

**IN THE INCOME TAX APPELLATE TRIBUNAL
Hyderabad ' A ' Bench, Hyderabad**

**Before Smt. P. Madhavi Devi, Judicial Member
AND
Shri S.Rifaur Rahman, Accountant Member**

ITA No.955/Hyd/2018
(Assessment Year: 2013-14)

Shri Challa Ramakrishna Vs Asstt. Commissioner of
Anantapur Income Tax, Circle – 1
PAN:AATPC3928N Anantapur
(Appellant) (Respondent)

For Assessee : Shri H. Guru Swamy
For Revenue : Smt. Nivedita Biswas

Date of Hearing: 17.01.2019
Date of Pronouncement: 12.04.2019

ORDER

Per Smt. P. Madhavi Devi, J.M.

This is assessee's appeal for the A.Y 2013-14 against the order of the Pr. CIT, Kurnool, dated 20.03.2018.

2. Brief facts of the case are that the assessee, an individual, filed his return of income for the A.Y 2013-14 on 19.03.2014, admitting a total income of Rs.1,50,16,090/-. The case was selected for scrutiny under CASS and accordingly, the AO completed the assessment by bringing to tax, (i) short term capital gain; (ii) long-term capital gains; and (iii) income from other sources and arrived at the total taxable income of Rs.2,26,59,354/-. Aggrieved by the same, the assessee preferred his appeal before the CIT (A).

3. Meanwhile, the Pr. CIT, Kurnool u/s 263 of the I.T. Act, perused the assessment order and observed that the assessee, along with his brother Shri C. Seetharam Babu, had purchased 24,960 sft of converted land (agricultural land converted to non-agricultural land) in survey No.16, situated at Anantapura Village of Bangalore vide Registered Sale Deed Document No.3153/2011-12, dated 07.09.2011 and that he had held it as a capital asset as on 31.03.2012, but converted the same to stock-in-trade in his books of account in the financial year 2012-13, and that in the same financial year, the assessee and his brother entered into a registered joint development agreement vide document No.779/2012-13 dated 16.05.2012 with M/s. Sri Sai Developers, Bangalore. He observed that as per Para 5 of the JDA, the assessee and his brother are entitled to 39% of the undivided share of land; super built up area and car parking area etc., while the Developer was entitled to 61% of the undivided share of land, super built up area and car parking area etc. He observed that the conversion of capital asset into stock-in-trade and entering into JDA is in the same year and therefore, attracts the provisions of section 45(2) of the Act. Therefore, he was of the opinion that the assessee ought to have offered the short term capital gain to tax on conversion of capital asset to stock-in-trade in the relevant A.Y and further that since the assessee's share value from the JDA has also accrued on account of transfer of 61% of land to the developer, the same should also be brought to tax in the A.Y 2013-14. He also observed that the assessee is in possession of vacant flats received vide the JDA dated 19.08.2011 with M/s. D.M. Builders, which was held as stock-in-trade as on 31.03.2013, but that the assessee has not offered the income

from house property from these flats. Therefore, according to the Pr. CIT, the order passed u/s 143(3), dated 31.03.2016 is erroneous in so far as the above issue is concerned and it is also prejudicial to the interest of the Revenue. He, therefore, issued a show-cause notice to the assessee and in reply to the same, the assessee filed its objections as under:

- i) *That the assessee, along with his brother, has purchased 24,960 sft of converted land and thereafter, entered into a registered joint development agreement vide document No.779/2012-13 dated 16.05.2012 with M/s. Sri Sai Developers, Bangalore in the previous year relevant to the A.Y 2016-17 and as such, capital gains thereon arose u/s 45(2) in the assessment year 2016-17. Further, it also submitted that the additions made by the AO are the subject matter of appeal before the CIT (A) regarding the chargeability of the STCG in the A.Y 2013-14 and since the issue is pending for adjudication before the CIT (A), the AO may be directed to submit before the CIT (A) for enhancement of short term capital gain. It is also submitted that since the AO has taken one of the possible views in computing the short term capital gain, the Pr. CIT does not have jurisdiction u/s 263 and in support of the same, the assessee relied upon the judgment of the Hon'ble Andhra Pradesh High Court in the case of CIT vs. Usha Kiran Movies Ltd (2014) 363 ITR 165 (A.P).*

ii) *Vide JDA with M/s. Sri Sai Developers, the assessee and his brother are having 39% of the rights of the super built up area, car parking etc., and income would arise only at the time of exercising the rights and since the assessee exercises his right in the previous year relevant to the A.Y 2016-17, the same is taxable in the same A.Y.*

iii) *The assessee is not in possession of vacant flats received vide JDA dated 19.08.2011. The assessee received 24 residential flats, out of which, 22 were sold in the financial year 2012-13, and the remaining flats were sold in the subsequent years. However, the new provision u/s 23(5) is applicable only w.e.f. 1.4.2018 and therefore, the said income cannot be brought to tax in the A.Y 2013-14.*

4. The Pr. CIT considered the above objections of the assessee and held that:

i) *The provisions of section 45(2) speaks about capital gain arising out of the transfer by way of the conversion of the capital asset into stock-in-trade which shall be chargeable to Income Tax in the previous year in which such stock in trade is sold or otherwise transferred by him. The CIT held that since the assessee has entered into JDA in the same financial year in which the capital asset was converted into stock-in-trade, as the*

assessee and his brother transferred the rights to exploit the stock in trade for construction of multi-storied building and therefore short term capital gain has accrued to the assessee in the previous year, relevant to the A.Y 2013-14. With regard to the computation of short term capital gain, he held that the difference between the fair market value of 61% of the share of the land on the date of conversion and the cost of acquisition of 61% of the land is short term capital gain.

- ii) *The assessee is following mercantile system of accounting and therefore, the business income on account of JDA had also arisen during the A.Y 2013-14. He observed that the difference between 39% of the total cost of construction of the project to the Developer based on the project report prepared by the Developer or Registered Engineers Evaluation Report and the fair market value of the 65% of the land on the date of conversion from capital asset to stock in trade, is assessee's business income for the A.Y 2013-14.*

He, therefore, directed the AO to assess the assessee's share of business income to tax in the A.Y 2013-14.

5. As far as the third issue is concerned, he observed that the provisions of section 23(5) are explanatory in nature and as such for the A.Y 2013-14, the income from house property on vacant flats is chargeable to tax. He accordingly directed the AO to bring it to tax.

6. Aggrieved by the order of the CIT u/s 263 of the Act. the assessee is in appeal before us by raising the following grounds of appeal:

“1. The impugned Revisionary Order dtd: 20-03-2018 passed U/s. 263 of the Act by the Learned PCIT, Kurnool is opposed to law, facts and circumstances of the case.

2. The Ld. PCIT has erred in assuming the jurisdiction u/s. 263 of the Act without appreciating the pendency of an Appeal filed by the Appellant against the Protective Assessment Order dtd:31-03-2016 and also in contravention of the explanation (c) provided to section 263 of the Act.

3. The Ld. PCIT has erred in holding that the STCG are exigible to Tax for the A. Y 2013-14 in respect of the Capital Asset which was converted into Stock in trade in the F.Y 2012-13 without appreciating the fact that the Capital Gains on conversion of Capital Asset into Stock in trade are chargeable to tax in the year in which such converted Stock in trade was sold as per section 45(2) of the Act.

4. The Ld. PCIT has erred in holding that the Assessee's share of Cost of Improvement of Rs. 63,67,500/- needs verification without appreciating the fact that such an issue did not form part of the Show Cause Notice dtd: 10-01-2018 and thereby the Principles of Natural Justice are defeated.

5. The Ld. PCIT has erred in holding that the Business income on account of transfer of Stock in trade vide JDA dtd: 16-05-2012 is taxable for the A.Y 2013-14 on the ground of Mercantile System of accounting followed by the Appellant without appreciating the fact that the taxability of Capital Gain arises in the previous year in which the stock in trade was sold and not in the year of JDA.

6. The Ld. PCIT has erred in holding that the taxable Business income is the difference between 39% of the Cost of Construction of the project to the Developer and the FMV of 61 % of the Land on the date of conversion of Capital Asset into Stock in trade in the A.Y 2013-14 without appreciating the fact that the Business Income is chargeable to tax in the previous year in which the stock in trade was sold and not in the A.Y 2013-14.

7. The Ld. PCIT has not appreciated the fact that the Appellant has voluntarily declared the business income in

the A.Y 2016-17 relating to the JDA entered into with M/s. Sai Developers.

8. The Ld. DIT has erred in holding that the notional rent being income from House Property of 2 unsold vacant flats received from M/s. D.M. Builders is chargeable to tax in the A.Y 2013-14 without appreciating the fact that the new provision of section 23(5) was applicable for the A.Y 2018-19 onwards and the provision was said to be explanatory in nature.

9. The Appellant craves leave to add, alter, amend and delete any of the grounds at the time of hearing.

For these and other grounds that may be urged at the time of hearing, the Appellant respectfully prays that your Hon'ble Authority be pleased to pass orders cancelling the Order dtd: 20-03-2018 passed u/s. 263 of the Act and further be pleased to pass such other orders granting such other relief that your Hon'ble Authority may deem fit in the interest of justice and equity”.

7. The learned Counsel for the assessee as well as the Revenue have filed written submissions and have also argued in detail. For the sake of ready reference, the written submissions of the assessee are reproduced as under:

“1. The Appellant is an individual engaged in the business of Development of Properties and he has filed his return of income on 19-03-2014 for the A.Y 2013-14, declaring income of Rs. 1,50,16,090/- consisting of income from Business, Capital Gains and income from other sources ..

2. The return of income so filed was selected for Scrutiny Assessment under CASS and thereafter a Scrutiny Assessment was completed on 31-03-2016 on protective basis determining the total income at Rs. 2,25,49,354/- as detailed below as against the declared income of Rs. 1,50,16,090/-.

Income from Business (D.M. Builders)	Rs.1,69,79,487/-
Long Term capital Gains (D.M. Builders)	Rs. 19,46,219/-
Short Term Capital Gains	Rs. 3,84,411/-
Income from Other Sources	Rs. 33,49,237/-

Total Taxable Income	Rs.2,26,59,354/-
Less: Deduction under Chapter VIA	Rs. 1,10,000/-

Balance Income

Rs.2,25,49,354/-

3. The Appellant submits that Assessment order was said to have been made on protective basis as per para 9.19 of the Assessment Order and the same is reproduced as under:

"9.19 The business income on transfer of land to the developer which works out to Rs. 1,46,43,223/arises in the A.Y 2012-13 as already discussed hereinabove. However, as the capital gains have also been protectively assessed in the A.Y 201314, this income on transfer of land is also protectively assessed in the A.Y 2013-14."

4. It is evident from the Assessment Order that the Assessment dtd: 31-03-2016 was made on protective basis without any indication in the said Assessment order as regards completion of a Corresponding Substantive Assessment and therefore the Assessment order dtd: 31-03-2016 said to have been made on protective basis is not maintainable in law in the absence of the corresponding Substantive Assessment for the same Assessment Year 2013-14. In this regard the Appellant has filed an Appeal on the above ground amongst other grounds, before the Ld. CIT(A), Kurnool and the Appeal so filed is pending for adjudication.

5 The Appellant submits that during the pendency of the Appeal against the Protective Assessment Order dtd: 31-03-2016 u/s. 143(3) of the Act for the A.Y 2013-14, the Ld. Pr. CIT Kurnool, has issued a Show Cause Notice dtd: 10-01-2018 and called upon the Appellant to show cause as to why the Assessment Order dtd: 31-03-2016 should not be set aside as it was held to be erroneous and prejudicial to the interest of Revenue on the following grounds:- .

i. The Short Term Capital Gains arising out of the deemed transfer of 61 % of the Land in favour of the Developers M/s. Sai Builders in the Scheme of JDA dtd: 16-05-2012 relating to the land situated at Sy. No. 16, Ananthapura Village, Yellahanka Hobli, amounting to Rs. 2,27,462/- was found to be erroneous as per the provisions of section 45(2) of the Act.

ii. The Business Income arising/acquiring in the hands of the Assessee and his brother u/s. 2(47)(v) of the Act r.w.s 53A of the TP Act on account of JDA should have been worked out based on the 29% of the Total Cost of Construction of the project for the Developer/Builder as per the project report prepared by the .Developer/Builder or as per the Registered Engineer's Valuation Report for the Project as 39% of the Super Built-up area, Car Parking Area acquiring to the share of the Assessee and his brother on the date of JDA .

iii. The Assessee was in possession of vacant Flats received vide JDA dtd:19-08-2011 entered into with the Developer M/s. D.M. Builders which was held as Stock in Trade as on 31-03-2013 situated at Jinke Thimanahalli Village, Bangalore.

6 The Appellant in compliance with the Show Cause Notice dtd: 10-01-2018 has submitted the reply as under:

"3. The Assessee submits that the accessibility of STCG u/s. 45(2) of the Act said to be arising out of the Land in Sy No. 16. " Ananathapura Village in respect of which JDA was entered into with M/s. Sai Builders for the A.Y 2013-14 is not chargeable. In this regard the Assessee submits that the aforesaid Land was purchased vide sale deed dtd: 07-09-2011 from one Smt. Uma Devi for a consideration of Rs. 46,48,990/- inclusive of Stamp Duty of Rs. 2,92,430/- and Registration Fee 43,560/- (Rs. 43,13,000/- + Stamp Duty of Rs. 2,92,430/- + Registration Fee of Rs. 43,560/- = Rs. 46,48,990/-) jointly by the Assessee and his brother. The Share of the Land Cost attributable to the Assessee was of Rs. 23,24,500/-- as shown in the Balance Sheet as on 31-03-2012. Later the Assessee and his brother have incurred the Development Expenditure to the aforesaid land and the Assessee's share of Development Expenditure was of Rs. 63,67,500/--. Thus the Total Cost of Acquisition of the aforesaid land incurred by the Assessee towards his share was of Rs. 86,92,000/-- as shown in the Balance Sheet as on 31-03-2013. The enhanced value of Rs. 86,92,000/-- as against the Cost of Acquisition of Rs. 23,24,500/- represents Cost of Improvement.

The aforesaid Capital Asset was converted in Stock in Trade between the date of Purchase to the date of JDA and therefore, the provision of section 45(2) of the Act is not applicable for the A.Y 2013-14 since the Converted Stock was sold subsequently in the previous year 2015-16 relevant to the A.Y 2016-17 for which the Capital Gains stands deferred and therefore the Proposal u/s 263 is not justifiable.

4. The Assessee further submits that the Capital Asset was converted into Stock in Trade for the previous year 2012-13 relevant to the A.Y 2013-14 and the exigibility of STCG or LTTCG arises only in the year of Sale of such converted Stock in Trade. "he Assessee submits that the Assessee was entitled to the 39% of the Super Built up area as per the terms of JDA and such Built up area was sold in the Previous year 2015-16 relevant to the A.Y 2016-17 and hence the Chargeability of LTTCG u/s. 45(2) of the Act is not at all applicable for the A.Y 2013-14 and the same is applicable for the A.Y 2016-17.

Therefore this issue cannot be considered as a ground for setting aside the Original Assessment u/s. 263 as proposed in the Show cause Notice dtd: 10-01-2018.

5. **Business Income:-** The Assessee submits that in the show cause notice it was proposed that the Business income is computable u/s. 2(47)(v) of IT Act r.w.s 53A of TP Act which is applicable only for transfer of Capital Asset and not to the Stock in trade. The 390/0 of the Super Built up area in the case of M/s. Sai Builders has not been received in the A.Y 2013-14.

However a right to receive accrued and the income would arise only at the time of exercising such right. What the Assessee has received or

likely to receive will fructify and would be realized only when the right is exercised either in part or full. Such a stage of exercising the right was not materialized for the A.Y 2013-14 and therefore there cannot be any business income taxable for the relevant A.Y 2013-14. The Assessee further submits that unlike in a case of capital Gain which arises on parting of the Asset at the first stage itself, it is a case of Business Transaction which was completed in the A.Y 2016-17 when the right so acquired was exercised in that year.

7. Assessee submits that the Super Built up area was not received in the A.Y 2013-14 to exercise the right of sale and more so the right itself cannot be construed as receipt of sale consideration since none can make profit by dealing with himself as per the decision of the Hon'ble Supreme Court in the case of Sir. Kikabhai Vs. CIT (1953) 24 ITR 506 (SC). Therefore, the Assessee submits that the business income is not chargeable to tax until and unless the Stock in Trade was sold. Hence the setting aside of the Original Assessment Order dtd: 31-03-2016 on this ground is not justifiable in law.

7. **Vacant Flats:-** The Assessee was not in possession of Vacant flats vide JDA dtd: 19-08-2011 with M/s. D.M Builders as stated in the Notice issued u/s. 263 of the Act. The Assessee was entitled to 400/0 of the Super Built up area receivable in the form of 24 Residential Flats out of which in the very same year 22 flats were sold and the consideration was offered to tax for the A.Y 2013-14 and the remaining were sold in the subsequent year.

Therefore, it cannot be said that the Assessee was in possession of Vacant Flats for arriving at the Income Chargeable to tax under the head Income from House Property.

8. Without prejudice it is submitted that a new Provision of section 23(5) was inserted in the Act with effect from 01-04-2018 applicable for the A.Y 2018-19 and onwards. Therefore the chargeability of income under the head Income from House property is not applicable for the A.Y 2013-14. Hence the setting aside of the Original Assessment Order dtd: 31-03-2016 on this ground is not justifiable in law.

8. The Assessee begs to place reliance on the Decision of the Hon'ble Supreme Court in the case of M/s. Malabar Industries vs. CIT (2000) 243 ITR 83 (SC) wherein it has been held that the order should be erroneous and prejudicial to the interest of Revenue.

Even though the computation of STCG amounting to Rs. 2,27,462/- arising out of the deemed transfer in the scheme of JOA said to be erroneous but it is not prejudicial to the interest of revenue for the A.Y 2013-14 since the liability gets deferred to the year of sale as per section 45(2) of the Act and therefore the 263 proposal on this ground is uncalled for.

10. Under these facts and circumstances it is submitted that the original Assessment Order was neither erroneous nor prejudicial to the interest of

revenue and therefore invoking the provision of section 263 of the Act is uncalled for in the eye of law."

9. The Ld. Pr. CIT has not appreciated the submissions made by the Appellant and ultimately passed an order u/s. 263 of the Act dated 20-03-2018 and set aside the Assessment Order dtd: 31-03-2016 holding that the said Assessment Order was erroneous and prejudicial to the interest of revenue for the reasons stated in para 5 of the Order u/s 263 of the Act, placing reliance on various judicial decisions mentioned in clause (a) to (p) on page 3 and 4 of the Impugned Order passed u/s. 263 of the Act.

10. Appellant submits that the facts of the Judicial Decisions relied upon by the Pr. CIT are distinguishable and majority of the cases, the decision was rendered based on the facts of each case and the said facts are neither similar nor identical and therefore the said decisions are not applicable to the facts of the Appellant's case.

11. The Appellant submits that the Order passed u/s. 263 of the Act dtd 20-03-2018 is arbitrary, unreasonable and opposed to the law and facts of the case.

12. The Ld. PCIT has not appreciated the fact that the Assessment Order dtd: 31-03-2016 was a Protective Assessment and therefore the same v.as not liable to be set aside u/s. 263 of the Act, since the AO has not completed a Corresponding Substantive Assessment. The Protective assessment cannot be held to be erroneous and prejudicial to the interest of revenue since its limited existence is in the nature of a stand by Assessment to a substantive Assessment.

13. The Ld. PCIT has not appreciated the ratio laid down by the Judicial decisions in general and particularly the decision dtd: 15-11-2017 of the Hon'ble ITAT Hyderabad in the case of DCIT Central Circle -2(4) vs Smt. Girija Rani in ITA No.165/Hyd/2017 for the A.V 2013-14, wherein it has been unambiguously held that the income would arise to the assessee only when the Assessee sells stock-in-trade but not when the land was contributed as her share of Capital.

14. The Appellant begs to place reliance on the decision dtd: 30-06-2014 of the Hon'ble ITAT Bangalore in the case of Dheeraj Amin vs. ACIT Circle - 2(1) Mangalore in ITA NO. 1709/Bang/2013 for the A.V 2013~14. The relevant findings of the decision of the Hon'ble ITAT is reproduced as under:-

"19. What the assessee has got today is only a right to sell the 1,28,940.26 fts of constructed area in the Alexandria

project and the profits, howsoever certain they may appear to be, will only fructify and be realized, and can even be quantified, only when this right is exercised- in part or in full. That stage has not yet come, and until that stage comes, in our considered view, such profit cannot be taxed. Unlike in a case of a capital gain which arises on parting the capital asset at the first stage itself, it is a case of business transaction which is completed when the rights so acquired by the assessee are exercised; none can make profits by dealing with himself, as is the settled legal position in the light of the settled legal position in the case of Sir Kikabhai Premchand Vs CIT [(1953) 24 ITR 506 (SC)]. It is for this reason that we are unable to uphold the action of the authorities below on the facts of this case. No matter how reasonable is it to assume that the assessee will make these profits, these profits cannot be brought to tax at this stage. That is what the legal position, for the detailed reasons set out above, is.

20. In our considered view, therefore, the authorities below indeed erred in bringing to tax the anticipated business profits on assessee's entering into a development agreement with Menorah Realities Pvt Ltd in respect of the land held by the assessee as stock in trade. The impugned addition of Rs RS.17,28,81,276 is thus deleted."

15. The Appellant begs to place reliance on the decision of the Hon'ble Supreme Court in the case of Malabar Industrial Co. Ltd. vs. CIT (2000) 243 ITR 83 (SC), wherein it has been held that the CIT cannot exercise jurisdiction u/s. 263 of the Act until and unless the assessment sought to be revised is erroneous and prejudicial to the interest of revenue and both the conditions should co-exist together and if any of the conditions is absent, then the Provisions of section 263 are not applicable.

16. The Appellant submits that the Ld. PCIT has exercised the Jurisdiction without the authority of law. He has held that the Capital gains arising on account of transfer of Stock-in-trade is chargeable to tax in the previous year in which the Capital Asset was transferred mainly based on the ground that the Appellant has been following the Mercantile System of Accounting, without appreciating the fact that the Appellant has transferred the Stock-in-trade and not the Capital Asset as such and therefore the Appellant is not liable to Capital Gain Tax. The Ld. PCIT has held that the consideration in the form of Built up area equivalent to 61 % of land transferred was not brought to tax. In this regard the Appellant submits that the Commissioner's Finding is not in accordance with law since the deemed provision of section 2(47)(v) is not applicable to the transfer of Stock-in-trade and

Therefore what is assessable to tax is the income earned on sale of stock-in-trade under the head Income from Profits and Gains of the Business and hence the Charging of Capital Gain Tax is not exigible to tax in the absence of transfer of Capital Asset. .

17. The Ld. PC IT has directed the AO to examine the Developmental expenditure incurred amounting to Rs. 1,27,35,000/- for improvement of the Land which does not form part of the Show cause Notice dtd: 10-01-2018 issued by the Ld. PCIT and therefore the Appellant did not have the opportunity to file objections in this regard. The findings of the Pr.CIT are opposed to the principles of natural Justice and therefore the Ld. PCIT has erred in giving directions to the AO for causing enquires.

18. The Ld. PCIT has held that the AO has omitted to bring to tax the deemed rent of 2 unsold flats relating to the Joint Development Agreement with M/s. D.M. Builders relating to the land situated at Jinkethimannahalli Bangalore. In this regard the Appellant submits that in view of the JDA with the above Builders he was entitled for 24 flats out of which 22 flats were sold in the construction stage in the year 2012-13 and 2 flats were left unsold. The Appellant has filed his objection that the Notional Rent in respect of 2 unsold flats is not applicable for the A.Y 2013-14 since a New Section 23(5) was introduced w.e.f 01-04-2018 and therefore the Ld. PCIT was, not justified to give directions to the AO to bring to tax the notional rent of 2 unsold flats. The objections filed by the Appellant were rejected by the Ld. PCIT on the ground that the New Section 23(5) was clarificatory in nature which is incorrect since the provision applicable w.e.f 01-04-2018. On this count also the order passed u/s. 263 of the Act was not justifiable.

19. Without prejudice to the above submissions the Appellant submits that he has offered the Business Income arising out of the transfer of Stock-in-trade on sale of flats in the A.Y 2016-17' and therefore in the guise of implementation of Order u/s. 263, the same -income cannot be subjected to tax twice for the A.Y 2013-14 and also ~. v 2016-17 which is opposed to the principles of Taxation. In this regard the Appellant begs to place reliance on the decision of the Hon'ble Madhya Pradesh High Court in the case of Smt Daya Bai vs. CIT 154 ITR 248 (MP).

Under these facts and circumstances the Appellant respectfully prays that your Hon'ble Authority be pleased to pass orders cancelling the Order u/s. 263 of the Act dtd: 20-03-2018 passed by the Ld. PCIT, Kurnool in the interest of equity and justice”.

8. The written submissions of the learned DR are as under:

“1. Assessee along with his brother Shri Sitaram Babu purchased 24960 Sq. Feet of land and in Survey no. 16, Anantapura Village, Bangalore dated 07.09.2011. This land was held as Capital asset and on 31.03.2012 it was converted by the Assessee as Stock-in-Trade in his books of account for the F.Y. 2012-13.

2. On 16.05.2012, the Assessee and his brother entered into Joint Development Agreement with M/ s Sai Developers, Bangalore in which the Assessee and his brother entitled for 39 per cent of undivided share of land, super built up area and car parking. The remaining 61 per cent of undivided share of land of the developer i.e. M/ s Sai Developers, Bangalore were entitled to share.

3. The facts of the case are that Assessee entered into JDA with M/s Sai Developers on 16.05.2012. As per the JDA the Assessee and his brother were entitled to 39% of built up area and the developer was entitled to 61% of the built up area. This land was purchased by Assessee along with his brother on 25.08.2010, this asset was held by Assessee as capital asset and in the F.Y. 2012-13 the Assessee converted this capital asset into stock trade and then entered into JDA. Hence as per provisions of sec 45(2) the Assessee is liable for capital gains on the conversion of the capital asset into stock in trade in the year in which such stock in trade is sold or otherwise transferred.

4. In this case of Assessee the converted stock in trade got divided into two parts 61% of stock transferred to builder and 39% held by the Assessee. The question is when is the income in respect of these two parts to be taxed.

5. In respect of stock of 39% the income is to be taxed in the year in which Assessee sells or otherwise transfers such stock in trade, in the present case the sale of such stock (land along with the built up area) happened in A.Y. 2016-17 and hence income is offered in A.Y. 2016-17.

6. Now the question is when is the balance 61 % of land sold or otherwise transferred and when is the income to be recognized.

7. As per the Audit report filed with ROI for A.Y. 2013-14 the Assessee is following mercantile system of accounting. The question that arises is whether income is to be taxed in the year in which the Assessee received the 39% constructed area in lieu of 61% of land transferred/sold to

builder, i.e., A.Y. 2016-17, if this is accepted the same will defeat the system of accounting followed by the Assessee as this will be cash system of accounting i.e., taxing the income in the year in which the sale consideration is received and not in the year the asset is sold on credit. As per provisions of Act, the AO cannot change the system of accounting consistently followed by Assessee. As per the Audit report the Assessee is following mercantile system of accounting. Hence as per accounting standards and as per sale of goods act (which is applicable to Assessee as Assessee has sold stock in trade) the income from sale of goods is to be recognized in the year when the significant 'risk and reward' pertaining to the stock is transferred.

8. The next question that arises in this case is when is the risks and reward in respect of 61 % of stock transferred, was it in A.Y. 2013-14 or was it in A.Y. 2016-17. As per the JDA dated 16.05.2012 para 13 which is reproduced as under.

'The Owners shall on the execution of this Agreement and registration of Joint Development Agreement and payment mentioned in Clauses below grant a specific Power of Attorney in favour of the Promoter or its nominees, empowering to proceed with obtaining of Licences, Plans, consents and in regard to the Building/ s to be constructed on the Schedule Property and authorizing the Promoter to represent before all and any of the Statutory Authorities and General Power of Attorney to sell Promoter's share;

The said power of Attorneys mentioned in clauses above, shall be duly registered before the jurisdictional Sub-Registrar. The Owner agrees not to revoke the said Power of Attorneys till the sale of the Promoter's 61 % (sixty one percent) share in the Schedule Property. '

The Owners shall sign and execute necessary applications, papers, documents and do all acts, deeds and things as the Promoter may lawfully require to obtain any licences, Plan, and consents as well as to and in order to legally and effectively vest in the Promoter's nominee/ s title to the undivided 61 % (sixty one percent) share in the Schedule Property. '

9. On execution of the JDA and registration of JDA and payment mentioned in JDA the Assessee was required to give a general power of attorney to promoter to sell its share. Further the Assessee cannot revoke the said power of attorney till the sale of promoters 61 % share in scheduled property and the JDA further in para 13.3 states that Assessee will sign and execute necessary documents,

papers in order to legally & effectively vest in the promoters nominees title to the undivided share in schedule property. (The scheduled property is the stock in trade created by Assessee on conversion of the capital assessment.)

10. Hence in view of the clauses in JDA the risk and reward of stock of 61 % became the ownership of the promoter from the date of JDA. The only other issue that could still give Assessee the ownership over stock was cancellation of JDSA or nonperformance by promoter as per terms of JDA.

11. It is important to verify what is the relief available either on cancellation or breach of terms of JDA.

12. As per para 16. 1 the only relief available is to insist the other party for 'specific performance' of terms of JDA and recover costs. So even if there is breach or cancellation the other party can only insist on specific performance and there is no clause to take back the possession of stock, hence the above clearly indicate the risk and reward in 61 % of stock was transferred to the promoter on the date of JDA, i.e., 16.05.2012 and the income as per mercantile system of accounting is to be taxed in A.Y. 2013-14 which is direction issued by the Pr. CIT, Kurnool in the 263 order, hence the Hon'ble ITAT should be requested to uphold the order U/s 263 passed by the Pr. CIT, Kurnool vide order dated 20.03.2018.

Long term capital gain

13. It is only reference to this property long-term capital gain calculated by the Assessing Officer on this issue. Since, this property has already converted into stock in trade, it was taken as a business income. However, no business income was calculated for the stock in the case of Anantapura property.

Short term capital gain

14. The assessee has purchased converted land on 7.9.2011 and the said land was held as capital asset as on 31.3.2012. Later on, the assessee has converted the same as stock in trade in the books of accounts in the financial year 2012-13.

14.1 On verification of the computation of income, the assessee has not offered any short term capital gain on this land.

14.2 The assessee's share of short term capital gain arising out of the conversion of land from the capital asset to stock in trade should be brought to tax under the provisions of sec. 45(2) of the Act.

14.3 Further, the assessee's share of business income accruing on account of 39% of the super built up area, car parking receivable in lieu of transfer of 61 % of the land to the developer should also be brought to tax in the A.Y. 2013-14.

14.4 In any of the computation of income filed by the assessee during the course of assessment proceedings, the assessee has not offered any short term capital gain on the converted agricultural land in to stock in trade.

15. The whole issue is with regard to land situated at Survey No. 16, Anantapura Village, Karnataka but not the other lands owned by the assessee. The STCG arising/ accruing in the hands of the assessee and his brother on account of JDA entered into with M/s. Sri Sai Developers should have been worked out based on the fair market value of 61 % share of land transferred to the developer.

Conclusion:

16. Short-term capital gain has been only in the case of Anantapura property, which was not reflected in the return filed by the appellant nor brought to the books regarding the conversion of the land in stock in trade on 02.05.2012. The Pr. Commissioner of Income Tax invoked 263 order for this purpose for calculating:

- a. Short-term capital gain in terms of conversion into stock in trade of Anantapura property.
- b. Business income in assessing out of alienation of stock in trade and other on development agreement during the Financial Year.

17. Since the Assessing Officer has not verified this fact while completing the assessment order, the order passed u/s. 143(3) dtd. 31.3.2016 is held erroneous and prejudicial to the interest of the revenue.

18. Therefore, the Pr. CIT has rightly invoked the provisions of sec. 264 and thereby directed the AO to verify the above aspects in detail”.

9. Having regard to the rival contentions and the material on record, our findings are as under.

10. An order u/s 263 is sustainable only if the assessment order is both erroneous as well as prejudicial to the interest of the

Revenue. In the present case, in order to determine whether the assessment order was erroneous and also prejudicial to the interests of the Revenue, we are of the opinion that the following questions need to be answered.

(i) The first objection taken by the assessee is that the assessment order was a protective assessment, therefore, it cannot be revised u/s 263 of the Act. The AO in the assessment order u/s 143(3) of the Act, after determining the taxable income has held that “since the substantive demand is less than the admitted income, the entire payment is kept in abeyance as protective assessment”. This observation of the AO is relied upon by the learned Counsel for the assessee to submit that the assessment was a protective assessment. He placed reliance upon various case law to submit that the protective assessment without a corresponding substantive assessment is not sustainable. We are, however, not inclined to accept or adjudicate this contention of the assessee at this stage for the simple reason that the said question is pending adjudication before the CIT(A) and if it is held to be not sustainable, then the order u/s 263 also would not be sustainable as the very basis would have been knocked down. Therefore, it cannot be said that the assessment itself is a protective assessment. Therefore, the first objection of the assessee is not adjudicated at this stage.

11. The next question for determination is, whether the assessment order u/s 143(3) of the Act can be said to be erroneous. The three grounds on which the order has been held to be erroneous by the CIT are being dealt with as under:

a) According to the CIT, the capital gain has arisen in the relevant A.Y because the assessee has entered into a joint development agreement (JDA) with M/s. Sri Sai Developers to develop the land which has been converted from capital asset into stock in trade during the relevant financial year. As per section 45(2) of the I.T. Act, where a capital asset is converted into stock in trade, the capital gain would be taxable in the year in which the stock in trade is transferred. Undisputedly, the joint development agreement has been entered into in the relevant financial year. The learned Counsel for the assessee had argued that the provisions of section 2(47)(v) are applicable only to transfer of a capital asset u/s 53A of T.P. Act. He submitted that the said provision is not applicable to stock-in-trade which can be considered as transferred only when it is sold. In support of this contention, he placed reliance upon the decision of the Coordinate Bench of this Tribunal in the case of Smt. Girija Rani in ITA No.165/Hyd/2017 wherein the Tribunal after considering the issue, (at para 4) has held as under:

“4. Having regard to the rival contentions and material on record, we find that the land in issue was treated by the assessee as her stock-in-trade and during the relevant financial year, she entered into the development agreement-cum-GPA with M/s. Ramky Estates & Farms Ltd.,. Therefore, the assessee entered into a business agreement for development of her piece of land. The year in which conversion of capital asset into stock-in-trade has taken place is not known nor is it the year before us. Where any capital asset is converted in to stock-in-trade, the income would arise U/s 45(2) of the Act only in the year when the stock-in-trade is transferred/sold by the assessee. There is no doubt that during the relevant financial year, the assessee has entered into a development agreement only by contributing the land as her share of capital, while the developer was to invest in construction of the villas. The income would arise to the assessee only when the assessee sells her stock-in-trade but not when she contributes her stock-in-trade as her share of capital. Therefore, as rightly pointed out by the CIT(A), no gains have arisen to the assessee during the year by entering into the JDA dated 10-05-2012 with M/s. Ramky Estates &

Farms Ltd., much less on accrual basis. Therefore, we see no reason to interfere with the order of the CIT(A) which is in consonance with the legal provisions on the issue. Accordingly, the grounds of the Revenue are dismissed”.

12. Further, the Coordinate Bench at Bangalore in the case of Dheeraj Amin vs. ACIT in ITA No.1709/Bang/2013 at Para 19 has held as under:

“What the assessee has got today is only a right to sell the 1,28,940.26 fts of constructed area in the Alexandria project and the profits, howsoever certain they may appear to be, will only fructify and be realized, and can even be quantified, only when this right is exercised – in part or in full. That stage has not yet come, and until that stage comes, in our considered view, such profit cannot be taxed. Unlike in a case of a capital gain which arises on parting the capital asset at the first stage itself, it is a case of business transaction which is completed when the rights so acquired by the assessee are exercised; none can make profits by dealing with himself, as is the settled legal position in the light of the settled legal position in the case of Sri Kikabhai Premchand vs. CIT (1953) 24 ITR 506 (SC). It is for this reason that we are unable to uphold the action of the authorities below on the facts of this case. No matter how reasonable is it to assume that the assessee will make these profits, these profits cannot be brought to tax at this stage. That is what the legal position, for the detailed reasons set out above is”.

13. The Hon'ble Karnataka High Court in the case of Wipro Ltd vs. DCIT (2016) 382 ITR 179 (Kar.) has also considered similar issue at page 6 of its order and held as under:

“136. Section 45(1) deals with profits or gains arising from the transfer of a capital asset. Therefore, it does not deal with transfer of a business asset or a stock in trade. It provides that the profits and gains arising from the transfer of the capital asset shall be chargeable to income tax under the head 'capital gains' and shall be deemed to be the income of the previous year in which the transfer took place. It is here that the definition of transfer under Section 2(47) assumes importance. The definition of transfer contemplated in the provision is only in relation to the capital asset and not in relation to the stock in trade or a business asset. However, sub-section (2) contains a non-obstante clause by saying not withstanding anything contained in sub-section (1), the profits or

gains arising from the transfer by way of conversion by the owner of a capital asset into or its treatment by him as stock in trade of business carried on by him shall be chargeable to income tax as his income of the previous year in which such stock in trade is sold or otherwise transferred by him. Therefore, in so far as stock in trade is concerned, the relevant year in which the capital gain tax is leviable is the previous year in which such stock in trade is sold. The word used is sold or otherwise transferred by him. In view of the expressed words used in Section 45(2), it is clear that Section 45(1) deals with capital gains on transfer of capital asset, Section 45(2) deals with payment of capital gains in a transaction where stock in trade is sold or otherwise transferred by him.

137. Under Sec. 45(1), the capital gains are chargeable to income tax of the previous year in which the transfer took place. The said transfer may be in any one of the modes prescribed under Sec. 2(47). It need not necessarily be by way of sale, exchange or relinquishment of the asset as evidenced by registered documents. It can be in any one of the modes contemplated in clause (i) to (vi) of Sec. 2(47). However, when it comes to levying of capital gains under sub-sec.(2) of Sec. 45, it deals with capital asset converted by the owner thereof into, or is treated by him as stock-in-trade of a business carried on by him as contemplated under Sec. 2(47)(iv). Once such capital asset which is converted as stock-in-trade is sold, it is also subjected to capital gains, but the said capital gains is chargeable to income tax in the previous year in which such stock-in-trade is sold. The word used is sold, not transferred. However, if the stock-in-trade is not sold, but is transferred otherwise, which has the effect of a sale, then the capital gains is chargeable to income tax in the previous year in which such stock-in-trade is otherwise transferred. Having regard to the scheme of the entire section and the express words used in sub-section (2) of Sec. 45, the case of considering stock-in-trade otherwise transferred, would arise only if stock-in-trade is not sold. If stock-in-trade is sold, the question of considering whether the stock-in-trade is otherwise transferred would not arise for consideration. The object of using the words 'otherwise transferred' as it is in the other provisions in the same section is to prevent avoidance of payment of capital gains by the owners thereof by resorting to modes which are not recognized in law, but which in substance has the same effect. In other words, if the owner by such transfer ceases to have any interest in the property and transfers all his interest in the property to the transferee and earns profits and gains, but declines to pay the capital gain, on the ground that such transfer is not one such transfer recognized in law, then the law in such cases to plug the loop hole has used the term otherwise transferred. Once it is sold, the question of considering whether it has been otherwise transferred would not arise.

138. In the instant case, the assessee entered into an agreement with M/s.Prestige Estates Pvt. Ltd. on 09-02-2000 to sell the aforesaid property for a sum of Rupees twelve crores fifty thousand. Clause (6) of the said agreement provides that, as desired by the

purchasers, in order to enable the purchasers to process with the preparation of the plan, sanction and other orders required for commencement of the construction in the schedule property, the vendors have this day executed a power of attorney in favour of the purchasers and their nominees to enable them to secure appropriate clearance and other sanctions as detailed therein which shall be valid till completion of sale in terms of this business. Further, it stated anything contained herein shall on delivery of possession of the said property or empower the purchasers to claim any prospective rights in the schedule property. In the power of attorney executed, there is no whisper of delivery of possession of the schedule property to the power of attorney holder. Under Sec. 2(47), any transaction involving the allowing of possession of immovable property be taken or retained in part performance of a contract of the nature referred to in Sec. 53A of the Transfer of Property Act is a deemed transfer in relation to a capital asset. Therefore even if the stock-in-trade which was prior to its conversion a capital asset, as treated by the Tribunal as a capital asset, as possession is not delivered, it would not become a transfer and question of payment of capital gains would not arise.

139. *The CBDT Circular No. 495 dt. 22-09-87 which came into effect from 01-04-1988 explains the purpose of sub- clause (vi) of Sec. 2(47) in these following words : pg. 129*

"the newly inserted sub-clause (6) of Sec.2(47) has brought into the ambit of transfer, the practice of enjoyment of property rights though words commonly known as power of attorney arrangement. The practice in such cases is adopted normally where transfer of ownership is not legally permitted. A person holding the power of attorney is authorized the power of owner, including that of making construction. The legal ownership in such case continues to be with the transferor. Therefore, with that object and in respect of such persons, clause (vi) was inserted which reads as under :

2(47)(vi) any transaction (whether by way of becoming a member of, or acquiring shares in, a cooperative society, company of other association of persons or by way of any agreement or any arrangement or in any other manner whatsoever) which has the effect of transferring, or enabling the enjoyment of any immovable property."

140. *Therefore, any transaction which has the effect of transferring or enabling the enjoyment of any immovable property is deemed to be a transfer under Sec.2(47). The Apex Court in the case of Suraj Lamp & Industries (P.) Ltd. v. State of Haryana [2012] 340 ITR 1/[2011] 202 Taxman 607/14 taxmann.com 103 explaining the scope of power of attorney has held as under :*

"a power of attorney is not an instrument of transfer in regard to any right, title or interest in an immovable property. A power of attorney is creation of an agency whereby the grantor authorises the grantee to do the acts specified therein, on behalf of grantor, which when executed will be binding on the grantor as if done by him (Sec. 1A

and 2 of Power of Attorney Act, 1882). It is revocable or terminable at any time unless it is made irrevocable in a manner known to law. Even an irrevocable attorney does not have the effect of transferring title to the grantee."

141. *In State of Rajasthan v. Basant Nahata [2005] 12 SCC 77, the Court held as follows :*

"A grant of power of attorney is essentially governed by Chapter X of the Indian Contract Act. By reason of a deed of power of attorney, an agent is formally appointed to act for the principal in one transaction or a series of transactions or to manage the affairs of the principal generally conferring necessary authority upon another person. A deed of power of attorney is executed by the principal in favour of the agent. The agent derives a right to use his name and all acts, deeds and things done by him and subject to the limitations contained in the said deed, the same shall be read as if done by the donor. A power of attorney is as is well known, a document of convenience".

142. *A deed of power of attorney is executed by the principal in favour of the agent. The agent derives a right to use his name and all acts, deeds and things done by him and subject to the limitations contained in the said deed, the same shall be read as if done by the principal. A power of attorney is a document of convenience. A power of attorney is not an instrument of transfer in regard to any right, title or interest in an immovable property. It is revocable or terminable at any time unless it is made irrevocable in a manner known to law.*

143. *Therefore even if Section 2(47) is held to be applicable to a stock-in-trade, unless the transaction in question has the effect of transferring or enabling the enjoyment of any immovable property, it would not amount to a transfer.*

144. *In the instant case, assessee executed a power of attorney after entering into an agreement of sale for the purposes mentioned therein. It is in pursuance of the power so conferred, coupled with the terms of the agreement of sale, the power of attorney holder has to develop the property, identify the purchasers and sell the undivided share of land as well as the built area to such purchasers. Neither in the agreement of sale nor in the power of attorney, possession of the property was given to him. Having regard to the terms of the power of attorney, the intention of the assessee was not a transfer of the right in a schedule property in favour of his agent nor was he permitted to enjoy the immovable property. Therefore the case would not fall under Sec. 2(47)(vi). The assessee though executed a power of attorney, received the entire consideration under the agreement and acknowledged the same in the books of account and showed it in the balance sheet, that by itself did not confer the power of transferring the stock-in-trade in favour of the power of attorney holder or in favour of the purchasers unless he has executed the sale deed on behalf of the purchasers. Therefore, in view of sec. 45(2) of the Act, the capital gains is not chargeable on*

receipt of the consideration in the year in which that consideration was received under Sec. 45(2). The income tax is charged in the previous year in which such stock-in-trade is sold. Sale took place in the assessment year 2004-05 and 2005-06. The power of attorney had been executed in assessment year 2001-02. When stock-in-trade is sold by executing a deed for conveyance and duly registered, the question of the said stock-in-trade being otherwise transferred would not arise at all. Therefore, the argument of the Revenue, that on the day the power of attorney was executed when the entire consideration due under the agreement of sale was received and by virtue of the power of attorney, the power of attorney holder is authorized to develop the property, to sell the property and to receive the entire consideration, it amounts to the stock-in-trade being otherwise transferred leading to the said income being chargeable to income tax in the previous year in which the power of attorney is executed is without any substance. As the stock-in-trade is sold by way of a registered deed, there is no intention to avoid payment of capital gains. On receipt of such capital gains, the capital gain tax has been paid in the previous year in which the stock-in-trade was sold and therefore the order of the Tribunal as well as the order of the assessing authority is contrary to the aforesaid statutory provisions. As such, it is unsustainable in law. Accordingly, the said two orders are set aside. The order passed by the Appellate Commissioner is restored”.

14. From the above judgments, it is clear that the stock-in-trade can be considered as transferred only in the year in which the assessee has executed the sale deed transferring the stock-in-trade and not when the assessee has given stock-in-trade for joint development to the builder. As already held in the above cases, the provisions of section 2(47)(v) would apply only to the capital asset and not to stock-in-trade. All the judgments relied upon by the learned DR which are filed in the form of Paper Book, relate to the power of the CIT to pass order u/s 263 wherein the AO has not made proper inquiry before completing the assessment. In the cases of P.T. Laskhani Ram, reported in 272 ITR 309, the Hon'ble Allahabad High Court was dealing with the powers of the CIT u/s 263, where the AO failed to make necessary inquiries and it was held that the CIT was well within his

jurisdiction in passing order u/s 263 based on record of assessment. Similar view has been expressed in the cases of CIT, Patiala vs. Himachal Pradesh Financial Corpn, reported in (2010) 186 Taxmann 10J (HP), Duggal & Co. vs. CIT, reported in (1996) 220 ITR 456 (Del.), CIT vs. South India Shipping Corpn. Ltd reported in (1998) 233 mITR 546 (Mad.), CIT vs. Deepak Kumar Garg; (2008) 299 ITR 435 (MP), CIT vs. Sanil Goyal, reported in (2009) 176 Taxmann 184 (Uttaranchal); CIT vs. Andhra Civil Constructions Ltd (2003) 216 ITR 461 (Madc); etc. In the case before us, even if it is considered that the AO has not made any enquiries and the CIT is justified in holding the assessment order to be erroneous, we find that the stock-in-trade cannot be considered as transferred in the relevant financial year and therefore, the assessment order cannot be considered to be prejudicial to the interest of the Revenue. Therefore, since of the twin conditions for initiating and also passing of an order u/s 263 is not satisfied and the first ground on which the assessment order has been revised is not sustainable, the CIT order u/s 263 has to be set aside on this ground alone. Further, since we have held that the stock-in-trade is not transferred in the relevant financial year, the business income on accrual basis also cannot be brought to tax in the relevant A.Y.

15. The second reason for the CIT exercising the jurisdiction u/s 263 is that the assessee has received flats from M/s. D.M. Builders and that the assessee has not offered the income from house property from the said flats. On this ground, we find that the assessee's contention that it has received 24 flats out of which 22 flats were sold at the construction stage itself in

the year 2013 and 2 flats were left unsold and that the notional interest on the two unsold flats can be brought to tax only w.e.f. 1/4/2018 and not during the relevant financial year, is not without any substance because the said provision has been introduced by the Finance Act, 2017 and it is settled in law that any liability can only be prospective and cannot be applied retrospectively. Therefore, when the assessment order was passed on 31.03.2016 when the relevant provision has not even been brought into statute book. The AO cannot be expected to apply the same. Therefore, on this account also, the assessment order cannot be said to be erroneous and prejudicial to the interest of the Revenue. Therefore, we set aside the order of the CIT u/s 263 of the Act.

16. In the result, assessee's appeal is allowed.

Order pronounced in the Open Court on 12th April, 2019.

Sd/-
(S.Rifaur Rahman)
Accountant Member

Sd/-
(P. Madhavi Devi)
Judicial Member

Hyderabad, dated 12th April, 2019.

Vinodan/sps

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- 6 Guard File

By Order