partner. The subject matter involved in this issue is also not being changed in as much as in the light of the facts available on record and that were considered by the authorities below and also relied upon by the assessee, the same very transaction of contributing the land by a partner to a firm as its capital contribution is the sole basis to decide the alternative contention raised by the revenue. By allowing department to raise this additional plea, we do not think that we traverse beyond the subject matter of dispute between the parties involved in this case. This alternative plea raised by the revenue does not altogether changes the complexion of the case, and only

change sought to be made is to determine the correct head of income on same set of facts. The various decision relied upon by the Id. counsel for the assessee are, therefore, not applicable to the present case in as much as those cases were rendered either in the situation where new facts were considered, benefit already granted to the assessee were sought to be withdrawn, the subject matter of the appeal was completely changed and the assessment was sought to be enhanced.

16.48.4 In this connection, a reliance was placed by the Revenue upon the decision of Special Bench of Income Tax Appellate Tribunal, Mumbai Bench “C” (SB) in the case of Sumit Bhattacharya vs. ACIT (2008) 112 ITD 1 (Mum)(SB), where the Special Bench has taken a view that the Hon’ble Bombay High Court in the case of Commissioner of Income-tax v. Gilbert & Barker Manufacturing Co., U.S.A. [1978] 111 ITR 529 (BOM.) has held that the Tribunal is competent to change the head of income even at the instance of the respondent when all the relevant facts are already on record as long as both the parties are heard on

that issue. This decision of Special Bench in the case of Sumit Bhattacharya vs. ACIT (supra) and Hon'ble Bombay High Court in the case of Commissioner of Income-tax v. Gilbert & Barker Manufacturing Co., U.S.A. (supra) are directly on the issue that arises in the present case before us. In the case of Commissioner of Income-tax v. Gilbert & Barker Manufacturing Co., U.S.A. (supra), which has been relied upon by the Tribunal in the case of Sumit Bhattarcharya vs. ACIT (supra), the High Court has held as under:-

“xxx xxx xxx xxx The Tribunal would have the discretion to allow any party to the appeal, may be the appellant or the respondent, to raise a new point or a new contention provided two things are satisfied. First, that for urging such a new point no new facts are required to be brought on record and the point is capable of being disposed of on the facts which are already on record and, secondly, an opportunity is given to the other side to meet that point that is being allowed to be raised for the first time in appeal. In the instant case, it cannot be disputed that all the facts that were required for determination of the point as to whether the income returned should be assessed under the heading "Business income" or not were already on record before the Tribunal and no further investigation of any other facts was necessary and it was on the basis of facts which were already on record that the respondent wanted to canvass the point before the

Tribunal that the income returned by it should be assessed under the heading "Business income". Secondly, the aspect whether a particular income returned by the assessee should be brought to tax under one or the other heading of income should not be regarded as such a new point as to make the other side taken by surprise, especially when all the facts necessary for that purpose are already on record and in the instant case the department was given full opportunity by the Tribunal to meet the contention that was being permitted to be raised by the respondent for the first time in appeal. In our view, therefore, there was no question of placing the appellant in a worse position, which seems to be the implication of the question as framed. The Tribunal, in our view, was justified in permitting the respondent to agitate before it its contention that its income was assessable under the heading "Business income" and, accordingly, the first question is answered in the affirmative.

16.48.5 The Special Bench in the case of Sumit Bhattacharya vs.

ACIT (supra) has observed and held as under(extracted from head-note):-

“It is well-settled that the Tribunal is competent to change the head of income even at the instance of the respondent when all the relevant facts are already on record and as long as both the parties are heard on that issue. In the instant case, it was the alternate contention of the revenue that in the event the Tribunal came to the conclusion that the amount in question was not taxable under the head ‘Income from salaries’, the Tribunal might also adjudicate on the question whether or not

the impugned amount be held as income from other sources. [Para 47]

The Supreme Court in the case of Emil Webber v. CIT [1993] 200 ITR 483/67 Taxman 532 has held that merely because an employment-related income/benefit cannot be taxed under the head 'Income from salaries', such a benefit cannot go outside the ambit of taxable income and such an income can be taxed under the head 'Income from other sources'. [Para 50]

Therefore, even if the amount received by the assessee on redemption of share appreciation rights was held to be not taxable under the head 'Income from salaries', this fact, by itself, would not take the same outside the ambit of taxable income. Since, in such an eventuality and following the Supreme Court's judgment in Emil Webber's case (supra), the said amount would be taxable under the head 'Income from other sources'. Therefore, even if it was held that the amount in question was received from a person other than the employer of the assessee, and that in order for an income to be taxed under the head 'Income from salaries' it is a condition precedent that the salary, benefit or the consideration must flow from employer to the employee, the amount received by the assessee on redemption of stock appreciation rights would still be taxable - though under the head 'Income from other sources'. The plea raised by the assessee that the amount in question could not be taxed as 'income from salaries' was thus irrelevant. [Para 51]"

16.48.6 In the instant case before us, all the facts required for deciding the point as to whether the surplus arising from the transaction can be assessed under the head "capital gain" or not are already on record.

No further investigation of any new fact is necessary. The provisions contained in section 45(3), on the basis of which the income can be assessed under the head “capital gain”, has been considered and deliberated upon by both the authorities below, and assessee has also furnished its comments upon the applicability of provisions contained in section 45(3) before the authorities below as well as before us. In the course of hearing of this appeal, a query was also raised by the Bench to both the parties to explain as to whether the income in question can be assessed under the head “capital gain”, and both the parties have advanced their arguments. As held by the Hon’ble Bombay High Court in the case of CIT vs. Gilbert & Barker Manufacturing Co. (supra), the question whether a particular income should be brought to tax under one or other head cannot be considered to be entirely new point. The assessee has been given full opportunities to meet the alternative contention raised by the department before us. In the case of the Sumit Bhattacharya vs. ACIT (supra), the Special Bench had taken a view that the income, which was assessed by the AO under the head “salary”, could be taxed under head “income from other sources”, and the issue was decided accordingly by

the Special Bench. In this respect, a reliance may also be placed upon the decision of Hon'ble Bombay High Court in the case of B.R. Bamasi v. Commissioner of Income-tax [1972] 83 ITR 223 (BOM.), where new ground before the Tribunal during arguments by the assessee in answer to appeal was permitted. The decision of Hon'ble Supreme Court in the case of Hukumchand Mills Ltd. vs. CIT (1976) 63 ITR 232 (SC) has held that the power of the Tribunal in dealing with appeals are expressed in Section 254(1) in the widest possible terms, however, with a restriction of its jurisdiction to the subject matters of appeal.

16.48.7 Further, having regard to the actual controversy involved in the present appeal, in response to the Bench's suggestions, and notings, the Hon'ble President vide his order dated 06.03.2009, after hearing both the parties, has directed this Special Bench to decide the appeal in its entirety without confining itself to the question earlier framed in the present case, in accordance with the law and in the light of the facts of the case including the High Court's direction as so agreed by both the parties. Therefore, the alternative plea raised by the revenue to the effect that the surplus arising to the assessee may otherwise be held be assessable under

the head” capital gain” instead of “business profit” is admitted for our consideration so that the income, if found us as to taxable, can be assessed under the correct head of income under the provision of the Act.

16.48.8 Before parting this aspect of the matter, we would like to make a reference to a decision of Hon’ble Supreme Court in the case of Commissioner of Income-tax in the case of Ram Kumar Aggarwal & Bros. [1994] 205 ITR 251 (SC) relied upon by the Id. counsel for the assessee to the effect that the respondent is not entitled to for the first time to claim before the Tribunal and the High Court that the shares ceased to be its stock in trade on the conversion of the company from public company to a private company. This case is rendered in the context of altogether different situation where it was an admitted position that the assessee held the shares of company as stock in trade of his business, and he received the money in lieu of his share holding in the company in which he had held shares as stock in trade and claimed relief as such in earlier years. This is not the case where assessee has converted its stock in trade into capital asset at any point of time. The assessee was all along claiming the benefit and being assessed by treating the shares as stock in

trade, and the surplus received by the assessee from a liquidator in the distribution of assets of the company, was, thus, held as business income assessable in assessee's hands, and not as a profit from investment. In this case, the assessee made a fresh claim by contending that the shares held by it as stock in trade seized to be its stock in trade on the conversion of the company from a public company to a private company of which the assessee was holding shares as stock in trade, though, in the present case before us, it is the conduct of the assessee itself that he decided to contribute the land in question as capital in a partnership firm in which assessee became a partner, and it is not the case of realization of any money by the assessee in lieu of land in question held by it as stock in trade before the same was contributed as capital to a firm.

Conclusion

16.49 Applying the propositions laid down by the Hon'ble Supreme Court in the case of Sunil Siddharthbhai v. Commissioner of Income-tax (supra) to the facts of the present case and in the light of the view we have expressed above, we hold as under:-

- i. When the assessee made over the said land in question to the partnership firm as his contribution to its capital, what right the

assessee has acquired, during the subsistence of the partnership firm, is to get its shares of profits from time to time, and after dissolution of the partnership or on his retirement from the partnership firm, to receive the value of the share in the net partnership asset as on the date of dissolution or retirement after deduction of liabilities and prior charges.

- ii. When the land in question being the personal asset of the present assessee was contributed by the assessee partner to a firm towards its capital, the assessee reduced his exclusive right in the land in question to shared rights in it with other partners of the firm, and to that extent to which the assessee's exclusive interest in the said land is reduced to a shared interest, there was a transfer of interest in the land notwithstanding, the fact whether the land in question was being held by the assessee as its stock in trade or capital asset or otherwise before the same was contributed to a firm towards capital.
- iii. Having regard to the nature of right acquired by the assessee in consideration of his making over his land to a firm as its capital

contribution to get his share of the profit from time to time during the subsistence of the partnership, and after the dissolution of the partnership or with his retirement from the partnership, to get the value of his shares in the net partnership asset as on the date of the dissolution or retirement after deduction of liabilities and prior charges, as understood in the general law, the land brought in by the assessee became the property of the firm, which would vest in all the partners, and in that sense, every partner has an interest in the property of the partnership, and during the subsistence of the partnership, no partner can deal with any portion of the property as his own, and the assessee's exclusive right in the said land has reduced to shared right in it. This position is undoubtedly applicable to all nature of assets whatsoever, brought in by any partner to firm towards its capital contribution.

- iv. The position of law which arises when a personal asset is brought in by a partner into a partnership as his contribution to the partnership capital and that which arises when on dissolution

of the firm or on retirement of a partner, share in the partnership asset passes to the erstwhile partner, are different to each other in as much as, in the case of dissolution or retirement of any partner, it is the realization of pre-existing right and that is why it has been held that there is no transfer though when a partner brings his personal asset in to the partnership firm as his capital contribution to its capital, an exclusive interest of a partner in his personal asset before the partner enters the partnership reduced to a shared interest. Therefore, the proposition laid down by the Hon'ble Supreme Court in the case of *Malabar Fisheries Co. v. Commissioner of Income-tax* [1979] 120 ITR 49 (SC), which was a case where on dissolution of partnership firm, a partner realized or received his interest in the partnership, has been distinguished by the Hon'bel Supreme Court in the case of *Sunil Siddharthbhai v. Commissioner of Income-tax* (supra). Therefore, the meaning of "transfer of property" given by the Hon'ble Supreme Court in the case of *Sunil Siddharthbhai v. Commissioner of Income-tax* in the cases where partner bring

his personal assets to a firm towards capital contribution is applicable to all kinds of assets brought in by the partners to a firm towards its capital contribution, and not only to a capital asset held by the partner before the same was contributed in the partnership. The analogy of reducing of exclusive interest of a partner, to shared interest in case partner brings in his personal asset into the partnership firm as his contribution to its capital is equally applicable to all kinds of assets belonging to a partner, and that is why the Hon'ble Supreme Court in the case of Sunil Siddharthbhai v. Commissioner of Income-tax (supra) has used the expression "personal asset" while laying down a law that *"it is apparent, therefore, that when a partner brings in his personal asset into a partnership as his contribution to its capital, an asset which originally was subject to the entire ownership of the partner becomes now the subject to the right of other partners in it xxx xxx xxx. Therefore, what was the exclusive interest of a partner in his personal asset is, upon its introduction into the partnership firm as his share to the*

partnership capital, transformed into an interest shared with the other partners in that asset. Qua that asset, there is a shared interest xxx xxx.” (see at page 518 and 519 of the Report). The Hon’ble Supreme Court has also used the expression “personal asset” while deciding the issue whether there is a transfer of property when the individual property of a partner is contributed to a firm towards capital contribution by observing that *“Therefore, when a partner brings in his personal asset into the capital of the partnership firm as his contribution to its capital, he reduces his exclusive rights in the asset to shared rights in it with the other partners of the firm”* (see at page 517 of the report). In this view of the matter even without applying of section 2(47), we may hold that there was a transfer of property when any personal asset of whatever character of a partner is brought into a partnership firm by the partner as his contribution to its capital in as much as the exclusive interest of a partner in that property or asset is, upon its introduction into the partnership firm as his share to the partnership capitals

transformed into an interest shared with the other partners in that property or asset.

- v. If we look carefully to the judgment in its entirety in the case of *Sunil Siddharthbhai v. Commissioner of Income-tax (supra)*, it would be clear that whatever may be the character of the property in the hands of a partner before the same is brought in by the partner to a firm, when the partnership is formed, there is a transfer of a capital asset either in the general sense of the term “transfer of property” or within the meaning of section 45 of the Act. The Hon’ble Supreme Court in that case was concerned with two appeal of two different assesses. In Civil Appeal No. 1841/1981, the assessee made over certain shares of limited company which were held by him as his capital asset to a firm as his contribution to the capital of the partnership firm. In Civil Appeal No. 1777/1981, the assessee introduced his share holdings in the partnership firms as his capital contribution. The partnership firm credited the accounts of the partners with the market value of the shares. In Civil Appeal No. 1841/1981, it

has been specifically observed by the Hon'ble Supreme Court that shares were held by the partner as his capital asset, but in Civil Appeal No.1777/1981 nothing is mentioned about whether share holdings by the partner was held as capital asset or as trading asset. While deciding the issue whether there was transfer of shares, the Hon'ble Supreme Court decided the issue by observing that *"we hold that when the assessee brought the shares of the limited companies into the partnership firm as his contribution to its capital, there was a transfer of a capital asset within the terms of section 45 of the Income Tax Act"* From the said observation and decision of Hon'ble Supreme Court, it cannot be said that the asset brought into a firm by a partner as capital contribution should be held by him as capital asset even before the same was contributed in order to treat the contribution of asset by a partner to a firm as a transfer of capital asset within the terms of section 45 of the Income Tax Act. Further, the Hon'ble Supreme Court referred to its own observation in the case of Addanki Narayanapa vs. Bhaskara Krishanappa (supra)

with approval where this Court explained that “whatever may be the character of the property which is brought in by the partner when the partnership is formed -----”, which goes to show that when any property of whatever character held by a partner is brought in to a firm by the partner, it becomes the property of the firm, and what a partner is entitled to is his share of profits, if any, in the profit of the partnership firm, and upon the dissolution of the partnership, a right to share in the money representing the value of the property after meeting all the liabilities and expenses. Further, while stating the words of caution by the Hon’ble Supreme Court in the said case, they have used the words *“if the transfer of the personal asset by the assessee to a partnership in which he is or becomes a partner is merely a device or ruse for converting the asset into money, which would substantially remain available for his benefit without liability to income tax on a capital gain”*, which goes to show that whenever the matter of transfer of assets by a partner to the partnership firm by way of capital contribution was under

their Lordship's consideration, their Lordships used the words "*transfer of personal asset by the assessee to a partnership in which he is or becomes a partner*" but when question had arisen whether it is an attempt to avoid liability to income tax, their Lordships has used the words "*liability to income tax on a capital gain*" or "*evading tax on a capital gain*". This goes to show that in order to decide whether there was an attempt on a part of a partner to avoid liability to income tax on capital gain, what is to be seen whether the transfer of any personal asset by the partner to a firm in which he is or becomes a partner is merely a device or ruse for converting his personal asset into money, and it is not necessary that there should be a transfer of capital asset only initially held by a partner to a firm. This proposition about avoiding liability to income tax on capital gain by way of transfer of asset by a partner to a firm is applicable to all classes of assets transferred by a partner to a firm. It thus makes it clear that whatever may be the nature of the asset initially held by a partner before the same is

contributed by him as capital contribution to a partnership firm, it shall assume the character of a capital asset at the time when it is contributed to a firm as capital contribution and any surplus arising there from is chargeable to tax as capital gain. Therefore, from this angle also, we hold that the decision of Hon'ble Supreme Court in the case of Sunil Siddharthbhai v. Commissioner of Income-tax (supra) is applicable not only to the cases where any capital asset of a partner is transferred by a partner to a firm as his capital contribution but, it is applicable to all kinds of personal assets of the partner transferred by him to a partnership firm as capital contribution, and in all such cases the liability of income tax on capital gain would arise.

- vi. There is no quarrel as to the proposition that no income chargeable to tax would arise on mere revaluation of the closing stock at a market value more than the cost to the assessee as in such a case the profits shown on revaluation is only notional. We do not find any difficulty in accepting this contention raised

by the learned counsel for the assessee in the light of the decision in the case of Sir Kikabhai Premchand v. Commissioner of Income-tax (supra), Chainrup Sampatram v. Commissioner of Income-tax (supra), Commissioner of Income-tax v. Hind Construction Ltd (supra), Commissioner of Income-Tax vs. Birla Gwalior Pvt. Ltd. (supra) and Sanjeev Woollen Mills v. Commissioner of Income-Tax. However, facts are different in the present case. It is not the case where increase in the value of land can be said to be notional. In the present case, the asset has been valued at market rate, which is more than the cost to the assessee, and it has been contributed to a firm as capital contribution in which the assessee became a partner, and the market value was credited in the capital account of the assessee in the books of the firm, and similar amount is credited in the books of the assessee and surplus has been shown as income in the profit and loss account out of which the dividend was also paid. Therefore, decisions rendered in the context of the fact where mere revaluation of asset was made in books

without anything more are not applicable to the facts of present case.

- vii. The contribution of land by the assessee to a firm as its capital contribution may in itself cannot be called as “sale”. But the same does not mean that it is also not a “transfer” because, in such a case what was the exclusive interest of the assessee in the said land has, upon its introduction into the partnership firm as its share to the partnership capital, transformed into an interest shared with the other partners in or upon that land. When one talks of the partnership firm’s property or firm’s assets all that is meant is property or asset in which all partners have a joint or common interest. Accordingly, upon introduction of land by the assessee into the partnership firm as its shares to the partnership capital, the land so contributed becomes the property of the firm and the partnership property will vest in all the partners and in that sense every partner has acquired an interest in the property of the partnership firm. Therefore, the assessee’s exclusive right

in the said land has reduced to a shared interest, and to that extent, there is a transfer of land from assessee to a firm.

- viii. When the assessee contributes its personal asset held by it to a firm as its contribution towards capital, the assessee cannot be said to have effected any trading or commercial transaction, but the transaction shall be considered to have been effected on capital field. Therefore, the nature and character of land contributed by the present assessee to a firm towards its capital contribution shall assume the character of “capital asset” at the time when it was contributed to a firm towards capital contribution.
- ix. There is no quarrel as to the proposition that there is no transfer on mere conversion of stock in trade into capital assets and/or on revaluation thereof in the assessee’s books and no income arising on such conversion. In other words, there could not be any actual profit or loss on withdrawal of stock in trade from a

trading business and its conversion into capital asset. There was no deeming fiction to deem the conversion of stock in trade into capital assets as a transfer or to deem the fair market value as on the date of conversion as the cost of acquisition of the capital assets. However, a transfer does take place when any personal asset of a partner is introduced into a firm as his capital contribution, and the value of the asset recorded in the books of the firm shall be deemed to be full value of the consideration received or accruing as a result of the transfer of such asset contributed by the partner. Consequently, in the present case, there was no transfer of land held by the assessee as stock in trade when the same was merely revalued at a market value in its books and it was converted into capital asset and no profit or gain did accrue or arise to the assessee merely on its revaluation at a higher value more than the cost to the assessee in its books or on its mere conversion from stock in trade to a capital asset. In such a case, the conversion of stock in trade into investment has to be at cost/book value. Thus, the legal proposition that no

man can make a profit out of himself or there could not be any actual or real profit or loss on withdrawal of stock from a trading business shall govern this type of cases. However, the position would be different in cases where on or after conversion of stock in trade into a capital asset either by implication of law or by act or conduct of the assessee, or otherwise, the asset is contributed to a firm as capital contribution by a partner at the value more than the cost to the assessee. In such a case, there is a transfer of asset being taken place and the value of the asset recorded in the books of the firm shall be deemed to be the full value of consideration received or accruing as a result of the transfer of the asset. Therefore, in the present case, when the land in question was contributed by the assessee to a firm as its capital contribution, in which the assessee became a partner, a transfer of capital asset had taken place, and the amount recorded in the books of account of the firm as the value of the land shall be deemed to be the full value of the consideration received or accruing as a result of the transfer of the land, and the profits or

gains arising from such transfer of a capital asset by a person to a firm in which he becomes or is a partner by way of capital contribution or otherwise, shall be chargeable to tax as his income of the previous year in which such transfer takes place.

- x. In the light of the view we have taken above, we, therefore, hold that the surplus arising to the assessee from the transaction of contribution of land held by it to a firm as capital contribution shall be assessable to tax as profit or gains under the head “capital gain” under section 45 of the Income Tax Act, and for that purpose, the amount of 11.50 crore recorded in the books of accounts of the partnership firm as the value of the land shall be deemed to be the full value of the consideration received or accruing as a result of the transfer of the land as so provided under sub-section (3) of the section 45 of the Act, effective from the A.Y. 1988-89.

- xi. Even otherwise, the surplus arising to the assessee from the transaction of contribution of land as capital contribution to a firm in which the assessee became a partner shall be chargeable to tax in view of our finding given above that the transaction of transferring the land in question to the partnership firm is a device or ruse to convert the land in question into money substantially for the benefit of the assessee as the assessee has withdrawn substantial amount as observed and pointed out above in para 16.19 to 16.24 of this order, for its benefit as a part of its well designed and calculated colourable strategy to convert the land into money for its own benefit.
- xii. without prejudice to the view we have taken above, we further hold that even in case it is otherwise held that the land contributed by the assessee to a firm towards capital contribution should be treated as stock in trade even during the course of making the transaction of transferring or contributing the land to the partnership firm as capital contribution, the surplus arising to

the assessee from the said transaction of contributing stock in trade to a firm shall then assessable under the head “business” in the view of the colourable device or ruse adopted by the assessee to convert stock in trade into money for its own benefit.

16.50 In the light of our finding that the transfer or contribution by the assessee of its personal land to the share capital of the firm represent a device or ruse for converting the land into money substantially withdrawn by the assessee from the firm for its benefit and even otherwise in view of our finding that the provisions contained in section 45(3) of the Act inserted w.e.f. assessment year 1988-89, are applicable to the present case in this assessment year 1992-93 under consideration and in view of other findings we have given above, we hold that the earlier decisions of the Tribunal passed in the A.Y. 1985-86 in the assessee’s case shall have no application to the present case. We, therefore, reject the claim of the assessee that the issue involved in ground no. 1.1 to 1.7 should be decided in the terms of earlier order of the Tribunal passed in the A.Y. 1985-86.

16.51 For the above reasons, we, therefore, direct the AO to compute the capital gain arising from the transfer of the said land by the

present assessee to a partnership firm, in which it became a partner, by way of capital contribution, after taking the value of the consideration received or accruing as a result of such transfer at Rs. 11.50 crores being the amount recorded in the books of account of the firm as well as in the books of the assessee. The capital gain to be so computed shall be chargeable to tax in the year under consideration as per provisions of computation of capital gain and rate of tax provided in the Act or the respective Finance Act, as the case may be. We further observe that for the purpose of determining the year of acquisition of land or right to purchase the land, period of its holding, and the cost of its acquisition, the AO may take into consideration the ratio of the following decisions after providing an opportunity to the assessee to have its say in that regard:-

- I. CIT v. Jannhavi Investments (P.) Ltd. [2008] 304 ITR 276 (Bom.) (For computing the capital gains tax the “cost of acquisition” and not the cost or value on the date on which the asset was treated as a capital asset is relevant. Cost of acquisition on date asset actually acquired and not date on

date of conversion to capital asset is relevant for the purpose of computing capital gain.)

- II. Keshavji Karsondas v. CIT [1994] 207 ITR 737 (BOM) (For the purpose of computing capital gain, the cost of acquisition is the cost on the date when the asset was acquired and not the cost or value on date when asset became capital asset.)
- III. Ranchhodbhai Bhajibhai Patel v. CIT [1971] 81 ITR 446 (GUJ.) (The only circumstances which must be satisfied in order to attract the charge to tax on capital gains u/s. 45 of the Act is that the property transferred must be a capital asset at the date of transfer and it is not necessary it should have been a capital asset on the date of acquisition by the assessee)
- IV. Kalyani Exports and Investments Pvt. Ltd. vs. Dy. CIT Tax 78 ITD 95 (TM) (Pune) (What is relevant for purpose of capital gain is cost of acquisition and not the value on date on which the asset became a capital asset.)

17. Ground no. 2 is in respect of the issue whether the interest received on FDRs made from internal development account is eligible for deduction and not to be included in assessee's assessable income. This issue was decided by the Tribunal in the first round by remitting the matter back to the file of the AO to decide the issue afresh by complying with the directions given by the Tribunal in other years as detailed in para – 35 of the Tribunal's order dated 30.03.2007, passed in the first round of this appeal before the Tribunal. At this stage, it is pertinent to note that the assessee went in appeal against the aforesaid order dated 30.03.2007 passed in the first round, before the Hon'ble High Court, and no ground were raised by the assessee in respect this issue before the Hon'ble High Court as would be clear from the memorandum of appeal filed by the assessee before the Hon'ble High Court. Thus, this ground no. 2 stand decided in the terms of order dated 30.03.2007 of the Tribunal passed in the first round of this appeal.

18. Similarly, the issue involved in ground no. 4, 5, 6, 7, 8, 9, and 11 relating to (ii) the disallowance of Rs. 2,74,702/-being local conveyance and other incidental expenses, (ii) the disallowance of Rs. 15,000/- u/s.

40A(12) of the Act, (iii) disallowance of Rs.4,49,485/- being 10% for common maintenance, (iv) ad-hoc addition of Rs. 1,00,000/-, on account of guest house expenses, (v) taxability of Rs. 1,35,850/- being the enhancement compensation received on acquisition of agricultural land, (vi) ad-hoc disallowance of Rs. 2,00,000/- out of foreign travelling expenses and (viii) the disallowance of Rs. 2,55,000/- being subscription paid in respect of companies senior employees membership of the health club operated by DLF Hotels Ltd., respectively shall stand disposed of in the terms of the Tribunal's earlier order dated 30.03.2007, passed in the first round, in as much as, in respect of these issues, no appeal were either preferred by the assessee or by the revenue before the Hon'ble High Court. The order of the Tribunal dated 30.03.2007 shall, therefore, be applied accordingly in so far as the issue involved in the aforesaid grounds no. 4, 5, 6, 7, 8, 9, and 11 are concerned.

19. Now, we shall come to the ground no. 3, wherein the assessee has challenged the order of the CIT(A) in confirming the disallowance out of sales and business promotion expenses of Rs. 5,30,258/-.

20. This issue has been discussed by the Tribunal in para 38 to 42 of its order dated 30.03.2007 passed in the first round, whereby the Tribunal has sustained the addition of Rs. 3,00,000/-, and allow the balance relief to the assessee. On this issue, the assessee had taken a ground before the Hon'ble High Court as could be seen from the memorandum of appeal filed by the assessee before the Hon'ble High Court. However, the Hon'ble High Court has remitted the matter back to the Tribunal for fresh consideration only in respect of the issue with regard to the addition of surplus arising on revaluation of the land, when the same was contributed to a partnership firm, in which the assessee has become a partner, and the only question framed by the Hon'ble High Court was with regard to this matter. Nothing is mentioned in the Hon'ble High Court's order about this issue of confirming addition to the extent of Rs. 3,00,000/- lacs out of sales promotion and business promotion expenses. However, even otherwise, in the course of hearing of this appeal in the second round, nothing new has been submitted by the assessee. We, therefore, decide this issue in the light of earlier order dated 30.03.2007 where by the

addition of Rs. 5,30,258/- sustained by the CIT(A) has been reduced to Rs. 3,00,000/- by the Tribunal. We order accordingly.

21. Ground no. 10 is with regard to the disallowance of Rs. 1,03,505/- being the amount written off out of advances and deposits. This issue has been discussed by the Tribunal in the first round at para 67 – 70 of the Tribunal's order dated 30.03.2007, whereby the Tribunal has upheld the order of the CIT(A) on this issue in the light of the Tribunal's order in the case of this very assessee in the A.Y. 1991-92. The assessee has raised this issue in the appeal filed before the Hon'ble High Court about Tribunal's order dated 30.03.2007 but nothing is mentioned in Hon'ble High Court's order whereby some other matter has been remitted to Tribunal for fresh consideration as observed above. Thus, this ground stands decided in terms of our order dated 30.03.2007 passed in the first round, and we do not find any reason to take a view other than the view already taken by the Tribunal in the first round. Thus, this ground stands rejected.

ITA No. 2546/Del/2001 : A.Y. 1997-98

22. Now we shall come to the appeal filed by the assessee for the A.Y. 1997-98, against the order dated 14.05.2001, passed by the Id. CIT(A) in the matter of an assessment made u/s. 143(3) of the Income Tax Act, 1961 (“the Act”).

23. The ground no. 1 is directed against the CIT(A)’s order in holding that the mercantile method of accounting followed by the assessee, is such that the income cannot properly be deduced there from, and there by upholding the action of the AO in invoking the provisions of the First proviso to section 145(1) of the Acct. In the course of hearing both the parties have submitted that this issue is covered by the order of the Tribunal passed in ITA no. 1884/Del/1998 for the A.Y. 1994-95, which has been followed by the Tribunal in subsequent assessment years 1995-96, 1996-97, and 20001-02. Respectfully following the earlier decision of the Tribunal, where the Tribunal has held that the recourse of proviso to section 145 of the Act is uncalled and book result are to be accepted. Thus, this ground is decided in favour of the assessee.

24. Ground no. 2 is directed against the CIT(A)’s order in disallowing the loss of Rs. 97,51,324/- by holding that the sale price in respect of the

constructed/built-up property should be accounted for at the time of handing over the possession or making convenience, which is earlier. In the course of hearing of this appeal, it has been pointed out by the representatives of both the parties that this issue is covered by the earlier decision of the Tribunal in the A.Y. 1994-95 in ITA no. 3232/Del/2001, which has been followed by the Tribunal in the subsequent assessment years 1995-96, 1996-97, and 2001-02. Respectfully following the Tribunal's earlier order in the A.Y. 2004-05, where the Tribunal has held that the loss was disallowed by the AO after rejecting the method of accounting for booking of revenue at the time of convincing on built-up property, and in the light of the Tribunal's decision that the department was not justified in invoking the provisions of section 145, and in rejecting the method of accounting regularly following by the assessee, the addition made by the AO on this account is not justified, and the ground is decided in favour of the assessee. We allow this ground raised by the assessee.

25. Ground no. 3 with sub-ground (a) and (b) is with regard to the re-working of the cost of land at the average price of the cost of the land in

phase I to III and IV, Qutab Enclave Complex, now known as DLF city by dividing the cost of land acquired till end of each year by sellable in each phase separately and treating the area year marked for schools, hospitals, clubs, and other community building as sellable area. In the course of hearing of this appeal its has been pointed out by the parties that identical issue has been decided by this Tribunal in A.Y. 1994-95 in ITA no. 3232/Del/2001, which has been followed in subsequent years i.e. assessment years 1995-96, 1996-97 and 2001-02, and thus, it is to be decided accordingly. Respectfully following the Tribunal's order, where the Tribunal has held that the revenue was not justified in restricting writing off cost of land pertaining to phases I to III of Qutab Enclave, and in holding that the assessee was justified in taking phases I to IV as one project, and accordingly writing off cost of land, and the re-working done by the department was set aside by the Tribunal. Respectfully following the aforesaid order, we decide this issue in favour of the assessee in the terms of Tribunal's order for A.Y. 2004-05, which has been followed in assessment years 1995-96, 1996-97, and 2001-02.

26. Ground no. 5 is against the CIT(A)'s order in holding that interest of Rs. 58,14,994/- accrued on FDRs made from internal development is assessable in the assessee's hands.

26.1 In the course of hearing of this appeal, it was pointed out by both the parties that this issue has been decided by the Tribunal in A.Y. 1994-95 in ITA no. 3232/Del/2001, which has been followed in subsequent assessment years 1995-96, 1997-98, and 2001-02. Respectfully following the aforesaid order, where it has been held that the identical issue has been decided by the Tribunal in this very assessee's own case for the A.Y. 1993-94, in ITA no. 6615/Del/1996, wherein the matter has been restored back to the file of the AO for fresh adjudication in accordance with the directions contained in earlier order of the Income Tax Appellate Tribunal, we restore this issue to the file of the AO, and decide the issue in accordance with the directions given by the Tribunal in earlier years.

27. Now we come to the ground no. 4, which is directed against the CIT(A)'s order in confirming the addition of Rs. 14,36,41,533/- being the surplus arising on land/rights in land held as stock in trade by the assessee,

and brought into the partnership firm M/s. Real Estate Builders as capital contribution.

27.1 During the relevant year corresponding to the A.Y. 1997-98, the assessee became a partner in the newly constituted partnership firm, viz., M/s. Real Estate Builders with profit/loss sharing ratio at 20%. The assessee company contributed its ownership in 61 plots of land admeasuring 30148.340 sq. mtrs. as well as its right to purchase 11 plots owned by its subsidiary company 6321.06 sq. mtrs. in Qutab Enclave Complex, as capital contribution in the said partnership firm. These plots of land were converted as capital investment in the firm at an agreed value of Rs. 21.15 crores. The transfer value of 21.15 crores was credited in assessee's capital account in the books of the firm. The transfer value of 21.15 crore resulted into the surplus of Rs. 14,36,41,533/-, which was not offered to tax by the assessee by giving a reason that same is not taxable in view of the decision of Hon'ble Supreme Court in the case of CIT vs. Hind Construction Ltd. 83 ITR 211 (SC). The assessee also stated before the AO that in A.Y. 1985-86, such surplus was held to be not taxable. However, the AO as well as the CIT(A) brought the said surplus

to tax in the light of their view taken in A.Y. 1992-93 after relying upon the decision of Hon'ble Supreme Court in the case of Sunil Siddharthbhai v. Commissioner of Income-tax[1985] 156 ITR509 (SC) and after making a reference to the provisions contained in section 2(47) and 45(3) of the Act.

27.2 We have heard both the parties and perused the materials on record.

27.3 It is admitted position that the assessee entered into a partnership with 12 nos. of its subsidiary companies with a view to start and carry on the business of constructing houses on 61 plots and 11 plots of land situated in the DLF Qutab Complex, which has been introduced by the assessee to the common stock of the firm for achieving the aforesaid purpose of the firm. The memorandum of partnership was executed on 25th day of February, 1997. However, it has been made effective from 31st day of January, 1997. The value of the 61 numbers of plot of lands brought in by the assessee partner to a firm was made at RS. 17,60,00,000/-. In the partnership, it was also stated that the assessee was also the absolute owner or otherwise well substantially entitled to another lot of 11 plots jointly with the Parties of 2nd to 5th parts described in the

deed of partnership, admeasuring about 6321.06 sq. mtrs. situated in the said complex, out of which the assessee was the owner to the extent area of land admeasuring about 3036.78 sq. mtrs and the balance area of 3257.28 sq. mtrs. was owned by the parties of 2nd to 5th parts. The assessee also agreed to contribute his right in the said plots to the extent of area on land admeasuring about 3063.78 sq. mtrs. to a common stock of partnership, and in consideration thereof the sum of Rs.1,80,00,000/- was credited to the account of the assessee in the books of the partnership firm as on 31st day of January, 1997. The assessee had also had its rights to purchase area of land admeasuring about 3257.28, which was also brought by the assessee in to the common stock on partnership, and in consideration thereof, the sum of Rs. 1,75,00,000/- was credited to the account of the assessee in the account books of the partnership firm as on 31st January, 1997. Thus, total amount of Rs. 21,15,00,000/- (17,60,00,000/- + 1,80,00,000/- + 1,75,00,000/-) was credited to the assessee's account in the account books of the partnership firm as on 31st day of January, 1997. It was further provided that w.e.f. 31st day of January, 1997, the said 61 plots an 11 plots of land had became absolute

property of the partnership firm. It was further provided that out of the aforesaid amount of Rs. 21,15,00,000/- (Rs. 21.15 crores) being value of the plot of land brought in by the assessee to a firm, the sum of Rs. 20,00,000/- (Rs. 0.20 crores) will be treated as assessee's capital and shall carry no interest, and the remaining amount of Rs. 20,95,00,000/- (Rs. 20.95 crores) will be treated as loan to the partnership firm, which may be either free of interest or carry interest at such rate as may be mutually agreed upon from time to time. We hold that the surplus arising to the assessee from the transfer of 61 plots of land and 11 plots of land is Rs. 14,36,41,533/-, which is liable to be taxed in the light of the provisions contained in section 45(3) of the Act for the reasons given on identical issue in the assessment year 1992-93.

27.4 Even otherwise in the light of the word of caution emphasized by the Hon'ble Supreme Court in the case of Sunil Siddharthbhai v. Commissioner of Income-tax (supra), where it has been emphasized that if the transfer of the personal asset by the assessee to a partnership in which he is or becomes a partner is merely a device or ruse for converting the asset into money which would substantially remain available for his

benefit without liability to tax, it will be open to the Income Tax Authority to go behind the transaction and examine, even where the partnership is genuine, whether the transaction of transferring the personal asset to the partnership firm represents a real attempt to contribute to the share capital of the partnership firm for the purpose of carrying on the partnership business or is nothing but a device or ruse to convert the personal asset into money substantially for the benefit of the assessee while evading tax on a capital gain. From the facts of the present case, it is more than clear that the transaction of transferring plots of land owned by the assessee to the partnership firm is not a real attempt to contribute to the share capital of the firm for the purpose of carrying the partnership business as out of the total value of land, amounting to Rs. 21.15 crores, which has been recorded as value of land in the books of the partnership firm, the only sum of Rs. 20,00,000/- has been allocated towards assessee's contribution to the share capital and a substantial portion amounting to Rs. 20,95,00,000/- (Rs. 20.95 crores) has been made available with the assessee for his benefit in the nature of loan payable by the firm to the partner. It is well known that the advances given in addition to the capital

by a partner to a firm occupies a better position for the benefit of a partner as could be seen from section 13(1)(c) vis.-a-vis. 13(1)(d) and section 48(b)(ii) vis.-a-vis 48(b)(iii) of the Indian Partnership Act where advances by a partner distinguished from capital are placed on better footing than the capital contributed by the partner for the purpose of partner's right to receive interest thereupon and to realize or recover the advances distinguished from capital. Moreover, the assessee has indulged into a well designed and colourable strategy to convert its stock in trade into money by constituting various partnership firms year after year and contributing part of its land out of total land held as stock in trade into various firms. The various partnership firms constituted by the assessee from year to year in A.Y. 1992-93 and then in assessment years 1997-98 to 2000-01, and also the details of total value of land contributed by the partners, the total amount treated as capital contribution, and the amount treated as loan by the assessee to a firm have been placed before us by the Id. counsel for the assessee, which are annexed as Annexure –A to this order. Therefore, in this view of the matter, the surplus arising from the

transaction of transfer of assessee's property to a partnership firm is chargeable to tax in terms of our order for A.Y. 1992-93.

ITA No. 3233/Del/2001 : A.Y. 1998-99

28. Now we shall come to the appeal filed by the assessee for the A.Y. 1998-99, directed against the CIT(A)'s order dated 13.06.2001, passed in the matter of an assessment made u/s. 143(3) of the Income Tax Act, 1961 ("the Act")

29. Ground no. 1, 2, 3, and 5 are identical to the ground no. 1, 2, 3, and 5 raised in the A.Y. 1997-98. Therefore, these grounds shall stand decided in terms of our order deciding the identical ground in A.Y. 1997-98. The decision given in A.Y. 1997-98, on these issues shall apply to the identical issues involved in the A.Y. 1998-99.

30. Ground no. 4 in A.Y. 1998-99 is directed against the CIT(A)'s order in confirming the addition of Rs. 17,12,17,554/- being the surplus amount arising on land/rights in land held as stock in trade and brought into the partnership firm as capital contribution by the assessee.

30.1 During the period relevant to the A.Y. 1998-99, the assessee company became a partner in two newly constituted partnership firms viz., M/s. DLF Office Developers and M/s. DLF Property Developers, with profit/loss sharing ratio of 12% in each firm. The assessee company contributed its right to purchase in one plot of land owned by its subsidiary companies at admeasuring about 1.152 acres in Phase-III DLF City, Gurgaon, into the common stock of the partnership firm viz., M/s. DLF Office Developers. The assessee company also contributed its ownership of nine residential plots of land in Phase-II admeasuring 4631.17 sq. meters as well its right to purchase 47 plots owned by its subsidiaries companies into the common stock of partnership firm viz., M/s. DLF Property Developers. These plots of lands were converted as a capital investment in the firm at an agreed value of Rs. 24.62 crores, which resulted in surplus of Rs. 17,12,17,554/- to the assessee. The assessee credited this surplus to the profit and loss account but it claimed it to be exempted from tax in the light of the decision of Hon'ble Supreme Court in the case of CIT vs. Hind Construction Ltd. 83 ITR 211 (SC), and in the light of the decision taken in the A.Y. 1985-86. However, the AO

had brought the surplus to tax for the reason given in the A.Y. 1992-93 by relying upon the decision of of Hon'ble Supreme Court in the case of Sunil Siddharthbhai v. Commissioner of Income-tax[1985] 156 ITR509 (SC) and after making a reference to the provisions contained in section 2(47) and 45(3) of the Act.

30.2 On an appeal, the CIT(A) confirmed the AO's order in view of the order of the CIT(A) passed in A.Y. 1992-93, which has also been followed by the CIT(A) in A.Y. 1997-98

30.3 We have heard both the parties and have carefully gone through the orders of the authorities below.

30.4 In this A.Y. 1998-99 two partnership firms viz., M/s. DLF Office Developers and M/s. DLF Property Developers were constituted vide memorandum of partnership executed on 23rd day of March 1998 made effective from 24th day of February, 1998, wherein the assessee became a partner alongwith eight its subsidiaries as partners in M/s. DLF Office Developers and with other sixteen its subsidiaries as partners in M/s. DLF Property Developers. The assessee brought certain plot of land

held by it into the common stock of partnership valued at 3,70,00,000/-, which amount was credited to the account of the assessee in the account books of the partnership firm. Out of the aforesaid amount of Rs. 3,70,00,000/-, the sum of Rs.12,00,000/- was treated as assessee's capital contribution without carrying any interest, and the remaining amount of Rs. 3,58,00,000/- has been treated as a loan by the assessee to a partnership firm, which may be either free of interest or carry interest at such rates as may be mutually agreed upon from time to time. The property brought in by the partners were treated as a property of a partnership firm on and from 24th day of February, 1998.

30.5 Similarly, in the firm under name and style of M/s. DLF Property Developers, the assessee brought certain plot of land held by it into the common stock of partnership, which were valued at Rs. 3,25,00,000/-, which amount was credited to the account of the assessee in the books of the partnership firm of 24th day of February, 1998. The assessee also brought its right to purchase the land in respect of certain 47 plots of land into the common stock of the partnership firm, which were valued at Rs. 17,75,00,000/-. Thus, the total amount credited to the

assessee's account was 21 crores out of which sum of Rs. 12 lacs was credited to the capital account of the assessee as its capital contribution without carrying any interest, and the remaining amount has been treated as loan by the assessee to the partnership firm, which may be either free of interest or may carry interest at such rates as may be mutually agreed upon from time to time. As a result of this transaction crediting the assessee's account by market value of the plot of land brought in by the assessee in a firm, the sum of Rs. 17,12,17,554/- resulted as surplus to the assessee, which was credit to the profit and loss account of the assessee to claim as exempted from tax relying upon the decision of Hon'ble Supreme Court in the case of CIT vs. Hind Construction Ltd.

30.6 In the light of our decision in the A.Y. 1992-93 and 1997-98, we hold that the amount of Rs. 17,12,17,554/- being surplus arising to the assessee is chargeable to tax as capital gain. The AO is directed to compute capital gain as per law as so held by us in A.Y. 1992-93 and 1997-98. **30.7** We further hold that our view in para 27.4 in the A.Y. 1997-98 shall also be applicable to this issue arising in this A.Y. 1998-99.

ITA no. 267/Del/2003 : AY 1999-2000

31. Now we shall taken up the appeal filed by assessee for the A.Y. 1999-2000, directed against the order dated 25.10.2002, passed by the Id. CIT(A) in the matter of an assessment made u/s. 143(3) of the Income Tax Act, 1961 (“the Act”).

32. Ground no. 1 and ground no. 3 relating to the issue about reworking of cost of land in phases I to III and IV in Qutab Enclave Complex and interest accrued on FDRs made from internal development account included in assessee’s hand are identical to the ground no. 3 and 5 respectively for the A.Y. 1997-98. Therefore, in terms of our order on the identical issue passed in the A.Y. 1997-98 vide this common order, this issue has been decided accordingly. In other words, the decision on the identical issues rendered in the A.Y. 1997-98 shall also apply to the identical issues raised in this A.Y. 1999-2000.

33. Ground no. 2 in A.Y. 1999-2000 against the CIT(A)’s order in confirming the addition of Rs. 54,82,91,077/- being surplus arising on contribution of land held as stock in trade by the assessee and contributed

to the partnership firm as capital contribution by the assessee in the capacity of a partner.

33.1 In this A.Y. 1999-2000, the assessee became a partner in five newly constituted partnership firms. The assessee company contributed its land and right to purchase land owned by its subsidiary companies in DLF City, Gurgaon to the partnership firms as capital contribution. Total value of all piece of lands were determined at an agreed value of Rs. 78.55 crores. These plots of lands were contributed by the assessee as capital contribution in the aforesaid five newly constituted partnership firm. As a result of this transaction, a surplus of Rs. 54,82,91,077/- had arisen to the assessee. The assessee has credited this surplus to its profit and loss account. The firm also credited the assessee's capital account by sum of Rs.78.55 crores. However, the assessee claimed the surplus to be exempted from tax in the light of of the decision of Hon'ble Supreme Court in the case of CIT vs. Hind Construction Ltd. 83 ITR 211 (SC). The assessee also stated before the AO that in A.Y. 1985-86, such surplus was held to be not taxable. However, the AO as well as the CIT(A) brought the said surplus to tax in the light of their view taken in A.Y.

1992-93 after relying upon the decision of Hon'ble Supreme Court in the case of Sunil Siddharthbhai v. Commissioner of Income-tax[1985] 156 ITR509 (SC) and after making a reference to the provisions contained in section 2(47) and 45(3) of the Act.

33.2 We have heard both the parties and have carefully gone through the orders of the authorities below.

33.3 In this year also five partnership firms were newly constituted in which the assessee became a partner. The assessee brought in certain plot of land in the common stock of this newly constituted firm at a value of Rs. 78.55 crores. The aforesaid amount of Rs. 78.55 crores was credited in the assessee's account in the books of account of the partnership firms. Out of the aforesaid amount of Rs. 78.55 crores credited in the assessee's account in the books of the firms sum of Rs. 9.50 was credited on account of assessee's capital contribution and balance amount of Rs. 69.05 crores (78.55 crores – 9.50 crores) was treated as loan by the assessee to the newly constituted firms.

33.4 In the light of our decision in the A.Y. 1992-93, 1997-98 and 1998-99, we hold that the amount of Rs. 54,82,91,077/- being surplus arising to the assessee is chargeable to tax as capital gain, and the AO is directed to compute capital gain as per law as so held by us in A.Y. 1992-93, 1997-98 and 1998-99.

33.5 We further hold that our view in para 27.4 in the A.Y. 1997-98 shall also be applicable to this issue arising in this A.Y. 1999-2000.

ITA No. 4986/Del/2003 : AY 2000-2001

34. The last appeal filed by the assessee is pertaining to the A.Y. 2000-01, directed against the CIT(A)'s order dated 13.09.2003, passed in the matter of a assessment made u/s. 143(3) of the Income Tax Act, 1961 ("the Act") by the AO.

35. Ground no. 1 is about the rejection of the method regularly employed by the assessee by the AO, and then confirming the addition on account of reworking of the cost of land at the average purchase price of

land in Qutab Enclave Complex, and thus, making addition of Rs. 34,30,308/-, and addition of Rs. 1,60,69,880/- on account of internal development expenses. This issue is covered by the Tribunal's decision in A.Y. 1994-95, which has been followed in A.Y. 1995-96, 1996-97, and 20001-02. The aforesaid decision of the Tribunal has been followed by us while deciding these issues in the A.Y. 1997-98, 1998-99, and 1999-2000. Therefore, this issue is decided in favour of the assessee in terms of our order of the aforesaid years following the decision of Tribunal passed in A.Y. 1994-95.

36. Ground no. 2 is with regard to the addition of Rs. 6,27,000/- on account of accrued interest on FDRS made after withdrawal under authority of Haryana Government from internal development bank account. This issue has also been considered in the A.Y. 1997-98, 1998-99, and 2000-01 above after following the earlier decision of the Tribunal. Therefore, this issue has been decided accordingly in terms of our order passed in the A.Y. 1997-98, 1998-99, and 2000-01.

37. Ground no. 3 is directed against the CIT(A)'s order in confirming addition of Rs. 5,60,00,000/- being the surplus arising on land held as stock in trade by the assessee but contributed to the partnership firm towards capital by the assessee.

37.1 During the period relevant to the A.Y. 2000-01, the assessee became a partner in a partnership firm M/s. DLF Phase – IV Commercial Developers and contributed certain land owned by it as well as its right of purchase of land, to the aforesaid firm towards its capital, and surplus of Rs. 5,60,00,000/-, being the difference between the value credited in assessee's capital account, and the cost to the assessee was credited in the profit and loss account, but claimed as exempted from tax in the light of the decision of the Hon'ble Supreme Court in the case of Commissioner of Income-tax v. Hind Construction Ltd [1972] 83 ITR 211 (SC) and in the light of the order decided in assessee's favour in the A.Y. 1985-86. However, the AO rejected the assessee's claim in the light of the assessment order for the A.Y. 1992-93 as well as for A.Y. 1999-2000.

37.2 In the A.Y. 2000-01, a partnership firm under name and style of M/s. DLF Phase IV, Commercial Developers, was constituted in which the assessee became a partner. The assessee brought in certain plot of land to the common stock of the partnership firm. These plots were valued at Rs. 8 crores, which was credited in the assessee's account in the books of the firm. Out of the aforesaid amount of 8 crores, the sum of Rs. 75,00,000/- has been credited in the capital account of the assessee as assessee's capital contribution, and the balance sum of Rs. 7,25,00,000/- has been treated a loan by the assessee to the firm. From this transaction a surplus of Rs. 5,60,00,000/- had arisen to the assessee, which was credited in the profit and loss account of the assessee but claimed as exempted in the return of income filed by the assessee.

37.3 In the light of our decision in the A.Y. 1992-93, 1997-98 and 1998-99, we hold that the amount of Rs. 5,60,00,000/- being surplus arising to the assessee is chargeable to tax as capital gain, and the AO is directed to compute capital gain as per law as so held by us in A.Y. 1992-93, 1997-98, 1998-99 and 1999-2000.

37.4 We further hold that our view in para 27.4 in the A.Y. 1997-98 shall also be applicable to this issue arising in this A.Y. 2000-2001.

38. In the result, all these appeals filed by the assessee are partly allowed in the manner as indicated above

39. This decision is pronounced in the open court on 4th January, 2010.

(I.P. BANSAL)
JUDICIAL MEMBER

(C. L. SETHI)
JUDICIAL MEMBER

Dated: 4th January, 2010

*Nitasha

Copy of the Order forwarded to:

1. Appellant;
2. Respondent;
3. CIT;
4. CIT(A);
5. DR;
6. Guard File

By Order

Dy. Registrar

ANNEXURE – A

S. No.	Name of Partnership Firm	Date of Partnership	Relevant Assmt. Year	Name of Partners	Land Contributed		Amount treated as Capital Contribution	Profit Sharing Ratio	Amount treated as Loan (Rs.)	Whether loan treated ? If yes, whether interest bearing or non interest bearing till.
					Area	Value				
1	DLF Commercial Developers	16.03.1992	1992-93	DLF Universal Ltd.	16.98	115,000,000	115,000,000	76	-	No.
				Apollo Land & Housing Co .Ltd (Acres)			100,000	5		
				Moonlight Builders & Developers Ltd.			100,000	5		
				Sunrise Land & Housing Co. Ltd.			100,000	5		
				DLF Builders & Developers Ltd.			100,000	5		
				Mr. Rajinder Singh			50,000	4		
				Total	16.98	115,000,000	115,450,000	100		
2	Real Estate Builders	31.01.1997	1997-98	DLF Universal Ltd.	33,212.12	211,500,000	2,000,000	20	209,500,000	Yes. Non interest bearing
				Kavicon Agro Farming Co. Pvt.	823.90	804565	200,000	2	604,565	" "
				Instant Batteries Ltd.	1,733.38	627047	200,000	2	427,047	" "
				Vee Dee Investment & Agenci	560.00	111752	200,000	2		
				Apollo Land & Housing Co .Ltd	140.00	22697	200,000	2		
				Aeshya Estates Pvt. Ltd. (Sq. Mtrs.)			900,000	9		
				Diwakar Estates Pvt. Ltd.			900,000	9		
				Pushpavali Builders & Developers Pvt. Ltd.			900,000	9		
				Ujagar Estates Pvt. Ltd.			900,000	9		
				Vanutsar Properties Pvt. Ltd.			900,000	9		
				Parvati Estates Pvt. Ltd.			900,000	9		
				Panchvati Estates Pvt. Ltd.			900,000	9		
				Kirtimaan Builders Pvt. Ltd.			900,000	9		
	Total				36,469.40	213,066,061	10,000,000	100	210,531,612	

3A	DLF Office Developers	24.02.1998	1998-99	DLF Universal Ltd.	1.15	37,000,000	1,200,000	12	35,800,000	Yes. Non interest bearing
				Aeshya Estates Pvt. Ltd.	(Acres)		1,100,000	11		
				Diwakar Estates Pvt. Ltd.			1,100,000	11		
				Ujagar Estates Pvt. Ltd.			1,100,000	11		
				Pushpavali Builders & Developers Pvt. Ltd.			1,100,000	11		
				Vanutsar Properties Pvt. Ltd.			1,100,000	11		
				Parvati Estates Pvt. Ltd.			1,100,000	11		
				Panchvati Estates Pvt. Ltd.			1,100,000	11		
				Kirtimaan Builders Pvt. Ltd.			1,100,000	11		
	Total				1.15	37,000,000	10,000,000	100	35,800,000	
3B	DLF Property Developers	24.02.1998	1998-99	DLF Universal Ltd.	4,613.17	177,500,000	1,200,000	12	176,300,000	Yes. Non interest bearing
				Anurag Construction Co. Ltd.	4,059.84	1,135,222	100,000	1	1,035,222	" "
				Apollo Land & Housing Co .Ltd	1,167.48	195,711	100,000	1	95,711	" "
				Delhi Land & Finance Ltd.	2,810.53	1,864,002	100,000	1	1,764,002	" "
				DLF Housing & Construction L	2,581.51	490,767	100,000	1	390,767	" "
				Instant Batteries Ltd.	2,634.34	962,929	100,000	1	862,929	" "
				Kavicon Agro Farming Co. Pvt.	2,461.27	2,445,627	100,000	1	2,345,627	" "
				Paragon Real Estates & Apartr	10,275.40	2,111,693	100,000	1	2,011,693	" "
				Vee Dee Investment & Agenci	542.22	110,472	100,000	1	10,472	" "
				Aeshya Estates Pvt. Ltd.	(Sq. Mtrs.)		1,000,000	10		
				Diwakar Estates Pvt. Ltd.			1,000,000	10		
				Ujagar Estates Pvt. Ltd.			1,000,000	10		
				Pushpavali Builders & Developers Pvt. Ltd.			1,000,000	10		
				Vanutsar Properties Pvt. Ltd.			1,000,000	10		
				Parvati Estates Pvt. Ltd.			1,000,000	10		
				Panchvati Estates Pvt. Ltd.			1,000,000	10		
				Kirtimaan Builders Pvt. Ltd.			1,000,000	10		
	Total				31,145.76	186,816,423	10,000,000	100	184,816,423	

4A	DLF City Centre	04.03.1999	1999-2000	DLF Universal Limited	32.87	200,000,000	15,000,000	11	185,000,000	Yes. Non interest bearing
				Apollo Land & Housing Co. Ltd (Acres)		14,251,374	2,000,000	3	12,251,374	" "
				Delhi Land & Finance Ltd.		2,495,494	2,000,000	3	495,494	" "
				Vee Dee Investment & Agencies Ltd.		1,658,000	1,658,000	3		
				Aeshya Estates Pvt. Ltd.			190,000,000	80		
	Total				32.87	218,404,868	210,658,000	100	197,746,868	
4B	DLF Golf Holdings (now known as: DLF Residential Builders)	21.12.1998	1999-2000	DLF Universal Limited	25,543.17	142,500,000	20,000,000	12	122,500,000	Yes. Non interest bearing
				Madhur Cultivations Limited (Sq. Mtrs.)		7,682,114	1,500,000	1	6,182,114	" "
				Renkon Estates & Farms Ltd.		1,444,622	1,444,622	1		
				Vidhur Cultivations Ltd.		305,522	305,522	1		
				Aravali Cultivations Ltd.		59,185	59,185	1		
				Kum Kum Cultivations Pvt. Ltd.		458,197	458,197	1		
				Queensdale Cultivations Pvt. Ltd.		201,932	201,932	1		
				Manavsthali Estates Pvt. Ltd.		511,252	511,252	1		
				Swastha Builders Pvt. Ltd.		490,997	490,997	1		
				Aeshya Estates Ltd.			1,500,000	1		
				Diwakar Estates Pvt. Ltd.			1,500,000	1		
				Ujagar Estates Pvt. Ltd.			1,500,000	1		
				Pushpavali Builders & Developers Pvt. Ltd.			1,500,000	1		
				Vanutsar Properties Pvt. Ltd.			1,500,000	1		
				Parvati Estates Pvt. Ltd.			1,500,000	1		
				Panchvati Estates Pvt. Ltd.			1,500,000	1		
				Kirtimaan Builders Pvt. Ltd.			1,500,000	1		
				Moonlight Builders & Developers Ltd.			110,000,000	72		
	Total				25,543.17	153,653,821	146,971,707	100	128,682,114	

4C DLF Home Builders	02.09.1998	1999-2000	DLF Universal Ltd.	24,950.58	134,500,000	20,000,000	13	114,500,000	Yes. Non interest bearing
			DLF Engineering Projects Ltd. (Sq. Mtrs.)		6,272,364	4,500,000	3	1,772,364	" "
			DLF Industrial Finance & Leasing Co. Ltd.		2,729,919	2,729,919	3		
			DLF Housing Finance Ltd.		3,221,008	3,221,008	3		
			Kavicon Agro Farming Co. Pvt. Ltd.		3,148,602	3,148,602	3		
			Realest Builders & Services Ltd.			115,000,000	75		
Total				24,950.58	149,871,893	148,599,529	100	116,272,364	
4D DLF Residential Developers	30.06.1998	1999-2000	DLF Universal Ltd.	26885.34	150,500,000	20,000,000	12	130,500,000	Yes. Non interest bearing
			Vee Dee Investment & Agency (Sq. Mtrs.)		1,016,916	1,600,000	1		
			Delhi Land & Finance Ltd.		501,896	1,600,000	1		
			Instant Batteries Ltd.		1,926,470	1,600,000	1	326,470	Yes. Non interest bearing
			Apollo Land & Housing Co. Ltd.		285,953	1,600,000	1		
			Kavicon Agro Farming Co. Pvt. Ltd.		3,311,981	1,600,000	1	1,711,981	Yes. Non interest bearing
			Mayur Recreational & Development Ltd.		494,084	1,600,000	1		
			Bhagirathi Investments Pvt. Ltd.		2,998,962	1,600,000	1	1,398,962	Yes. Non interest bearing
			Moonlight Builders & Developers Ltd.			108,000,000	65		
			Aeshya Estates Pvt. Ltd.			3,200,000	2		
			Diwakar Estates Pvt. Ltd.			3,200,000	2		
			Ujagar Estates Pvt. Ltd.			3,200,000	2		
			Pushpavali Builders & Developers Pvt. Ltd.			3,200,000	2		
			Vanutsar Properties Pvt. Ltd.			3,200,000	2		
			Parvati Estates Pvt. Ltd.			3,200,000	2		
			Panchvati Estates Pvt. Ltd.			3,200,000	2		
			Kirtimaan Builders Pvt. Ltd.			3,200,000	2		
Total				26,885.34	161,036,262	164,800,000	12	133,937,413	

4E	DLF Residential Partners	02.09.1998	1999-2000	DLF Universal Ltd.	26,806.13	158,000,000	20,000,000	11	138,000,000	Yes. Non interest bearing
				Vee Dee Investment & Agency (Sq. Mtrs.)		77,405	1,800,000	1		
				Delhi Land & Finance Ltd.		1,475,288	1,800,000	1		
				Landsdale Estates Pvt. Ltd.		6,302,405	1,800,000	1	4,502,405	Yes. Non interest bearing
				Instant Batteries Ltd.		351,200	1,800,000	1		
				DLF General Finance Ltd.		251,856	1,800,000	1		
				Anurag Construction Co.Ltd.		718,606	1,800,000	1		
				Apollo Land & Housing Co. Ltd.		84,477	1,800,000	1		
				Kavicon Agro Farming Co. Pvt. Ltd.		5,396,284	1,800,000	1	3,596,284	Yes. Non interest bearing
				DLF Industrial Finance & Leasing Co. Ltd.		155,772	1,800,000	1		
				Paragon Real Estates & Apartments Ltd.		425,993	1,800,000	1		
				DLF Housing & Construction Ltd.		113,933	1,800,000	1		
				DLF Housing Finance Ltd.		210,040	1,800,000	1		
				Mayur Recreational and Development Ltd.		308,079	1,800,000	1		
				Bhagirathi Investments Pvt. Ltd.		7,342,713	1,800,000	1	5,542,713	" "
				Sunrise Land & Housing Co.Ltd.			140,000,000	75		
	Total				26,806.13	181,214,051	185,200,000	100	151,641,402	
5	DLF Phase - IV Commercial Developers	10.06.1999	2000-01	DLF Universal Ltd.	0.68	80,000,000	7,500,000	14	72,500,000	Yes. Non interest bearing
				Diwakar Estates Pvt. Ltd. (Acres)			70,000,000	80		
				DLF Financial Services Ltd.			2,200,000	6		
	Total				0.68	80,000,000	79,700,000	100	72,500,000	

PER DEEPAK R. SHAH, ACCOUNTANT MEMBER:

40. I have perused the draft order proposed by my esteemed colleague. In so far as the appeal for A.Y. 1992-93 is concerned, I am unable to concur with the proposition laid down as regards ground No. 1 (divided into sub-ground No. 1.1 to 1.7). As regards other grounds I fully agree with the finding given in relation thereto. Therefore, I proceed to hold as under in relation to ground No. 1 for A.Y. 1992-93:-
- 40.1 In the draft order proposed by my learned brother the facts and arguments are elaborately discussed and hence I do not propose to comment upon the same. However, in Para 16 of the draft order the proposition is laid down to which I am unable to agree and hence I proceed to hold as under.
41. The facts which are never in dispute are that the assessee was holding certain land as its stock-in-trade. The lands were brought in by the assessee as its capital contribution in a firm when the partnership firm was constituted. The partnership deed was constituted on 23/03/1992 but made effective from 16/03/1992. The cost of the said land in the hands of assessee was 5.49 crores. At the time of introduction of the said land the market value was determined at 11.5 crores. The amount credited to the account of partner in the books of firm when the land was contributed was taken as 11.5 crores. The difference of Rs. 6.01

crore was credited by the assessee to its profit and loss account. The assessee claimed the difference as not exigible to tax, relying on the decision of the Hon'ble Supreme Court in the case of Hind Construction Limited (83 ITR 211). The Assessing Officer treated the difference as chargeable income under the head "Profits and Gains of Business or Profession". Learned CIT(A) also confirmed the same and held in Page 24 of his order as under :

"4) Since the land so transferred represented the stock-in-trade, the profits were chargeable u/s 28 of the Act which stands on a different footing than the gains arising from transfer of a capital or fixed asset."

In light of the above undisputed facts the issue which arises for consideration is whether the surplus credited to the profit and loss account on introduction of the land as its capital contribution, held by the assessee as stock-in-trade is chargeable to tax or not.

42. The question is regarding taxability of the land held by assessee as its stock-in-trade and introduced in the partnership firm as its capital contribution when the assessee became partner of the said firm. The words 'Firm', 'Partner' and 'Partnership' are defined under the Income Tax Act, 1961 (hereinafter referred to as 'The Act') in Section 2(23) of the Act. As per the said definition the words Firm, Partner and Partnership have the meaning respectively assigned to them in the Indian Partnership Act 1932 and the expression 'partner' shall also

include any person who being a minor has been admitted to the benefits of partnership. Therefore, it is clear that the relation of firm and partner are the same as commonly understood under the Partnership Act. The firm is not a separate legal entity but only for the purpose of Income Tax Act it is a separate taxable entity. Therefore, under normal provision the partner and firm are not separate. A person individually is a partner and collectively is called a firm. The firm is not distinct and separate from the partners constituting it. Therefore when any transaction takes place in normal course between a partner and a firm, no new rights are created. The full bench of Hon'ble Supreme Court in the case of Sunil Siddharthbhai Vs CIT (156 ITR 509) made observation as to the right of partner when the partner introduces his assets as its capital contribution in the firm. These observations are elaborately noted in Para 16.30, 16.31, 16.32, 16.33, 16.35, 16.36 and 16.37 of the draft order proposed by my learned brother. Various propositions laid down by Hon'ble Supreme Court in the said case is also summarized in Para 16.38 of the draft order. In para 16.28 of the draft order the effect of introduction of the asset by a partner to a firm in which he become the partner has been summarized as to give following rights accruing in favour of a partner at the time of so introduction:

- i. "Right to get his share of profit from time to time during the subsistence of the partnership; and

- ii. On the dissolution of partnership or with his retirement from the partnership, the right to get the value of his shares in the net partnership asset as on the date of dissolution or retirement after deduction of liabilities and prior charges.”

42.1 As per the ratio laid down by various courts including Hon’ble Supreme court in the case of Sunil Siddharthbhai (Supra), the amount credited to the account of partner in the books of the firm and the resultant surplus will not amount to any income accruing or arising to the partner for the reason that—

1. The firm is no separate legal entity than the partners constituting it.
2. The partner is not legally entitled to claim the amount standing to the credit of his capital account as debt due by the firm in favour of the partner.
3. The right is merely to share profits from time to time during subsistence of partnership and only on dissolution or on retirement to get the value of his share in the net partnership asset.

Thus it will be incorrect to hold that the amount of Rs. 11.5 crores credited to the account of the partner in the books of the firm is giving rise to any income chargeable to tax in the hands of the partner when he introduced his stock-in-trade as his capital contribution.

42.2 Hon'ble Supreme Court in the case of Sunil Siddharthbhai (Supra) held that when the assessee, a partner in a firm, made over to the firm certain shares in a company which were held by him as 'Capital Asset', there was a "transfer" of the shares, but that he received no consideration within the meaning of section 48. Nor did any profit or gain accrue to him for the purpose of section 45. To overcome the situation the Income Tax was amended whereby Sub Section (3) was inserted in Section 45 of the Act by Finance Act 1987 w.e.f. 01/04/1988. According to Section 45 (3) the profit or gain arising out of the transfer of a 'capital asset' by a person to a firm in which he becomes a partner by way of capital contribution or otherwise shall be chargeable to tax as his income. Section 45 is a section to charge the capital gain arising on transfer of a capital asset affected in the previous year. The phrase "capital asset" has been defined in the Act in section 2 (14) of the Act. According to the definition 'capital asset' means property of any kind held by an assessee but does not include any 'stock-in-trade' held for the purpose of his business or profession. Thus when "stock-in-trade" is specifically excluded from the definition of "capital asset" the charging provision of section 45 and the computation provision contained in section 48 cannot be applied in relation to stock-

in-trade. As per section 2 (47) the word “transfer” in relation to a ‘capital asset’ is defined to include various types of transactions. However, the said definition of transfer is only in relation to a capital asset and since the phrase “capital asset” excludes “stock-in-trade”, the definition contained in section 2 (47) cannot be applied to a stock-in-trade. When the profits of business is to be computed under section 28 of the Act, the income chargeable under the head ‘Profits and Gains of Business or Profession’ shall be of any business or profession which was carried on by the assessee at any time during the previous year. The business can be carried on by the person either alone or in partnership with other partners. However, when the asset held by the partner individually is introduced by him as its capital contribution, it cannot be said that the assessee has carried on business with the firm in which he became the partner. Therefore, merely because the surplus was credited in the profit and loss account due to introduction of the stock-in-trade in the firm, will not be assessable as ‘Profits and Gains of Business or Profession’. In the draft order in para 16.24 it has been agreed that the partnership firm as such is genuine. It is also a matter of record that all along the partnership firm has been assessed to tax and it is also found that after the land was contributed by the assessee in the partnership firm as its capital contribution, the said land was developed by the firm and profit was earned by the firm which has been assessed as such. This fact has been reiterated in para 16.25 of the draft order also. Even in para 16.20 of the draft order it has been accepted as under :

“From the material placed on record, we find that the partnership firm so constituted has been assessed to tax as such from year to year by the department, and the department has not considered the firm as bogus or sham. Thus, we do not find any material to hold that the very transaction of creating the partnership itself is not genuine but a sham transaction.”

If this factual situation prevails then it cannot be said that when the assessee introduced its stock-in-trade as its capital contribution in the firm at the time when it became the partner gives rise to any profit or gains chargeable to tax under the head ‘Business Income’.

42.3 This proposition has been laid down by Hon’ble Supreme Court in the case of CIT Vs. Hind Construction Limited (83 ITR 211). While dismissing the civil appeal filed by the revenue against the order of Hon’ble Calcutta High Court reported in CIT Vs. Hind Construction Limited (78 ITR 664), Hon’ble Supreme Court held :

“If a person revalues his goods and shows a higher value for them in his books, he cannot be considered as having sold these goods and made profits therefrom. Nor can a person by handing over his goods to a partnership of which he is a partner and that as his share of capital be considered as having sold the goods to the partnership”.

(emphasis supplied)

It is also useful to refer the proposition laid down by Hon'ble Calcutta High Court in Hind Construction case (Supra) wherein after referring to various case laws on the subject it was held:

“In our view, the taxability of a sum as income or profit would depend upon the real character or the substance of the transaction which yields such income or profit. In the instant case, we cannot agree with the contention that any transfer or sale has taken place between the assessee-company and the partnership firm. The transfer or sale is a bilateral transaction and there must be at least two persons-the transferor or the vendor on the one hand and the transferee or the purchaser on the other. In the facts of this case, the assessee-company's share of the machinery was valued originally at Rs. 2,06,745. Before the assets were transferred to the partnership firm, the assessee's share of the machinery was revalued at Rs. 6,06,372 and the said amount was entered in the assessee's books of account before the transfer. Whether this appreciated value is the market value or not, we do not know. The assessee might have increased the value for future advantage. The assessee-company formed a partnership in which the assessee-company had a half share. Whatever interest the assessee had in its own share of the machinery was transferred at the said appreciated value of Rs. 6,06,372 of the assessee's share of the capital in the partnership firm. Thus, the assessee is really investing or depositing its own assets in a partnership firm which was constituted by it and in which it has substantial control. In doing the same, it has only appreciated the value of the machinery. Whether the appreciation of the shares has been done before the transfer or after the transfer, there is no question of any purchase or sale of machinery. Nor can it be said that there was any profit motive in it. A notional or fictional income might have been caused in the records of the company or in the records of the firm. But no real income was received by the assessee. The nature and the character of the transaction is such that it is impossible to believe that there is any question of profit having been received in the

accounting year. As a result of the appreciation of the value of the machinery the assessee as a partner in the partnership firm might get a future advantage. But, as the Supreme Court has said in Kikabhai's case (supra), tax cannot be imposed on the future advantage which might be available to the assessee. Further, there is no question of withdrawal of a part of the stock-in-trade, in the instant case, as it took place in Sharkey v. Wernher [1956] AC 58; 29 ITR 962 (HL). In fact, in the latter case, reduction of stock-in-trade took place but the original business with its reduced stock-in-trade was carried on by the assessee. In the instant case, the assessee has transferred the entire value of the machinery to the partnership firm with the whole object of increasing the capital of the partnership firm. The assessee has transferred its own property to his partnership account in the firm. The facts and circumstances in which the transaction took place repel the idea of a transfer for consideration or a sale. In the instant case also, the market value of the disposal machinery was not gone into at all.

The next point which repels the contention of the revenue is that there is no question of any transfer or sale in the instant case because the firm is not a juristic person. The partnership has been defined in section 4 of the Indian Partnership Act, 1932, which reads as follows:

"Partnership is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.

Persons who have entered into partnership with one another are called individually 'partners' and collectively 'a firm' and the name under which their business is carried on is called the firm name".

It appears from this definition that a firm cannot be called a separate entity. The same persons who are individually called partners are collectively known as the firm for the purpose of their business. The firm always consists of partners and the partners always are parts of the firm. Procedurally and for limited purpose a firm has been separately described, but in no sense, can a firm be called a juristic entity like a limited company. The name of a firm is the business name of the partners and, thus, when a person in individual capacity transfers his assets to his own firm, it cannot be said that the partner is transferring his assets to a distinct person. We agree with Mr. Pal that a firm may have a character distinct from a partner but such

distinction is not because the firm and the partners are different entities. The distinction is for a limited purpose because a firm is only a descriptive name of the business of the partners. To illustrate, ordinarily, a firm comes to an end with the death of a partner, but there may be cases where a firm can continue although the old partners have died and the new partners have joined the firm. That contingency occurs where the terms of the partnership agreement provide that on the death of a partner the firm will not be dissolved. Juristically speaking, a person is one which is capable of rights and duties. In analysing the concept of "right", it appears that a "person" is a subject and object of "right". Such a "person" may be natural or legal or artificial. A natural person, like a human being, is a being to whom law attributes personality in accordance with the reality and truth. A legal and artificial person, however, is a persona real or imaginary to whom law attributes personality by way of fiction, when there is none in fact. Thus, natural person is a person in fact as well as in law, whereas a legal or artificial person is a person in law but not in fact. A firm accordingly is neither a natural nor an artificial person. It is not natural, because a firm represents only a relationship or arrangement between persons who carry on business with a view to profit. It is not a living being. If a firm represents individual partners and, as such, is called a natural person, there is a relationship of identity between partners and their firm. Nor can it be called a legal or artificial person because there is no general law by which its personality is recognized. It is suggested that because a firm carries on business in its firm name and because a firm can sue and be sued, under the Code of Civil Procedure, it has a distinct personality. Such personality can at best be a matter of procedural law. In substance, the firm name is only the business name of partners. It is allowed to sue and be sued as a matter of procedural law by way of convenience or expediency. It is not a corporate body with the right of perpetual succession nor its existence depends upon substantive law. The creation, continuation and extension of a firm is purely contractual and depends on the agreement between the partners. It is in that sense that Mr. D. N. Pritt in the latest edition of Pollock & Mulla's The Sale of Goods Act and The Partnership Act, 3rd edition, has made the following observations:

"A firm is currently regarded as something distinct from its members; they may have claims on the firm's property but it is not theirs; it has separate accounts, and is their debtor and creditor. Quite possibly some person who

is not a member of the firm may have authority to do certain things in its name which some or one of the partners have not. In short, the firm is treated very much as if it were a corporation; it is an artificial or 'moral' person for business purposes ... "

Thus, a partnership firm in India, although for limited purposes, is an individual or person or an entity, a legal personality cannot be attributed to it. In this connection reference may be made to a judgment of the Supreme Court in Dulichand Laxminarayan v. Commissioner of Income-tax [1956] 29 ITR 535; [1956] SCR 154(SC), where S. R. Das C. J., after discussing the juristic character of a partnership firm, held that a firm is not an entity or a person in law but merely a person or individual and a firm name is the collective name of these individuals who constitute the firm. The Judicial Committee also has held in Bhagwanji Morarji Goculdas v. Alembic Commercial Works [1948] LR 75 IA 147; AIR [1948] PC 100, that Indian law has not given legal personality to a firm apart from its partners. This view is also supported by another decision of the Supreme Court in Commissioner of Income-tax v. A. W. Figgies & Co. [1953] 24 ITR 405; [1954]SCR 171 (SC) James Mackintosh in his book on Roman Law in Modern Practice (Tagore Law Lectures, 1933) at page 126, has made the following observations:

"In Scotland and on the Continent generally the firm is recognised as a person distinct from the partner; in England it is not and here English and Roman laws are in accord. The latter held the persons engaged in ordinary partnership (societas) or joint adventure are just so many individuals acting together under contract; the property they contribute or acquire is their joint property; every debt due to the firm belongs in rateable shares to the various partners, and they are individually liable for the debts owing by the firm".

Thus, it is obvious that unlike a company where there is perpetual succession a firm, although an entity for a limited prpose, cannot be considered as a juristic person. In the instant case, the assessee has got 50 per cent. share in the fund and the other partner, Patel Engineering Co., who also owned the remaining 50 per cent. share in the disposal machinery also transferred his share in the partnership capital. Thus, the assessee and Patel Engineering Co. have only transferred their respective interests in the disposal machinery to their own firm. The transfer, if at all, is a transfer to

itself or to its own account. We are convinced that the nature of the transaction could at best be described as a readjustment of their assets in such a way that they can do their business in a different way. There is no question of ownership being transferred from one distinct person to another nor was there any consideration received by one individual from the other. Thus, there is no question of the assessee making any profit or gain and, therefore, the mere fact that the assessee transferred its interest to the assessee's firm at an appreciated value does not make the assessee liable to pay tax on the difference between the original price and the appreciated price.”

42.4 Under the Income Tax Act what is chargeable to tax is the income accruing to the assessee.

The income can be said to have accrued provided the assessee either receives the sum or any legally enforceable right is acquired. Such right should be accruing immediately and should not be inchoate or contingent. The amount credited to the account of the partner is not a debt due by the firm to the partner. The partner cannot legally enforce the claim to receive the amount standing to the credit to his account in the books of the firm. Thus the amount due by the firm to the partner standing to the credit of partner's account whether by way of capital or by way of loan will not be a legally enforceable right in favour of partner against the firm or the other partners constituting such firm. For this purpose the entries made in the books of account of the assessee are not the criteria. This view has been reiterated by various courts time and again including Supreme Court. In the case of Tuticorin Alkalies Chemicals & Fertilisers Limited Vs. CIT (227 ITR 172) the full bench of Hon'ble Supreme Court observed :

“It is true that the Supreme Court has very often referred to accounting practice for ascertainment of profit made by a company or value of the assets of a company. But when the question is whether a receipt of money is taxable or not or whether certain deductions from the receipt are permissible in law or not, the question has to be decided according to the principles of law and not in accordance with accountancy practice. Accounting practice cannot override section 56 or any other provision of the Act.”

Since the facts admitted are that the land held by the assessee was held as stock-in-trade till it was introduced in the partnership firm and since the said transaction as also the firm so constituted are found to be genuine, by introduction of such stock-in-trade no income accrues to the assessee as chargeable under the head ‘Profits and Gains of Business or Profession’.

42.5 The reason given in the draft order for holding that surplus is chargeable to tax as business income is because of:

1. The amount is credited in the profit and loss account of the assessee.
2. The decision of Hon’ble Supreme Court in the case of McDowell and Co. Ltd. 154 ITR 148 applies.
3. The assessee has withdrawn substantial sum from the firm in subsequent years.

42.5.1 As discussed earlier the entries in the books of accounts are not the determinative factor for computation of income under the Income Tax Act. For this proposition, further reliance is placed on following decisions:

- i. Kedarnath Jute Mfg. Co. Ltd. V. Commissioner of Income Tax [1971]82 ITR 363 (SC).
- ii. Sutlej Cotton Mills Ltd. Vs. CIT (1979) 116 ITR 1 (SC).
- iii. United Commercial Bank Vs. Commissioner of Income tax [1999] 240 ITR 355 (SC).
- iv. Karnataka Small Scale Industries Development Corpn. Ltd. Vs. Commissioner of Income Tax [2003] 258 ITR 770 (SC).

42.5.2 As regards applicability of decision of Hon'ble Supreme court in the case of McDowell and Co. (Supra), the facts in the said case are entirely different than the facts of the present case. In the said case the transaction was found as a colourable device, whereas in the present case the transaction is not found to be a colourable device. The assessee is genuine; the land was held by it as stock-in-trade and is also found to be genuine. The firm constituted wherein the land was brought in as capital contribution is also found to be genuine. Therefore, there is no reason to hold that merely because higher amount was recorded in the capital account of the assessee partner, the transaction becomes a colourable device. On the

contrary value of the land as agreed by the partners on the basis of valuation report at the time of formation of the firm was 11.5 crores. Therefore when identical amount is credited to the account of assessee as partner in the books of account of firm, such transaction cannot be branded as colourable device so as to bring the surplus as chargeable to tax as business income. Therefore the ratio laid down by Hon'ble Supreme Court in the Case of McDowell & Co. cannot be applied. Hon'ble Supreme Court itself in its later decisions in the case of CWT Vs. Arvind Narottam (173 ITR 479) held :

"9. It is vehemently urged by Dr. Gauri Shanker that the approach to be adopted in this case is not that which finds favour under the income-tax law, and different considerations prevail under the Act. As I am proceeding on the basis of the true construction of the deeds of settlement, I fail to see any substance in that contention. Reliance was also placed by the learned counsel for the revenue on McDowell & Co. Ltd. Vs CTO [1985] 154 ITR 148 (SC). That decision cannot advance the case of the revenue because the language of the deeds of settlement is plain and admits of no ambiguity."

Justice Mukherjee agreeing with the judgment of Hon'ble Chief Justice further observed :

"2. Dr. V. Gauri Shanker appearing on behalf of the revenue made an appeal before us stating that we should really construe the three trust deeds together and see 'the game of the hidden purpose' behind these trust deeds which were in fact, for the sole and exclusive benefit of the assessee. He drew our attention to the observations of Justice Chinnappa Reddy, with which other learned Judges of the Full Bench agreed in McDowell & Co. Ltd.'s case (supra). He invited us that having

regard to the taxing statute the tax avoidance device should be exposed. Justice Chinnappa Reddy has noticed the change in judicial attitude to the tax avoidance devices. Justice Reddy mentioned that in the country of its birth the principles of Westminster of condoning tax avoidance have been given a decent burial. In that very country, the phrase 'tax avoidance' is no longer condoned or looked upon with sympathy.

3. It is true that tax avoidance in any under-developed developing economy should not be encouraged on practical as well as ideological grounds. One would wish, as noted by Reddy, J. that one could get the enthusiasm of Justice Holmes that taxes are the price of civilization and one would like to pay that price to buy civilization. But the question which many ordinary taxpayers very often in a country of shortages with ostentuous consumption and deprivation for the large masses ask is, does he with taxes buy civilization or does he facilitate the wastes and ostentuousness of the few. Unless wastes and ostentuousness in the government's spending are avoided or eschewed, no amount of moral sermons would change people attitude to tax avoidance.

4. In any event, however, where the true effect on the construction of the deed is clear, as in this case, the appeal to discourage tax avoidance is not a relevant consideration. But since it was made it has to be noted and rejected. With these observations I agree"

The observation of Hon'ble Supreme Court in McDowell & Co. Limited (Supra) has been further watered down by Hon'ble Supreme Court itself in its later decisions in the case of

Union of India Vs. Azadi Bachao Andolan (263 ITR 706), [2003] 132 TAXMAN 373 (SC) wherein the rule in McDowell case (Supra) has been explained in following words :

“Far from being exorcised in its country of origin, IRC Vs. Duke of Westminster [1936] AC 1 continues to be alive and kicking in England. Interestingly, even in McDowell, though Chinnappa Reddy, J., dismissed the observations of J.C. Shah, J. in CIT Vs. A. Raman & Co. [1968] 67 ITR 11 (SC) based on Duke of Westminster’s case (supra) and IRC Vs. Fisher’s Executors [1926] AC 95, it does not appear that the rest of the Judges of the Constitutional Bench contributed to this radical thinking. [Para 130].

The basic assumption made in the judgment of Chinnappa Reddy, J. in McDowell & Co. Ltd.’s case (supra) that the principle in Duke of Westminster’s case (supra) has ben departed from subsequently by the House of Lords in England, is not correct. [Para 131].

One cannot agree with the view that Duke of Westminster’s case (supra) is dead, or that its ghost has been exorcised in England. The House of Lords does not seem to think so, the principle in Duke of Westminster’s case (supra) is very much alive and kicking in he country of its birth. And as far as India concerned, the observations of Shah, J., in A Raman & Co. (supra) are very much relevant even today. [Para 132].

One may usefully refer to the judgment of the Madras High Court in M.V. Valliappan Vs. CIT [1988] 170 ITR 238/37 Taxman 46 which has rightly read as laying down that every attempt at tax planning is illegitimate and must be ignored, or that every transaction or arrangement which is perfectly permissible under law, which has the effect of reducing the tax burden of the assessee must be looked upon with disfavour. Though the Madras High Court had occasion to refer

to the judgment of the Privy Council in IRC Vs. Challenge Corpn. Ltd. [1987] 2 WLR 24, and did not have the benefit of the House of Lords's pronouncement in Craven Vs. White [1988] 3 All ER 495, the view taken by the Madras High Court appears to be correct [Para 132].

Not only is the principle in Duke of Westminster's case (supra) alive and kicking in England, but it also seems to have acquired judicial benediction of the Constitutional Bench in India, notwithstanding the temporary turbulence created in the wake of McDowell & Co. Ltd.'s case (supra). [Para 135].

In Waman Rao Vs. Union of India [1981] 2 SCC 362 and Minerva Mills Ltd. Vs. Union of India [1980] 3 SCC 625 the Court considered the import of the word 'device' with reference to Article 31B which provides that the Acts and Regulations specified in Ninth Schedule shall not be deemed to be void or even to have become void on the ground that they are inconsistent with the Fundamental rights. The use of the word 'device' was not pejorative, but to describe a provision of law intended to produce a certain legal result. [Para 143].

If the Court finds that notwithstanding a series of legal steps taken by an assessee, the intended legal result has not been achieved, the Court might be justified in overlooking the intermediate steps, but it would not be permissible for the Court to treat the intervening legal steps as non est based upon some hypothetical assessment of the 'real motive' of the assessee. The court must deal with what is tangible in an objective manner and cannot afford to chase a will-o'-the-wisp.

The judgment of the Privy Council in Bank of Chettinad Ltd. Vs. CIT [1940] 8 ITR 522 (PC), wholeheartedly approving the dicta in the passage from the opinion of Lord Russel in Duke of Westminster's case (supra), was the law in India when the Constitution came into force. This was the law in force then, which continued by

reason of Article 372. Unless abrogated by an Act of Parliament, or by a clear pronouncement of the court, this legal principle would continue to hold good. Having anxiously scanned McDowell & Co. Ltd.'s case (supra), one finds no reference therein to having dissented from or overruled the decision of the Privy Council in Bank of Chettinad's case (supra). If any, the principle appears to have been reiterated with approval by the Constitutional Bench of the court in Mathuram Agrawal Vs. State of Madhya Pradesh [1999] 8 SCC 667. Thus, one cannot accept the contention of the respondents that there has been a very drastic change in the fiscal jurisprudence, in India, as would entail a departure. From Duke of Westminster's case (supra) to Bank of Chettinad's case (supra) to Mathuram Agrawal's case (supra), despite the hiccups of McDowell, the law has remained the same [Para 145].

One could not accept the submission that an act which is otherwise valid in law can be treated as non est merely on the basis of some underlying motive supposedly resulting in some economic detriment or prejudice to the national interests, as perceived by the respondents. [Para 146].

Therefore, the surplus cannot be brought to tax as business income applying the ratio laid down in the case of McDowell & Co. (Supra).

42.5.3 Another reason ascribed is that the assessee has withdrawn huge sum from the firm in subsequent years and the figures are noted in Para 16.21 of the draft order. From the figures as noted itself, it is clear that till 31/03/1996 the assessee has withdrawn only so much of the sum as is even less than the cost of land introduced as its capital contribution. Substantial

sum is withdrawn only during financial year relevant to assessment year 1997-1998. How the amount withdrawn five years after the introduction of capital will determine the nature of transaction as a colourable device in the year when such land was contributed as capital contribution in the firm. What is to be taxed is the income accruing or arising during the year and the transaction cannot be viewed at that point of time on the basis of likely effect five years after the transaction has been effected. Therefore in my humble opinion the withdrawal by the assessee from the firm during the financial year relevant to assessment 1997-1998 will not determine the nature of transaction on 23/03/1992 when the land was contributed as capital contribution in the firm in which the assessee became partner.

42.5.4 The 'word of caution' as given by Hon'ble Supreme Court in the case of Sunil Siddharthbhai (supra) which has been heavily relied upon in the draft order is in the words of Hon'ble Supreme Court itself in following context as observed in page 523 of the report as extracted herein –

“We have decided these appeals on the assumption that the partnership firm in question is a genuine firm and not the result of a sham or unreal transaction and that the transfer by the partner of his personal asset to partnership firm represents a genuine intention to contribute to the share capital of the firm for the purpose of carrying on the partnership business.”

In the present case, the fact, as also the draft order reveal that the firm is genuine and even the transfer by the partner of his asset to the partnership firm is a genuine intention to contribute to the capital of the firm for the purpose of carrying on the partnership business. It is not a case that the land was not contributed in the firm for the intended purpose but merely to walk away with the fund introduced by other partners. On the contrary the land has been developed by the firm by constructing building thereon and also subsequent sale thereof. Therefore, neither the firm is ingenuine nor the transaction of contributing to the capital of the firm is an ingenuine intention. The assessee holding the land can either develop it itself or the land can be developed by the firm in which the assessee is a partner. In both the cases the intended purpose of developing the land by the assessee is carried on and cannot be viewed with suspicion or to hold it as a colourable device.

42.6 After the decision of Hon'ble Supreme Court in the case of Sunil Siddharthbhai (supra) the law as regards charging of capital gain has been amended by introduction of section 45 (3) of the Act. Even the definition of word "transfer" in section 2(47) of the Act is substituted w.e.f. 01/04/1985 but the definition is only in relation to a 'capital asset' and not for 'stock-in-trade'. The definition of 'capital asset' itself excludes the 'stock-in-trade'. In absence of any

specific provision in the Income Tax Act to tax such nature of transaction within the ambit of taxation, the tax cannot be imposed merely on the ground of morality. If the charge fails, no words of morality or equity can bring to tax a transaction, as held in the following cases :

- i. Commissioner of Income Tax Vs. Keshavlal Lallubhai Patel [1965]55 ITR 637 (SC).
- ii. Smt. Mohini Thapar Vs. commissioner of Income Tax [1972] 83 ITR 208 (SC).
- iii. Commissioner of Income Tax Vs. C.P. Sarathy Mudaliar [1972] 83 ITR 170 (SC).

I therefore hold that the above nature of transaction cannot be considered as chargeable to tax under the head 'Profits and Gains of Business or Profession'.

43. In the draft order it is also held that what was transferred was a capital asset and hence in view of section 45(3) of the Act the surplus is also taxable under the head 'capital gains'. In para 16.39 it has been concluded as under :

"In other words, whatever may be the character of the property in the partner's hand before the same is brought in by the partner as capital contribution when a partnership is formed and he becomes a partner, the property brought in partakes the character of a capital asset,"

Similarly in para 16.40 it has been concluded that -

“In the present case, when the assessee withdraws some plot of land being part of stock-in-trade for making contribution to a partnership firm as its capital at the time when he became a partner, there is a conversion on withdrawal of stock-in-trade into capital asset in as much as, as already discussed above, the act of contributing personal asset into a partnership firm as its capital when assessee becomes a partner in a firm is a transaction on capital field.”

In view of the above finding in the draft order the surplus is treated as capital gain and brought to tax under section 45(3) of the Act.

I am unable to concur with the above finding for the reasons stated below:

- 43.1 What was transferred was whether a capital asset or stock-in-trade was never the subject matter of dispute before the authorities below. On the contrary the concurrent finding by the assessing officer and by CIT(A) is that what was introduced by the partner was its stock-in-trade and was charged to tax only under the head ‘Profits and Gains of Business or Profession’. Even in the draft order it has been accepted that the land was held by the assessee as its stock-in-trade immediately before it was introduced as its capital contribution

in the firm of which it became the partner. It is never demonstrated or claimed by the assessee that such land was ever converted from stock-in-trade to capital asset. When the assessee held the land as stock-in-trade, he could deal with such land either himself alone or in partnership with other partners. The partnership is not a distinct legal entity from the partners constituting it. The assessee chose to deal with the land in partnership. In such a situation the assessee continues to deal with such land as its stock-in-trade only. A partner may contribute his part of capital in any form and bringing different nature of assets whether stock-in-trade or capital asset. But in absence of any specific action on the part of assessee to convert such land from stock-in-trade to capital asset, the tribunal is not competent to change such nature when it was never an issue before it.

43.2 The draft order while holding that it has widest power u/s 254(1) so as to “pass such orders thereon as it thinks fit” fail to notice that the powers are limited by the words ‘thereon’ contained in section 254(1) of the Act itself.

Appeal on the issues involved has been filed by the assessee only. There is no cross appeal or cross objections by the department. So department’s role is only to defend the orders of AO or for that matter CIT(A).

The issue to be decided by the ITAT should arise from the orders of the authorities below. The assessee cannot be put into any adverse situation at this stage of the appeal as is a settled law on this matter.

Various authorities while dealing with the powers of ITAT, in an appeal before it, has held as under: -

Hon'ble Bombay High Court in the case of The Motor union Insurance Co. Ltd. Vs. CIT (13 ITR 272), has held as under : -

“The word “thereon” used in Section 33(4) of the Indian Income Tax Act only means “on the appeal” which must mean on the grounds raised in the appeal. The sub section only gives power to the Appellate Tribunal to give its decision and pass orders in respect of all grounds urged on behalf of the appellant in respect of the decision appealed against. In deciding those grounds it can pass appropriate orders. But it is not open to the Tribunal itself to raise a ground or permit the party, who has not appealed to raise a ground, which will work adversely to the appellant. The words of the section are not wide enough to include a power to enhancement, without an appeal by the Commissioner.

Rule 21 of the Appellant Tribunal Rules, in terms, limits the appellant to the grounds urged in his memorandum of appeal and prescribes that if he wishes to raise any further ground, he has to do so after obtaining the leave of the Tribunal. The provision only says that the Tribunal is not obliged to rest its decision on the grounds urged by the appellant and does not enlarge the powers of the Tribunal to raise grounds of appeal against the appellant. It recognizes the principle that the judgment of the lower court may be supported on any grounds, even though it is not raised in the memorandum of appeal. That, however, does not allow the Tribunal to suggest another mode of assessment altogether.”

(emphasis supplied)

Hon’ble Bombay High Court in Indira Balakrishna, Manager of “Estate of Balakrishna Purshottom Purani Vs. CIT (30 ITR 320), has held as under:-

“Held further, that in giving findings and expressing opinions the Tribunal must confine itself to the questions that really arise in the appeal before it, and should not travel outside the ambit of its jurisdiction and express opinions prejudicial to the assessee on matters which do not really arise for decision in the appeal before it, which may help the Department in taking proceedings against the assessee e.g. under section 34 of the Act”.

Hon’ble Bombay High Court in the case of Pokhraj Hirachand Vs. CIT (49 ITR 293), has held as under :-

“Though the powers of the Tribunal in dealing with an appeal under section 33 are very wide, they are not absolute.

The expression “thereon” occurring in sub-section (4) of section 33 means the “subject-matter of the appeal” So section 33(4) gives power to the Tribunal to consider only the subject-matter of the appeal. The subject-matter of the appeal before the Tribunal is the grounds of appeal raised by the appellant in his memorandum of appeal, the grounds which the Tribunal allows him to raise and the contentions raised by the respondent before the Tribunal in support of the order made by the Appellate Assistant Commissioner by challenging the adverse finding against him.

(emphasis supplied)

Hon’ble Supreme Court in the case of Estate of Kerala Vs. Vijaya Stores (116 ITR 15),, has held as under : -

“Apart from statute, it is elementary that if a party appeals, he is the party who comes before the Appellate Tribunal to redress a grievance alleged by him. If the other side has any grievance, he has a right to file a cross-appeal or cross-objections. But, if no such thing is done, the other party, in law, is deemed to be satisfied with the decision. He is, of course, entitled to support the judgment of the first officer on any ground open to him, but he is not entitled to raise a ground so as to work adversely to the appellant and in his favour.”

Hon'ble Mysore High Court in the case of Pathikonda Balasubba Setty (Deceased) Vs. CIT (65 ITR 252) held :

“The effect of provision of section 33(4) of Act 1922 and section 254(1) of the 1961 the Appellate Tribunal's powers were limited to passing such orders as they may think fit on the appeal. The expression on 'on the appeal' clearly and indubitably points to the conclusion that the powers of the appellate authority, the Tribunal, are limited to the subject-matter of the appeal.

This necessarily so because every point dealt with by the lower appellate court, the AAC, need not be the subject of attack before the Tribunal. The interests of the revenue are sufficiently protected by the extensive powers given to the first appellate authority, the AAC. At that stage, the only appellant would be the assessee, not the department, although it is entitled to be represented by an officer of the department in support of the order of the original court. A mistake, if any, committed by the original authority, which is adverse to the interests of the assessee, will be canvassed by the assessee before the AAC. A mistake, if any, committed by the original assessing authority which is detrimental to the interests of the revenue is capable of being corrected by the AAC even without an appeal having been presented by the department. At the next stage of second appeal to the Tribunal, the liberty is given to both the sides to go up in appeal to the Tribunal and when the Tribunal comes to deal with the matter, the law regards it sufficient to leave it to the parties going up as appellants before the Tribunal to limit their attack on the order of the first appellate authority and to seek the intervention of the Tribunal only to the extent necessary to correct the errors in the order of the AAC according to the case of the appellant.

It should be noted that in comparison to the sections describing the power of the AAC, the sections which describe the appellate powers of the Tribunal do not make any reference to a power to enhance the assessment or to enhance the tax in the same way as the AAC is empowered to do while dealing with an appeal against the order of the assessing authority.

As the appellate power is a power which is conferred by statute, both its existence as well as its extent has to be gathered from the relevant statutory provision. The fundamental idea is that an appellant seeks a relief from an appellate court, and not detriment to himself. Even under the general provisions of the law of procedure, the worst detriment which an appellate court may visit on an appellant is to dismiss the appeal with a direction in an appropriate case to pay costs to the opposite side. An order adverse to the interests of the appellant – adverse in the sense that it takes away from him a benefit which he has already acquired under the order appealed from – is possible only by means of an order made either upon a cross-appeal filed by the other side or on the basis of a memorandum of cross-objections presented by him wherever the law permits him to do so.”

In light of the above, I am of the opinion that the Tribunal cannot go into the question whether the asset introduced in the firm as capital contribution was a capital asset or not.

43.3 In the draft order it has been held that the land held as stock-in-trade before the same was contributed to a firm as capital has been converted into a capital asset at the time when the same was contributed as a capital contribution to a firm in which the assessee became a

partner. There is no basis to hold that the nature of asset changed its colour from 'stock-in-trade' to 'capital asset'. The admitted position by authorities below as also in the draft order is that the land held by the assessee was stock-in-trade immediately before it was introduced as capital contribution. If that be so there is no change in the circumstances or any factors affecting the holding of land. In such circumstances, on introduction of such land as capital contribution do not change its character from stock-in-trade to capital asset. Just as the assessee can hold the land as stock-in-trade and deal with the same either individually, he continues to hold as stock-in-trade in the capacity as partner of the firm. In both the cases the person holding the land can be said to deal with such land only in capacity of trader and not in the form of capital asset. The admitted fact is also that the firm was also treating the land as its stock-in-trade and after the land was developed and sold with building thereon, the profit was also assessed as business income in the hand of firm. Therefore if it is held that the land held by assessee as stock-in-trade before the same was contributed to a firm has been converted into a capital asset, on introduction of same as capital contribution by partner there will be conversion of such land at two point of time i.e. firstly at the time when assessee introduced as capital contribution when the asset gets converted into capital assets and secondly when the firm receives the land and at that point of time is reconverted into stock in trade. In absence of any material to hold that that land was at all converted firstly

into capital asset and reconverted into stock in trade, the finding given in the draft order is contrary to the facts on record.

44. The Tribunal while deciding the question as to whether it has power to change the head of income, the draft order holds that the Tribunal has such power under section 254(1) and for this purpose reliance is placed on the decision of special bench of Tribunal in the case of Sumit Bhattacharya which in turn has relied upon the decision of Hon'ble Bombay High Court in the case of CIT Vs. Gilbert and Barker Mfg. Company 111 ITR 529. The issue before the special bench was whether the amount received by assessee on realization of 'stock appreciation rights' which was *per se* income but whether chargeable under the head "salaries". There was no dispute as to the nature of receipt which was in the form of income. In such a situation having found that when the amount received was income *per se*, the Tribunal within its power u/s 254(1) may bring it to tax under any head of income. However in the present case it is not an issue regarding change of head of income but issue is regarding whether there was transfer of stock in trade or capital asset i.e. nature of asset.

- 44.1 With regard to the rights of the Defendant in appeal before the Tribunal and the scope of Powers of the Tribunal, I may refer to the recent decision of the Hon'ble Special Bench,

Mumbai in the case of Mahindra & Mahindra Ltd. Vs. DCIT, as reported in (2009) 122 TTJ 577.

In that case also, the Departmental Representative wanted to set up a totally new case on facts, which required a different finding of fact from what the AO and the CIT(A) has found.

The Tribunal in para 19.6 at page 635 of the said judgment has held as under : -

“After considering the rival submissions and perusing the relevant material on record we find that the AO has undoubtedly examined the provisions of DTAA between India and UK for deciding the taxability or otherwise of the sums paid to the non-resident. The assessee vide its letter dated 6th Feb, 199, reproduced on p. 9 onwards of the assessment order, categorically stated in para 5.3 that the DTAA between India and UK was applicable. The AO has also not disputed this fact. He has referred to various articles of DTAA between India and UK at several places of his order viz. paras 49, 50, 52 and 55 etc. At no stage it has been denied by the AO that DTAA between India and UK was not applicable. In such a situation it is impermissible for the learned Departmental Representative to come out with a submission contrary to the finding of the AO that DTAA with UK was not relevant as both the lead managers were resident of countries other than UK. In view of the admission of the AO and the further elaboration of the point in the light of DTAA between India and UK, we cannot permit the learned Authorised Representative to take contrary stand from the one taken by the AO. In our considered opinion the learned Departmental Representative has no jurisdiction to go beyond the order passed by the AO or CIT(A). His scope of arguments is confined to supporting or defending the impugned order. He cannot set up an altogether different case. If the learned Departmental Representative is allowed to take up a new contention de hors the view taken by the AO hat would mean the learned Authorised Representative (sic-Departmental Representative) stepping into the shoes of the CIT exercising jurisdiction under s. 263. We, therefore, do not permit the learned Departmental Representative to transgress the boundaries of his arguments. Similar view has been taken by the Jodhpur

Bench of the Tribunal in the case of Kawal Pro Exports Vs. Asst. CIT (2007) 109 TTJ (Jd) 869 : (2008) 110 ITD 59 (Jd). This contention is therefore repelled as devoid of any permit.

44.2 I also find that almost similar issue arose before Hon'ble Supreme Court in the case of CIT Vs. Ram Kumar Aggarwal and Bros. 205 ITR 251 (SC). In the said case the facts as noted by the Hon'ble Supreme Court in para 2 and 3 as under –

“2. The assessee is a partnership firm. The accounting year relevant to asst. yr. 1956-57 was the year ending on 31st Dec, 1995. The ITO made an assessment on a total income of Rs. 36,41,544 which included a sum of Rs. 32,25,550 representing the surplus which he assessee received during the previous year from the liquidator of Chrestian Mica Co. Ltd. Which went into voluntary liquidation in the year 1955. The assessee preferred an appeal to the AAC objecting to the inclusion of the said surplus amount. The appeal was dismissed. But on further appeal, the Tribunal agreed with its contention.

3. The assessee was a regular dealer in shares. In the year 1945, it purchased all the equity shares of “Chrestian Mica Co. Ltd. Which was hen a public limited company. The assessee took over its management. In 1947, the company was converted into a private limited company. For the asst. yr. 1949-50, the assessee claimed a trading loss of Rs. 20,88,735 stated to be the loss suffered on account of depreciation o the value of the shares of the said company. This claim was made on the basis that all the shares of the company were held by it as stock-in-trade. It's claim was allowed by the Tribunal on appeal. In all the subsequent

assessments, the said shares were created as its stock-in-trade and value of those shares as claimed by the assessee was adopted.

In the assessment proceedings relating to the assessment year concerned herein (1956-57), the assessee admitted that the shares of the said company were held by it as stock-in-trade. On that basis, the said surplus amount received by it from the liquidator was included in its total income by the ITO and the AAC. On appeal, however, there was a difference of opinion between the Judicial Member and the Accountant Member whereupon the matter was referred to the Vice-President. He upheld the assessee's plea. Then followed the reference to the High Court."

The High Court answered the question in favour of assessee. At the instance of revenue further appeal was filed before Hon'ble Supreme Court and following questions were referred for the opinion of the Hon'ble Supreme Court.

"(1) Whether, on the facts and in the circumstances of the case, the Tribunal was justified in investigating the nature of the shares held by the assessee in Chrestian Mica Co. Ltd. When both the assessee and the IT authorities had treated them as the stock-in-trade of the assessee as a dealer in share for every assessment year since 1949-50 and proceeded on the same basis for the instant assessment year?

(2) Whether, on the facts and in the circumstances of the case, the Tribunal was justified in law in holding that the shares held by assessee in Chrestian Mica co. Ltd. Were not its stock-in-trade for dealing in shares?

(3) If the answer to question (2) be in the negative then whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the sum of Rupees thirty two lacs twenty five thousand and five hundred and fifty was not assessable in the hands of the Assessee?"

Hon'ble Supreme Court held as under : -

"6. Whether shares of a company held by a person constitute his capital or his stock-in-trade, is not a pure question of law but essentially one of fact. While one person may hold the shares of a company by way of investment, the other may hold them as his stock-in-trade. In this case, it is clear beyond any doubt that the assessee has been holding the shares of the aforesaid company as is stock-in-trade. In the earlier years, it claimed a trading loss on the footing that they represented its stock-in-trade. Even in the present assessment proceedings for the asst.yr. 1956-57 (concerned herein), it took the very same stand though at the stage of Tribunal and High Court, it sought to wriggle out of the said admission unsuccessfully. The High Court has held rightly that it cannot do so and that it is bound by its admission and its course of conduct over the past several years. The High Court, it may be recalled, has also rejected its further submission that the said shares ceased to be its stock-in-trade on the conversion of the company from a public limited company to a private limited company. If so, it follows that if the assessee receives any surplus amount in lieu of the said shares, it must be held to be a revenue receipt in his hands. It cannot be denied that the amount received by the assessee from the liquidator in this case was in lieu of its shareholding. In effect and in truth, the amount received by it represented the recompense for its shares, even though it is true there was no transfer of shares from the assessee to the liquidator or to any one else. It was a case of return for the money paid by the assessee for acquiring the said shares. In one case, the return may be more than what the holder paid for them while in another it may be less; the character of the receipt remains the same. The High Court has however held in favour of the

assessee opining that (i) whatever is received by the shareholder on a liquidation of a company is “no income of the property but the property itself”; (ii) that whatever is distributed in a liquidation is capital, whatever may have been its source, as held in Brogan Vs. Stafford Coal and Iron Co. Ltd. 41 Tax Cases 305; (iii) in the course of liquidation of the company the liquidator sells company is liquidated and the liquidator distributes the surplus assets, there is no transaction in the trading sense between the liquidator and the shareholders. By virtue of his holding, a shareholder is entitled to surplus assets on the liquidation of the company and such surplus assets are in the nature of an accretion to the shares held by him.

The question is whether the opinion of the High Court is correct in law? We find it difficult to say so. Sec. 511 of the Companies Act applies to every voluntary winding up. It says hat “subject to the provisions of this Act as to preferential payments, the assets of a company shall, on its winding up, be applied in satisfaction of its liabilities pari passu and, subject to such application, shall unless the articles otherwise provide, be distributed among the members according to their rights and interests in the company”. The concluding words of this section indicate that the assets of a company, on its liquidation, shall be distributed among the shareholders according to their rights and interests in the company which necessarily means according to their shareholding. What each shareholder gets is proportionate to his shareholding in the company. Once the distribution takes place, he shares and the shareholding come to an end. The fact that the shares may technically continue until the name of the company is struck off the register of the company is of little significance. After the distribution of the assets, nothing remains of the shares. To say that the assets a shareholder receives on the liquidation of the company are unrelated to his shareholding is to be blind to the reality. Such an argument ignores the basic reality recognized by s. 511 of the Companies Act. The same comment holds good about the argument that the amount received is an accretion to the shares. It is true that a liquidator does not sell the shares. It is equally true that there is no transfer of shares by the shareholder to the liquidator or to any other person. That is not really necessary.

So long as money is received in lieu of shares, there is a receipt and where an assessee is a dealer in shares, any surplus amount received by him constitutes his income. As stated above, where a company goes into liquidation and the liquidator distributes the assets of the company among the shareholders, what each shareholder gets is in lieu of his shareholding. That is the worth, the value and the price of his shareholding. A shareholder participates in the distribution of the assets of a company on its liquidation by virtue of and because of his shareholding. We therefore, find it difficult to agree with the High Court that a shareholder participates in the distribution of assets on the liquidation of the company de hors his shareholding. Once this is so, it follows that the money received by the assessee in lieu of its shareholding partakes the same character in which he held the shares. If he held the shares as stock-in-trade, the money received by it represents his income, i.e. a revenue receipt in its hands. If it held them by way of investment, the money it receives represents a capital receipt by it."

(emphasis supplied)

In the concluding paragraph Hon'ble Supreme Court set aside the judgment of the High Court and answered all the three questions referred in the negative i.e. in favour of revenue and against the assessee.

44.3 What follows from the above decision of Hon'ble Supreme Court is that when both the assessee and the Income Tax Authorities had treated the nature of shares held by assessee as stock-in-trade and proceeded on the same basis for the relevant assessment year, the Tribunal was not justified in investigating the nature of the shares held by the assessee so as

to hold the same as not part of stock-in-trade. Thus it was concluded that the admitted position of the nature of asset between the assessee and the revenue authorities cannot be allowed to be changed by the Tribunal in view of the plea raised before it. Applying the same principle in the present case also since there is no dispute between the assessee and the revenue regarding nature of asset being stock-in-trade, the Tribunal is not called upon to give a finding as to whether such asset was at all converted to capital asset and whether such land is part of capital asset or not.

44.4 There is a difference between changing the head of income in respect of receipt which are income *per se* and changing the nature of asset itself. While the receipt which is income *per se* may be brought to tax under a different head, the Tribunal will exceed its jurisdiction if it decides the nature of asset itself in a dispute raised for the first time at the instance of respondent. The Counsel for the respondent represents the assessing officer and hence his role is confined to the dispute before the assessing officer and the Counsel for the respondent cannot for the first time raise a fresh issue before the Tribunal which is not a subject matter of dispute.

Section 254(1) of the Income Tax Act reads as under:-

“S.254(1) The Appellate Tribunal may, after giving both the parties to the appeal, an opportunity of being heard, pass such orders thereon as it thinks fit.”

The powers of the Income Tax Appellate Tribunal are in the widest terms. The only restriction on the powers of the Hon'ble Tribunal is contained in the word “thereon”. The word ‘thereon’ has been interpreted to mean the subject matter of the controversy before the Tribunal. (Ref: Hukam Chand Mills Ltd. Vs. CIT 63 ITR 232 at pages 236-237). The appellate Tribunal can deal with only that part of the order of the first appellate authority which has been made the subject matter of attack in the appeal before it.

It is not open to the Tribunal to adjudicate or give a finding on a question which is not in dispute and which does not form the subject matter of the appeal before it as held in Indira Balakrishna v. CIT, (1956) 30 ITR 320, 327 (Bom), affirmed, CIT v. Indira Balakrishna, (1960) 39 ITR 546 (SC); M.R.M. Periannan Chettiar v. CIT (1960) 39 ITR 159 (Mad.); V. Ramaswamy Iyengar v. CIT, (1960) 40 ITR 377 (Mad.) Pokhraj Hirachand v. CIT, (1963) 49 ITR 293 (Bom); J.B. Greaves v. CIT, (1963) 49 ITR 107 (Bom.), Pathikonda Balasubba Setty v. CIT, (1967) 65 ITR 252 (Mys); P.R. Mukherjee v. CIT. (1979) 116 ITR 554(Cal). On the same reasoning, where

the controversies is precisely limited to a narrower compass, the Tribunal is not competent to so widen it as to traverse beyond the subject matter which was to dispute before the Income Tax authorities (R.L. Rajgharia v ITO, (1977) 107 ITR 347 (Cal), affirmed in ITO v R.L. Rajgharia (1979) 119 ITR 872 (Cal.).

The Tribunal can decide only issues which were the subject matter of the appeal before the first appellate authority. An additional plea which altogether changes the complexion of the case as originally brought before the first appellate authority and the Tribunal in second appeal cannot be permitted to be raised at the stage of hearing of the Tribunal appeal as held in Indian Steel & Wire Products Ltd. v. CIT, 208 ITR 740, 743 (Cal).

The Supreme Court in the case of Malik & Sons 74 ITR at pages 1 and 5 held as under:-

“The undertaking must therefore be ignored. Under section 33 (4) of the Indian Income Tax Act, 1922, the Income-tax Appellate Tribunal may, after giving both parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit. The power conferred by that sub-section is wide, but it is still a judicial power which must be exercised in respect of matters that arise in the appeal and according to law. The Tribunal in deciding an appeal before it must deal with questions of law and fact which arise out of the order of assessment made by the Income-tax Officer and the order of the Appellate Assistant Commissioner. It

cannot assume powers which are inconsistent with the express provisions of the Act or its scheme”.

It can, therefore, be concluded that the Income Tax Appellate Tribunal cannot decide an issue which does not arise out of the orders of the appellate authorities below. In this case, both the AO and the CIT (Appeals) have held that the asset contributed by the appellant to the partnership firm was stock-in-trade and the assets continued to be held as stock-in-trade in the partnership firm. There is no difference of opinion between the authorities below on this issue and a finding of fact recorded by both the authorities below is not under challenge in the appeal filed before the Tribunal by the appellant or the Revenue.

I therefore, hold that -

- (a) The nature of asset when contributed by assessee was and continued to remain as stock-in-trade only and was neither intended to be converted as capital asset nor there is any material on record to hold that the asset contributed were capital asset.

- (b) Since there was never a dispute between assessee and revenue authorities regarding nature of asset of land being stock-in-trade, the tribunal cannot go into the question whether the asset contributed was capital asset or not.

45. In the draft order it is proposed that primarily the surplus is chargeable to tax under the head 'capital gains' and also held that in the situation that it is not chargeable as capital gain, it is taxable as business income also. This is so opined in sub para (xii) of para 16.49 wherein the conclusion is arrived at. The Tribunal is a final authority on the finding of facts. The Tribunal is not an Assessing Authority but an Appellate Authority. Therefore, the Tribunal is required to give a finding of facts finally and not to give an alternative finding. This will be against the basic law giving power to the Tribunal to decide as final fact finding authority. In the draft order before deciding regarding head of income, in the concluding portion of para 16.47 of the draft order it has been held :

"This question whether the land in question was a capital asset or stock in trade in nature at the time when the same was contributed by the assessee to a partnership firm as its capital contribution when the assessee became a partner in that firm, is not one of fact: though it is dependent on the facts and the circumstances of the present case, the question does involve conclusions of law to be drawn from those facts. We, therefore, do not find any force or merit in the contention of the learned counsel for the assessee that the fact admitted by the revenue authorities below are now being changed."

The aforesaid finding is contrary to the ruling of Hon'ble Supreme Court in the case of CIT Vs Ram Kumar Aggarwal & Bros. 205 ITR 251 wherein at para 6 of the decision it was held :

“Whether shares of a company held by a person constitute his capital or his stock-in-trade, is not a pure question of law but essentially one of fact.”

45.1 I therefore hold that the Tribunal should have restricted itself to the controversy as raised by the Appellant and to give a finding only to the extent whether the surplus realized on introduction of land being held by it as stock-in-trade in the form of its capital contribution was chargeable as business income or not. Since I have earlier held that such introduction do not amount to giving rise to business income as no legal right is accruing in favour of assessee because of the credit to the account of partner by the firm, no income can be brought to tax. The law laid down by Hon'ble Supreme Court in the case of Hind Construction 83 ITR 211 and the decision of Hon'ble Supreme Court in the case of Sunil Siddharthbhai (Supra) are squarely applicable. Since the land was always held as stock in trade, which continued to be stock in trade even at the time of introduction and subsequently by the firm also, section 45(3) which is applicable in respect of the capital asset cannot be applied to the stock-in trade held by the assessee and introduced as capital contribution.

46. The issue which arises in appeal for A.Y. 1992-93 in relation to ground No. 1 also arises in appeals for A.Y. 1997-98, 1998-99, 1999-2000 and 2000-01. The discussion in relation thereto in the draft order is tabulated below : -

Assessment Year	Ground No.	Paragraph No. of Draft Order
1997-98	4	27 to 27.4
1998-99	4	30 to 30.6
1999-2000	2	33 to 33.5
2000-01	3	37 to 37.4

- 46.1 In relation to other grounds in appeals for A.Y. 1997-98, 1998-99, 1999-2000 and 2000-01, I am in complete agreement with the view in the draft order. However, I am unable to agree in relation to issue regarding taxability of surplus arising on introduction of land into partnership firm as capital contribution by the assessee as discussed in table referred above.

47. For all these years it has been held that in view of the finding given in Para 16 of the draft order pertaining to A.Y. 1992-93 is being followed and since I am unable to concur with finding given in Para 16 of the draft order and in respect of which I have proposed a separate

order, my finding for all these years in relation to the above referred issue will be the same. Therefore, in view of my finding given for A.Y. 1992-93, the surplus is not chargeable to tax.

47.1 For A.Y. 1997-98 to 2000-01, there is one more aspect. In relation to A.Y. 1997-98 in Para 27.4 of the Draft Order, reference is made to section 13(c) and 13(d) as also to section 48(b)(ii) and 48(b)(iii) of the Indian Partnership Act, 1932 to hold that the advances by partner is distinct from capital and are placed on better footing than the capital contributed by the partner for the purpose of partner's right to receive interest thereupon and to realize or recover the advance distinguished from capital. Section 13 of the Partnership Act is extracted herein : -

"13. Subject to contract between the partners –

(a) xx xx;

(b) xx xx;

(c) where a partner is entitled to interest on the capital subscribed by him such interest shall be payable only out of profits;

(d) a partner making, for the purposes of the business, any payment or advance beyond the amount of capital he has agreed to subscribe, is entitled to interest thereon at the rate of six percent, per annum;

(e) xx xx;"

47.2 As per section 13(c), subject to the contract between the partners, a partner is entitled to interest on the capital subscribed by him and such interest is payable only out of profits. Similarly as per section 13(d) a partner is also entitled to interest if so agreed on the advance beyond the amount of capital he has agreed to subscribe. However, in both the cases the amount contributed by partner whether by way of capital or by way of advance do not partake the character of debt due by firm to the partner. Section 13 only regulates only relation of the partner inter se. Section starts with the words "subject to the contract between the partners" i.e. if the partners agree amongst themselves, a partner is entitled to interest on the capital as also on the advance beyond the amount of capital. However, in either case, it does not amount to a debt by the firm to the partner and in the event of dissolution the firm is not obliged to pay such sum to the partner. This proposition will be clear on reading section 48 of the Partnership Act as extracted herein :-

"48. In setting the accounts of a firm after dissolution, the following rules shall, subject to agreement by the partners be observed:

- (a) *Losses, including deficiencies of capital, shall be paid first out of profits, next out of capital, and, lastly, if necessary, by the partners individually in the proportions in which they were entitled to share profits.*
- (b) *the assets of the firm, including any sums contributed by the partners to make up deficiencies of capital, shall be applied in the following manner and order:-*
 - (i) *in paying the debts of the firm to third parties;*
 - (ii) *in paying to each partner rateably what is due to him from the firm for advances as distinguished from capital;*
 - (iii) *in paying to each partner rateably what is due to him on account of capital; and*
 - (iv) *the residue, if any, shall be divided among the partners in the proportions in which they were entitled to share profits."*

47.3 Section 48 of the Partnership Act provides for the manner in which the accounts of the partners are to be settled after dissolution. Section 48 sets out priority in order of which the partnership assets are to be distributed. Firstly, it goes to pay the losses. Next it goes to pay the debts to the third parties. Only after the debts are paid to third parties, the priority will be first accorded to the advances given by the partner over and above his share of capital.

Therefore, if there are no assets left after paying of the losses and debts to the third party, a partner will not receive any amount either towards his capital or towards advance given over and above his capital. In either case it is not debt due by the firm to the partner which is like debt due to third parties. Therefore, merely because part of the value of land brought in as capital contribution is treated as loan over and above the capital agreed upon, it will not have an effect of creating a right in favour of assessee at the time of entering into partnership to receive such sum so as to treat the surplus as income accruing in favour of the partner.

47.4 It is also to be noted that in these years there is no finding that any amount was withdrawn by the assessee from the firm even though the accounts of the firm records the capital of the assessee as brought in. On the contrary, the facts remain that after introduction of land held as stock-in-trade as capital contribution, no part of the amount credited to capital account has been withdrawn till date. Therefore, the situation in this year is distinct than the situation prevailing for A.Y. 1992-93 which has been extensively discussed in Para 16.21 of the Draft Order and heavily relied upon to hold that the transaction is a colorable device. Thus even the “Word of Caution” as found in the case of Sunil Siddharthbhai case (supra) are not applicable in all these years which are heavily relied upon to hold the introduction of capital as colorable device and for applying the ratio of McDowell case (supra). This factual situation is absent in relation to appeal for A.Y. 1997-98, 1998-99, 1999-2000 and 2000-01. Therefore

even the finding for 1992-93 given in para 16 of the draft order will not apply in relation to other years as the factual situation differs materially.

In view of above discussion, the surplus is not chargeable to tax for A. Y. 1997-98, 1998-99, 1999-2000 and 2000-01. Accordingly grounds raised in this regard as tabulated above are allowed and are decided in favour of the assessee.

(DEEPAK R. SHAH)

ACCOUNTANT MEMBER

Date: 31st December 2009.