

**IN THE INCOME TAX APPELLATE TRIBUNAL  
CHANDIGARH BENCHES 'A' CHANDIGARH**

**BEFORE SHRI. BHAVNESH SAINI, JUDICIAL MEMBER AND  
SHRI T.R. SOOD, ACCOUNTANT MEMBER**

**ITA No. 1098/Chd/2014**  
Assessment Year: 2011-12

M/s Punjab Urban Planning and  
Development Authority,  
Mohali

Vs.

The Addl. CIT,  
Range VI, Mohali

PAN No. AAALP0045J

(Appellant)

(Respondent)

Appellant By : Ms Richa Gupta  
(for Shri Parikshit Aggarwal)

Respondent By : Shri Manjit Singh

Date of hearing : 09/06/2015

Date of Pronouncement : 16/06/2015

**ORDER**

**PER T.R.SOOD, A.M.**

The appeal by the assessee is directed against the order dated 29.10.2014 passed by CIT(A), Chandigarh.

2. In this appeal the assessee has raised the following ground:-

- 1. That on the facts and in the circumstances of the case and in law, the Worthy CIT(A) through his order dated 29.10.2014 has erred in passing that order in contravention of provisions of Section 250(6) of the Income Tax Act, 1961.*
- 2. That on facts, circumstances and legal position of the case, the Worthy CIT(A) has erred in confirming the action Of Ld. AO wherein he has erred in making an addition of Rs. 2,96,76,773/- on account of installments*

*for sale of houses/flats received during the year. As per the policy of the appellant and in terms of Hire Purchase agreement entered into between the assessee and the allottees of houses/flats, the ownership rights of the said premises remain with the appellant till the completion of the scheme and the allottees only enjoy the tenancy rights till then. The ownership of the premises is transferred to the assessee only on the receipt of the last installments there from. This fact was brought to the notice of the learned assessing officer, but while framing the assessment, the assessing officer has ignored the said facts and has acted in an arbitrary manner to the total disregard of law.*

3. After hearing both the parties we find that during assessment proceedings the Assessing Officer noticed that assessee was accounting for the installments received against sale of allotment of house as capital receipt. Such receipts were Rs. 2,96,76,773/-. After detailed discussion, this amount was added to the income of the assessee.

4. On appeal, the Ld. CIT(A) confirmed the action of the Assessing Officer by following the order of Tribunal in ITA No. 762/Chd/2007.

5. Before us a letter dated 19.05.2015 has been filed by the authorised representative of M/s Rupesh Parikshit & Associates, Chandigarh. In this letter after reproducing the ground No.2 it has been mentioned as under:-

*“The above question in the case of appellant itself has already been adjudicated in ITA No. 762/2007 for assessment year 2003-04 decided on 06.12.2013 by the Hon'ble Bench. At page 56, Para 72 of this order, the Hon'ble Bench laid down as under:-*

*"72. , In these circumstances we set aside the order of the Ld. CIT(A) and direct the AO to include installments received on sale of various houses and flats under hire purchase agreement and at the same time allow corresponding expenditure which has been expended by the assesses in cash (including through*

*cheque). Further in the year of completion of a particular scheme effect has to be given in respect of accumulated installments as well as accumulated expenditure which has not been already considered in a particular year on cash basis as observed earlier. We have observed right in beginning that this issue is involved in all the years before us. Therefore, similar treatment as observed by us should be given in each of the year."*

*For the year in question, while passing the assessment order, Ld. AO made the addition of Rs. 2,96,76,773/- on account of receipt of installments for sale of houses/flats and has also allowed benefit of cost incurred there against on cash basis. Hence, the directions of Hon'ble ITAT in ITA no. 762/2007 (Supra) has already been followed by the Ld. AO and the appellant is not aggrieved to that extent. But the appeal of appellant against order of Hon'ble Bench in ITA No. 762/2007 (Supra) is pending adjudication before the Hon'ble P&H HC.*

*Exactly identical situation was there before the Hon'ble Bench in case of appellant itself in ITA No. 680/CHANDI-2014 for AY 2010-11 decided on 19.02.2015 by the Hon'ble Bench, whereby the appeal of the appellant was dismissed. The present appeal is also having identical facts. It is prayed that this appeal may also be disposed off according to the assessee's own past history. We shall be highly obliged."*

6. On the other hand Ld. DR strongly supported the order of Ld. CIT(A).

7 .After considering the rival submissions we find that this issue was adjudicated in the assessee's own case for assessment year 2003-04 in ITA No. 762/Chd/2007. The issue was adjudicated vide paras 52 to 72 which are as under:-

*"52 Ground No. 5 – After considering the rival submissions we find that during assessment proceedings it was noticed by the Assessing Officer that receipts from sale of houses and flats where complete payments by the purchaser were not made, were being accounted as capital receipt by*

*the assessee. In response to the query it was mainly stated that such houses and flats have been sold on hire purchase basis and as per the "Hire Purchase Agreement" sale is not complete unless all payments have been made by the purchaser. However, the Assessing Officer observed that since the assessee has adopted cash system of accounting of receipts and therefore, the amount of such installments were required to be treated as revenue receipt and should be accounted in "income expenditure statement". The assessee was asked to furnish the details. In response the assessee filed the details and it was again stated that in such cases buyer would not become owner of the property till all the hire purchase installments are paid and till then such houses and flats continued to rest with the seller i.e. assessee authority. Therefore, in legal sense sale can not be said to have completed unless the property passes on to the buyer. However, the Assessing Officer observed that this can not be treated as hire purchase if the allottees were termed as tenant till all the installments are paid by him. He further observed that as per Section 145 of the Act the assessee can compute his income either on mercantile system or cash system of accounting regularly employed by him and the assessee had option either to adopt cash system or mercantile system as long as it is feasible to compute the income through different activities by different methods. Since the assessee had adopted cash system of accounting, therefore, income has to be computed on the basis of installments received during the year minus any amount which has already been accounted for as revenue receipt during the year under consideration. Accordingly from the details it was observed that total installments received during the period 1.4.2002 to 31.3.2003 was Rs. 23,00,77,465/- out of which a sum of Rs. 3,22,06,541/- was already accounted for as revenue during the year and therefore, net amount of Rs. 19,78,70,924/- was added to the income of the assessee.*

*53 On appeal similar contention as have been made before the Assessing Officer, were reiterated. The ld. CIT(A) discussed the issue in detail and found merit in the submissions of the assessee and deleted the addition by holding that since the assessee was following the Project Completion Method, therefore, the income would be shown only on the completion of the scheme.*

*54 Before us, the ld. DR for the revenue submitted that as per Section 4 of the Act income tax is chargeable in respect of total income of each Assessment year and therefore, income received during the year cannot be deferred to future years by adopting the method of accounting which is inconsistent with the method of accounting which the assessee is following regularly. Since the assessee has started following the cash system of accounting during the year and therefore, income received during the year has to be subject to taxation. She also referred to the provisions of section 145 and submitted that though the assessee had the option to adopt the mercantile system or cash system of accounting but the assessee has no right to follow hybrid system of accounting i.e. one method for one particular source of income and another method for other source of income. She further submitted that it was stated by the ld. counsel of the*

*assessee that the assessee was recognizing revenue on the completion of the scheme because assessee was selling houses and flats on hire purchase agreement but it has to be noted that the assessee is in the business of development and selling houses and not in the business of providing finance /credit to various customers. The assessee has basically received installments in construction of flats and houses and was following cash system of accounting and therefore, such installments are to be taxed in the current year. In any case the provision of Hire Purchase Act cannot over ride the provisions of the Act and in this regard she relied on the decision of Hon'ble Supreme Court in case of Southern Technologies Ltd. Vs. JCIT (supra).*

55 *It was further submitted that Hon'ble Punjab & Haryana High Court in case of CIT v Chandigarh Industrial and General Development Corporation Ltd. 319 ITR 85 (PH) has clearly held in the similar circumstances that amount received on account of installments are taxable during the year. Similarly the same view was taken in case of CIT Vs. Fair Deal Traders, 327 ITR 34 by Hon'ble Punjab & Haryana High Court wherein the assessee after purchasing the land divided the same into plots and received installments but the same was held to be taxable because possession of the flats had already been given. She also referred to the decision of Hon'ble Delhi High Court in case of Tirath Ram Ahuja (P) Ltd. Vs. CIT, 103 ITR 15 (Del) where contract was not complete but it was held that it was open to the revenue to estimate the profit on the basis of receipt in each year of consideration even when the contract is not complete. She also relied on the decision of Hon'ble Punjab & Haryana High Court in case of CIT V. Dhir and Co. Colonisers P. Ltd, 288 ITR 561 (PH) wherein it was held that once possession of the plots was transferred then the receipts could not be held to be merely a deposit.*

56 *On the other hand, the ld. counsel of the assessee reiterated the submissions made before the Assessing Officer. It was emphasized that in case of houses and flats the assessee authority was entering into hire purchase agreement. He referred to various provisions of the agreement and submitted that this hire purchase agreement clearly provide that ownership of the property would remain with the authority till last installments is paid. It was further provided in the agreement that status rights of the hirer shall be exclusively that of a tenant and not as owner. It was contended that installments consist of two elements namely interest embedded in such installments and secondly the principle amount. It was submitted that as far as interest is concerned, the same was being accounted for in every year because it was possible to quantify the same even during the year a sum of Rs. 24,76,01,075/- has already been accounted for as interest on installments. On account of installments the assessee has already credited a sum of Rs. 6,71,56,134/-. This is the only the amount which can be recognized on account of revenue. It was further submitted that it was not possible to quantify the profit during the mid of the scheme because even true expenses on account of construction of last house was also carried over as stocks and therefore, the expenditure is not being debited and the profit could not be worked in respect of*

*uncompleted schemes. In fact there was unclaimed expenditure during the year as per following detail:*

<i>Particulars</i>	<i>Balance as on 31.3.2003</i>	<i>Balance as on 1.4.2002</i>
<i>Receipt from allottees pending recognition of revenue due to schemes for incomplete</i>	<i>Rs. 210,66,64,803.65</i>	<i>Rs. 19,08,79876.72</i>
<i>Expenditure pending debit to profit and loss account due to schemes for incomplete</i>	<i>Rs. 233,72,05,032.55</i>	<i>Rs. 226,43,47,998.60</i>
<i>Excess of expenditure over receipt</i>	<i>Rs. 23,05,40,228.90</i>	<i>Rs. 35,55,54,119.88</i>

57 *It was further contended that the assessee was following completed contract method which was one of the recognized method as per accounting standard AS 7 which was enforced for all the contracts entered upto 31.3.2003 and therefore, same would not violate the charging section and true profit can still be worked out by following this method. Moreover this method was consistently followed by the assessee in the earlier year when the income was exempt u/s 10(20A) of the Act. No doubt there is change in the system of accounting to cash system from mercantile system followed earlier, however, the method of recognition of the income from housing schemes continued to remain the same as in the past and receipt as well as expenditure were accumulated in the scheme and in this regard reliance was made to schedule "F" of the balance sheet filed in the paper book. He also referred to the definition of "hire purchase" in Hire Purchase Act, 1972 as well as other relevant provisions. This definition clearly shows that allottee of a house would become owner of the same only on the completion of the terms of the agreement.*

58 *The ld. counsel of the assessee further submitted that addition on account of installments have mainly been made because the assessee was following cash system. The Assessing Officer failed to realize that Section 145 which is a machinery section and provides for system of accounting, can not over ride charging section. Since in the present case, the sale is not complete and till completion of the tenure the receipt of installments could not be recognized as income and the same have to be treated as advance only irrespective of the system of accounting followed by the assessee. In this regard reliance was placed on the decision of Delhi Bench of the Tribunal in case of K.K. Khullar Vs. DCIT, 304 ITR (AT) 295 (Delhi). Unless and until there is a realistic income the same cannot be charged to tax and in this regard reliance was placed on the decision of Hon'ble Supreme Court in case of CIT Vs. Messrs. Shoorji Vallabhdas and Co. 46 ITR 144 (S.C). The ld. counsel of the assessee also referred to the decision of Hon'ble Punjab & Haryana High Court in*



*case of CIT Vs. Punjab Financial Corporation, 295 ITR 502 (PH) wherein it was clearly held that a mere system of accounting can not create a income. In view of these decisions simply because the assessee was following cash system of accounting the receipt cannot be given colour of income.*

59 *It was further submitted that receipts were accumulated in the balance sheet and at the same time the cost was also accumulated in a particular scheme in the balance sheet. The Assessing Officer again simply picked up the receipt without allowing corresponding cost. Therefore, in the alternative even if it is held that advance receipt of installments is in the nature of the income then suitable directions for allowing the actual cost incurred should also be given. In this connection reliance was placed on the decision of Hon'ble Supreme Court in case of CIT Vs. Bilahari Investment P. Ltd. 299 ITR 1 (S.C). It was further submitted that the decision of Hon'ble Punjab & Haryana High Court in case of CIT Vs. Chandigarh Industrial and General Development Corporation (supra) and CIT Vs. Dhri and Co. Colonisers P. Ltd (supra) have been reversed in view of the decision of Hon'ble Supreme Court in case of CIT v Realest Builders and Services Ltd. 307 ITR 202 (S.C).*

60 *He also submitted that there is no force in the contention of the ld. DR for the revenue that income of one particular year cannot be deferred to future years because first of all no income has materialized and secondly profit of each year being determinable at the year end is one thing and profit of each year are required to be essentially to be determined at the end of the year, is another thing. Simply because the method of accounting exists for determination of profit of each year, it cannot be followed that the profits of the project must be determined when the whole project got completed in the future and this method was consistently followed. He also placed reliance on the decision of Special Bench of the Tribunal in case of DCIT Vs. Nagarguna Investment Trust Ltd. 65 ITD 17 and Taparia Tools Ltd. Vs. JCIT, 260 ITR 102.*

61 *In the rejoinder the ld. DR for the revenue submitted that there is no force in the submissions that Section 145 can not over ride the charging section because in the present case installments received would come under the purview of income under the charging section also. She also submitted that decision in case of CIT v Realest Builders and Services Ltd (supra) is totally distinguishable because in that case the issue was whether it was for the department to give vital aspects regarding method of accounting followed by the assessee which resulted in under estimation of profit whereas in the case before us, is regarding consequences of following of cash system of accounting.*

62 *We have heard the rival submissions carefully. Section 145 of Income Tax Act reads as under:*

*“Section 145 – (1) Income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" shall, subject to the provisions of sub-section (2), be computed in*

*accordance with either cash or mercantile system of accounting regularly employed by the assessee.*

*(2) The Central Government may notify in the Official Gazette from time to time accounting standards to be followed by any class of assesseees or in respect of any class of income.*

*(3) Where the Assessing Officer is not satisfied about the correctness or completeness of the accounts of the assessee, or where the method of accounting provided in sub-section (1) or accounting standards as notified under sub-section (2), have not been regularly followed by the assessee, the Assessing Officer may make an assessment in the manner provided in [section 144](#).*

*The above provision was substituted by Finance Act, 1995 w.e.f. 1.4.1997. Before this substitution the assessee had choice to follow mercantile or cash or even hybrid system of accounting i.e. the assessee could choose cash system of accounting for one source of income and mercantile system of accounting for other sources. This choice have been removed and now the assessee could follow either cash system of accounting or mercantile system of accounting. Plain reading of the provision shows that the assessee could follow only one system of accounting in respect of income under the head "profits and gains of business or profession or income from other sources". These restrictions have not been prescribed for other heads of business. In case before us, income of the assessee is chargeable under the head "profits and gains of business" therefore, the assessee could have adopted only one system of accounting. Before the present assessment year the assessee was following mercantile system of accounting and in this year system has been changed from mercantile system of accounting to cash system of accounting. Though it is very surprising how a large organization such as the assessee, could follow cash system of accounting but it is admitted fact that the assessee followed cash system of accounting. In fact in respect of other additions like receipt of interest from bank and receipt of interest from Government of Punjab, it was vehemently argued on behalf of the assessee that these receipts can be taxed only when the same have been actually received by the assessee because the assessee was following cash system of accounting. Therefore, admitted position is that the assessee is following cash system of accounting.*

63 *Normally people other than the traders keep accounts in cash system i.e. people like Doctors, Advocates or other professionals keep their accounts in cash basis because they are not selling any merchandise and it is very easy to follow cash system for them. As we have already observed that it is surprising that the assessee had followed cash system of accounting. Therefore, when the traders follow cash system and whenever such traders sell any merchandise on credit he would enter the transaction only in a memorandum account or in some other rough account as a record so that he does not forget the same. This is the reason we are surprised that assessee is following cash system of accounting when in assessee's case large number of transactions are*



*involved then how can an organization follow cash system because in the transaction where no cash is incoming or outgoing such transactions are not recorded under this system and they are only noted as memorandum entries or in rough jotting. Under the cash system of accounting such trader would not enter the sale proceeds on the income side in his books of account or cash book until the same is actually received. Similarly an item of expenditure will be booked only when actual cash payment is made. In case of mercantile system of accounting income as well as expenditure would be recognized on the principle of accrual. In fact this issue was considered by the Hon'ble Supreme Court in case of Raja Mohan Raja Bahadur Vs. CIT, 66 ITR 378 (S.C). In that case the assessee was a money lender and had given loan to one Shri Nisar Ahmad Khan, Taluqdar of Mohana Estate. The assessee was maintaining books of account on cash system of accounting. The assessee commenced an action in Civil Court for a decree for recovery of Rs. 2,58,000/-. Ultimately Judicial committee of the Privy Council decreed in favour of the assessee. Shri Nisar Ahmad Khan obtained under the UP Encumbered Estates Act, 25 of 1934 an order applying the provision of the Act to him. The Special Judge, Sultanpur, passed an order for payment of Rs. 5,00,992/- to the assessee. Pursuance to the order the assessee received in 1946, Rs. 1,54,692/- from the debtor and for the balance the Government of the United Provinces gave to the assessee Encumbered Estate Bonds of the face value of Rs. 3,46,300. The amount received in the year 1946 was appropriated by the assessee towards the principal due. The assessee split up the amount of the face value of the bonds into two sums of Rs. 2,22,097-9-11 and Rs. 1,24,202-6-1 and credited the first amount in the books of account towards the balance of principal and the second amount to an account styled "interest Accrued". In submitting the return of his taxable income for the Assessment year 1948-49 the assessee did not disclose any receipt of income from interest due on the loans advanced to Nisar Ahmad Khan. The assessee was duly assessed to tax on the income disclosed by him. In Oct 1948, the assessee sold the Encumbered Estates Bonds and realized a total sum of interest received during the year on account the difference between the amount realized by sale of the bonds and the amount due as principal. The ITO issued a notice u/s 34(1)(a) of the Indian Income Tax Act and brought to tax the difference between the face value of the bonds and the amount due as principal as escaped income of the previous year relevant to the Assessment year 1948-49. The order was confirmed by the Appellate Assistant Commissioner and the Income-tax Appellate Tribunal. The High Court also decided the issue against the assessee. On further appeal before the Hon'ble Supreme Court it was mainly contended that the assessee was maintaining books of account on cash system of accounting and until the assessee realized the value of bonds, no interest can be said to have been received by the assessee because it was further submitted that when the accounts are maintained on cash system of accounting, receipt of money alone may be taken into account in determining the taxable income. The Hon'ble Apex Court mainly observed at page 382 as under:*

*“Under section 4 of the Income-tax Act, 1922, the total income of any previous year of a resident assessee includes all income, profits and gains from whatever sources derived which are received or are deemed to be received in the taxable territories in such year by or on behalf of such person, or accrue or arise or are deemed to accrue or arise to him in the taxable territories during such year, or accrue or arise to him without the taxable territories during such year, or having accrued or arisen to him without the taxable territories before the beginning of such year and after the 1<sup>st</sup> day of April, 1933, are brought into or received in the taxable territories by him during such year. The Act does not contain much guidance as to cases in which tax is to be levied on income received, and cases in which tax is to be levied on income accrued or arisen. Section 13 however requires that income, profits and gains for the purposes of sections 10 and 12 shall be computed in accordance with the method of accounting regularly employed by the assessee. If accounts are maintained according to the mercantile system, whenever the right to receive money in the course of a trading transaction accrues or arises, even though income is not realized, income embedded in the receipt is deemed to arise or accrue. Where the accounts are maintained on cash basis receipt of money or money’s worth and not the accrual of the right to receive is the determining factor. Therefore, if commercial assets are received by a trader maintaining accounts on cash basis in satisfaction of an obligation, income which is embedded in the value of the assets is deemed to be received: the receipt of income is not deferred till the asset is realized in terms of cash or money. It makes no difference whether the receipt of assets is in pursuance of an agreement or that the trader is compelled by law to accept the assets from the debtor. Once title of the trader to an asset received is complete, whether by a consensual arrangement or by operation of law, he receives the income embedded in the value of the asset. In *Californian Copper Syndicate v. Harris Lord Trayner* in dealing with a case of assessee to income-tax of a company, formed for the purpose, inter alia, of acquiring and re-selling mining property, which resold the whole of its assets to a second company and received payment in fully paid shares of the purchasing company, observed:*

*“ A profit is realized when the seller gets the price he has bargained for. No doubt here the price took the form of fully paid shares in another company, but, if there can be no realized profit, except when that is paid in cash, the shares were realizable and could have been turned into cash, if the appellants had been pleased to do so. I cannot think that income-tax is due or not according to the manner in which the person making the profit pleases to deal with it.”*

*The other observations have been summarized in the head note which read as under:*

*“If accounts are maintained according to the mercantile system, whenever the right to receive money in the course of a trading transaction accrues or arises, even though income is not realized, income embedded in the receipt is deemed to accrue or arise. Where*

*the accounts are maintained on cash basis, receipt of money or money's worth and not the accrual of the right to receive is the determining factor. Therefore, if commercial assets are received by a trader maintaining accounts on cash basis in satisfaction of an obligation, income which is embedded in the value of the assets is deemed to be received; the receipt of income is not deferred till the asset is realized in terms of cash or money. It makes no difference whether the receipt of assets is in pursuance of an agreement or that the trader is compelled by law to accept the assets from the debtor. Once title of the trader to an asset received is complete whether by a consensual arrangement or by operation of law, he receives the income embedded in the value of the asset. "*

*Therefore, in cash system of accounting for determination of the income receipt on money (cash) or money's worth instruments are determining factor and in accrual of right to receive such money is a material. In other words, whenever the cash is received on income side the same has to be taxed if the cash is received on capital side for example loan from bank then the same would not be required to be taxed. However, if there is simply a right to receive such cash the same cannot be taxed in the cash system of accounting. In our opinion, this would answer the question and or contention raised by the ld. counsel of the assessee that before taxing an item the same has to pass through the test of charging section. Section 4 of the Act which is charging section, reads as under:*

*"Section 4 - (1) Where any Central Act enacts that income-tax shall be charged for any assessment year at any rate or rates, income-tax at that rate or those rates shall be charged for that year in accordance with, and [subject to the provisions (including provisions for the levy of additional income-tax) of, this Act] in respect of the total income of the previous year [\* \* \*] of every person :*

***Provided** that where by virtue of any provision of this Act income-tax is to be charged in respect of the income of a period other than the previous year, income-tax shall be charged accordingly.*

*(2) In respect of income chargeable under sub-section (1), income-tax shall be deducted at the source or paid in advance, where it is so deductible or payable under any provision of this Act.*

*Plain reading of this provision would show that tax can be charged at the rate prescribed by any Central Act which is practically done through passing of Finance Act in every year by the Parliament. Such tax can be charged in respect of total income of the previous year. Total income has been defined in Section 5 of the Act. The word "Income" has been defined in Section 2(24) so therefore, before charging tax it has to be seen that an item is in the nature of "income" and covered by the definition of income given in Section 2(24) of the Act. It is further to be noted that income has been defined in inclusive manner. This is very complex issue and without going into the details we would simply take the simple meaning of the "income". In the normal commercial parlance an item*

which is of revenue nature, is taken as income. Now in a case where an organization which is carrying out the business of construction and development of houses and if such organization sells the same outrightly or on installments basis then such installments would be in nature of income. Therefore, there is no force in the submissions of the ld. counsel of the assessee that installments received by the assessee do not come under the charging section and therefore, same cannot be taxed simply because u/s 145 the receipt under cash system has to be taxed. No doubt Section 145 is a machinery section but machinery section also have lot of bearing on determination of income and cannot be ignored lightly. In this connection we would like to refer to one of the celebrated judgment of Hon'ble Supreme Court in case of CIT Vs. B.C. Srinivasa Setty, 128 ITR 294 (S.C). In that case the assessee was a Regd firm. Clause 13 of the Instrument of Partnership deed showed that goodwill of the firm have not been valued and valuation would be made at the dissolution of the partnership. Period of the partnership was extended and subsequently partnership was dissolved on 31.12.1965. At the time of dissolution goodwill was valued at Rs. 1,50,000/-. The new partnership with the same name was constituted through another deed of partnership. New firm booked over all the assets including goodwill and liability of the dissolved firm. Originally no addition was made on account of gain arising out of transfer of goodwill but this assessment order was found erroneous and prejudicial to the interest of the revenue and therefore, Ld. Commissioner passed revisionary order directing the Assessing Officer to make fresh assessment after taking into account the capital gain arising out of sale of goodwill. The assessee maintained that no sale took place to attract the tax on capital gain u/s 45 of the Income Tax Act . The Tribunal allowed the appeal. When the matter traveled to the Hon'ble Supreme Court the matter was argued in great detail. One of the issue arose whether there was transfer and it was held yes it was a transfer. Another issue arose whether the gain of such transfer of goodwill would be taxed u/s 45 of the Act. It was found that goodwill is a self generated asset and no cost of acquisition can be attributed to self generated assets. Since Section 48 which is mode of computation of capital gain prescribes reduction of cost of acquisition from the sale consideration it was held that in the absence of cost of acquisition computation of capital gain, was not possible. Therefore, same was held to be not taxable. This clearly shows that computation provision which is again a machinery provision, had lot of bearing on the taxability of gain received on transfer of goodwill. Therefore, even if section 145 being machinery section has its own implications. Implications are very clear that the assessee has a right to follow either mercantile system of accounting or cash system of accounting for determination of the income. The assessee has been given a choice and in the case before us, the assessee has deliberately and after applying its mind decided to follow cash system of accounting, therefore, the assessee has to bear the consequences of such system of accounting.

64 The ld. counsel of the assessee has strongly relied on the decision of K.K. Khullar Vs. DCIT (supra). In this case the assessee was an



*Advocate and received certain amounts for services to be performed over a period of time. The amount received from the client in respect of services rendered in the year under consideration, was shown as income and the balance amount was shown as advance. The Assessing Officer held that as per the provisions of section 145 the assessee was following cash system of accounting and therefore, whole amount was taxable. The Tribunal decided the issue in favour of the assessee vide following paras:*

*We have considered the facts of the case and rival submissions. We may refer to the charging section 4 of the Act to the effect that income-tax shall be charged for any assessment year at the rate or rates provided in any Central Acts in respect of the total income of the previous year of every person. Section 5 deals with the "scope of total income", which is defined in respect of any previous year in terms of accrual, deemed accrual, receipt and deemed receipt etc. Section 145 deals with the method of accounting in respect of "profits and gains of business or profession" or "income from other sources." Thus, while sections 4 and 5 deal with the scope of income and its charge to income-tax, section 145 is a procedural section regarding the method to be followed for recording of income in the books of account. It is no doubt true that for the assessment year 1997-98 and onwards, the assessee can follow either the cash or the mercantile system of accounting and the hybrid system of accounting is prohibited. However, what is to be taxed is income and receipt of an amount is not to be the basis for the levy of the tax. In the case of Messrs. Shoorji Vallabhdas and Co. [1962] 46 ITR 144, the hon'ble Supreme Court pointed out that the Income-tax Act takes into account two points of time on which the liability to tax is attracted, namely, -(i) accrual of income or (ii) receipt of income. It is further mentioned that the substance of the matter is "income". It may be emphasized that it is accrual of income or receipt of income that can become the subject-matter of tax and it is the income which has to be recorded as per system of accounting followed by the assessee in view of section 145 of the Act, because the substance of the matter is "income". Therefore, there is an infirmity in the order of the learned Commissioner of Income-tax (Appeals) in paragraph 4.7 where it was stated that the entire amount received, whether arrears or advance, is to be shown as income under the cash system of accounting. **The correct position would be that the entire income received, whether arrear or advance of income, has to be shown as income under the cash system of accounting.** "*

*The highlighted portion of the above paragraph clearly shows that in cash system of accounting the receipt of money whether arrears or advance, has to be shown as income, therefore, this decision is totally distinguishable.*

65 *Another decision relied on was that of CIT Vs. Messrs, Shoorji Vallabhdas and Co. (supra). In that case the assessee firm was the managing agent of two Shipping companies and under the Managing Agency Agreement, the assessee was entitled for commission @ 10% of the freight charges. Between April 1, 1947 and December 31, 1947 an*



amount of Rs. 1,71,885/- from one company and Rs. 2,56,815/- from other company became due to the assessee as commission @ 10%. This amount was credited in the books of account and debited to managing agent. In November 1947 the assessee desired to have managing agency transferred to two Private Companies and in this connection agreed in December, 1948 to accept 2½% as commission and gave up 7½% of its earnings. The revenue sought to assess the amounts to Rs. 1,36,903/- and Rs. 2,00,625/- being 7½% of the foregone amount as income. On these facts it was held as under:

*“Held, that the subsequent agreement had altered the rate of commission in such a way as to make the income which really accrued to the assessee different from what had been entered in the books of account. This was not a case of a gift by the assessee to the managed companies of a portion of income which had already accrued, but an agreement to receive a lesser remuneration than what had been agreed upon. The assessee had in fact received only the lesser amount in spite of the entries in the account books, and this lesser amount alone was taxable.*

*Income-tax is a levy on income. Though the Income-tax Act takes into account two points of time at which the liability to tax is attracted, viz., the accrual of the income or its receipt, yet the substance of the matter is the income. If income does not result at all, there cannot be a tax, even though in book-keeping, an entry is made about a “hypothetical income”, which does not materialize. Where income has, in fact, been received and is subsequently given up in such circumstances that it remains the income of the recipient, even though given up, the tax may be payable. Where, however, the income can be said not to have resulted at all, there is obviously neither accrual nor receipt of income, even though an entry to that effect might, in certain circumstances, have been made in the books of account. “*

*Thus it is clear from above that the amount which was sought to be assessed was not in nature of income because the assessee has clearly agreed to reduce the rate of commission on conversion of the agency in the name of Private companies. In case before us, nowhere it has been denied that installments received by the assessee firm from the allottees of the houses is not in the nature of the income. Therefore, the proposition laid down in case of CIT v Messrs Shooroji Vallabhdas and Co. Supra) are not applicable.*

66 We would also like to note that in original return filed by the assessee, was for income of Rs. 21.19 crores whereas in the revised return a loss of Rs. 19.12 crores was claimed. The Assessing Officer examined the reasons for loss and he found that main reason was that expenditure accounts show the figures of cost of plots and therefore, sale which was not there in the original income and expenditure account. Result of these figures is as under:

<i>Cost of plots</i>	Rs.	<i>Sale of plots</i>	Rs.
	05,42,88,169/-		65,18,29,803/-
		<i>Loss</i>	Rs.
			40,24,58,366/-
	Rs.		Rs.
	105,43,88,169/-		105,42,88,169/-

*This matter was investigated in detail and ultimately the reason for these entries was analyzed and discussed by the Assessing Officer as mentioned in the assessment order as under:*

*As regards the reason for huge loss from purchase and sale of plots, it was explained by the counsel, during discussion and also explained by the assessee in its letter No. 1567 dated 08.03.2006 that since the assessee has changed its system to cash system of accounting, only the amount actually received out of total sale amount has been shown as sale whereas the plots which have been sold but only a part of the sale amount of which has been received are not reflected in the closing stock which is the reason for the loss in the purchase and sale of plots for the assessment year 2003-04. But in the subsequent years i.e. assessment year 2004-05 onwards, there is profit from purchase and sale of plots. During discussion, it was explained by the counsel by giving an example. Suppose, the cost of plot is Rs. 1,00,000/- and it is sold for Rs. 1,50,000/- during this year but only 25% of the cost of the plot i.e., Rs. 37,500/- is actually received during the year. Actually, the profit earned is Rs. 50,000/-. But since the assessee has adopted cash system, sale will be shown at Rs. 37,500/- for the year. The value of closing stock of that plot will be Nil as the plot has been sold and is in the possession of the purchaser. So this will result into loss of Rs. 62,500/- for that year. Now in the next year, there will be no opening stock in respect of that plot but if the balance amount of sale consideration i.e. Rs. 1,12,500/- is actually received in that year that will be shown as the amount of sale for which there will be no opening stock or corresponding purchase and the same, already-sold plot will give a profit of Rs. 1,12,500/- in that next year. This is the reason that there is steep rise in the profit from sale of plots in the next year. The assessee's counsel referred to the original and revised return for the succeeding assessment year 2004-05. Perusal of these returns shows that in the original return for the assessment year 2004-05, the income as per the profit and loss account and after deducting depreciation as per Income Tax Rules has been shown at Rs. 7,67,61,289/-, In the revised return, the income as per the profit and loss account and after deducting depreciation as per the Income Tax Rules has been shown at Rs. 39,50,14,907/-. There is a steep rise of Rs. 31,82,53,618/- in the income for the assessment year 2004-05 which is mainly on account of recognizing revenue on purchase and sale of plots on cash method of accounting. "*

*This explanation of the assessee was found to be convincing and accepted. Thus it is clear that the assessee itself contended that sale of plots has to be accepted on the basis of actual cash receipt on sale effected during*

*the year. Therefore, the assessee could not take a different stand in respect of sale of houses and flats.*

*67 Coming to the facts of the case, the assessee sold certain houses and flats under the Hire Purchase agreement. The allottees were treated as tenant during the completion of such hire purchase agreement till all the installments were paid by such allottees. The installments as well as expenditure incurred by the assessee, was being accumulated in various schemes and was reflected in the balance sheet because the assessee was following mercantile system of accounting till Assessment year 2002-03. However, in this year the assessee has changed accounting system and now adopted cash system of accounting. We have already expressed our surprise on adoption of cash system by the assessee but admittedly this system has been adopted and therefore, the assessee has to bear the consequences. First contention was that houses and flats were sold on hire purchase basis and under the Hire Purchase Act, 1972 the buyer does not get the ownership right till the completion of the purchase as provided in the agreement and as per the agreement till all the installments are paid such buyer or allottees will not become the owners. However, we find no force in this contention because no other Act can over ride the provisions of the Act and this has been clarified by the Hon'ble Supreme Court in case of Southern Technologies Ltd. Vs. JCIT (supra). Therefore, the installments received against such sales which are in the nature of revenue receipts, are required to be taken into consideration for determination of income in this year because the assessee has adopted cash system of accounting during the year. Next contention was that the assessee was following continuously Project completion method and therefore, no income can be determined unless the projects are completed. Again as discussed above in detail the issue of system of accounting and the meaning of cash system of accounting, this contention cannot be accepted because the assessee can not follow two different systems of accounting under the same head. Therefore, in our opinion, the Assessing Officer has correctly included all the installments received from the allottees of the houses and flats in the income of the assessee.*

*68 However, we find that the submissions of the ld. counsel of the assessee that if such installments are included then the corresponding expenditure which has been incurred should also be allowed on matching principle. The ld. counsel of the assessee had relied on the decision of CIT Vs. Bilahari Investment P Ltd. (supra). In that case the assessee subscribed to chits as their business activities. They maintained their accounts on the mercantile basis and computed the profit/loss at the end of the chit period following the completed contract method. This was accepted by the Department, but for the assessment years 1991-92 to 1997-98 the Assessing Officer came to the conclusion that the completed contract method for chit discount was not accurate in recognizing /identifying income and that the percentage of completion method was to be preferred. The High Court held that the completed contract method of*

*accounting adopted by the assessee for chit discount was valid and the Department erred in spreading the discount over the remaining period of the chit under the percentage of completion method on proportionate basis. On appeal by the Department to the Supreme Court, it was held as under:*

*“Held accordingly, affirming the decision of the High Court, that, since, from the various statements produced, the entire exercise arising out of the change of method from the completed contract method to deferred revenue expenditure was revenue neutral, the completed contract method was not required to be substituted by the percentage of completion method. “*

69 *in our opinion, the above case is not very relevant because in this case the assessee was continuously following the method of completed contract under mercantile system of accounting which was found to be correct. However, the matching principle was laid down in case of Calcutta Company Ltd. Vs. CIT, 37 ITR 1 by the Hon'ble Supreme Court. In that case the assessee purchased certain lands and developed the same for building purposes by laying roads, providing drains system and installing lights etc. The flats were sold on installment basis. At the time of sale the assessee undertook to carry out more developments. In the relevant year the assessee received a sum of Rs. 29,392/- towards sale price of land. However, the assessee was following mercantile system of accounts and credited to its account a sum of Rs. 43,692/- representing full sale price of the land. At the same time the assessee also debited an estimated sum of Rs. 24,809 as expenditure for the developments. This was disallowed by the Revenue. On appeal it was held as under:*

*“Held,(i) that the undertaking to carry out the developments within six months from the dates of the deeds of sale (which, in view of the fact that time was not of the essence of the contract, meant a reasonable time) was unconditional, the appellant binding itself absolutely to carry out the same. That undertaking imported a liability on the appellant which accrued on the dates of the deeds of sale, though that liability was to be discharged at a future date. It was thus an accrued liability and the estimated expenditure which would be incurred in discharging the same could be deducted from the profits and gains of the business, and the amount to be expended could be debited in accounts maintained in the mercantile system of accounting before it was actually disbursed. The difficulty in the estimation thereof did not convert the accrued liability into a conditional one, because it was always open to the Income-tax authorities concerned to arrive at a proper estimate thereof having regard to all the circumstances of the case.*

*(ii) That the sum of Rs. 24,809 represented the estimated amount which would have to be expended by the assessee in the course of carrying on its business and was incidental to the business and, having regard to the accepted commercial practice and trading principles, was a deduction which, if there was no specific provision for it under section 10(2) of the Income-tax Act, was certainly an allowable deduction, arriving at the profits and gains of the business of the appellant, under section 10(I) of the Act, there being no prohibition against it, express or implied, in the Act.*

*The expression “profits or gains” in section 10(I) of the Income-tax Act has to be understood in its commercial sense and there can be no computation of such profits and gains until the expenditure which is necessary for the purpose of earning the receipts is deducted there from- whether the expenditure is actually incurred or the liability in respect thereof has accrued even though it may have to be discharged at some future date. “*

70 Thus from above it is clear that for determining true profits cost incurred by the assessee towards the construction of the houses and flats which has been accumulated in the schemes is also to be recognised. However, it has to be noted that in case of *Calcutta Company Ltd Vs. CIT (supra)* the assessee was following mercantile system of accounting and had credited whole amount received or receivable towards sale of proceeds i.e. why the amount still to be incurred on development was allowed as expenditure but still the principle is there. Therefore, in case where cash system of accounting is followed then what ever expenditure has been incurred in cash during the year, has to be allowed. In the case before us, the assessee has neither offered the installments as income nor claimed expenditure incurred. Since we have already held that installments received have been rightly included in the income of the assessee, therefore, corresponding expenditure which has been incurred in cash towards construction of such houses and flats sold under hire purchase is also to be allowed.

71 One more angle needs to be considered that is what would happen to the opening stock as well as closing stock. In the cash system of accounting closing stock is not considered, therefore, what has been accumulated in the schemes is also required to be considered. Considering the contentions of the parties and the principles we have already discussed, we are of the opinion that whatever installments were accumulated in the schemes needs to be considered along with the opening stock whenever a particular scheme was completed. This is so because it was pointed out by the ld. counsel of the assessee that the profit in each of the scheme was offered for taxation when a particular scheme was completed. Therefore, the results of individual schemes have to be recalculated and installments accumulated should be taken as income and expenditure incurred after reducing the expenditure incurred in cash which has been allowed in various years, should be reduced from the such installments and net results should be considered in the year of completion of each of the housing schemes in the year in which profits of such completed scheme were actually offered by the assessee.

72 In these circumstances we set aside the order of the Ld. CIT(A) and direct the AO to include installments received on sale of various houses and flats under hire purchase agreement and at the same time allow corresponding expenditure which has been expended by the assessee in cash (including through cheque). Further in the year of completion of a particular scheme effect has to be given in respect of accumulated



*installments as well as accumulated expenditure which has not been already considered in a particular year on cash basis as observed earlier. We have observed right in beginning that this issue is involved in all the years before us therefore, similar treatment as observed by us, should be given in each of the year.*

8. Following the above, we decide this issue raised by the assessee against the assessee.

9. In the result, appeal is dismissed.

Order pronounced in the open Court on 16/06/2019.

Sd/-  
**(BHAVNESH SAINI)**  
**JUDICIAL MEMBER**

Dated : 16<sup>th</sup> June, 2015  
Rkk

Copy to:

1. *The Appellant*
2. *The Respondent*
3. *The CIT*
4. *The CIT(A)*
5. *The DR*

Sd/-  
**(T.R. SOOD)**  
**ACCOUNTANT MEMBER**