IN THE INCOME TAX APPELLATE TRIBUNAL
LUCKNOW BENCH "B", LUCKNOW

BEFORE SHRI SUNIL KUMAR YADAV, JUDICIAL MEMBER
AND SHRI. A. K. GARODIA, ACCOUNTANT MEMBER

ITA No.61/LKW/2012
Assessment Year:2004-05

Asstt. CIT Range VI Lucknow	v.	M/s Upper India Paper Mills Company Pvt. Ltd. Nishatganj, Lucknow
		TAN/PAN:AAVCT5709M
(Appellant)		(Respondent)

C.O. No.18/LKW/2012
[Arising out of ITA No.61/LKW/2012]
Assessment Year:2004-05

M/s Upper India Paper Mills Company Pvt. Ltd. Nishatganj, Lucknow	v.	Asstt. CIT Range VI Lucknow
TAN/PAN:AAVCT5709M		
(Appellant)		(Respondent)

ITA No.62/LKW/2012
Assessment Year:2008-09

Asstt. CIT Range VI Lucknow	v.	M/s Upper India Paper Mills Company Pvt. Ltd. Nishatganj, Lucknow
		TAN/PAN:AAVCT5709M
(Appellant)		(Respondent)

C.O. No.19/LKW/2012
[Arising out of ITA No.62/LKW/2012]
Assessment Year:2008-09

M/s Upper India Paper Mills Company Pvt. Ltd. Nishatganj, Lucknow	v.	Asstt. CIT Range VI Lucknow
TAN/PAN:AAVCT5709M		
(Appellant)		(Respondent)

ITA No.301/LKW/2013

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Assessment Year:2009-10

DCIT Range VI Lucknow	v.	M/s Upper India Couper Paper Mills Company Pvt. Ltd. Near Metro City, Nishatganj, Lucknow
		TAN/PAN:AACCT7347N
(Appellant)		(Respondent)

C.O. No.19/LKW/2013
[Arising out of ITA No.301/LKW/2013]
Assessment Year:2009-10

M/s Upper India Couper Paper Mills Company Pvt. Ltd. Near Metro City, Nishatganj, Lucknow	v.	Asstt. CIT Range VI Lucknow
TAN/PAN:AACCT7347N		
(Appellant)		(Respondent)

Department by:	Shri. Punit Kumar, D.R.		
Assessee by:	Shri. Yogesh Agrawal, Advocate		
Date of hearing:	31	03	2015
Date of pronouncement:	23	06	2015

ORDER

PER SUNIL KUMAR YADAV:

These appeals are preferred by the Revenue against the respective orders of the ld. CIT(A). The assessees have also filed cross objections in support of the orders of the ld. CIT(A).

1. Since these appeals and cross objections were heard together, these are being disposed of through this consolidated order. We, however, prefer to adjudicate them one after the other.

I.T.A. No. 61/LKW/2012 & C.O. No.18/LKW/2012:

2. The Revenue has assailed the order of the ld. CIT(A), inter alia, on the following grounds:-

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1. The CIT(A) has erred in law and on facts of the case in falling to appreciate that by entering into a project development agreement during the year with a builder, the assessee has transferred this land and was thus liable to capital gains during the year under consideration.
2. The C1T(A) has also erred in in law and also in facts of he case in failing to appreciate that as per agreement with the builder the consideration for the transfer of the land had also been settled being a certain area of constructed property. As such capital gains has already arisen during the year order consideration, since section 2(47) defines 'transfer' as including 'exchange'. In the present case the assessee has exchanged unbuilt land for built up area.

3. Through the cross objection, the assessee has supported the order of the ld. CIT(A) by raising the following grounds:-

1. Because the First Appellate authority had decided the appeal on merit within the four corners of the law.
2. Because It is settled law that once the capital asset is converted its into stock in trade provisions of section 2(47)(iv) read with section 45(2) the Income Tax Act 1961 were applicable and the capital gain is taxable in the year such stock is sold or transferred.
3. Because the Project development agreement dated 26.06.2003, does not give rise to any "Transfer" for the assessment year 2004-05 within the meaning of section 45(2) of the Income Tax Act 1961.
4. Because in the subsequent assessment years orders passed u/s 143(3) of the Income Tax Act 1961 - A.Y. 2007-08 and A.Y. 2008-09 and A.Y. 2009-10, assessing authorities -the Appellant, had accepted the project development agreement

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being entered into for construction of metro city and not for transfer of land to Developers and had lawfully applied the provisions of section 45(2) of the Act on the transfer of land – stock in trade. Hence the appeal is infructuous and a frivolous attempt for double taxation.

5. Because the Ground No.2 of the Appeal No. 61/LKW-2012 totally illegal and is based on conjecture and surmises and as well as on misleading facts and wholly new facts which did not arise from the assessment order dated 28.12.2006 as well as from CIT (Appeal) order dated 05.12.2011 and which is even contradictory to itself and to the stand taken by the assessing officer in the assessment order. The concept of exchange of unbuilt land for built up area is a frivolous one and an illegal attempt to reframe the assessment order.

4. The sole controversy involved in this appeal is with regard to the assessment year in which capital gain accrued to the assessee on transfer of land initially held as capital asset into stock-in-trade and later on flats constructed thereon under project development agreement were sold to different buyers.

5. The facts in brief borne out from the record are that the assessee has entered into a project development agreement with M/s Arif Industries Ltd. to develop company's group housing-cum-shopping project on the company's land having plot area of 61299.69 sq. mtr. In the revised return filed by the assessee, long term capital loss was claimed at Rs.68,42,57,966.30. For this purpose, the land of the assessee-company was converted into stock-in-trade. The value of the land as on 1.4.2003 relevant to the financial year 2003-04, on conversion into stock-in-trade was taken at Rs.1,25,93,70,545.20. The value of the land as on 1.4.1981 was worked out at Rs.1,94,36,28,541.50 (indexed cost) on the basis of valuation reports dated 19.3.2001, 25.3.2001 and 13.6.2002 of the

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Government Approved Valuer, Shri. B.M. Gupta. The difference being Rs.68,42,57,966.30 was claimed as long term capital loss. The Assessing Officer examined the transactions of transfer of land into stock-in-trade with reference to provisions of section 2(47) of the Income-tax Act, 1961 (hereinafter called in short "the Act") and held the same to be a transfer within the meaning of section 2(47)(v) and 2(47)(vi) of the Act. Accordingly, the Assessing Officer worked out the long term capital gains at Rs.37,31,686/-. The Assessing Officer, on the basis of certain advances received by the assessee from M/s Arif Industries Ltd., concluded that conversion of the company's land into stock-in-trade and agreement with the said company constituted transfer under section 2(47) of the Act and assessed the long term capital gains as above.

6. The assessee preferred an appeal before the ld. CIT(A) with the submission that out of the advance of Rs.1.98 crores received by the assessee during the period 19.5.2003 to 31.7.2005, an amount of Rs.1.87 crores has been refunded on 2.6.2007 and only an amount of Rs.11 lakhs is available with the company as security deposit. It was contended on behalf of the assessee that there was no transfer within the provisions of section 2(47) of the Act and provisions of section 45(2) of the Act are available. It was also contended before the ld. CIT(A) that after conversion into stock-in-trade, the asset in question no longer remains a capital asset, as nothing was sold in the year and when the land was converted into stock-in-trade, one cannot go back to section 2(47) of the Act. It was further submitted that the role of section 2(47) of the Act was relevant only in the year 2003-04 for the limited purpose because section 2(47) of the Act provides that any conversion of capital asset into stock-in-trade shall be regarded as a transfer. This transfer arises in the year in which such conversion takes place and accordingly capital gain would normally arise in that very year. However, section 45(2) of the Act postpones the assessment of such capital gains to the year in which the stock-in-trade is actually sold or otherwise

transferred by the assessee. It was further contended that this stock-in-trade was sold in financial year 2007-08 relevant to the assessment year 2008-09 by the assessee in part and these facts are not disputed. Therefore, the real profit that arises on sale of stock-in-trade is business profit which assessee itself has offered for taxation in assessment year 2008-09 in consonance with the provisions of section 45(2) of the Act which only fixed the year of liability and which by fiction had already arisen on 1.4.2003 when the assessee concerted its land into stock-in-trade. He has also filed copy of the assessment order for assessment year 2008-09. Copy of the project development agreement executed on 20.6.2003 was also produced before the Assessing Officer. It was further contended before the ld. CIT(A) that the entire land belonging to the assessee-company being lease hold property and hence cannot assign or part with the possession of the demised premises without the consent of the lessor because lease rights will be expiring on 31.3.2032 and this has been clearly mentioned in clauses 2 and 3 of the project development agreement and it is further provided in clause 6 that the assessee shall get the said land converted into freehold as per Government policy at their cost and expenses subject to clause 17 of the project development agreement.

7. The ld. CIT(A) re-examined the entire claim of the assessee and being convinced with it, the ld. CIT(A) has held that capital gains on conversion of land into stock-in-trade in the financial year relevant to the impugned assessment year i.e. 2004-05 is chargeable to tax in the year in which it is sold and not in the year under consideration. Accordingly the capital gain computed by the Assessing Officer was deleted. It was also held by the ld. CIT(A) that as a corollary, the long term capital loss shown by the assessee at Rs.68,42,57,966.30 shall also not arise in the year under consideration. The relevant observations of the ld. CIT(A) are extracted hereunder for the sake of reference:-

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"6(1) I have examined the facts and circumstances of the case. The Assessing Officer assessed the long term capital gains by taking recourse to provisions of clauses (iv), (v) and (vi) of sub-section 47 of section 2 of the Act. The relevant provisions of the Act are -

(47) transfer", in relation to a capital asset, includes,-

(iv) in a case where the asset is converted by the owner thereof into, or is treated by him as, stock- in- trade of a business carried on by him, such conversion or treatment; or

(v) any transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882 1 (4 of 1882); or

(vi) any transaction (whether by way of becoming a member of, or acquiring shares in, a co�perative society, company or 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. Explanation.- For the purposes of sub- clauses (v) and (vi)," immovable property" shall have the same meaning as in clause (d) of section 269UA;]

Now the project development agreement dated 20.06.2003 needs to be examined to see whether clause (v) and (vi) of section 2(47) of the Act are applicable in which case the capital gains if it arises is to be taxed in the year under consideration and if the provisions of section 2(47)(iv) of the Act are applicable then the capital gains will be chargeable in accordance with provisions of section 45(2) of the Act.

6(2) As per the project development agreement the appellant-company is in possession of leased land bearing khasra numbers 50(P) to 54(P), 81(P) and 82(P) all situated in Poora Imam Bux, Nishatganj, Lucknow. The total area of land is 61299.69 square meters out of which 3125 square meters is in illegal encroachment and after leaving an area of 7739.3 square meters for roads etc.,

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area of 50435.39 square meters of land is available to the appellant-company for development. The appellant-company converted the said land to its stock in trade and got building plans approved from Lucknow Development Authority vide permit number 21/2009 dated 06.01.2001. The appellant-company with a view to developing a group housing scheme and shopping complex entered in to a project development agreement with a builder, M/S Arif Industries limited. The land therefore on which the project is being developed was provided by the appellant-company and the builder, M/S Arif Industries limited was obliged to commit to construction thereon. A refundable advance was also provided to the appellant-company by the builder as a security. The appellant-company gave possession of land to the builder for the purpose of executing the construction work and not in pursuance of any agreement to sale.

6(3) The entire land belonging to the assessee-company being lease hold property, and therefore the appellant-company cannot assign or part with the possession of the premises without the consent of the lessor because lease rights are expiring on 31.03.2032 and this has been clearly mentioned in the clause 2 and 3 of the project development agreement. It is further provided in clause 6 that the appellant shall get the said land converted into freehold as per government policy at cost and expenses subject to clause 17 of the project development agreement. From the development agreement aforesaid it is evident that the assessee handed over the possession of the property for construction of project by the developer. The assessee did not receive any consideration for handing over the possession of the property to the developer but as per the agreement the assessee got the right to get the built-up area. From the development agreement, the possession was handed over for carrying out the construction work by the developer and there is no other document except the development agreement which transfers the title of the property to the developer. In the absence of the transfer of the title of the property and any consideration at the time of development agreement, the handing over of the possession was merely a temporary measure for carrying out the construction work

by the developer and the exclusive possession of the property in legal sense remained with the assessee which was finally handed over at the time of execution of the sale deed of the constructed flats by the assessee. One cannot presume any intension in executing the documents between the parties other than what was stated or can be inferred reasonably from the documents itself. A regard must be given to the words used in the documents. The nature the transaction between the parties by way of development agreement cannot be said to be a sale of immovable property which is stock-in-trade or otherwise transfer as provided in the Transfer of Property Act. In the present case, the business profit arises to the assessee on the sale of the stock-in-trade only when the constructed apartments were sold and not at the time when the development agreement was entered into. Moreover, in the development agreement, the assessee has not agreed for sale of the entire constructed property on the land.

6(4) In view of the above discussion, I am of the opinion that clauses (v) and (vi) of section 2(47) of the Act have no role to play in the, transaction entered into by the assessee. The provisions of section 2(47)(iv) of the Act are clearly applicable. By assessee's own action, the asset had assumed the characteristic of stock-in-trade. As per the inclusive definition of the term "transfer" given in section 2(47) of the Act, sale is one of the several modes of transfer. Conversion of capital asset into or its treatment as stock-in-trade of the business carried on by the assessee is another mode of transfer as per the said definition. Section 45(2) of the Act acts as an exception to section 45(1) of the Act. Section 45(2) of the Act lays down as under-

Section45(2) Notwithstanding 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 a 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 and, for the purposes of section 48, the fair market value of the asset on the date of such conversion

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or treatment shall be deemed to be the full value of the consideration received or accruing as a result of the transfer of the capital asset.

6(5) Section 45(2) of the Act provides that capital gain arising on account of conversion of capital asset into or its treatment as stock-in-trade shall be chargeable to tax in the previous year in which such stock-in-trade sold or otherwise transferred. The Assessing Officer treated the transaction of handing over the possession of the land and building to the developer as transfer under section 2(47) of the Act read with section 53A of Transfer of Property Act. The provisions of Section 2(47) of the Act is applicable only in case of capital asset. As per Section 2(14) of the Act, capital asset does not include stock-in-trade. Therefore, once capital asset is converted into stock-in-trade provisions of section 2(47) of the Act becomes irrelevant and does not apply. Section 45(2) of the Act starts with a non obstante clause. Therefore, the provision of Section 45(2) of the Act supersedes all the other provisions. Under this Sub-section (2) of Section 45 of the Act, it is clear that capital gain shall be charged in the previous year in which such stock-in-trade which is known to be so only after conversion, is sold or otherwise transferred. In the instant case, the role of section 2(47) of the Act is relevant only when conversion took place. Thereafter, it has no role to play to all, because it is meant for capital asset and does not include stock-in-trade. It has been laid down in the context of Chapter XXC of the Act in the case of R Vijayalakshmi Vs Appu Hotels Ltd (2002) 257 ITR 4 that Capital gain will not accrue provided possession is handed over to developer purely as a licensee.

6(6) The Legislature in its wisdom, considering the fact that on conversion only notional income has arisen, postponed the tax liability thereon till real income was earned on that asset. In short, tax liability on the capital gain on conversion will arise in the same year in which business profit arises to the assessee on sale of such asset. The asset cannot have dual characteristic at the same point of time in the hands of the same person. This is not contemplated by any of the provisions of the Act. By assessee's own action, the asset

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had assumed the characteristic of stock-in-trade. Hence, when business profit on sale of such stock-in-trade accrues to the assessee, tax on capital gain also will be levied in the same year as is envisaged by section 45(2) of the Act. Section 45(2) of the Act fixes the year of liability. The year of liability is the year in which stock-in-trade is sold. In the instant case the conversion into stock in trade has taken place in the Financial Year 2003-04. After conversion in stock in trade, the asset in question no longer remained a capital asset. As nothing was sold in the year when the land was converted into stock in trade, one cannot go back to section 2(47) of the Act. In fact, in the instant case, the role of section 2(47) of the Act was relevant only in the year 2003-04 for the limited purpose because Section 2(47) of the Act provides that any conversion of capital assets into stock-in-trade shall be regarded as a transfer. This transfer arises in the year in which such conversion takes place and, accordingly, capital gain would normally arise in that very year. However, section 45(2) of the Act postpones the assessment of such capital gains to the year in which the stock-in-trade is actually sold or otherwise transferred by the assessee. The issue has been examined in detail by Hon'ble ITAT, Chennai bench in the case of R. Gopinath (HUF) v. ACIT [2010] 5 taxmann.com 80 (Chennai - ITAT).

6(7) It suffices to say therefore that as per section 45(2) if a capital asset is converted into stock-in-trade, the capital gain is taxable in the year such stock is sold, and the fair market value of the asset on the date of such conversion or treatment shall be deemed to be the full value of consideration received or accruing as a result of the transfer. Thus capital gain gets computed by taxability is postponed to the year of sale of such converted capital asset i.e., stock-in - trade. The provisions of section 45(2) of the Act have been given effect by the Assessing Officer in the assessment proceedings for the assessment year 2008-2009 when in the order dated 30.12.2010 passed under section 143(3) of the Act, the capital gains arising on transfer of land as stock in trade have been considered as taxable in that assessment year.

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6(8) The issue regarding capital gains on conversion of land to stock in trade was considered in the Circular: No. 791, dated 2-6-2000 which considered the question Whether the date of transfer, as referred to in section 54E of the Act, is the date of conversion of the capital asset into stock-in-trade or the date on which the stock-in-trade is sold or otherwise transferred by the assessee. The paragraph 1 of the circular lays down that -

Section 2(47) of the Income-tax Act provides that any conversion of capital assets into stock-in-trade shall be regarded as a transfer. This transfer arises in the year in which such conversion takes place and, accordingly, capital gain would normally arise in that very year. However, section 45(2) of the Act postpones the assessment of such capital gains to the year in which the stock-in-trade is actually sold or otherwise transferred by the assessee.

6(9) In view of the discussion above, I am of the opinion that the capital gains of conversion of land into stock in trade in the financial year relevant to the impugned assessment year 2004-2005 is chargeable to tax in the year in which it is sold and not in the year under consideration. The long term capital gains computed by the Assessing Officer at Rs. 37,31,686/- do not arise in the year under consideration. The long term capital gains assessed as income of the year under consideration are directed to be deleted giving consequential relief to the assessee. As a corollary, the long term capital loss shown by the assessee at Rs.68,42,57,966.30 shall also not arise in the year under consideration. The loss or gain whatsoever as per section 45(2) of the Act will be relevant in the year in which the land converted to stock in trade is sold and not in the year under consideration. The grounds of appeal are allowed."

8. Aggrieved, the Revenue has preferred an appeal before the Tribunal and placed heavy reliance upon the assessment order. The ld. D.R., Shri. Punit Kumar has also invited our attention to the project development agreement appearing at pages 1 to 41 of the compilation of the assessee and supplementary agreement appearing at pages 43 to 46 of the

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compilation of the assessee with the submission that through these agreements dated 20.6.2003, the assessee has transferred the land to M/s Arif Industries Ltd., developer after receiving substantial amount of Rs.51 lakhs. Therefore, the transfer of capital asset in the impugned assessment year i.e. assessment year 2004-05 attract the provisions of section 2(47)(v) of the Act.

9. The ld. counsel for the assessee, besides placing reliance upon the order of the ld. CIT(A), has invited our attention to the project development agreement dated 20.6.2003 with the submission that the assessee has entered into an agreement with M/s Arif Industries Ltd. to develop a major part of the land into a township as per terms of lease deed together with the Lucknow Master Plan. The Building Plan was submitted by the assessee to the Lucknow Development Authority (LDA) for sanction to construct residential towers and the sanctioned plans were released by the LDA on 8.1.2002 in respect of the residential towers. Accordingly the project development agreement was executed, in which proper description of the land was made. Since the land was obtained on lease by the assessee, it has undertaken the responsibilities to get the title cleared and make it marketable title free from all encumbrances, attachments, etc. and as per clause 6, the assessee shall get the said land converted into freehold as per the Government policy at their cost and expenses within a reasonable time required by the authorities subject to clause 17 and any unexplained delay in getting the land converted into freehold may result in suppressing the sales in turn affecting the timely completion of the project which shall be attributable to the assessee and not to the second party i.e. M/s Arif Industries Ltd.

10. As per clause 7, the assessee was responsible to get the project plans approved from the LDA in two phases and whatever expenses are incurred in getting the plan sanctioned with the authorities, the first party would be responsible to bear with it. He has also invited our attention to

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clause 12 of this project development agreement, according to which construction and development of the building earmarked for religious purposes will be carried out by the first party i.e. the assessee at their cost and expenses. It was also clarified that the assessee will get the same simultaneously constructed and completed for the purpose of obtaining completion certificate from the competent authority. The ld. counsel for the assessee has also invited our attention to clause 15 of the project development agreement, according to which the first party i.e. the assessee would get 1/3rd portion in each of the residential towers (floor-wise) commercial shopping, garages, parking stilts, open parking, value added facilities, educational school building, clubs, swimming pool, etc. and rest of the portion would be taken by the second party i.e. M/s Arif Industries Ltd. Besides, 10 shops already constructed by the first party would exclusively belong to the first party. He has also invited our attention to clause 1, according to which second party i.e. M/s Arif Industries Ltd. has given a sum of Rs.11 lakhs as interest free refundable amount to the first party through cheque. Through supplementary agreement dated 20.6.2003, the assessee has also received Rs.40 lakhs on different dates. The object of giving advance to the assessee was to meet the expenses to be incurred at different places and also for getting the said land converted into freehold and depositing various charges and fee as per clause 9 to the concerned authorities. He has invited our attention to clause 18 of project development agreement, according to which interest free advances received by the assessee were to be refunded at different stages. Therefore, the assessee has not received any consideration against transfer of land to the second party.

11. The ld. counsel for the assessee has further contended that as per clause 27 of the project development agreement, the assessee has handed over the possession of the vacant part of the said land to the second party at the time of signing of the agreement for project development work. The

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second party shall commence the construction of the building as soon as the revised plans are sanctioned by the LDA. The first party has also agreed to get the balance part of the said land vacated at the cost and expenses within one year or so from the date of this agreement and simultaneously handover the possession to the second party. In case of delay in getting the said land vacated by the first party and for handing of over the possession of the same to the second party, the resultant delay in construction and development would be solely attributable to the first party i.e. the assessee. Therefore, there is no absolute transfer of possession to the second party i.e. M/s Arif Industries Ltd. as per clause 18 of the project development agreement. The ld. counsel for the assessee has further contended that in the light of this project development agreement, the impugned land was never transferred in view of the provisions of section 2(47)(v) of the Act. Therefore, the capital gain cannot be computed in the impugned assessment year i.e. 2004-05. It can only be assessed in the year in which constructed portion of the project/flat was sold to different buyers and the assessee has already offered capital gain in those assessment years 2008-09. Copy of the assessment order is placed on record. The business profit on sale of stock-in-trade was also offered to tax in the same assessment year i.e. 2008-09 in consonance with provisions of section 45(2) of the Act. He has also invited our attention to the CBDT Circular No.719 in support of his contention. The ld. counsel for the assessee has also placed reliance upon the following judgments:-

1. Chaturbhuj Dwarkadas Kapadia vs. CIT, 260 ITR 491 (Bombay).
2. CIT vs. K. Jeelani Basha, 256 ITR 282 (Madras).
3. R. Vijayalakshmi vs. Appu Hotels Ltd. and Others, 257 ITR 4 (Madras).
4. R. Gopinath(HUF) vs. ACIT, 133 TTJ 595 (Chennai).

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5. DCIT vs. Crest Hotels Ltd., 78 ITD 213.
6. Shri. Ramesh Abaji Walavalkar, Thane vs. ACIT, Thane, I.T.A. No. 852/Mum/2009 and 1534/Mum/2010.

12. Having carefully examined the orders of the lower authorities in the light of the project development agreement, other documents placed on record and the rival submissions, we find that undisputedly the assessee has transferred its capital asset in the form of land to the stock-in-trade and there is no quarrel on this aspect. The assessee has entered into a project development agreement with M/s Arif Industries Ltd. for construction of commercial and residential tower. Accordingly, the project development agreement was executed stipulating certain terms and conditions, according to which construction is to be undertaken by the developer i.e. the second party, M/s Arif Industries Ltd. The first party i.e. assessee has to handover possession to the second party for construction of the residential towers, shops and garage etc. and after construction, the constructed portion is to be divided amongst the parties as per clause 15 of the project development agreement. During the course of construction activities, the assessee was also required to get the religious building constructed at its own cost and expenses. It is also an undisputed fact that the land in question was obtained on lease and the remaining term of lease was about 28 years and 9 months expiring on 31.3.2032. It was the responsibility of the assessee to get the said land converted into freehold as per Government policies at their own cast and expenses within a reasonable time by depositing various charges etc. to the concerned authorities as per clause 7 of the project development agreement. No doubt, the assessee has received a sum of Rs.51 lakhs from the second party i.e. M/s Arif Industries Ltd., but as per clause 17, this amount was received as interest free refundable amount through cheque from the first party. Thereafter the assessee was to receive certain more amount as per

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clause 1 of the supplementary agreement. But as per clause 2 of the supplementary agreement, the entire amount of advance of Rs.300 lakhs is to be refunded at different stages specified in clause 18 of the project development agreement. Therefore, it is clear from the different clauses of the agreement that whatever amount was received by the assessee from M/s Arif Industries Ltd., it was simply interest free advance to meet certain expenses to be incurred in getting the land converted into freehold and also for construction of building for the religious purposes. It is also evident from this agreement that possession of the entire land was not given to the developer, M/s Arif Industries Ltd. for construction, as some portion of the land was occupied by different persons and the assessee has undertaken the responsibility to get it vacated and thereafter vacant portion would be given to the second party for construction. For the sake of reference, we extract the relevant clauses of the project development agreement and supplementary project development agreement as under:-

> CLAUSE No.2,6,12,15 to 18 and 27 OF THE PROJECT DEVELOPMENT AGREEMENT
>
> *"2. THAT the subject matter of this agreement is the Nazul lease hold land with a remaining term of about 28 years and 9 months expiring on 31.03.2032 bearing Khasra Nos.50 (P), 51 (P), 52 (P), 53 (P), 54(P), 81(P) and 82(P) all situated adjacent to Chakkar Ka Purwa facing Baba Ka Purwa, Poora Imam Bux, Lucknow having a nett area of 50435.39 Sq. Mtrs. herein referred to as THE SAID LAND.*
>
> *6. THAT THE FIRST PARTY shall get THE SAID LAND converted into FREEHOLD as per the Government policy at their cost and expenses within a reasonable time required by the authorities subject to Clause 17. Any unexplained delay in getting the land converted into FREEHOLD may result in suppressing the sales in turn affecting the timely completion of the project which shall not be attributable to THE SECOND PARTY.*
>
> *12. THAT THE SECOND PARTY would develop and construct the residential towers, commercial and shopping blocks. Community*

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facility, educational school and value added facilities clubs, restaurants, cafeteria, Swimming pool, health club as per the sanctioned or revised sanctioned plans at their cost and expenses. The construction and development of the buildings ear marked for religious purposes will be carried out by THE FIRST PARTY at their cost and expenses, but THE FIRST PARTY will get the same simultaneously constructed and completed for the purpose of obtaining completion certificate from the Competent Authority. .However, the Completion Certificate from the Competent Authority shall be obtained by THE SECOND PARTY.

15. THAT THE SAID LAND on which the Project is agreed to be executed is being provided by THE FIRST PARTY, while THE SECOND PARTY is obliged to honor its commitments both financial and otherwise in respect of the construction/ developments proposed to be made on THE SAID LAND in accordance with this Agreement.. Accordingly it is mutually agreed upon by the parties that as per the already sanctioned plans or as per revised approved plans, THE SECOND PARTY, in lieu of their development/construction cost, shall be entitled to as under and on the pattern as appearing in the Agreement.

1. FIRST PARTY – 1/3rd portion (one third portion) in each of the Residential Towers (Floor wise), commercial shopping, garages, parking stilts, open parkings, value added facilities, educational school building, clubs, swimming pool etc.

2. SECOND PARTY – 2/3rd portion (two third portion) in each of the Residential Towers (Floor wise), commercial shopping, garages, parking stilts, open parkings, value added facilities, educational school building, clubs, swimming pool etc.

3. The ten (10) shops already constructed by THE FIRST PARTY would exclusively belong to THE FIRST PARTY

However, all the Towers and Buildings etc. as per sanctioned plans or the revised plans shall be demarcated and identified through a separate Memorandum of Understanding.

16. THAT the portion allocated for religious purposes would exclusively belong to THE FIRST PARTY and the construction, development, disposal and management of this part would be the exclusive liability of THE FIRST PARTY and THE SECOND PARTY would have no say or portion in the same.

17. THAT THE SECOND PARTY has given a sum of Rs.11.00 Lacs (Rupees Eleven Lacs) as interest free refundable amount to THE FIRST PARTY through Cheque No. 605062 dated 25.03.2003 drawn on ICICI Bank Limited, Lucknow along with the offer dated 25.03 2003 which THE FIRST PARTY hereby acknowledges having received the same. THE SECOND PARTY further agrees to give interest free refundable amount to THE FIRST PARTY as mutually agreed between [he parties hereto for getting THE SAID LAND converted into free hold and depositing various charges and fee as per clause 9 to the concerned authorities by reducing the terms in writing through Supplementary Agreement(s) which shall always be treated as part of THE PROJECT DEVELOPMENT AGREEMENT dated 20.06.2003 and would always be read together.

I8. THAT THE FIRST PARTY agrees to return/repay such amounts advanced by THE SECOND PARTY as under:

a) On handing over l/3rd built up area in First phase by THE SECOND PARTY to THE FIRST PARTY	*25% of the total amount deposited including amounts if any through Supplementary Agreement*

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b)On handing over 1/3rd built up area of the Second Phase by THE SECOND PARTY to THE FIRST PARTY	*50% of the total amount deposited including amounts if any through Supplementary Agreement*
c) On final completion and handing over the balance l/3rdbuilt up area by THE SECOND PARTY to THE FIRST PARTY	*25% of the total amount deposited including amounts if any through Supplementary Agreement*

The word "final completion" occurring in Clause 18 (c) above shall mean that upon the completion of construction and receipt of the completion certificate from the LDA/Competent Authority by 'THE SECOND PARTY'.

27. THAT certain part of THE SAID LAND is occupied with buildings thereon as some staff members of THE FIRST PARTY are living in the same. A major part of THE SAID LAND is absolutely vacant and is in complete possession of THE FIRST PARTY. THE FIRST PARTY has handed over the possession of the vacant part of THE SAID LAND to THE SECOND PARTY at the time of signing of this Agreement for project development' work. THE SECOND PARTY shall. commence the construction of the Building as soon as the revised plans are sanctioned by the Lucknow Development Authority or with in 30 days from the date of the receipt of the revised plans. THE FIRST PARTY agrees to get the balance part of THE SAID LAND vacated at the cost and expenses within one year or so from the date of this Agreement and simultaneously hand over the possession to THE SECOND PARTY.' In case of delay in getting THE SAID LAND vacated by THE FIRST PARTY and /or handing over of the possession of the same to THE SECOND PARTY the resultant delay in construction and development would be solely attributable to THE FIRST PARTY, It is further agreed by and between the party that THE FIRST PARTY will remove the rubble of the existing structures and

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also the trees. The rubble and the trees will exclusively belong to THE FIRST PARTY including any valuable article if found beneath the earth and THE SECOND PARTY shall have no claim over the same."

CLAUSE NO. 1 & 2 OF THE SUPPLEMENTARY PROJECT DEVELOPMENT AGREEMENT

AND WHEREAS THE FIRST PARTY and THE SECOND PARTY have mutually agreed and arrived at a figure and pattern of advancing the amount culminating the same in writing by executing this Supplementary Agreement which will always be considered as part of the original PROJECT DEVELOPMENT AGREEMENT dated 20.06.2003 and would be read together:

NOW THIS SUPPLEMENTARY AGREEMENT WITNESSES AS UNDER:

1. THAT THE FIRST PARTY and THE SECOND PARTY in continuation of the Agreement dated 20.06.2003 executed between them and more especially in terms of clause No. 17 on page 16 hereby agree and quantify the amount required to be advanced by THE SECOND PARTY to THE FIRST PARTY as Rs.300 Lacs (Rupees Three Hundred Lacs) in totality paid and to be paid as under:

a) Cheque No 605062 dated 25/03/03 Prawn on ICICI Bank Ltd enclosed with offer dated 15703/03	*Rs. 11.00 Lacs*
b) Cheque No. 570885 dated 20.06.2003 drawn on Punjab National Bank, Hazratganj, Lucknow at the time of signing of this agreement	*Rs. 40.00 Lacs*
c) Within 30 days of receiving demand note for freehold	*Rs. 150.00 Lacs*
d) Within 30 days of depositing freehold charges by THE FIRST PARTY with the Authorities	*Rs. 49.00 Lacs*
e) Amount for payment of charges	

as per clause 9 of THE PROJECT DEVELOPMENT AGREEMENT to the concerned authorities as and when demands are raised. *Rs. 50.00 Lacs*

2. THAT it is further confirmed by THE FIRST PARTY and THE SECOND PARTY to refund the entire sum of advance amounting to Rs.300 Lacs(Rupees Three Hundred Lacs) as per para 18 on page 17 as appearing in THE PROJECT DEVELOPMENT AGREEMENT dated 20.06.2003."

13. The Assessing Officer has invoked the provisions of section 2(47)(v) of the Act and treated this handing over of the possession of vacant land to the second party i.e. M/s Arif Industries Ltd. for the purpose of construction of residential/commercial towers as a transfer of capital asset and computed the capital gain in the hands of the assessee; whereas the provisions of section 2(47)(v) of the Act can only be invoked where absolute possession of capital asset was given to the buyer against certain consideration, but in the instant case no consideration was ever fixed for handing over the possession to the developer and whatever amount was received it was received as interest free advance to meet the expenses to be incurred in discharging certain responsibilities agreed upon in this agreement. Our attention was also invited to the balance sheet and list of sundry creditors as on 31.3.2004 in which M/s Arif Industries Ltd. was shown as sundry creditors and a sum of Rs.51 lakhs was credited to its account. Therefore, from any angle there is no transfer of asset as per provisions of section 2(47) of the Act.

14. We have also carefully perused the judgments referred to by the assessee.

15. In the case of Chaturbhuj Dwarkadas Kapadia vs. CIT (supra), their Lordships of the Hon'ble Bombay High Court has held "in order to attract section 53A for the following conditions need to be fulfilled. There should

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be a contract for consideration; it should be in writing; it should be signed by the transferor; it should pertain to transfer of immovable property; the transferee should have taken the possession of the property; lastly the transferee should be ready and willing to perform his party of the contract.

16. In the case of R. Gopinath (HUF) vs. ACIT (supra), the Tribunal has held that section 53A of the Act of the Property Act does not provide the conditions for transfer but it provides protection to the transferee of any immovable property by a written contract, the terms of which constitute the transfer and can be ascertained with reasonable certainty and the transferee as part performance of the contract has taken the possession of the property and has performed or willing to perform his part of contract, then even the said contract though required to be registered has not been registered and the transfer has not been completed in the manner prescribed therefore by law, the transferor is barred from enforcing against the transferee any right in respect of the property other than the right expressly provided by the terms of the contract. The Tribunal further held that under the I.T Act, 1961 by inserting clause (v) and (vi) of section 2(47), the definition of the term transfer includes the transaction which fulfils the conditions provided under s. 53A of Transfer of Property Act. Therefore, section 53A of the I. T Act, 1961 is borrowed only with respect to the transfer of capital asset as provided under s. 2(47) of the IT Act, 1961 and the same is not applicable in other cases which do not fall under s. 2(47) of the IT Act, 1961. In that case, facts are almost similar to the present case and the Tribunal has held that where the assessee has converted its land into stock-in-trade and thereafter a development agreement was entered into by the assessee with the developer, whereby the assessee provided his land measuring 44,000 sq. ft. to the developer for construction of residential apartments and the assessee was to get constructed an area of 21,130 sq. ft.. the capital gain arising from the conversion of the land converted into stock-in-trade were assessable

proportionately in the previous year in which the constructed property was sold by the assessee and not in the year of development agreement.

17. Similar views were expressed by the Tribunal in the case of Shri. Ramesh Abaji Walavalkar, Thane vs. ACIT, Thane (supra) by holding that where there was a conversion of capital asset of land into stock-in-trade by the assessee for business of real estate development and capital gain arising from the transfer of land by way of such conversion was chargeable to tax in the previous year relevant to the assessment year 2005-06 when the constructed portion is sold as per the provisions of section 45(2) of the Act.

18. Again in the case of DCIT vs. Crest Hotels Ltd. (supra), similar view was expressed by the Tribunal by holding that capital gain on conversion of capital asset into stock-in-trade to be assessed in those years in which the said stock-in-trade is sold out. The Tribunal has further held that the Legislature in its wisdom, considering the fact that on conversion only notional income has arisen, postponed the tax liability thereon till real income was earned on that asset. In short, the tax liability of capital gain on conversion will arise in the same year in which business profit arise to the assessee on sale of such asset. The asset cannot have dual characteristic at the same point of time in the hands of the same person.

19. Turning to the facts of the case, we find that as per project development agreement, the possession was given for construction/development of project with certain conditions stipulated in the agreement. Whatever amount was received, it was simply interest free advance to meet certain expenses to be borne by the assessee in order to discharge certain responsibilities conferred upon it through the agreement. The said advance would be refundable at different phases stipulated in the agreement. Therefore, in the light of the aforesaid judgments, we are of the view that there was no transfer of possession of the land in favour of

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the developer, M/s Arif Industries Ltd. to attract provisions of section 2(47)(v) of the Act. Therefore, capital gain would only be chargeable in the years in which stock-in-trade would be sold. Therefore, we find ourselves in agreement with the order of the ld. CIT(A) who has rightly dealt with the issue. Accordingly we confirm the same.

20. Since we have confirmed the order of the ld. CIT(A), the cross objection of the assessee has become infructuous and we accordingly dismiss the same.

I.T.A. No. 62/LKW/2012 & C.O. No.19/LKW/2012:

21. In the Revenue's appeal, the Revenue has assailed the order of the ld. CIT(A), inter alia, on the following grounds:-

1. The CIT(A) has erred in law and on facts of the case in failing to appreciate that the AO has correctly adopted the cost price of the land in question as on 01.04.81 to be the circle rate fixed by the DM for stamp duty purposes;

2. The CIT(A) has erred in law and on facts of the case in calculating the value of the land in question as on 01.04.81 by considering the Valuation Report of the approved valuer. He overlooked the fact that the valuer's report is based on the value of a very small piece of land which was sold by auction in 1985. The valuer has projected this value backwards to obtain a hypothetical value as on 1.4.81. This is not an accepted method of valuation and is variance with the circle rate fixed by DM and also of the comparable sale instances of that year;

3. The CIT(A) has also erred in law and also on facts of the case in failing to appreciate that the land of the assessee is leasehold land and that the lease is about to expire. The correct valuation as on 01.04.81 would therefore have been even lower than the circle rate fixed by the DM;

4. The CIT(A) has failed to appreciate that the facts of the

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various judicial pronouncements cited by him in his order are different from the facts of the present case. His conclusion is therefore erroneous both on facts and in law;

5. The CIT(A) has also erred in law and on facts of the case in observing that the AO has neither identified any income shown by the assessee which does not form part of total income or that he has not identified any expenditure which has been incurred by him for such income while deleting the disallowance made u/s 14A of the I.T. Act, 1961. Such items of income and expenditure have been clearly identified and are a part of the record. The decision of the CIT(A) on this issue is clearly incorrect.

22. In support of the order of the ld. CIT(A), the assessee has filed the cross objection.

23. The dispute raised through various grounds in the Revenue's appeal is with regard to the cost of land as on 1.4.1981 adopted by the Assessing Officer for computing the capital gain accrued to the assessee on account of conversion of capital asset into stock-in-trade.

24. The facts in brief borne out from the record are that the assessee has converted its land into stock-in-trade during the financial year 2003-04 and the corresponding capital gain is to be computed as per provisions of section 45(2) of the Act by the Assessing Officer. In the impugned assessment year i.e. assessment year 2008-09, the assessee has sold 9 flats measuring 1492.01 sq. mtr. The assessee has taken the deemed cost of land as on 1.4.1981 at Rs.95/- per sq. mtr. on the basis of the report of the Government approved Registered Valuer to determine the fair market value as per provisions of section 55(2)(i) of the Act. The assessee has calculated the capital gain as per provisions of section 45(2) of the Act by adopting the fair market value as per said valuation report. The Valuation

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Report of the Government approved valuer filed by the assessee is based on the land sold through public auction in 1985 which is very close to the land of the assessee. The Assessing Officer has disputed the rate of the land adopted by the assessee as on 1.4.1981. The Assessing Officer has adopted the deemed cost as on 1.4.1981 at Rs.15 per sq. mtr. and recomputed the capital gain for the purpose of section 45(2) of the Act and accordingly the capital gain at Rs.84,27,065/- was computed against the claim of capital loss of the assessee resulting into an addition of Rs.84,27,065/-.

25. The assessee preferred an appeal before the ld. CIT(A) with the submission that the assessee has taken the deemed cost of land as on 1.4.1981 at Rs.95/- per sq. ft. on the basis of the report of the Government approved Registered Valuer. With respect to the valuation report of the valuer, it was contended that the valuation report is based on the lawfully recognized comparable sale method and the assessee has calculated the capital gain as per provisions of section 45(2) of the Act by adopting the fair market value as per said valuation report on the basis of the land sold through public auction in the year 1985 which is very close to the land of the assessee. The ld. CIT(A) has re-examined the claim of the assessee in the light of the written submission and the computation of long term capital loss furnished before the ld. CIT(A) and being convinced with the explanations furnished by the assessee, the ld. CIT(A) has deleted the addition having observed that the Assessing Officer has rejected the valuation report of the registered valuer for no apparent reason. In case the Assessing Officer was not satisfied with report of the registered valuer, a reference could have been made to the Valuation Officer under section 55A of the Act. The ld. CIT(A) has also observed that the said valuation report of the registered valuer relied upon by the assessee has been accepted in the assessment proceedings for assessment years 2004-05 and 2007-08 while framing the assessment under section 143(3) of the Act.

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The relevant observations of the ld. CIT(A) are extracted hereunder for the sake of reference:-

"4(4) I have examined the facts and circumstances of the case. I have considered the findings of the Assessing Officer and the submissions made by the appellant in writing and before me during the course of the appellate proceedings. The registered valuer whose report has been submitted by the assessee, adopted a rate of 95 per square feet as on 01.04.1981 on the basis of auction rate of 2650 per square feet of an adjacent land auctioned in 1985 as is evident from page 2 of the valuation report. The value of land at the date of conversion of the land to stock in trade as on 01.04.2003 was taken as 285 per square feet being 3 times of the rate as on 01.04.1981. The value of land so arrived was proportionately apportioned to the flats sold during the year under consideration and thereby the assessee worked out the capital loss on sale of land at Rs. 44,85,016/-. The Assessing Officer on the other hand adopted a circle rate of 15 per square feet as on 01.04.1981 and 325.27 per square feet as on 01.04.2003 and thereafter worked out long term capital gains at Rs. 84,27,065/-. The issue involved is value of land as on 01.04.1981 and value of land to be adopted as at 01.04.2003. These values will determine the cost of acquisition in the financial year 2007-2008 relevant to the impugned assessment year 2008-2009 for the purpose of computing the capital gains. The related issue is the basis to be adopted for the purpose of arriving at the value of impugned land as on the relevant dates.

4(5) Section 55(2)(b)(i) of the Act prescribes that in case where the capital asset became the property of the assessee before 01.04.1981, the cost of acquisition for the purpose of section 48 and section 49 of the Act means cost of acquisition of the property to the assessee or the fair market value of the asset as on 01.04.1981 at the option of the assessee. In the impugned case the assessee chose to exercise its option in favour of market value of the asset as on 01.04.1981.

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Now the term 'Fair Market Value' is defined in section 2(22B) of the Act as under -

Section 2(22B)"fair market value", in relation to a capital asset, means—

(i) the price that the capital asset would ordinarily fetch on sale in the open market on the relevant date ; and

(ii) where the price referred to in sub-clause (i) is not ascertainable, such price as may be determined in accordance with the rules made under this Act ;

It is evident that circle rate fixed by the District Authorities is not a prescribed method for valuation of fair market value of an asset under the section 2(22B) of the Act. Although section 50C of the Act prescribes for substitution of value fixed by stamp valuation authority for the purpose of stamp duty i.e. the circle rate as deemed consideration of sale of a capital asset in case the sale consideration shown is less than such value, the above provision is strictly not applicable for the purpose of determination of cost of acquisition. Yet the provision of section 50C of the Act does give credence to the opinion that the fair market value of an asset could be greater than, less than or equal to the circle rate. To put it in simple words, the fair market value of an asset is the price that the capital asset would ordinarily fetch on sale in the open market on the relevant date and this value could be any value and not necessarily the circle rate.

4(6) Now therefore having ascertained that the cost of acquisition of the impugned land sold by the assessee in the form of proportionate value apportioned to constructed flats is to be valued at fair market value i.e. the price that the asset would ordinarily fetch on sale in the open market, the issue is ascertainment of that price. In this connection a reference may be made to the decision of Hon'ble Apex Court in the case of Special Land Acquisition Officer, Davangere V.P. Veerabhadrappa and Others (1984) 18 Taxman 1 (SC), 42 CTR 357, 154 ITR 190. The relevant portions are reproduced as under:-

In Vyricherla Narayana Gajapatiraju v. Revenue Divisional Officer, Vizagapatnam [1939] LR 6b I A 104, the Privy Council adopted to traditional legal definition of the value as the price at which the property would sell "as between a willing buyer and a willing seller". In its a narrowest sense, it is designed to preclude a valuation based on as assumed forced sale; the property must be appraised at what it would probably bring the owner allowed a reasonable opportunity for negotiations. But the courts have invoked a mythical willing buyer to justify a valuation higher than any attainable sale price. According to the Privy Council, "market value" of the land within the meaning of s. 23 of the Act is the price the property may fetch in the open market, if sold by a willing render unaffected by the special needs of a particular purpose. The owner is entitled to the value of the property in its actual condition at the time of expropriation, with all its advantages and with all its possibilities, excluding any advantage due to the carrying out of the scheme for the purpose for which the property is acquired. It is not only realized possibilities but also the future possibilities that must be taken into consideration. The Privy Council further observed that there is not in general any market for land in the sense that one speaks of the market for shares or commercial goods. The value of the any such article at any particular time can really be ascertained by the price being obtained for similar articles in the market. In the case of land, its value can also be measured by a consideration of the prices that have been obtained in the past for lands of the similar quality and in similar positions, and that is what must be meant in general by the "market value" in s. 23.

The function of the court in awarding compensation under the Act is to ascertain the market value of the land at the date of the notification under s. 4(1) of the Act and the methods of valuation may be : (1) opinion of experts, (2) the prices paid within a reasonable time in bona fide transactions of purchase or sale of the lands acquired on of the lands adjacent to those acquired and possessing similar advantages, and (3) a number of years' purchase

of the actual or immediately prospective profits from the lands acquired. Normally, the method of capitalizing the actual or immediately prospective profits or the rent of a number of years' purchase should not be resorted to if there is evidence of comparable sales or other evidence for computation of the market value. It can be resorted to only when no other method is available.

It is axiomatic that the best evidence to prove what a willing purchaser would pay for the land under acquisition would be the evidence of sales of comparable properties, proximate in time to date of the acquisition, similarly situate, and possessing the same or similar advantages and subject to the same or similar disadvantages. Market value is the price the property may fetch in the open market if sold by a willing seller unaffected by the special needs of a particular purchase. Where definite material is not forthcoming either in the shape of the sales of similar lands in the neighborhood at or about the date of the notification under s. 4(1) or otherwise, the court has no other alternative but to fall back on the method of valuation by capitalization. In valuing land or an interest in land for purpose of land acquisition proceedings, the rule as to number of years' purchase is not a theoretical or legal rule but depends upon economic factors such as the prevailing rate of interest in the money investments. The return which an investor will expect from an investment will depend upon the characteristic of income as compared to that of idle security. The main features are : (1) security of the income; (2) fluctuation; (3) chances of increase; (4) cost of collection, etc. The most difficult and yet the most important and crucial part of the whole exercise is the determination of the reasonable rate of return in respect of the investment in various types of properties. Once this rate of return and, accordingly, the rate of capitalization are determined, there is no problem in valuation of the property.

It is thus clear from the above enunciation that the method of determining the value of the property by the application of a

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multiplier to the net annual income or profit should only be adopted when there is no evidence of comparable sales of similar lands in or about the neighborhood at the relevant time, i.e., on the date of the notification under s. 4(1) of the Act. In certain circumstances, however, the court has no other alternative but to fall back on the capitalized value.

"It is evident, therefore, from the foregoing definitions as well as from numerous other definitions which may be cited, that the fair market value of the property taken by eminent domain is the price that the property will being when offered for sale by one desiring, but not obliged, to sell; and purchased by one desiring to purchase but under no necessity of buying. It is the price which a piece of property will bring in the market when offered for sale and purchased by another, taking into consideration all the elements of the availability of the property, its use, potential or prospective, and all other elements which combine to give of property a market value."

Hon'ble Allahabad High Court also considered the issue in the case of Commissioner Of Income-tax V. Jumramal Son. (1985) 154 ITR 689 (All) and laid down that Rates of auction sales of properties in neighborhood should be considered while ascertaining the market value of an asset on a particular date.

4(7) The aforesaid decisions give credence to the view that the fair market value of a property could be taken as the rate of auction of a property in the vicinity of the impugned land. The registered valuer whose report forms the basis of valuation of land as on the relevant date and adopted by the assessee has referred to a land measuring 504.0 square meter in the vicinity of impugned land which was auctioned in 1985 for a rate of 246.3 per square feet. The said land was commercial land and therefore the registered valuer worked out the rate in 1985 for residential purposes at half of the said rate and thus in 1985 the rate was taken at 98.5 per square feet. This rate was therefore reduced to Rs. 95/- per square feet as on 01.04.1981. The rate was increased by a multiple of 3 for arriving at the rate of

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285 per square feet as on 01.04.2003. I find that the multiple is itself reasonable as the circle rate of 15 per square feet as on 01.04.1981 was revised to 325.27 per square feet as mentioned by the AO in the computations. The rate adopted by the registered valuer has reference to the rates that corresponding properties were fetching in the vicinity of the impugned land in auction at relevant period of time. The rate is also in accordance with the decisions cited supra where auction rates have been accepted as fair market value of property.

4(8) The AO rejected the valuation report of the registered valuer for no apparent reasons. In case the AO was not satisfied about the correctness of the valuation done by the registered valuer, a reference could have been made to the Departmental Valuation Officer under section 55A of the Act which lays down as under -

Reference to Valuation Officer.

55A. With a view to ascertaining the fair market value of a capital asset for the purposes of this Chapter, the Assessing Officer may refer the valuation of capital asset to a Valuation Officer—

(a)in a case where the value of the asset as claimed by the assessee is in accordance with the estimate made by a registered valuer, if the Assessing Officer is of opinion that the value so claimed is less than its fair market value;

(b)in any other case, if the Assessing Officer is of opinion—

(i)that the fair market value of the asset exceeds the value of the asset as claimed by the assessee by more than such percentage of the value of the asset as so claimed or by more than such amount as may be prescribed in this behalf; or

(ii)that having regard to the nature of the asset and other relevant circumstances, it is necessary so to do,

Evidently, the Assessing Officer is entitled to make the reference to the Valuation Officer under section 55A(b)(ii) of the Act on recording

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an opinion that having regard to the nature of the asset and other relevant circumstances, it is necessary to make such a reference. In the instant case, the assessee had claimed the fair market value of property as per the Government approved registered valuer's report. Therefore, under sub clause (ii) of clause (b) of section 55A of the Act, the Assessing Officer was required to form an opinion as mentioned and refer the property for ascertain the fair market value on the relevant date. Further, the valuation report of the registered valuer relied upon by the assessee has been accepted in the assessment proceedings for the assessment years 2004-05 and assessment year 2007-2008 when the assessment order have been passed under section 143(3) of the Act. Since the impugned valuation report has been accepted by the Assessing Officer in the earlier years, there is no occasion to reject the same report without any basis and without taking the opinion of the departmental valuation officer on the fair market value of the property under the powers granted under the provisions of the Act.

4(9) In view of the discussion above, I am of the opinion that the Assessing Officer is not justified in taking the fair market value of the impugned land for the purpose of computing the capital gains as circle rate. The circle rate is not a necessary parameter in arriving at the fair market value and on the other hand rate of auction of a nearby property has been accepted as fair value in the judicial decisions cited supra. In absence of any other material, jt would be reasonable to accept the report of the registered valuer which is based on auction rates of neighborhood property and does give an indication of the value the property in the vicinity was fetching in the open market and hence the fair market value. I am therefore of the considered view that the cost of acquisition being fair market value of the property in question, the rate for the purpose of valuing the property requires to be,, taken as that ascertained by the registered valuer. The addition of Rs.84,27,065/- made by b the AO by working

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out the capital gains on the basis of circle rate for cost of acquisition is directed to be deleted. The ground of appeal is allowed."

26. Aggrieved, the Revenue has preferred an appeal before the Tribunal and placed heavy reliance upon the order of the Assessing Officer.

27. In opugnation, the ld. counsel for the assessee, besides placing reliance upon the order of the ld. CIT(A), has submitted that the Assessing Officer has not raised any dispute with regard to the deemed value of the land as on 1.4.1981 in assessment year 2003-04 when the land was transferred to stock-in-trade by the assessee-company. No disallowance was also made during the assessment year 2007-08 while framing the assessment under section 143(3) of the Act. It was further contended that the assessee has adopted the deemed value of the land as on 1.4.1981 on the basis of the valuation report prepared relying upon the land sold through public auction in the year 1985 which is very close to the land of the assessee. It was further contended that the Assessing Officer is not an expert in determining the value of the land. If he has any doubt with regard to the valuation adopted by the assessee as on 1.4.1981, he could have made a reference to the DVO for the determination of the value of the land, but he did not do so and has adopted the value of his own without any basis. Therefore, the value adopted by the Assessing Officer is not sustainable in the eyes of law.

28. Having carefully examined the orders of the lower authorities and the documents placed on record in the light of the rival submissions, we find that the assessee has adopted the deemed value as on 1.4.1981 of the land on the basis of the registered valuer's report which was prepared on the basis of the land sold through public auction in the year 1985 which is very close to the land of the assessee. We also find force in the contentions that if the Assessing Officer has any doubt with regard to the valuation adopted

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by the assessee as on 1.4.1981, he could have made reference to the DVO either in those years in which the land was converted into stock-in-trade or in those years when the capital gain is to be worked out, but the Assessing Officer has not made any effort to make reference to the DVO. On perusal of the Valuation report of the Registered Valuer filed by the assessee, it is noticed that the Registered Valuer has determined the value on the basis of land sold through public auction in the year 1985 which was claimed to be close to the land of the assessee. While determining the market value of the impugned land as on 1.4.1981, the Registered Valuer should have scaled down the value of the land by applying certain formula, but he did not do so. He adopted the market value of the land sold through public auction in the year 1985. Therefore, we are of the view that the fair market value determined by the registered valuer is not correct. On the other hand, the Assessing Officer has adopted the circle rate as on 1.4.1981 without looking to the fact that the assessee has filed the registered valuer's report to determine the fair market value of the land as on 1.4.1981. We find force in the contention of the assessee that the Assessing Officer is not expert in the field of determining the value of land, therefore, he should have made reference to the DVO to determine the value of land as on 1.4.1981, but he did not do so. He adopted the circle rate as fair market value of land as on 1.4.1981 ignoring the registered valuer's report submitted by the assessee and computed the long term capital gain. The approach adopted by the Assessing Officer does not appear to be correct. Since the market value of the land as on 1.4.1981 was not determined correctly either by the assessee or the Assessing Officer, this issue requires a fresh adjudication by the Assessing Officer. Accordingly, we set aside the order of the ld. CIT(A) in this regard and restore the matter to the file of the Assessing Officer with a direction to re-adjudicate the issue afresh after determining the fair market value of the land as on 1.4.1981. Since the assessee has filed the registered valuer's

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report and disputed the circle rate, the Assessing Officer may make reference to the DVO in order to determine the fair market value of the land for the purpose of long term capital gain.

29. The other issue involved in this appeal is with regard to the disallowance made under section 14A of the Act.

30. The Assessing Officer has made disallowance of Rs.13,99,150/- having invoked the provisions of section 14A of the Act read with rule 8D(2)(iii) of the rules for the reason that the assessee has shown dividend income at Rs.2,08,13,952 which does not fall part of the total income of the assessee. The disallowance was challenged before the ld. CIT(A) with the submission that the said disallowance is not called for as the assessee has not booked any expenditure on account of relevant investment. It was also contended before the ld. CIT(A) that before invoking the provisions of section 14A of the Act, the Assessing Officer has to record an objective satisfaction that the accounts prepared by the assessee with respect to the provisions of section 14A of the Act are incorrect. The ld. CIT(A) has examined these aspects in the light of the assessee's contentions and was of the view that the Assessing Officer has not identified any expenditure in relation to the income which does not form part of the total income of the assessee. He was also of the view that the provisions of section 14A of the Act are not attracted in the case of the assessee. He accordingly deleted the addition. The relevant observations of the ld. CIT(A) are extracted hereunder for the sake of reference:-

> *"5(4) I have examined the facts and circumstances of the case. I have considered the findings of the Assessing Officer and the submissions made by the appellant in writing and before me during the course of the appellate proceedings.*
> *Section 14A of the Act reads as under:*
> *14A (1) For the purposes of computing the total income under this chapter, no deduction shall be allowed in respect of expenditure*

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incurred by the assessee in relation to income which does not form part of the total income under this Act….."

Evidently, section 14A of the Act contemplates disallowance of expenditure incurred by the assessee in relation to the income which does not form part of the total income. Such expenditure is not to be allowed as deduction in computing the total income under the provisions of chapter IV of the Act. The incomes which do not form part of total income are those contained under chapter III of the Act. To put it differently, an expenditure which has been incurred by the assessee to earn income which does not form part of total income under chapter III of the Act is not allowable as deduction in computing the income forming part of total income under chapter IV of the Act. The Assessing Officer has neither identified any income shown by the assessee which does not form part of the total income nor has identified any expenditure which has been made merely b application of Rule 8D(2)(iii) as the assessee has shown income from dividends amounting to Rs.2,08,13,952/-.

5(5) The appellant has neither claimed nor incurred any expenditure on the investments. Once this is an undisputed fact, no disallowance under section 14A of the Act is called for. Even the Assessing Officer has not brought out any nexus between the expenditure incurred and income generated which is not part of the taxable income. In the case of CIT Vs. Winsome Textile Industries Ltd. (2009) 319 ITR 205 (P&H), Hon'ble Court held that if the expenditure has not been incurred for making the investment for the purchase of shares no disallowance is warranted under section 14A of the Act. In the case of CIT Vs. Hero Cycles Ltd. (2010) 323 ITR 518 (P&H) Hon'ble Court held that if there is no nexus between the expenditure incurred and the income generated and merely because the assessee had incurred interest expenditure on funds borrowed for the main business, it would not ipso-facto invite disallowance of under section 14A, unless there was evidence to show that such interest bearing funds have been invested in the investment which had generated the "tax exempt dividend income". Further, in the case of CIT Vs.

Gujrat Power Corporation Ltd. Hon'ble Court held that if the borrowed funds have not been diverted to earn tax free income provisions of section 14A would not apply. Again, in the case of Walfort ShareandStock Brokers Ltd. Vs. ITO (2009) 310 ITR 421 (Bom) Hon'ble High Court held that section 14A contemplates the expenditure actually incurred for earning tax free income and not assumed expenditure or deemed expenditure. The aforesaid judgment of Bombay High Court has been affirmed by the Hon'ble Supreme Court in the case of CIT Vs. Walfort Share & Stock Brokers (P) Ltd. reported in (2010) 326 ITR 1, wherein their Lordships after analyzing the scope and purpose of section 14A of the Act held that there has to be proximate cause for disallowance which is its relationships with the tax exempt income.

5(6) I find that in the case of the appellant the AO has not identified any expenditure incurred in relation to income which does not form part of total income. The expenditure of Rs.13,99,150/- disallowed by the AO was incurred by the appellant in relation to his business activities. In the calculations made by the AO the direct expenditure on exempted income has been shown as NIL in the assessment order. The provisions of section 14A of the Act are not attracted in the case of the appellant. I therefore delete the addition of Rs.13,99,150/- made by the AO by taking recourse to the provisions of section 14A of the Act as the said expenditure is business expenditure incurred during the normal course of business activities. Provisions of section 14A of the Act do not contemplate disallowance of business expenditure incurred during the normal course of business activities and such expenditure has no nexus with dividend income of the appellant. In the result the addition of Rs. 13,99,150/- made by the Assessing Officer is deleted resulting in relief of equivalent amount to the appellant. In view of above, this ground of the appellant is allowed."

31. Aggrieved, the Revenue has preferred an appeal before the Tribunal and has placed heavy reliance upon the order of the Assessing Officer; whereas the ld. counsel for the assessee, besides placing reliance upon the

order of the ld. CIT(A), has invited our attention to the assessment order with the submission that the Assessing Officer has simply computed the disallowance under section 14A of the Act read with rule 8D(2)(iii) of the rules without recording any satisfaction with regard to the incorrectness of the accounts of the assessee with respect to the dividend income and the expenditure incurred in relation thereof. He has also invited our attention to the order of the Tribunal in the case of U.P. Electronics Corporation Ltd. vs. DCIT(TDS), Lucknow in I.T.A. No. 538/LKW/2012, in which the issue of recording of objective satisfaction while invoking the provisions of section 14A of the Act was dealt with by this Bench of the Tribunal and the Tribunal has conclusively held that the Assessing Officer is required to record objective satisfaction before invoking the provisions of section 14A of the Act. The ld. counsel for the assessee has further invited our attention to the balance sheet available on record with the submission that the assessee has not booked any expenditure with respect to the investments wherefrom the dividend income is earned. Whatever expenditures are booked, it was general business expenditures and no part of the same can be disallowed only for the reason that the assessee earned dividend income which does not form part of the total income of the assessee.

32. Having carefully examined the orders of the lower authorities in the light of the rival submissions, we find that the Assessing Officer has made disallowance under section 14A of the Act read with rule 8D(2)(iii) of the rules straightaway without recording any objective satisfaction or otherwise with respect to the correctness of the accounts relating to dividend income. We have also carefully examined the balance sheet filed before us wherefrom no interest expenditures are booked on the investment in shares wherefrom dividend income was earned. We do not find much force in the argument of the ld. counsel for the assessee that where no expenditures are booked under the head of payment of interest on the

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investment, no disallowance can be made under section 14A of the Act. For computing the disallowance under rule 8D of the rules a procedure has been provided which takes care of every situation. If no expenditure is booked on account of payment of interest on investment, disallowance can be made while computing the same as per rule 8D(2)(iii) of the rules.

33. But we find force in the second limb of argument of the assessee that the Assessing Officer has straightaway computed the disallowance under section 14A of the Act read with rule 8D(2) of the rules without recording any objective satisfaction with respect to the correctness of the accounts relating to the dividend income of the assessee. This issue was examined by this Bench of the Tribunal in the case of U.P. Electronics Corporation Ltd. vs. DCIT(TDS), Lucknow (supra) in the light of various judicial pronouncements and the Tribunal was of the view that before invoking the provisions of section 14A of the Act read with rule 8D of the rules for computing the disallowance, the Assessing Officer is required to record objective satisfaction with regard to the incorrectness of the expenditure or accounts relating to investment on which dividend income was earned. If satisfaction is not recorded, no disallowance under section 14A of the Act can be made. The relevant observations of the Tribunal are extracted hereunder for the sake of reference:-

> *"9. Having carefully examined the orders of the lower authorities in the light of the rival submissions, we find that out of total investments of Rs.82,16,45,416/-, investment in subsidiary companies were of Rs.60,90,10,559/- as per balance sheet appearing at pages 26 to 38 of compilation of the assessee. The assessee has raised a specific dispute with regard to the invocation of provisions of rule 8D with the contention that before invoking the provisions of rule 8D, the Assessing Officer has to record objective satisfaction with regard to the correctness of the accounts relating to provisions of section 14A of the Act. In support of his contention, the ld. counsel for the assessee has invited our attention to the judgment of*

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the Hon'ble Bombay High Court in the case of Godrej And Boyce Mfg. Co. Ltd. vs. Dy. CIT & Another [2010] 328 ITR 81 (Bom.) and the orders of the Tribunal in the cases of M/s JM Financial Limited vs. Addl. CIT (supra) and Kalyani Steels Ltd. vs. Addl. CIT (supra).

10. In the case of M/s JM Financial Limited vs. Addl. CIT (supra), the Tribunal has examined the issue of recording objective satisfaction by the Assessing Officer before proceeding for computation of corresponding expenditures as per rule 8D and possibility of disallowance in case where strategic investment was made in the subsidiary companies and the Tribunal has finally concluded that sub-section (2) of section 14A of the Act does not ifso facto empower the Assessing Officer to apply the method prescribed by Rules straightaway without considering whether the claim made by the assessee is correct.

11. With regard to the investment in subsidiary companies, the Tribunal has also held that in the absence of any finding that any expenditure has been incurred for earning exempted income, the disallowance made by the Assessing Officer is not justified. The relevant observations of the Tribunal in the case of M/s JM Financial Limited vs. Addl. CIT (supra) are extracted hereunder for the sake of reference:-

> *"7. Having considered the rival submissions as well as relevant material on record, we note that so far as applicability of Rule 8D is concerned, there is no quarrel on this point that for the A.Y. under consideration Rule 8D is applicable. Further for the A.Y. 2008-09, the Tribunal held in para 15 as under:-*

"We have considered the rival arguments made by both the sides, perused the orders of the AO and CIT(A) and the paper book filed on behalf of the assessee. We have also considered the various decisions cited before us. In the instant case, the only dispute is regarding determination of disallowance of expenditure for earning tax free dividend income of Rs. 18,17,68,458/- the assessee disallowed on its own Rs.16.50 lakhs u/s 14A. Despite being asked by the AO to furnish the disallowance under rule 8D, the assessee did

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not furnish the details. The provisions of rule 8D inserted by the IT (Fifth Amendment) Rules 2008 with effect from 24.3.2008 are applicable for A.Y. 2008-09 and onwards. Therefore, the revenue authorities are bound to follow the mandatory provisions for calculation of disallowance u/s 14A. Therefore, we do not find any infirmity in the order of the CIT(A) upholding the action of the Assessing Officer for disallowing the deduction u/s 14A read with rule 8D. The contention of the assessee that the AO without satisfaction being reached invoked the provisions of Rule 8D, in our opinion, does not hold good especially in absence of non-furnishing of details for the purposes of calculation of disallowance at Rs. 16.50 lakhs by the assessee on its own. In this view of the matter and in absence of any distinguishable feature brought to our notice by the learned Counsel for the assessee against the order of the CIT(A), we do not find any infirmity in the same. Accordingly the same is upheld and the ground raised by the assessee is dismissed."

8. As it is clear from the finding of Tribunal that the assessee failed to furnish the details of disallowance under section 14A and, therefore, the disallowance made by the AO was found by the Tribunal without any infirmity. For the year under consideration the assessee has specifically raised a point before the AO that 97.82% of the investment is in the subsidiary companies and joint venture companies and, therefore, no expenditure was incurred for maintaining the portfolio on these investments or for holding the same. The assessee has also pointed out that these investments are long term investment and no decision is required in making the investment or disinvestment on regular basis because these investments are strategic in nature in the subsidiary companies on long term basis and, therefore, no direct or indirect expenditure is incurred. We find that the department has not disputed this fact that out of the total investment about 98% of the investment are in subsidiary companies of the assessee and, therefore, the purpose of investment is not for earning the dividend income but having control and business purpose and consideration. Therefore, prima facie the assessee has made out a case to show that no expenditure has been

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incurred for maintaining these long term investment in subsidiary companies. The Assessing Officer has not brought out any contrary fact or material to show that the assessee has incurred any expenditure for maintaining these investments or portfolio of these investments. In the case of Godrej & Boyce Mfg. Co. Ltd. (supra) Hon'ble Jurisdictional High Court while dealing with the issue of disallowance u/s 14A and application of Rule 8D has recorded the principles as laid down by the Hon'ble Supreme Court in the case of WalfortShare and Stock Brokers P. Ltd. [2010] (326 ITR 1,) in para 31 as under:-

> *(a) "The mandate of section 14A is to prevent claims for deduction of expenditure in relation to income which does not form part of the total income.*
>
> *(b) Section 14A(1) is enacted to ensure that only expenses incurred in respect of earning taxable income are allowed;*
>
> *(c) The principle of apportionment of expenses is widened by section 14A to include even the apportionment of expenditure between taxable and nontaxable income of an indivisible business;*
>
> *(d) The basic principle of taxation is to tax net income. This principle applies even for the purpose of section 14A and expenses towards non-taxable income must be excluded;*
>
> *(e) Once a proximate cause for disallowance is established – which is the relationship of the expenditure with income which does not form part of the total income – a disallowance has to be effected. All expenditure under the provisions of the Act has to be disallowed under section 14A Income which does not form part of the total income is broadly adverted to as exempt income as an abbreviated appellation."*

9. After considering these principles as emerged from the decision of Hon'ble Supreme Court in the case of Walfort Share

and Stock Brokers P. Ltd. (supra), Hon'ble Jurisdictional High Court has held in para 32 and 33 as under:-

"32. Sub-section (2) and (3) to section 14A were inserted by an amendment brought about by the Finance Act of 2006 with effect from April 1, 2007. Sub Sections (2) and (3) Provide as follows.

"14A.(2) The Assessing Officer shall determine the amount of expenditure incurred in relation to such income which does not form part of the total income under this Act in accordance with such method as may be prescribed, if the Assessing Officer, having regard to the accounts of the assessee, is not satisfied with the correctness of the claim of the assessee in respect of such expenditure in relation to income which does not form part of the total income under this Act.

(3) The provisions of sub-section (2) shall also apply in relation to a case where an assessee claims that no expenditure has been incurred by him in relation to income which does not form part of the total income under this Act :

Provided that nothing contained in this section shall empower the Assessing Officer either to reassess under section 147 or pass an order enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee under section 154 for any assessment year beginning on or before the 1st day of April,2001."

(The proviso was inserted earlier by the Finance Act of 2002 with retrospective effect from May 11, 2001)

33. Under sub-section (2), the Assessing Officer is required to determine the amount of expenditure incurred by an assessee in relation to such income which does not form part of the total income under the Act in accordance with such method as may be prescribed. The method, having regard to the meaning of the expression "prescribed" in section 2(33), must be prescribed by rules made under the Act. What merits emphasis

is that the jurisdiction of the Assessing Officer to determine the expenditure incurred in relation to such income which does not form part of the total income, in accordance with the prescribed method, arises if the Assessing Officer is not satisfied with the correctness of the claim of the assessee in respect of the expenditure which the assessee claims to have incurred in relation to income which does not part of the total income. Moreover, the satisfaction of the Assessing Officer has to be arrived at, having regard to the accounts of the assessee. Hence, sub-section (2) does not ipso facto enable the Assessing Officer to apply the method prescribed by the rules straightaway without considering whether the claim made by the assessee in respect of the expenditure incurred in relation to income which does not form part of the total income is correct. The Assessing Officer must, in the first instance, determine whether the claim of the assessee in that regard is correct and the determination must be made having regard to the accounts of the assessee. The satisfaction of the Assessing Officer must-be arrived at on an objective basis. It is only when the Assessing Officer is not satisfied with the claim of the assessee, that the Legislature directs him to follow the method that may be prescribed. In a situation where the accounts of the assessee furnish an objective basis for the Assessing Officer to arrive at a satisfaction in regard to the correctness of the claim of the assessee of the expenditure which has been incurred in relation to income which does not form part of the total income, there would be no warrant for taking recourse to the method prescribed by the rules. For, it is only in the event of the Assessing Officer not being so satisfied that recourse to the prescribed method is mandated by law. Sub-section (3) of section 14A provides for the application of sub-section (2) also to a situation where the assessee claims that no expenditure has been incurred by him in relation to income which does not form part of the total income under the Act. Under the proviso, it has been stipulated that nothing in the section will empower

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the Assessing Officer, for an assessment year beginning on or before April 1,2001, either to reassess under section 147 or pass an order enhancing the assessment or reducing the refund already made or otherwise increasing the liability of the assessee under section 154."

10. It has been made clear by the Hon'ble High Court that sub-section (2) does not ifso facto empower the AO to apply the method prescribed by Rules straightaway without considering whether the claim made by the assessee is correct.

11. The assessee has relied upon various decisions of this Tribunal wherein an identical issue has been considered. In the case of Garware Wall Ropes Limited Vs. Addl. CIT (supra), the Tribunal while deciding an identical issue has held in para 2.4 as under:-

"We have considered the rival submission and carefully perused the relevant records. So far as the issue regarding disallowance u/s 14A in the case where no dividend has been received, the same is covered against the assessee by the order of Tribunal in assessee's own case for the assessment year 2008-09, wherein the Tribunal has followed the decision of special bench of Tribunal while deciding the issue. Therefore, we do agree with the finding of the Tribunal on this point. Further since the assessee has raised the new plea in the year under consideration that no expenditure had been incurred by the assessee for earning the exempt income or for the investment in question. We find merit and substance in the contention of the assessee on this point because the investment has been made by the assessee in the group concern and not in the shares of any un-related party. Therefore, the primary object of investment is holding controlling stake in the group concern and not earning any income out of investment. Further the investment were made long back and not in the year under consideration. Therefore, in view of the fact that the investment are in the group

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concern we do not find any reason to believe that the assessee would have incurred any administrative expenses in holding these investments. The Assessing Officer has not brought on record any material to show that the assessee has incurred any expenditure in relation to the income which does not form part of the total income. Section 14A has within it implicit the notion of apportionment in the cases where the expenditure is incurred for composite/indivisible activities in which taxable and non taxable income is received but when no expenditure has been incurred in relation to the exempt income then principle of apportionment embedded in section 14A has no application. The object of section 14A is not allowing to reduce tax payable on the non exempt income by deducting the expenditure incurred to earn the exempt income. In the case in hand it is not the case of the revenue that the assessee has incurred any direct expenditure or any interest expenditure for earning the exempt income or keeping the investment in question. If there is expenditure directly or indirectly incurred in relation to exempt income the same cannot be claimed against the income which is taxable. For attracting the provisions of section 14A- "there should be proximate cause for disallowance which has relationship with the tax exempt income as held by the Hon'ble Supreme Court in case of CIT Vs. Walfort Share and Stock Brokers P. Ltd. (326 ITR 1). Therefore, there should be a proximate relationship between the expenditure and the income which does not form part of the total income. In the case in hand the assessee has claimed that no expenditure has been incurred for earning the exempt income, therefore, it was incumbent on the AO to find out as to whether the assessee has incurred any expenditure in relation to income which does not form part of the total income and if so to quantify the expenditure of disallowance. The AO has not brought on record any fact or material to show that any expenditure has been incurred on the activity which has resulted into both taxable and non taxable income. Therefore,

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in our view when the assessee has prima facie brought out a case that no expenditure has been incurred for earning the income which does not form part of the total income then in the absence of any finding that expenditure has been incurred for earning the exempt income the provisions of section 14A cannot be applied. Accordingly we delete the addition/disallowance made by AO u/s 14A r.w. Rule 8D."

12. A similar view was taken by the Delhi Bench of this Tribunal in the case of M/s Oriental Structural Engineers (P) Ltd (supra) which has been confirmed by the Hon'ble Delhi High Court vide decision dated 15.01.2013 in para 6.3 as under:-

"6.3 We have carefully considered the submissions and perused the records. We find that Ld. Commissioner of Income Tax (Appeals) has given a finding that only interest of Rs 2,96,731/- was paid on funds utilized for making investments on which exempted income was receivable. Further, Ld. Commissioner of Income Tax (Appeals) has observed that in respect of investment of Rs 6,07,775,000/- made in subsidiary companies as per documents produced before him, they are attributable to commercial expediency, because as per submission made by the assessee, it had to form Special Purpose Vehicles (SPY) in order to obtain contracts from the NHAI and the SPVs so formed engaged the assessee company as contract to execute the works awarded to them (i.e. SPVs) by the NHAI. In its profit and loss account for the year, the assessee has shown the turnover from execution of these contracts and therefore no expense and interest attributable to the investments made by the appellant in the PSVs can be disallowed u/s 14A LW. Rule 8D because it cannot be termed as expense/interest incurred for earning exempted income. Under the circumstances, Ld. Commissioner of Income Tax (Appeals) is correct in holding that disallowance of a further sum Rs 40,556/- calculated@2%ofthedividend earned is

sufficient. Under the circumstances, we do not find any infirmity in the order of the Ld. Commissioner of Income Tax (Appeals), hence we uphold the same."

13. In view of the above discussion and facts and circumstances of the case we agree with the view taken by this Tribunal in the above stated cases and accordingly hold that the assessee has brought out a case to show that no expenditure has been incurred for maintaining the 98% of the investment made in the subsidiary companies, therefore, in the absence of any finding that any expenditure has been incurred for earning the exempt income, the disallowance made by the AO is not justified, accordingly the same is deleted."

12. The issue of recording objective satisfaction by the Assessing Officer, before proceeding to determine the amount of expenditure incurred in relation to such income which does not form part of the total income under the Income-tax Act, was also examined by the Pune Bench of the Tribunal in the case of Kalyani Steels Ltd. vs. Addl. CIT (supra) and the Pune Bench, following the judgment of the Hon'ble Bombay High Court in the case of Godrej And Boyce Mfg. Co. Ltd. vs. Dy. CIT & Another (supra), was also of the view that recording of objective satisfaction by the Assessing Officer with regard to the correctness of the claim of the assessee is mandatorily required in terms of section 14A(2) of the Act. The relevant observations of the Tribunal are also extracted hereunder:-

"8. We have carefully considered the rival submissions. Section 14A of the Act contemplates that for the purposes of computing the total income, no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to income which does not form part of the total income under the Act. Sub-section (2) of section 14A of the Act prescribes that the Assessing Officer shall determine the amount of expenditure incurred in relation to such income which does not form part of the total income in accordance with such method as may be prescribed, such prescribed method being contained

in rule 8D of the Rules. However, the aforesaid empowerment of the Assessing Officer to invoke application of rule 8D of the Rules is superscribed by a condition contained in sub-section (2) of section 14A of the Act which is to the effect that the Assessing Officer, having regard to the accounts of the assessee, is not satisfied with the correctness of the claim of the assessee in respect of expenditure incurred in relation to the income which does not form part of the total income. Therefore, the invoking of rule 8D of the Rules in order to compute the disallowance u/s 14A of the Act is neither automatic and nor is triggered merely because assessee has earned an exempt income. The invoking of rule 8D of the Rules is permissible only when the Assessing Officer records the satisfaction in regard to the incorrectness of the claim of the assessee, having regard to the accounts of the assessee. In other words, section 14A(2) of the Act envisaged a condition precedent for invoking rule 8D of the Rules and computing disallowance thereof only if the Assessing Officer records that he is not satisfied with the correctness of the claim of the assessee in respect of such expenditure, having regard to the account of the assessee. In this context, it would be appropriate to refer to the following observations of the Hon'ble Bombay High Court in the case of Godrej & Boyce Manufacturing Co. Ltd. (supra) :-

"70. Now, in dealing with the challenge it is necessary to advert to the position that sub-section (2) of section 14A prescribes a uniform method for determining the amount of expenditure incurred in relation to income which does not form part of the total income only in a situation where the Assessing Officer, having regard to the accounts of the assessee is not satisfied with the correctness of the claim of the assessee in respect of such expenditure. It, therefore, merits emphasis that sub-section (2) of section 14A does not authorize or empower the Assessing Officer to apply the prescribed method irrespective of the nature of the claim made by the assessee.

The Assessing Officer has to first consider the correctness of the claim of the assessee having regard to the accounts of the assessee. The satisfaction of the Assessing Officer has to be objectively arrived at on the basis of those accounts and after considering all the relevant facts and circumstances. The application of the prescribed method arises in a situation where the claim made by the assessee in respect of expenditure which is relatable to the earning of income which does not form part of the total income under the Act is found to be incorrect. In such a situation a method had to be devised for apportioning the expenditure incurred by the assessee between what is incurred in relation to the earning of taxable income and that which is incurred in relation to the earning of non-taxable income. As a matter of fact, the memorandum explaining the provisions of the Finance Bill, 2006, and the Central Board of Direct Taxes circular dated December 28, 2006, state that since the existing provisions of section 14A did not provide a method of computing the expenditure incurred in relation to income which did not form part of the total income, there was a considerable dispute between taxpayers and the Department on the method of determining such expenditure. It was in this background that sub- section (2) was inserted so as to provide a uniform method applicable where the Assessing Officer is not satisfied with the correctness of the claim of the assessee. Sub-section (3) clarifies that the application of the method would be attracted even to a situation where the assessee has claimed that no expenditure at all was incurred in relation to the earning of non-taxable income.

71. Parliament has provided an adequate safeguard to the invocation of the power to determine the expenditure incurred in relation to the earning of non-taxable income by adoption of the prescribed method. The invocation of the power is made conditional on the objective satisfaction of the Assessing Officer in regard to the correctness of the claim of the assessee, having regard to the accounts of the assessee. When

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> *a statute postulates the satisfaction of the Assessing Officer "Courts will not readily defer to the conclusiveness of an executive authority's opinion as to the existence of a matter of law or fact upon which the validity of the exercise of the power is predicated". (M. A. Rasheed v. State of Kerala [1974] AIR 1974 SC 2249*). A decision by the Assessing Officer has to be arrived at in good faith on relevant considerations. The Assessing Officer must furnish to the assessee a reasonable opportunity to show cause on the correctness of the claim made by him. In the event that the Assessing Officer is not satisfied with the correctness of the claim made by the assessee, he must record reasons for his conclusion. These safeguards which are implicit in the requirements of fairness and fair procedure under article 14 must be observed by the Assessing Officer when he arrives at his satisfaction under sub-section (2) of section 14A. As we shall note shortly hereafter, sub-rule (1) of rule 8D has also incorporated the essential requirements of sub-section (2) of section 14A before the Assessing Officer proceeds to apply the method prescribed under sub-rule (2). [underlined for emphasis by us]*

9. The aforesaid observations of the Hon'ble High Court clearly show that the satisfaction of the Assessing Officer with regard to the correctness or otherwise of the claim made by the assessee must be based on reasons and on relevant considerations. Ostensibly, the invoking of rule 8D of the Rules in order to compute the disallowance u/s 14A of the Act is to be understood as being conditional on the objective satisfaction of the Assessing Officer with regard to the incorrectness of the claim of the assessee, having regard to the accounts of the assessee. At this stage, we may also touch-upon a similar view expressed by the Hon'ble Delhi High Court in the case of Maxopp Investment Ltd. & Ors. vs. CIT, (2012) 247 CTR 162 (Del), wherein reference has been made to the judgment of the Hon'ble Bombay High Court in the case of Godrej & Boyce Manufacturing Co. Ltd. (supra). As per the Hon'ble Delhi High Court, the requirement of the Assessing Officer embarking upon a determination of the amount

of expenditure incurred in relation to exempt income in term of rule 8D of the Rules would be triggered only if the Assessing Officer records a finding that he was not satisfied with the correctness of the claim of the assessee in respect of such expenditure. According to the Hon'ble Delhi High Court, sub-section (2) of section 14A of the Act deals with cases where the assessee specifies a positive amount of expenditure in relation to income which does not form part of the total income under the Act and sub-section (3) applies to cases where the assessee asserts that no expenditure has been incurred in relation to such exempt income. Explaining further, as per the Hon'ble High Court in both the cases the recourse to rule 8D of the Rules is possible only if the Assessing Officer records a finding that he was not satisfied with the correctness of the claim of the assessee in respect of such expenditure.

10. In the aforesaid background, now, we may examine the facts of the present case. In this case, assessee has earned by way of dividends a sum of Rs.5,45,58,685/-, which is exempt u/s 10(38) of the Act and thus the same does not form part of the total income under the Act. In the computation of income, assessee having regard to section 14A of the Act, determined the amount of expenditure incurred in relation to such income at Rs.5,00,000/-. The Assessing Officer has not found it acceptable and has instead determined the amount of expenditure in relation to such income by applying rule 8D of the Rules. Ostensibly, the action of the Assessing Officer cannot be upheld unless he has complied with the pre-requisite of invoking rule 8D of the Rules, namely, recording of an objective satisfaction with regard to the claim of the assessee that an expenditure of Rs.5,00,000/- has been incurred in relation to the exempt income, is incorrect. In order to examine the aforesaid compliance with the pre-condition, we have perused the para 4 to 4.2 of the assessment order and find that no reasons have been advanced as to why the disallowance determined by the assessee was found to be incorrect, having regard to the accounts of the assessee. The only point made by the Assessing Officer is to the effect that "the said disallowance was not acceptable". In-fact, we

find that the assessee made detailed submissions to the Assessing Officer, which have been reproduced by the CIT(A) in para 3.2.1 of his order. As per the assessee, the determination of disallowance u/s 14A of the Act of Rs.5,00,000/- was based on the employee costs and other costs involved in carrying out this activity. Further, assessee also explained that the shares which have yielded exempt income were acquired long back out of own funds and no borrowings were utilized. The mutual fund investments were claimed to be also made out of surplus funds. It was specifically claimed that no fresh investments have been made during the year under consideration in shares yielding exempt income. All the aforesaid points raised by the assessee have not been addressed by the Assessing Officer and the same have been brushed aside by making a bland statement that the disallowance is "not acceptable" . Therefore, in our view, in the present case, the Assessing Officer has not recorded any objective satisfaction in regard to the correctness of the claim of the assessee, which is mandatorily required in terms of section 14A(2) of the Act and therefore his action of invoking rule 8D of the Rules to compute the impugned disallowance is untenable. Accordingly, the orders of the authorities below are set-aside on this aspect and the Assessing Officer is directed to retain the disallowance u/s 14A of the Act to the extent of Rs.5,00,000/-, as returned by the assessee."

13. In that case, before proceeding to determine the amount of expenditure, the Assessing Officer has recorded that the said allowance was not acceptable. The statement recorded by the Assessing Officer was not considered to be objective satisfaction by the Tribunal. In the instant case, the Assessing Officer has simply recorded that the contention of the assessee is not acceptable. Therefore, in the light of the aforesaid orders of the Tribunal and other judicial pronouncements, we are of the view that the Assessing Officer has not recorded any objective satisfaction with regard to the correctness of the claim of the assessee.

14. In the case of DCIT vs. M/s Jindal Photo Limited in I.T.A. No. 814/Del/2011, the Delhi Bench of the Tribunal has also expressed

similar view, in which it has been held that satisfaction of the Assessing Officer is pre-requisite to invoke the provisions of Rule 8D. Therefore, in the absence of objective satisfaction by the Assessing Officer, the disallowance made under rule 8D is not sustainable in the eyes of law. Moreover, the investment was made in the case of subsidiary companies, therefore, in those cases disallowance under section 1A(2) of the Act cannot be worked out unless and until it is established that certain expenditures are incurred by the assessee in these investments.

15. Keeping in view the totality of the facts and circumstances of the case, we are of the considered opinion that invocation of rule 8D without recording objective satisfaction by the Assessing Officer is not proper and we accordingly set aside the order of the ld. CIT(A) on this issue and delete the addition made in this regard."

34. Undisputedly, in the instant case, the Assessing Officer has not recorded any objective satisfaction with regard to the correctness of the accounts relating to dividend income of the assessee. He straightaway computed the disallowance as per provisions of section 14A of the Act read with per ruled 8D of the rules. Therefore, in view of the aforesaid order of the Tribunal, we are of the view that invocation of provisions of section 14A of the Act without recording an objective satisfaction is not proper, therefore, we set aside the order of the ld. CIT(A) in this regard and delete the addition of the disallowance made under section 14A of the Act.

35. The cross objection is preferred by the assessee in support of the order of the ld. CIT(A). Since the issue relating to cost of land adopted by the Assessing Officer is restored to the file of the Assessing Officer, the cross objection is partly allowed for statistical purpose.

I.T.A. No. 301/LKW/2013 & C.O. No.19/LKW/2013:

36. In this appeal, the dispute was raised with regard to the deemed cost of land as on 1.4.1981 adopted by the Assessing Officer. This issue was

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examined by us in the foregoing appeal, in which we have set aside the order of the ld. CIT(A) and restored the matter to the file of the Assessing Officer to determine the fair market value of the land as on 1.4.1981 for computing the capital gain. Following the view taken in the foregoing appeal, the issue relating to the deemed cost of land is restored to the file of the Assessing Officer with a direction to determine the fair market value of the land as on 1.4.1981 for computing the long term capital gain. Accordingly, this appeal of the assessee is allowed for statistical purposes.

37. The cross objection is filed in support of the order of the ld. CIT(A). Since the issue relating to cost of land adopted by the Assessing Officer is restored to the file of the Assessing Officer, the cross objection is partly allowed for statistical purpose.

38. In the result, the appeals of the Revenue in I.T.A. No. 61/LKW/2012 is dismissed and I.T.A. No. 62/LKW/2012 and 301/LKW/2013 are partly allowed for statistical purposes and cross objections of the assessee in C.O. No.18/LKW/12 is dismissed and C.O. No.19/LKW/12 and C.O. No.19.LKW/2013 are partly allowed for statistical purposes.

Order was pronounced in the open court on the date mentioned on the captioned page.

Sd/-	Sd/-
[A. K. GARODIA]	[SUNIL KUMAR YADAV]
ACCOUNTANT MEMBER	JUDICIAL MEMBER

DATED: 23rd June, 2015

JJ:2704

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1. Appellant
2. Respondent
3. CIT(A)

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4. CIT
5. DR

Assistant Registrar