2013-2014
22nd Year

ALL GUJARAT FEDERATION OF TAX CONSULTANTS

Room No. 114, Income Tax Office, 1st Floor, Narayan Chambers, Nr. Nehru Bridge, Ashram Road, Ahmedabad - 380 009. Phone : 2657 6311 Extn. : 603 Email : president@agftc.co.in Web : www.agftc.co.in

TAX GURJARI

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Voice of All Gujarat Federation of Tax Consultants

PRESIDENT'S MESSAGE

My Dear Follow Members,

It is a mixed feeling as this shall be my last formal communication from the office of the President of All Gujarat Federation of Tax Consultants.

All of us, men and women; have dreams. I also had a dream of my journey in this prestigious Federation. I firmly believe, we may be able to exist, but we will cease to live in the absence of dreams. I tried my best to keep them alive through my various actions and programmes during this year.

When I look back, I find that we have really come a long way since the inception of this Federation in the year 1992. Our Federation consists of all the Tax Associations of the State of Gujarat. It has completed 22 years of its meaningful existence and shall be soon celebrating its Silver Jubilee. Growing at a slow and steady pace, we have crossed the membership of 1100 consisting of all the Associations and tax practitioners in the nook and corner of our State of Gujarat. We have worked proactively to create awareness and popularize the importance of our Federation. With our strong conviction to practice our profession ethically, we have increased our endeavors to assist the Income Tax Department to improve the administration and resolve the problems of tax payers as well as tax consultants.

This is the 4th and last issue of Tax Gurjari being published in soft copies. If you recall, I promised in the first meeting that every quarter we shall be publishing the Tax Gurjari Magazines and send it by mail covering important latest decisions of Tribunals, High Courts and Supreme Courts as well as informative articles on varied subjects on Direct and Indirect taxes. During this year, we did various activities and programmes which I am not repeating or reproducing as they have been elaborately mentioned in the Annual Report recently circulated to you along with the notice of Annual General Meeting. While conducting these activities by way of organizing seminars and conventions at different places in small and big cities and while meeting various senior departmental officers, I realized that tax practice is an unending process. Every year there are new issues, new problems and new officers and bureaucrats to resolve or deal with the same. I also experienced finest moments in my life while meeting and listening to various members of the Federation of different age group hailing from different places and having different kinds of practices. It was not only a thrilling but life time memorable experience.

This communication would not be complete if I do not thank my membership fraternity, all my members from Palanpur and Mehsana to Petlad, from Dahod, Godhra to Rajkot and Bhavnagar, from Nadiad to Baroda and Surat and above all my local members from Ahmedabad. I thank each one of you for carrying out my dreams so as to make them reality. The most heartening experience of this entire journey was the continuous non-stop support and guidance from the team of Hon. Past Presidents. I have yet to find out an institution where involvement, participation and guidance from the Hon'ble Past Presidents is so sincere, continuous and selfless.

A special mention is required for Past President Shri Biharibhai B. Shah and Shri Rajesh C. Shah for taking lots of pain and devoting substantial time for carrying out long pending and overdue amendments in the Constitution of the Federation. The same are now for consideration of Hon'ble Members in the ensuing Annual

General Meeting to be held on Sunday, the 20th July, 2014. I am also thankful to my Vice President Shri Samir Jani. Inspite of geographical distance, he had been a continuous support to me in all my endeavors and actions with a smiling face.

Last but not the least; I must convey my deep sense of thanks and gratitude to my Hon. Secretary, CA. Rutvij P. Shah. He had done his article training in my office, and is now well established independent practicing Chartered Accountant, but was available to me 24 x 7 for any and every kind of work pertaining to the Federation. His company in all professional endeavors and also in tours and visits were extremely comfortable, since both of us share the goal of doing something positive for the professional fraternity. His enthusiasm; to do something for the members allowed the Federation to have all the latest circulars, notes, decisions and other matters of professional interest at the earliest possible in soft copies and by mail.

I can only end by wishing the incoming President and his team of All Gujarat Federation of Tax Consultants all the very best with an assurance that I shall strive equally hard and work also with same enthusiasm after handing over the charge to him. Long live the Federation.

With best regards,

3rd July, 2014

(SUNIL TALATI)
PRESIDENT

EDITORIAL

Dear friends,

It is a matter of joy to come out with fourth issue of Tax Gurjari during the year 2013-14. It is a wonderful journey and we have received great support from the contributors for articles and other materials published in the e-journal.

You may recall that I had stated about desire of the President and Journal Committee to publish the e-journal at a shorter interval. Though the support received by us is tremendous, we could not go beyond quarterly issue of the e-journal. Publishing the e-journal on monthly basis requires even greater efforts on the part of all of us. I hope the future Editor would get greater contributions from various sections of the Federation for eventually publishing the e-journal on monthly basis.

The economy of the country is in shatters since last 4 years. It requires great efforts on the part of government, bureaucracy, business community as well as professionals, being an integral part of the society, to rebuild the vibrant economy. We owe our duty to carry out our profession in ethical manner and assist the clients in better compliance of law, while guarding their interest. This would be a small but crucial step in the revival of the economy and creating brighter image of our country throughout the world.

I am thankful to the President and Honorary Secretary of the Federation for extending their whole-hearted support throughout the year.

I wish you all fulfilling and prosperous professional career ahead.

Warm regards,
K. V. Karkar
Editor

Notarians honour their President Dhiresh T. Shah with Life Time Achievement Award

Mr. Dhiresh T. Shah, President of All India Notaries Association and Notaries Association Gujarat was honoured with Life Time Achievement Award by Notarians for his selfless services in carving deserving status for Notarians in Government and in public by providing dynamic leadership in securing their rightful privileges and hike in Notary fees.

Mr. Dhiresh Shah, an eminent Tax Consultant by profession has been responsible in helping a number of social, medical and educational institutions to strengthen their administration. His motto has been nothing but the best whether it is selection of staff or required equipment machinery. Mr. Shah received the award at the worthy hands of Justice Mohit Shah, Chief Justice of Bombay High Court who described Mr. Dhiresh T. Shah as Parasmani whose one touch turns everything gold.

ACCOUNTING AND DIRECT TAXES ISSUES IN CONTRUCTION INDUSTRY

CA. Vimal C. Punmiya
vimalpunmiya@gmail.com

1. INTRODUCTION

Income–tax Act, 1961 (hereinafter referred to as 'The Act') is the only legislation of our country which refers to 92 Central Acts and various State Legislations. To understand the various taxation issues relating to Real Estate Transactions, it is very essential to know the provisions of general law with special reference to Transfer of Property Act, Registration Act, Stamp Act, Development Control Regulations, etc. In this article, we have made an attempt to discuss some of the very important taxation issues relating to Real Estate Transactions.

Mumbai is supposed to be seventh biggest city in the world with beautiful coastal line. Mumbai is the commercial and financial capital of India and also a Gateway of International Trade and Industrial Development of India.

2. METHODS OF ACCOUNTING

a. PROJECT COMPLETION METHOD

A method of recognizing revenues and costs from a long-term project in which profit is recorded only when the project has been completed. Even if payments are received while the project is in progress, no revenues are recorded until its completion. The completed-contract method is a conservative way of accounting for long-term undertakings and is used for certain types of construction projects.

It is held that recognition/identification of income under the Act, is attainable by several methods of accounting. It may be noted that the same result could be attained by any one of the accounting methods. Completed contract is one such method. Similarly, percentage of completion is another such method.

CIT v/s Bilahari Investments (P) Ltd. [(2008) 299 ITR 1 SC]

b. PERCENTAGE COMPLETION METHOD

Project completion method is a method of recognizing revenues and costs from a long-term project in relation to the percentage completed during the course of the project. Thus, the percentage of completion method allows a business profits (or losses) on a project before its completion.

It is held that assessee-contractor having offered profits for tax on the basis of percentage completion method which is a standard accounting practice and has been constantly followed by the assessee in subsequent years, the same could not be rejected.

CIT vs. Advance Construction Co. (P) Ltd. [(2005) 275 ITR 30 (Guj)]

c. CHANGE OF METHOD OF ACCOUNTING

Disclosure of changes in an accounting policy used for construction contracts should be made in the financial statements giving the effect of the change and its amount. However, if a contractor changes from the percentage of completion method to the completed contract method for contracts in progress at the beginning of the year, it may not be possible to quantify the effect of the change. In such cases, disclosure should be made of the amount of attributable profits reported in prior years in respect of contracts in progress at the beginning of the accounting period.

It is held that the assessee having changed his method of accounting from work-in-progress in original return to project completion method in revised return, assessment had to be made as per revised return.

Satish H. Patel [93 TTJ 458 (Pune)]

3. DISCLOSURE IN THE COURSE OF SEARCH – WHETHER INCOME MUST BE TAXED ON COMPLETION OF THE PROJECT?

The conduct of search and seizure operation in a particular year does not lead to an inference that the undisclosed income detected as a consequence thereof has to be taxed in the assessment year relevant to the previous year in which search was conducted. In other words, accounting of profits has yet to be made on the basis of method of accounting followed by the assessee.

It is held that undisclosed income in the form of 'on money' stood established by seizure of document read with statement recorded under s. 132(4); however in computing undisclosed income, expenditure incurred has to be allowed; income discovered has to be taxed in assessment years as per method of accounting followed by assessee. ***Dhanvarsha Builders & Developers (P) Ltd. vs. DCIT [(2006) 102 ITD 375 (Pune)]***

4. FINANCE COST, INDIRECT COST AND COMPUNDING CHARGES

A. INTEREST ON BORROWED CAPITAL – SCOPE OF SECTION 36(1)(iii)

The amount of the interest paid in respect of capital borrowed for the purposes of the business or profession is allowed as deduction.

[Provided that any amount of the interest paid, in respect of capital borrowed for acquisition of new asset for extension of existing business or profession (whether capitalised in the books of account or not); for any period beginning from the date on which the capital was borrowed for acquisition of the asset till the date on which such asset was first put to use, shall not be allowed as deduction.]

It is held that construction project undertaken by the assessee-builder constituted its stock-in-trade and the assessee was entitled to deduction under s. 36(1)(iii) in respect of interest on loan obtained for execution of said project.

CIT vs. Lokhandwala Construction, (2003) 260 ITR 579 (Bom)

It is held that the assessee following project-completion method of accounting, the interest identifiable with that project should be allowed only in the year when the project is completed and the income from that project is offered for taxation. The same cannot be deducted as period cost from year to year. True profits in such a case can be determined only when entire cost of the project, direct or indirect, including finance cost is added to the value of work-in progress.

Wallstreet Constructions Ltd. & Anr. Vs. JCIT 2006 101 ITD 156 (Mum) (SB)

It is held that even though assessee was following competed contract method for returning its income, its claim of finance cost as a period cost in nature of interest was allowable in the year in which it was incurred or accrued, in accordance with AS – 7 issued by the ICAI.

JCIT vs. Raheja (P) Ltd. (2006) 102 ITD 414 (Mum.)

B. ADVERTISEMENT EXPENSES TO BE CAPITALISED AS WORK-IN-PROGRESS

It is held that assessee following project completion method, and advertisement expenses of the two projects being allocable to individual project, such advertisement expenses have to be capitalized as work–in–progress to be allowed deduction in the year of completion of project.

Income Tax Officer vs. Panchvati Developers [115 TTJ 139 (Mum)]

C. WHETHER COMPOUNDING CHARGES PAID BY BUILDERS ALLOWED AS A DEDUCTION

In this case, it was held in the order passed by a competent authority of Town Planning in unmistakable terms stated that he had permitted the payment of compounding charges by erring builders to regularize the infirmity in the building construction. There could not be any doubt that what had been done was to permit the assessee to *compound the offence committed by it putting up an unauthorized construction.*

Explanation to sec. 37(1) defines that any expenditure incurred for any purpose which is an offence or which is prohibited by law is not entitled to deduction. Hence, compounding of the offence under Corporation Act cannot take away the rigour of explanation to sec 37 and the deduction is not available.

Mamta Enterprises – [135 Taxman 393 (Karnataka)]

5. PROPERTY V/S BUSINESS INCOME

With several malls and business centers remerging taxability of rental income arising therefrom is an important issue. Supreme Court in **Shambhu Investment (P) Ltd. v. CIT (2003) 263 ITR 143 (SC)** has held that "*income derived from letting is assessable as income from property and not business income. In this case assessee was letting out furnished premises on monthly rent basis to various parties along with furniture, fixtures, light, air-conditioners, etc., for being used as "table space*".

Under the agreement, the assessee is also providing services like watch and ward staff, electricity, water and other common amenities to the occupiers. These services are not separately charged. Entire cost of property is already recovered by way interest–free advance by the assessee. Only intention was to let out the portion of premises to respective occupants. It was held that income derived from letting rightly held assessable as income from property and not business income.

It was held that income derived by assessee from shopping malls/business center was assessable as business income and not as income from house property. It held that "The fact that the apex court held that the income earned by Shambhu Investment (P) Ltd. is assessable as property income has no relevance in the facts and circumstances of the present case. Because in that case facts showed that the main intention was to earn rental income. That was why the entire cost of the property was recovered from the tenants by way of interest–free advance. In the instant case, on the other hand, the assessee had taken bank loans to finance his projects like any other businessman. As discussed hereinabove, every action of the present assessee appears to be with the sole object of commercial exploitation of the premises."

PFH MALL AND RETAIL MANAGEMENT LTD. V. ITO (2008)110 ITD 337 (KOL)

Letting out of all the rooms of a property, used as a guest house by the assessee to a bank to be used as a training centre was a part on running of the lodge business and, therefore, income from such leasing was assessable as business income and necessary income was assessable as business expenditure.

CIT V. PATESHWARI ELECTRICAL & ASSOCIATED INDUSTRIES (P) LTD. (2006) 282 ITR 61 (ALL)

When property has been let out not only as property but with services which is a complex letting, the income cannot be said to be derived from mere ownership of house property but may be assessable as income from business. If the owner of a property carries on upon the property some activities which results in profits and gains arising, not from the ownership of the property but from the owners used thereof, letting various services to the tenants, those profits and gains may be chargeable under section 28 as income from business, apart from the assessment u/s 22 in respect of income from house property.

CIT V. SARABHAI (P) LTD. (2003) 263 ITR 197 (GUJ.)

6. INTEREST EARNED ON SURPLUS MONEY PARKED AS FIXED DEPOSIT WITH BANK TAXED UNDER THE HEAD THE BUSINESS

It is held that advances from customers intending to purchase flats, deposit of surplus money with bank in course of business – the accrued interest arises out of business activities, hence such interest income is assessable as business income and not as income from other source.

CIT V. LOK HOLDINGS 308 ITR 356 (BOM)

It is held that merely because the income has been assessed as business income, it will not *automatically confer the benefit of a particular deduction once there is a rider provision that such income should be derived from a particular source.*

TRICOM INDIA LTD V. ACIT, ITA NO. 1924/ MUMBAI/08, ITAT MUMBAI BENCH E

7. CAPITAL GAIN vs. BUSINESS INCOME

Whether a particular asset is stock-in-trade or capital asset does not depend upon the nature of the article, but the manner in which it is held. The same item may be stock-in-trade in the hands of the assessee who deals in that item. But it will be capital asset in the case of an assessee who uses it for earning income or holds as an investment. For example, a dealer in real estate holds a piece of land or house property as stock-in-trade. But it will be a capital asset in the hands of a person who holds it as an investment and derives income from leasing or renting of the property.

Even stock-in-trade may become capital asset in certain circumstances and *vice versa*. If an assessee who deals in certain goods or commodities as trader, on closure of the business, retains the existing stocks as investment, the stocks will become capital asset in his hands from the time of closure, notwithstanding that they were stock-in-trade earlier in his hands. Even in the course of a business, an assessee may try to transfer some of the stock-in-trade from his trading activity and decide to hold them as investment.

The stocks so held would assume the character of capital asset from the date of such holding. This may usually happen in the case of dealer in shares and real estate. But in all these cases, the finding will be one of fact depending upon the intention and conduct of the assessee supported by direct and circumstantial evidence. Similarly, when a capital asset is converted into stock-in-trade, the same will no longer be capital asset. However, this situation is covered by section 45(2).

The activity of an assessee in dividing the land into plots and not selling it as a single unit as he purchased, goes to establish that he was carrying on business in real property and it is a business venture.

RAJA J. RAMESHWAR RAO V CIT (1961) 42 ITR 179 (SC)

Ordinarily, where a person acquired land with a view to selling it later after developing it and actually divided the land into plots and sold the same in parcels, the activity could only be described as a business adventure. Generally speaking, the original intention of the party in purchasing the property, the magnitude of the transaction of purchase, the nature of the property, the length of its ownership and holding, the conduct and subsequent dealings of the assessee in respect of the property, the manner of its disposal and the frequency and multiplicity of transactions afforded valuable guides in determining whether the assessee was carrying on a trading activity and whether a particular transaction should be stamped with the character of a trading adventure.

CIT V TRIVEDI (V.A.) (1988) 172 ITR 95 (BOM)

However, on some different facts and circumstances, it was held that profit on the sale of land after plotting it out to secure better price cannot be taxed as profit from an adventure in the nature of trade. It shall be taxed under the head 'capital gain'. ***CIT V SHASHI KUMAR AGRAWAL (2003) 131 TAXMAN 823 (ALL)***

Assessee had purchased a plot of land in 1958. In view of the Urban Land (Ceiling and Regulation) Act, 1976, she applied for construction of group housing on the excess land and sold the land to a developer and builder. The Assessing Officer held that the installments received from the builder are business income. The Tribunal held that it is not business income as there was no adventure in the nature of trade. On reference, the Delhi High Court upheld the decision of the Tribunal and held as under:

"The plot was purchased in the year 1958 and after the operation of law, namely, the Urban Land (Ceiling and Regulation) Act, 1976, it was not possible for the assessee to retain the land. It was very clear that on the assessee's part there was only an intention to transfer the land

and not the portion that may be constructed by the builder on a future date. Clause 3 of the agreement merely provided the mode of payment. On the facts and in the circumstances of the case, the Tribunal was right in holding that there was no adventure in the nature of trade and thereby deleting business income of Rs. 11,87,387 from the income of the assessee."

CIT v Radha Bai (2005) 272 ITR 264 (Del)

Where some land, which was contributed by partners as capital and used as brick field and later given for development, upholding the finding of the Tribunal, it was held that the firm did not acquire the land, with a view to sell it at a profit. It was treated in the accounts as a fixed asset given to other for outright development without the assessee itself plotting it out, so that it had continued to be a capital asset. There was no scope, it was found, for holding it either as business or even an adventure in the nature of trade. ***CIT v Mohakampur Ice & Cold Storage (2006) 281 ITR 354 (All)***

What was necessary was to find out the intention of the assessee at the time of the purchase of land. Where the land was never purchased by the assessee, she acquired the same on the basis of a will on the death of her husband. She sold the same in parcels because the huge area could not be sold in one transaction. Such an activity could not amount to trade or business within the meaning of the Act.

CIT V SUSHILA DEVI JAIN (2003) 259 ITR 671 (P&H)

A company can hold shares as stock-in-trade for the purpose of doing business of buying and selling of such shares, while at the same time it can also hold other shares as its capital for the purpose of earning dividend income. Thus, where the finding was that the shares in question were never treated by the assessee as stock-in-trade and they were held for earning dividend only, it was held that the Tribunal was right in law in holding that the profit on sale of such shares was to be treated as capital gains.

CIT v N.S.S. Investments Pvt. Ltd. (2005) 277 ITR 149 (Mad)

Where it was an admitted position that the land in question was held as a capital asset by the assessee and not as a business asset and it had also been noticed that the assessee had relinquished the land in lieu of forest department allowing use of their land for laying down the drainage and the question was as to whether loss arising on such transfer could be allowed as a business loss, it was held that the loss arising on account of transfer of land to the forest department in lieu of the use of forest land for laying the drainage for discharge of effluent, was capital loss and could not be allowed as a business loss.

Shreyans Industries Ltd. v Jt. CIT (2005) 277 ITR 433 (P&H)

8. <u>80-IB(10) [DEVELOPING AND BUILDING HOUSING PROJECTS]:</u>

The amount of deduction in the case of an undertaking developing and building housing projects approved on or before the 31st day of March, 2008 by a local authority shall be hundred per cent of the profits derived in the previous year relevant to any assessment year from such housing project if:

(a) Such undertaking has commenced or commences development and construction of the housing project on or after the 1st day of October, 1998 and completes such construction

  (i) in a case where a housing project has been approved by the local authority before the 1st day of April, 2004, on or before the 31st day of March, 2008;

  (ii) in a case where a housing project has been, or, is approved by the local authority on or after the 1st day of April, 2004 but not later than the 31st day of March, 2005, within four years from the end of the financial year in which the housing project is approved by the local authority.

  (iii) in a case where a housing project has been approved by the local authority on or after the 1st day of April, 2005, within five years from the end of the financial year in which the housing project is approved by the local authority.

Explanation: For the purposes of this clause, -

- Ø in a case where the approval in respect of the housing project is obtained more than once, such housing project shall be deemed to have been approved on the date on which the building plan of such housing project is first approved by the local authority;
- Ø the date of completion of construction of the housing project shall be taken to be the date on which the completion certificate in respect of such housing project is issued by the local authority;

(b) The project is on the size of a plot of land which has a minimum area of one acre;

(c) The residential unit has a maximum built-up area of one thousand square feet where such residential unit is situated within the cities of Delhi or Mumbai or within twenty-five kilometres from the municipal limits of these cities and one thousand and five hundred square feet at any other place;

(d) The built-up area of the shops and other commercial establishments included in the housing project does not exceed three per cent of the aggregate built-up area of the housing project or five thousand square feet, whichever is higher.

(e) Not more than one residential unit in the housing project is allotted to any person not being an individual; and

(f) in a case where a residential unit in the housing project is allotted to a person being an individual, no other residential unit in such housing project is allotted to any of the following persons, namely: -

(i) The individual or the spouse or the minor children of such individual,

(ii) The Hindu undivided family in which such individual is the karta,

(iii) Any person representing such individual, the spouse or the minor children of such individual or the Hindu undivided family in which such individual is the karta.

IMPORTANT JUDICIAL PRONOUNCEMENTS:

Ø *One of the issues for consideration is whether the assessee must be the owner of the land on which the housing project is constructed is now settled by the Special Bench in* ***RADHE DEVELOPERS & ORS. VS. ITO & ORS. (2008) 23 SOT 420 (AHD.)*** *In this case, the land was not registered in the Assessee's name. Contention of the Revenue was that in order to claim a deduction u/s. 80-IB(10) the assessee must be the owner of the land on which the housing project is constructed. It was held that there was no such condition in the provisions of the section 80-IB(10). Deduction u/s. 80-IB(10) is allowable to an undertaking developing and building housing projects, whether it is developed by it as a contractor or as an owner. It was also held that the term "contractor" is not contradictory to the term "developer".*

In this case, another important issue before the Bench was whether the profit earned by the assessee included sale of extra FSI which was unutilised was eligible for deduction. It was held that there was no condition as to FSI under the scheme of sec. 80-IB(10). It is not mandatory requirement to fully utilise permissible FSI. In the facts of the case it was held that development agreement with the land owners makes reference to the land area only. Also, the sale deeds executed in the favour of the buyers of the residential houses are for the sale of the plot of the land. In both the documents, the assessee has not acquired or relinquished rights with reference to FSI.

There is no question of selling the unused FSI to the individual buyers or calculating profitability on FSI as the same is not contemplated u/s. 80-IB(10). Calculation given in the approved plan is for the *maximum permissible FSI. By giving such calculation, it is not mandatory to make construction to the fullest extent of maximum permissible FSI. Therefore, deduction could not be denied to the assessee on the ground that the profit earned by the assessee are not for developing and building housing projects done but for the sale of extra FSI which has not been utilised for developing and building the housing projects.*

- Ø *The issue was where an undertaking developing and building housing projects is engaged as a sub-developer and all the sanctions are obtained by the developer whether the sub-developer would be eligible for the deduction or main developer or both. It was held that the sub-developer is eligible for deduction.*

SAROJ SALES ORGANISATION vs. ITO (2008) 115 TTJ 485.

- Ø *The Tribunal noted that subsequent to the two buildings being constructed on the said plot, the plan of building 'C,' in respect of which the assessee acquired the development right, was approved by the local authority. The original plan was approved in 1995, but final approval was given to the modified plan 10-9-1998 and permission for construction of the building was finally given on 9-10-1998. The Tribunal also noted that in the original approved plan/layout building 'C' was not shown. Having observed that the commencement certificate (CC) was in the name of the original owner since the title of the property was not in the name of the assessee, the Tribunal held that:*

  (a) merely because the commencement certificate is issued in the name of the original land owner, the assessee cannot be deprived of deduction u/s.80-IB(10), as nowhere it is a mandate of the said provision that the assessee must be the owner of the property which he undertakes to develop;

  (b) merely because the agreement is not registered, the assessee cannot be deprived of the deduction u/s.80-IB(10) as the assessee has developed building 'C';

  (c) merely because the CC was obtained prior to 1-10-1998 that does not mean that the assessee has commenced the development and commencement of the building 'C';

  (d) CC was granted for the first time on 24-2-1995 and hence, building 'C' was not part of the original project. It observed that on the said plot the owner had constructed building 'A' consisting of 95 flats and tenements and also building 'B'. Just because the plot of land remained the same, it cannot be construed that building 'C' is a part of the original housing project;

  As regards the objection of the CIT(A) on the area of plot of land on which the project was constructed, the Tribunal on facts found that there was no clear cut finding by the AO and CIT(A) hence it restored the issue to the file of the AO to verify whether the area of the plot on which the building 'C' is constructed is one acre or not. The appeal filed by the assessee was allowed.

Essem Capital Markets Ltd. v. ITO (2011) TIOL 196 ITAT-Mum. [BCAJ]

- Ø *Whether the benefit of extension of the date of completion of project upto 31st March, 2003 were applicable to Asst. Yr. 2001-02 and subsequent years only. In the case it was held that the contention of the Revenue that the amendment on the section 80-IB(10) extending the date of completion of the project upto 31st March, 2003 were applicable to the Asst. Yr. 2001-02 and subsequent years and the assessee in the instant case for the Asst. Yr. 2000-01 was not eligible to avail the benefit of the said amendments is not acceptable.*

DY. CIT vs. ANSAL PROPERTIES & INDUSTRIES LTD. (2008) 22 SOT 45 (DEL.)

- Ø *If the plan is approved before 01.10.1998 but the construction of the project starts* *after 01.10.1998, then the Assessee is eligible to claim deduction u/s. 80-IB(10).*

Also, if the plan is approved in the name of Sonal Venture (original owner), but the construction activity was carried out by Shree Ostwal Builders Ltd. (Assessee), then the deduction can be claimed by the Assessee.

Further, commercial units are entitled for deduction u/s. 80-IB(10), if the project is approved before 01.04.2005 as commercial project by the local authority.

Further, ITAT held that if the project is approved as a residential project, but later on if any flat purchaser converts the flats into godown then as the builder has no control on the same, the builder is entitled to claim deduction in respect of the same u/s. 80-IB(10).

ACIT v. SHREE OSTWAL BUILDERS LTD., I.T.A. No. 2144/MUM/2010.

Points to remember:

Ø For the removal of doubts, it is hereby declared that nothing contained in this sub-section shall apply to any undertaking which executes the housing project as a works contract awarded by any person (including the Central or State Government).

Ø Provided that nothing contained in clause (a) or clause (b) shall apply to a housing project carried out in accordance with a scheme framed by the Central Government or a State Government for reconstruction or redevelopment of existing buildings in areas declared to be slum areas under any law for the time being in force and such scheme is notified by the Board in this behalf;

Ø Proportionate deduction for eligible housing units in a project containing ineligible housing units.

It is held that provisions of sec 80-IB(10), do not provide for denial of deduction, if a housing complex contains both the smaller and larger residential units. It concluded that profits attributable to eligible residential units are entitle for deduction inspite of the fact that the other residential units are greater than 1500 sq. ft. built-up area.

BENGAL AMBUJA ITA NO./ 1735 (CAL.) 2007

Ø Deduction in case of individual projects, if they are part of bigger project but got sanction separately:

It is held that where some of the residential units in a bigger housing project, treated independently, are eligible for relief u/s 80-IB(10), relief should be given pro–rata and should not be denied by treating the bigger project as a single unit, more so, when assessee obtained all sanctions, permissions and certificates for such eligible units separately.

DY. CIT V. BRIGADE ENTERPRISE (P) LTD 119 TTJ 269

Ø Restriction on commercial area – prospective or retrospective?

It is held that the restrictions on built-up area of commercial constructions are effective for projects stated after 1.4.2005. As a result, projects started before 1.4.2005 will not be barred by such limitations.

ARUN EXCELLO FOUNDATION VS. ACIT 108 TTJ 71

In the **High Court of Bombay**, it was held that, *"Direct Taxation Deduction under 80-IB(10) of Income Tax Act, 1960 - Whether a housing project having commercial area up to 10 per cent of the project is eligible for deduction on the entire profits of the project under section 80-IB(10) up to 1st April, 2005 - Held, Where a project fulfils the criteria for being approved as a housing project, then deduction cannot be denied under section 80-IB(10) merely because the project is approved as residential plus commercial. Section 80-IB(10) allows deduction to the entire project approved by the local authority and not to a part of the project. If the conditions set out in section 80-IB(10) are satisfied, then deduction is allowable on the entire project approved by the local authority and there is no question of allowing deduction* *to a part of the project. In the present case, the commercial user is allowed in accordance with the DC Rules and hence the assessee was entitled to section 80-IB(10) deduction on the entire project approved by the local authority."*

Ratio Decidendi: *"Where a project fulfils the criteria for being approved as a housing project, then deduction cannot be denied under section 80-IB(10) merely because the project is approved as residential plus commercial and section 80-IB(10) allows deduction to the entire project approved by the local authority and not to a part of the project."*

CIT-II v. BRAHMA ASSOCIATES (2011) 239 CTR 30, 197 TAXMAN 459 (Bom)

The assessee, a builder and land developer, had entered into an agreement to develop and construct a building project on land situated at Mira Taluka, Dist. Thane. For A.Y. 2005-06, the assessee filed a return of income in which it claimed deduction u/s.80-IB(10) of the Act. The AO noted that the housing project which consisted of 94,255 sq. ft. had shopping area to the extent of 7,935 sq. ft. The AO denied the deduction on the ground that in view of the amendment to section 80-IB(10) w.e.f. 1-4-2005, the assessee was not entitled to deduction u/s.80-IB(10) of the Act. Aggrieved, the assessee preferred an appeal to CIT(A) who allowed the appeal. Aggrieved by the order passed by the CIT(A), the Revenue preferred an appeal to the Tribunal.

Held: *The Tribunal noted that the assessee's project had commenced prior to 1-4-2005. It also noted that in the case of Brahma Associates, the High Court has held that the amendment to section 80-IB is prospective in operation. Since the assessee's project had commenced in December 2003, the Tribunal held the amendment to be not applicable to the assessee's case. The Tribunal dismissed the appeal filed by the Revenue.*

ITO v. Chheda Construction Co. (Joint Venture) ITA No. 2764/Mum./2009 [BCAJ]

- Ø One acre area interpretation where eligible and ineligible projects are constructed:

  It is held that as per clause (b) to section 80-IB(10), the project should be on a size of plot of land which has the minimum area of one acre. As a result eligible projects should be allowed deduction even though ineligible projects are constructed on the same piece of land.

VANDANA PROPERTIES ITA NO. 1253 / MUMBAI / 2007

- Ø A **TERRACE** is known as a paved outdoor area adjoining a residence. It adjoins the residence externally and is not a part of the structure that composes the residential unit. Hence, the terrace area allotted to the flat owners for the exclusive use should not be clubbed with the built-up areas of the flats to ascertain whether the maximum built up area of the flat is less than 1000 sq. ft. Built-up area in order to satisfy the eligibility condition in clause (c) of section 80-IB(10).

- Ø **COMPLETION OF PROJECTS –** as per the requirement of section 80-IB(10), the project is required to be completed by 31.03.2008. For the purpose, whether occupation certificate obtained from the Appropriate Authorities to the effect that the development is as per the approval and is ready for occupation is sufficient or will the department insist on any other certificate like completion certificate from appropriate authorities?

  In our opinion, the occupation certificate given by the BMC would be sufficient proof that the housing project is completed. Even in ***DY. CIT vs. ANSAL PROPERTIES & INDUSTRIES LTD. (2008) 22 SOT 45 (DEL),*** it was considered sufficient. But, occupation certificate are sometimes given building-wise. If all the buildings constructed by the developers have occupation certificate before 31.03.08, may be sufficient compliance.

  If, by any reason the occupation certificate was not granted or disputed, despite the fact that the project is completed, some other proof like the architect certificate may also help. It is preferable that the certificate should elaborately describe the completed project item-wise.

When construction is completed before 31.03.2008, but the sale of some flats take place in subsequent years, deduction u/s 80–IB(10) can be claimed. Generally, in incentive provisions granting tax holidays, there is always a specification as to the number of years the tax holiday can be enjoyed. But, in section 80–IB(10), there is no specification as to the number of years the tax holiday is available.

As on date, it appears that once an approved project is completed before the cut off date fixed as per section 80–IB(10) and other eligibility conditions are also fulfilled, there is no terminal year for claiming the tax holiday. The assessee will be entitled to deduction u/s 80–IB(10) in respect of income from the sale, provided that the legislature has not made any amendments curtailing the availability of the deduction upto A.Y. 2009–10 or deleted the provisions of the said section with effect from 01.10.2010.

RELIANCE JUTE & IND. LTD. v. CIT(1979)120 ITR 921 (SC).

9. DEVELOPMENT RIGHTS

DEVELOPMENT RIGHTS – WHO ARE ENTITLE – SOCIETIES OR MEMBERS?

In respect of tenants co-partnership co-operative societies, which are of the nature of "Flat Owners Societies" in which the flats are acquired by the society from the builder on ownership basis and thereafter society is formed, and land is conveyed to the society and individual members acquire ownership rights over the building and underneath the development rights.

This concept has been recognized under Bombay Stamp Act as on the conveyance in favour of the housing societies, stamp duty paid by the purchasers of flats on ownership agreements is deducted from the stamp duty payable on the market value of the property transferred in favour of the society as per proviso to Article 25 of Schedule 1 of Bombay Stamp Act.

Circular No. F.N. 4/28/68–WT dated 10.0.1969 and 27.01.1969 explaining the provisions of section 5(1)(iv), the Board clarified that flats vested with individual members of society and wealth tax exemption will be available to individual members.

<u>I] Additional Area expected at Redevelopment</u>

Liability of Income/Capital Gain Tax, if any, on:-

(A) Additional area in the hands of individual members.

Ans. As per section 54 of the Income Tax Act, 1961, if any residential property which was held for a period of more than 3 years is sold or given for redevelopment and the new flat is purchased or acquired within a period of 1 year before or 2 years after the sale or constructed within 3 years after the sale then capital gain arising on the transfer of the old flat will be exempt from tax u/s. 54 of the Income Tax Act, 1961 to the extent of the cost of such new flat.

In the case of redevelopment, the new flat to be acquired is treated as constructed for the purpose of the section 54. Thus, if the new flat is acquired by the owner within a period of 3 years from the surrender of the original flat then the capital gain arising from the sale of the original flat can be claimed to be exempted u/s. 54 of the Income Tax Act.

If the new flat is not acquired by the owner within a period of 3 years then the Assessing Officer at his discretion can disallow the same at any time during the assessment.

However, allotment of a flat or a house by a co-operative society, of which the assessee is the member, is also treated as construction of the house [Circular No. 672, dated 16-12-1993]. Further, in these cases, the assessee shall be entitled to claim exemption in respect of capital gains even though the construction is not completed within the statutory time limit. [*Sashi Varma* v *CIT* (1997) 224 ITR 106 (MP)]. Delhi High Court has applied the same analogy where the assessee made substantial payment within the prescribed time and thus acquired substantial domain over the property, although the builder failed to hand over the possession within the stipulated period. **[*CIT* v *R.C. Sood* (2000) 108 Taxman 227 (Del)]**.

Hence, relying upon the above judgments, even if in the case of development, the new flat is acquired by the owner after a period of 3 years from the surrender of the old flat, an assessee can claim exemption u/s. 54.

If the new flat acquired to claim exemption u/s. 54 is sold within a period of three years from the date of purchase then the capital gain exemption claimed earlier would become taxable in the year the new flat is transferred.

Thus, in your case, the Receipt of extra carpet area over and above the existing area could be claimed as exemption u/s. 54 of the Income Tax Act, 1961.

Further, we would like to state that under the definition of "Transfer" according to sec 2(47) Income Tax Act, 1961, transfer, in relation to a capital asset, includes sale, exchange, or relinquishment of the asset or the extinguishment of any rights therein or the compulsory acquisition thereof under any law.

An exchange involves the transfer of property by one person to another and reciprocally the transfer of property by that other to the first person. There must be a mutual transfer of ownership of one thing for the ownership of another. Hence, the acquisition of new flat would be considered as exchange and would be considered as transfer for the purpose of capital gain.

Argument could not be made that no cost is incurred by any member for the acquisition of the new flat and hence capital gain cannot be computed and the case does not fall within the ambit of section 55(2). The member is forgoing his rights in the old flat. And hence, it would be considered as the cost of acquisition of the new flat.

However, if the residential flat is held for a period of less than 3 yrs than the receipt of extra area by the individual members would be taxable in the hands of the individual members.

(B) Cash compensation received upon surrender of entitled additional area, in part or in full, by an individual member.

Ans. If the individual member is surrendering a part of the existing area then the individual member would be liable to pay capital gain tax. The sale consideration would be calculated as per **<u>section 50C of the Income Tax Act</u>**, which is as follows:

"Where the consideration received or accruing as a result of the transfer by an assessee of a capital asset, being land or building or both, is less than the value adopted or assessed or assessable by any authority of a State Government for the purpose of payment of stamp duty in respect of such transfer, the value so adopted or assessed or assessable shall, for the purposes of <u>section 48</u>, be deemed to be the full value of the consideration received or accruing as a result of such transfer."

However, if the individual member is surrendering a part of the additional area then the individual member would not be liable to pay any income tax or capital gain tax on the same.

(C) The society for receiving amenities and facilities for the common use of its members and their families.

Ans. If the society is receiving any consideration for amenities and facilities for the common use of its members and their families then the same is not taxable in the hands of the society or the individual members as there is no cost of acquisition of the same.

In deciding the case of ***JETHALAL D.MEHTA V. DY. CIT [(2005) 2 SOT 422 (MUM.),*** Hon. Income Tax Appellate Tribunal mainly relied upon Supreme Court decision in the case of ***CIT V. B.C. SRINVASA SHETTY 128 ITR 294*** in which it was decided that if there is no cost no capital gain can be worked out hence amount received is to be treated as exempt receipt.

II] <u>Corpus Money expected at Redevelopment</u>

Liability of Income/Capital Gain Tax, if any, on:-

(A) Corpus Money received by the individual members from the developer in lieu of surrender of part entitlement of FSI/development rights.

Ans. If the individual member is receiving an area which is same or more than the present area then the individual member is not liable to pay capital gain tax on the same.

If, however, individual member is receiving an area which is less than the present area than the individual member is liable to pay capital gain tax as per section 50C of the Income Tax Act, 1961 as already explained above.

(B) Corpus money received by the society from the developer in lieu of surrender of part entitlement of FSI/development rights, such funds being invested by the society to earn interest income to meet/subsidize the maintenance costs of its redeveloped premises and property.

Ans. If at the time of redevelopment, the society was in not in possession of unutilized FSI/development rights, then the society would not be liable to pay any capital gain tax on the receipt of the Corpus Money on surrender of a part of FSI/development rights.

Further, if the society has unutilized FSI/development rights in its possession at the time of redevelopment, then the receipt of the Corpus Money on surrender of the part of FSI/development rights would be taxable in the hands of the society.

Also, in the case of (1) ***New Shailaja CHS v. ITO (ITA NO. 512/M/2007 BENCH B dated 2nd Dec, 2008 (mum.) and (2) ITO v. LOTIA COURT CO- OP. HSG. SOC. LTD. (2008) 12 DTR (MUMBAI) (TRIB) 396*** it was held that *where the assessee, a Co-op. Hsg. Soc. Ltd. became entitled, by the virtue of Development Control Regulations, to Transferable development Rights (TDR) and the same was sold by it for a price to a builder, the question arose whether the transaction of sale receipt could be taxed. It was held that though the TDR was a capital asset, there being no 'cost of acquisition' for the same, the consideration could not be taxed.* The same is held in the cases of **NEW SHAILAJA CHS LIMITED (ITA NO. 512/MUM./2007), OM SHANTI CO-OP. HSG. SOC. LTD. (ITA NO. 2550/MUM/2008)** & **LOTIA COURT CO-OP. HSG. SOC. LTD. (ITA NO. 5096/MUM/2008).**

Further, in the case of **MAHESHWAR PRAKASH 2 CHS LTD. 24 SOT 366 (MUM.)**, it was held that *the assessee-society acquired the right to construct the additional floors by virtue of DCR, 1991 which could not be available to the assessee on expenditure of money. Prior to DCR, 1991, no society had any right to construct the additional floors, so it was not a tradable commodity. Suddenly by virtue of DCR, 1991, the right was conferred by the Government on the assessee. Such right exclusively belonged to the building owned by the society. It could not be transferred to any other building.*

Similarly, similar right belonging to other societies could not be purchased by the assessee for the purpose of constructing additional floors in its own building. Therefore, such right had no inherent quality of being available on expenditure of money and, therefore, cost of such asset could not be envisaged. Hence, the said view was fully justified in terms of the decision of the Apex Court in the case of B.C. Srinivasa Shetty.

Therefore, the right acquired by the assessee did not fall within the ambit of section 45 itself. The amended provisions of section 55(2) were also not applicable, since such right was not covered by any of the assets specified in section 55(2)(a).

Therefore, the sum of Rs. 42 lakhs received by the assessee from the developer was not chargeable to tax under section 45. Therefore, the impugned orders passed by the lower authorities were to be set aside.

(C) Corpus money received by the society from the developer (as described in (B) above) and subsequently distributed to its members.

Whether such incomes enlisted above at A, B and C, if taxable, shall be treated as capital gains or deemed to be income earned in the year of receipt?

Ans. As per Maharashtra Co-op. Societies Act, 1960, a co-operative society cannot distribute the corpus funds to its individual member, it can only declare dividends.

However, the declaring of dividends has lots of restrictions and formalities.

(D) Liability for income tax, if any, on interest income arising from investment of such corpus money by the society/individual members in the co-operative/other banks.

Ans. If the society receives interest income form a co-operative bank then the same is exempt from tax.

And, if the interest income is received from other banks than the same is taxable and the society has to pay tax on the same.

However, as per recent Hon'ble **Tribunal Judgment** in the case of **ITO v. Sagar Sanjog C.H.S. Ltd., ITA Nos. 1972 to 1974 and 2231 to 2233/ Mum/ 2005(BCAJ)** it was held that *the interest income earned out of the fund money invested went to reduce the maintenance. According to the Tribunal, the interest would have been taxable, had there been surplus left after it being adjusted against the maintenance expenses. The Tribunal also noted that there was nothing on record to suggest that the interest income would be given to members on dissolution of the Society.*

Thus, even the interest income received from other than co-operative bank and spent on Society's work then the concept of mutuality will apply and is not liable to tax but this view is not free from litigation.

<u>III] Rent for Temporary Alternative Accommodation including Deposits, if any:</u>

Rental allowance may be received by individual members in the event of need for relocation during redevelopment. Such amounts may be utilized in part or in full towards rent paid for alternative premises or may remain entirely unspent if the member already has his/her own alternative accommodation. Such allowance may be received for about three years, either together in one tranche in advance or in installments on a staggered basis.

Liability for income tax, if any, on such rental allowance, including deposits, if any, received by the individual members:

Whether such income, if taxable, shall be treated as income earned in the year of receipt (if received on a staggered basis) or entirely as income in one year (if received fully in advance)?

Ans. In order to get the old building redeveloped, the existing structure of the old building is required to be demolished and hence, it is necessary to vacant the same. To facilitate redevelopment and to compensate the flat owners for the hardship to be faced by them in this regard, the developer might offer them rent compensation which they would be paying for the temporary accommodation during the period of redevelopment.

The rent compensation so provided by the developer to the owner should be expended by the owners for the purpose of their temporary accommodation and other expenditure related thereto.

If the actual rent paid by the flat owners is less than the rent compensation received by them from the redeveloper then the excess of such amount received will be taxable under the head **income from other sources,** otherwise, the rent compensation received by the flat owners from the redeveloper is not taxable.

The rent compensation given to the individual members shall be taxable in the year of receipt if the rent compensation is received on staggered basis and the whole is not spend by the individual members on their alternative accommodation.

However, if the rent compensation is given to the individual members in one tranche in advance, then the rent compensation received by the individual members would be taxable on proportionate basis if the same is not spend on the alternative accommodation.

IV] Hardship Allowance/ Compensation for Inconvenience

Members opting not to be temporarily relocated during the redevelopment may receive “hardship allowance” from the developer.

Members agreeing to be temporarily relocated during redevelopment may receive “compensation for inconvenience” from the developer.

Liability for income tax, if any, on such allowance/ compensation and if taxable, mode of computation, i.e., whether as income in the year of receipt or whether on a staggered basis as received.

Ans. Along with extra area and rent compensation, the redevelopers also offer lump sum amount to the flat owners in addition to extra area and compensation. The transfer of TDR to builder for development of property does not attract capital gain tax.

In deciding the case of ***JETHALAL D. MEHTA V. DY. CIT [(2005) 2 SOT 422 (MUM.),*** Hon. Income Tax Appellate Tribunal mainly relied upon Supreme Court decision in the case of ***CIT V. B.C. SRINVASA SHETTY 128 ITR 294*** in which it was decided that if there is no cost no capital gain can be worked out hence amount received is to be treated as exempt receipt.

Hence, the hardship allowance and the compensation for inconvenience is not taxable in the hands of the individual members as hardship allowance and compensation for inconvenience can’t be worked out in monetary terms and have no cost. Since there is no cost of acquisition, as per Income-tax Act, 1961, the receipt would not be treated as a capital receipt and thus, is exempt from tax.

V] White Goods/ Household Amenities received by Members from Developer

Liability for income tax, if any, on individual members for white goods/household amenities such as air-conditioners, washing machine, modular kitchen, etc. that are sometimes included by developers in the new premises on a complimentary basis.

Ans. All the white goods/ household amenities which are attached to the flat, i.e., fixtures, modular kitchen, centralized AC, etc. are treated as a part of the flat and thus, are exempt and not taxable in the hands of the individual members.

Other movable items such as refrigerator, sofa set and other furniture which are not attached to the walls of the flat and exceeds 50,000/- in value in totality are not treated as a part of the flat and are thus taxable in the hands of the individual members in the year of receipt of such amenities u/s. **56(2)(vii) of the Income Tax Act, 1961**, which is as follows:

"where an individual or a Hindu undivided family receives, in any previous year, from any person or persons on or after the 1st day of October, 2009,—

(a) any sum of money, without consideration, the aggregate value of which exceeds fifty thousand rupees, the whole of the aggregate value of such sum;

(b) any immovable property, without consideration, the stamp duty value of which exceeds fifty thousand rupees, the stamp duty value of such property.

*** The following sub-clause (b) shall be substituted for the existing sub-clause (b) of clause (vii) of sub-section (2) of section 56 by the Finance Act, 2013, w.e.f. 01.04.2014.**

(b) any immoveable property,-

(i) without consideration, the stamp duty value of which exceeds fifty thousand rupees, the stamp duty value of such property;

(ii) for a consideration which is less than the stamp duty value of the property by an amount exceeding fifty thousand, the stamp duty value of such property as exceeds such consideration:

Provided that where the date of the agreement fixing the amount of consideration for the transfer of immoveable property and the date of registration are not the same, the stamp duty value on the date of agreement may be taken for the purposes of this sub-clause:

Provided further that the said proviso shall apply only in a case where the amount of consideration referred t therein, or part thereof, has been paid by any mode other than cash on or before the date of agreement for the transfer of such immoveable property;

(c) any property, other than immovable property,—

(i) without consideration, the aggregate fair market value of which exceeds fifty thousand rupees, the whole of the aggregate fair market value of such property;

(ii) for a consideration which is less than the aggregate fair market value of the property by an amount exceeding fifty thousand rupees, the aggregate fair market value of such property as exceeds such consideration"

****Amendments made by the Finance Act, 2013- Transactions for inadequate consideration in immoveable property made taxable w.e.f. assessment year 2014-15.***

The provisions of section 56(2) (vii) are amended, with effect from 01.04.2014, so as to provide that where any immoveable property is received by an individual or HUF for a consideration which is less than the stamp duty value of the property by an amount exceeding Rs. 50,000, the stamp duty value of such property as exceeds such consideration, shall be chargeable to tax in the hands of the individual or HUF as income from other sources.

In other words, if the difference between stamp duty value and the purchase consideration is Rs. 50,000 or less, nothing will be chargeable to tax in the hands of the recipient of property. If the purchase consideration is less than the stamp duty value of the property and such difference is more than Rs. 50,000, then the difference between the stamp duty value and purchase consideration will be taxable under section 56 under the head 'income from other sources'.

The following are important points to be noted:

- The immoveable property received should be land or building or both.
- The immoveable property is received during the previous year.
- The immoveable property is received on or after 01.04.2013
- The immoveable property received may be situated anywhere [whether in India or abroad].
- The immoveable property should be a capital asset as defined under section 2(14).
- The immoveable property so received should be for a consideration less than the stamp duty value and the difference between the two should exceed Rs. 50,000. In such a situation, difference between the stamp duty value and purchase consideration will be taxable.
- Rs. 50,000 limit for difference to be applied property wise, i.e., specially to each property received for consideration less than stamp duty value and not to all such properties received during the previous year.
- It would appear that the provisions would apply only if consideration is quantifiable in money terms. If not, it would appear that the provisions would not apply.

<u>VI] Reimbursement of Expenses from Developer</u>

Liability for income tax, if any, on the society/ individual members for reimbursement from developer of expenses such as stamp duty, fees of consultants (Architect, Lawyers, Chartered Accountants, etc.) cost of updating members and holding general body meetings, administrative expenses towards the redevelopment process, etc. incurred/ to be incurred.

Ans. Any amount which is reimbursed by the developer is not taxable either in the hands of the society or the individual members, provided that the entire amount of reimbursement has been spent on the expenses it is reimbursed for.

Thus, if excess amount is reimbursed by the developer than the amount which is actually spent for the purpose than the excess amount would be taxable on the receipt of the same.

However, in the case of a society, if excess amount is reimbursed to a society by the developer than actually spent by the society, and the excess amount so received has been used by the society for payment of expenses which are for the welfare of the society or the individual members than the excess amount received by the society would not be taxed and hence, would be exempt. Otherwise, the excess amount received by the society would be taxable.

<u>VII] Liquidation & Disbursement of Existing Sinking Fund</u>

Liability for income/capital gain tax, if any, on the society/ individual members upon liquidation and disbursement to existing members (with permission from Registrar/ any other authority) of existing, unutilized sinking fund (generated by annual contributions from members and bank interest earned thereon.) prior to induction of new members arising from saleable portion of redeveloped premises.

Ans. In our view, the sinking fund is to be used on the property itself either for the purpose of development or heavy repair.

However, if the Registrar gives permission then the sinking fund could be distributed amongst the individual members, which again has a number of restrictions.

This distribution of sinking fund after the permission of the Registrar would be taxable in the hands of the individual members to the extent of the interest on such a fund. The distribution of the principal amount would not be taxable in the hands of the society or the individual members.

<u>VIII] TDS on receipt</u>

Whether tax shall be deducted at source (TDS) from corpus money, allowances, compensations, reimbursement of fees of consultants and other expenses, rent for temporary alternative accommodation and deposits or any other form of receipt in the hands of the society/ its individual members?

Ans. As per the Income-tax Act, 1961, no tax is to be deducted on the amount reimbursed by the developer to the society or the individual members or on other items such as corpus money, allowances, compensations, reimbursement of fees of consultants and other expenses, rent for temporary alternative accommodation and deposits or any other form of receipt.

However, when the society makes payments such as professional fees, contractor, etc, the society is to deduct tax at source at the rate given hereunder and pay the same to the Income Tax Department and file the quarterly returns:

Contractor	1% in the case of individual/ HUF
	2% in the case of others u/s 194C
Rent	10% u/s 194I
Professional fees	10% u/s 194J
Commission & brokerage	10% u/s 194H

IX] Tax Planning (Saving) Instrument.

Recommendation of umbrella of designated schemes, funds, securities, etc. under which the society/ its individual members may invest taxable proceeds, if any, to minimize the impact of income/ capital gain tax.

Ans. In our view, whether there would be any capital gain tax liability arising on account of such transactions of redevelopment, is not free from litigation, in view of the fact that various litigations are going on in various courts in our country and the issue would finally be settled when the Supreme Court decides the matter.

It is also to be noted that even the Supreme Court changes its view from time to time depending on the frequent amendments in the Income-tax Act.

Further, we would like to state that Income Tax Department have filed appeal before Hon. High Court and, if the court allows them against the assessees then the same would be taxable for the society otherwise till now it is tax free. Even assuming that Hon High Court decides the case against the assessee then assessee will be liable to pay tax with interest but no penalty can be charged in view of recent decision of Supreme Court in the case of ***Reliance Petro products Pvt. Ltd. Vs. CIT (2010) 322 ITR 158 (SC)*** on the principle that if assessee gives all particulars of income in return and claim certain wrong deduction due to ignorance of highly technical law then that will not attract penalty u/s 271(1)(c) of the Income Tax Act, 1961.

Further we would like to say that based on the above, till now the corpus money received by the society and the individual members is tax free but in case the High Court decides the case against the society then to be on the safer side and to avoid litigation with the Income Tax Department, we suggest that recipient can invest the same in specified bonds to claim exemption u/s. 54EC of the Income-tax Act. One can earn interest by investment in the bonds for 3 yrs which would be an added benefit. The interest so earned would be taxable. Section 54EC of the Income Tax Act, 1961, is produced here below:

"Where the capital gain arises from the transfer of a long-term capital asset and the assessee has, at any time within a period of six months after the date of such transfer, invested the whole or any part of capital gains in the long-term specified asset, the capital gain shall be dealt with in accordance with the following provisions of this section,

(a) if the cost of the long-term specified asset is not less than the capital gain arising from the transfer of the original asset, the whole of such capital gain shall not be charged under section 45;

(b) *if the cost of the long-term specified asset is less than the capital gain arising from the transfer of the original asset, so much of the capital gain as bears to the whole of the capital gain the same proportion as the cost of acquisition of the long-term specified asset bears to the whole of the capital gain, shall not be charged under* section 45*:*

Provided that the investment made on or after the 1st day of April, 2007 in the long-term specified asset by an assessee during any financial year does not exceed fifty lakh rupees.

"long-term specified asset" for making any investment under this section during the period commencing from the 1st day of April, 2006 and ending with the 31st day of March, 2007, means any bond, redeemable after three years and issued on or after the 1st day of April, 2006, but on or before the 31st day of March, 2007, -

(i) *by the National Highways Authority of India constituted under* section 3 *of the National Highways Authority of India Act, 1988 (68 of 1988); or*

(ii) *by the Rural Electrification Corporation Limited, a company formed and registered under the Companies Act, 1956 (1 of 1956),*

and notified by the Central Government in the Official Gazette for the purposes of this section with such conditions (including the condition for providing a limit on the amount of investment by an assessee in such bond) as it thinks fit

X] Implications of VAT / Service Tax

Whether all receipts in the hands of the society/ its individual members shall be net of VAT and service tax

Responsibility/ liability of society/its members towards the same for services rendered to it by professionals/consultants.

Ans. As Society is not providing any services to the developer, the society is not liable to pay service tax or VAT on any of the payments received by the society in the form of reimbursements or corpus money or compensations, etc.

If the society is making any payment of fees to the professionals or contractors, then the society is liable to pay service tax @ 12.36% to the professionals and service tax or VAT to contractors on such a payment.

The professionals and the contractors would in turn pay the same to the Central Government or respective State Government as applicable.

XI] Responsibility / Liability towards stamp duty

Responsibility/liability of the society/its individual members towards stamp duty, if any, in transition from surrender of existing premises to the develop to the occupation and registration of the redeveloped premises

Ans. Normally, in the cases of redevelopment, the stamp duty and the registration charges on surrender of the existing premises to the developer for the purpose of redevelopment would be paid by the developer.

Whereas, when the individual member receives the redeveloped premises from the developer, he is liable to pay stamp duty and registration charges on the same. The stamp duty payable would be on the cost of construction of the present area of the premises and on the market value for the extra area received as per the ready reckoner value published by the Government of Maharashtra every year on 1st January.

XII] Restructuring of Society

Whether the composition of the society may need to be restructured in any manner so as to facilitate minimization of the tax liability?

Whether admission of new members (from saleable portion) in the existing society or their accommodation as an independent new society would have any bearing on the tax liability of the society/its individual members?

Ans. No, the composition of the society need not be restructured in any manner so as to facilitate minimization of the tax liability.

The admission of the new members to the existing society or their accommodation to the new society would not make much difference to the tax liability of the society or its individual members.

However, it would be advisable to admit the new members to the existing society because due to increase in the number of the members of the society, the fixed charges or expenses of the society like maintenance, etc would be distributed amongst the members.

10. SECTION 194LA

As per Section 194LA of the Income-tax Act, 1961, *"Any person responsible for paying to a resident any sum, being in the nature of compensation or the enhanced compensation or the consideration or the enhanced consideration on account of compulsory acquisition, under any law for the time being in force, of any immovable property (other than agricultural land), shall, at the time of payment of such sum in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct an amount equal to ten per cent of such sum as income-tax thereon :*

Provided that no deduction shall be made under this section where the amount of such payment or, as the case may be, the aggregate amount of such payments to a resident during the financial year does not exceed one hundred thousand rupees."

The specific definition of the term "**agricultural land"** for the purpose of section 194LA as given under explanation to the said section reads "agricultural land" means agricultural land in India including.....................It is thus clear that what is purported to be included is any land classified as "agricultural land" in India and includes such land situated in area referred to in sub clause (iii) of section 2(14).

The definitions of the two sections are reproduced hereunder:

Section 194LA states as follows: **"agricultural land" means agricultural land in India including land situate in any area referred to in items (a) & (b) of sub–clause (iii) of clause (14) of section 2.**

Section 2(14)(iii) states as follows: agricultural land in India, not being land situate

(a) in any area which is comprised within the jurisdiction of a municipality (whether known as a municipality, municipal corporation, notified area committee, town area committee, town committee, or by any other name) or a cantonment board and which has a population of not less than ten thousand according to the last preceding census of which the relevant figures have been published before the first day of the previous year; or

(b) in any area within such distance, not being more than eight kilometres, from the local limits of any municipality or cantonment board referred to in item (a), as the Central Government may, having regard to the extent of, and scope for, urbanisation of that area and other relevant considerations, specify in this behalf by notification in the Official Gazette;

Section 194LA is a much wider definition in its scope and the same cannot be restricted by the definition of section 2(14). Section 2(14) cannot curb the provisions of section 194LA, since section 194LA includes not only section 2(14) but also any agricultural land situated anywhere in India whether within municipal limits or outside municipal limits.

11. TAX AUDIT

Amount received as advance by builder following project completion method whether tax audit applicable and penalty under section 271B imposable

In case it is taken that assessee is following the system in which income is returned on completion of the project and in case project goes on for more than 5 years and assessee gets its books of account audited for last year in which project is completed, then from where A.O. will be able to verify the figures of expenses and receipts etc. of earlier years. So, it is against the very principle of section 44AB that in project completion assessee would get the books of account audited in the last year and not in earlier years when he is debiting the expenses and showing sundry debits and different types of receipts are also there. On the basis of above, it can be concluded that audit is to be carried on for all the assessment years during which the project was constructed and the expenses were debited to the P & L A/c.

It is held that amounts received as advance by the assessee-builder from customers had an element of profit and same were to be adjusted towards the cost of flats booked by each customer and thus, the amounts of advance have to be included in "gross receipts" for the purpose of s. 44AB; assessee being under obligation to get its accounts audited under s. 44AB. It cannot be contended that the assessee following project completion method would get the books of account audited in the last year and not in earlier years when he is debiting the expenses and other items and showing different types of receipts penalty under s. 271B was imposable for its failure to get the same done

Gopal Krishna Builders [2006] 92 TTJ 215 (Luck)]

12. <u>CAPITAL GAIN</u>

12.1 CAPITAL ASSET

Capital asset means any property of any kind held by an assessee, whether or not connected with his business or profession

However, agricultural land in India is not a capital asset provided it is not situated:-

1. In any area wherein the territorial jurisdiction of Municipality or Cantonment Board having a population of 10,000 or more;
2. In any area within 8 km. from a municipality stated above.

   <u>Note:</u> In order to qualify for agricultural land in India, it is not necessary that the land was once agricultural land. It must be an agricultural land at the time of sale. In order to determine whether a particular land is agricultural land or not, it is first necessary to ascertain what is the use to which the land is been actually put. If it has been used for agricultural purposes or even if the agricultural use has ceased but it is apparent that the land is meant to be used for agricultural purpose, it would be an agricultural land.

   Ranchhodbhai Bhaijibhai Patel V. CIT (1971) 81 ITR 446 (Guj)

12.2 TRANSFER IS A PRE-REQUISITE FOR TAXING CAPITAL GAIN

Capital gain arises only when there is a *transfer* of capital asset. If the capital asset is not transferred or if there is any transaction which is not regarded as transfer, there will not be any capital gain. However, w.e.f. assessment year 2000-2001 section 45(1A) has been inserted to provide that in case of profits or gains from insurance claim due to damage or destruction of property, there will be capital gain on such deemed transfer although no asset has been actually transferred in such case.

<u>Judicial pronouncements — Whether a transaction constitutes transfer or not?</u>

<u>Where an assessee gives up the right to claim specific performance for purchase of immovable property is it relinquishment of a capital asset and thus transfer?</u>

The assessee had entered into an agreement to purchase certain property. Both parties reserved the right to specific performance of the agreement. Nearly four years thereafter, again another agreement was entered into in the nature of deed of cancellation, by which the assessee agreed for termination of the earlier agreement and allowed the owner of the land to sell the said property to any person and at any price of his choice. As a consideration for this, the assessee was paid a sum of Rs. 6,00,000 apart from being refunded the advance of Rs. 40,000. The question that *arose for consideration was as to whether the amount of Rs. 6,00,000 received by the assessee from the vendor could be treated as capital gains in the hands of the assessee.*

K.R. Srinath v Asstt. CIT (2004) 268 ITR 436 (Mad)

There is no transfer in family settlement:

Where a family settlement/ arrangement is arrived at in order to avoid continuous friction and to maintain peace among the family members, the family arrangement is governed by the principles which are not applicable to dealing between strangers. So, such *bona fide* realignment of interest, by way of effecting family arrangements among the family members would not amount to transfer. ***CIT v A.L. Ramanathan (2000) 245 ITR 494 (Mad).*** In this case, the court followed the decision of the Supreme Court in general law laid down in the case of ***Kale v Deputy Director of Consolidation (1976) AIR 1976 SC 807.***

Giving up the right to obtain conveyance of immovable property amounts to transfer of a capital asset:

Where the assessee had paid the earnest money and acquired right to obtain conveyance of immovable property, such earnest money paid shall be cost of acquisition of such right and if such right is given up, there is a transfer of a capital asset and the compensation received for giving up such right is the consideration price. ***CIT* v *Vijay Flexible Container* (1990) 186 ITR 693 (Bom)**

In case of litigation pending, no capital gain tax unless the case is decided:

The AO held that the income accrues on the date when an enforceable debt is created in favour of the Assessee. However, the Court held to consider the issue as to whether the income would accrue even when the very existence of the income is under doubt and a subject matter of litigation. Further, the subject matter of litigation cannot be a subject matter of tax avoidance.

ITO v. M/s. S. P. BUILDERS, CIT(A) XII/ 12(3)(4)/ IT – 184/07-08.

12.3 CONVERSION OF CAPITAL ASSET INTO STOCK– IN–TRADE

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.

12.4 CONVERSION OF STOCK–IN–TRADE INTO CAPITAL ASSET

It was held that there is no provision similar to section 45(2) with respect to conversion of stock–in–trade into capital asset. It was further held that holding period is to be considered from the date of acquisition.

***CIT V. BRIGH*T STAR INVESTMENTS (P) LTD (2008) 24 SOT 288 (BOM.)**

KALYANI EXPORTS & INV (P) LTD & ORS. V. DY. CIT (2001) 78 ITD 95 (PUNE) (TM)(139 AND 140)

*However, in **SPLENDOR CONSTRUCTIONS (P) LTD VS. ITO (2009) 27 SOT 39 (DELHI)**, it was held that the period is to be considered from the date of conversion to investment. This decision has not considered the decision of the Mumbai Tribunal in Bright Star (supra).*

12.5 PIECEMEAL TRANSFER

In **AJAI KUMAR SHAH JAGATI V ITO (1995) 55 ITD 348 (DEL.) AND M/S G. G. DANDEKAR MACHINES WORKS LTD V. JCT, ITA NO. 181/MUM/2001, BENCH–F, DATED 28TH FEBRUARY,2007,** possession of only a part of property was transferred against proportionate consideration received during the relevant assessment year. It was held that capital gains arising only on the said proportion amount of consideration could be charged in the relevant year and not on the entire consideration stipulated in the sale agreement.

12.6 CAPITAL ASSETS CAN EITHER BE SHORT-TERM CAPITAL ASSET OR LONG-TERM CAPITAL ASSET

(A) Short-term capital asset: A capital asset held by an assessee for not more than 36 months *immediately preceding the date of its transfer* is known as a short-term capital asset.

(B) Long-term capital asset: It means a capital asset which is not a short-term capital asset. In other words, if the asset is held by the assessee for more than 36 months or 12 months, as the case may be, such an asset will be treated as a long-term capital asset.

Thus, period of holding of a capital asset is relevant for determining whether capital asset is short-term or long-term.

Exclusion/inclusion of certain period for computing the period of holding of an asset:

Case *Exclusion/Inclusion of period*

(*ii*) Property acquired in any mode given under section 49(1) (*e.g.* by way of gift, will, etc.) Include the holding period of previous owner also.

Judicial decisions for determining period of holding

Property constructed on a land purchased earlier: In case, a property is constructed on a site purchased much earlier, the question arises whether the period of holding the asset, *i.e.*, the property, should be reckoned from the date of completion of the construction of the property or from the date of acquisition of the land.

The correct position is that the asset consists of two components: (1) Land and (2) Building. When the property is sold, the period of holding has to be reckoned separately for the land and the building. The consideration received can also be split into two parts relating to each component.

In ***CIT v Vimal Chand Golecha (1993) 201 ITR 442 (Raj)****, the land was purchased in 1962 and building was constructed thereon in the accounting years relevant to assessment years 1968-69, 1969-70 and 1970-71. The building was sold in 1970. It was held that the gains attributable to land were assessable as long-term capital gains. The gains attributed to the building were, however, short-term capital gains. Similar view was held in the cases of* ***CIT v Lakshmi B. Menon (2003) 264 ITR 76 (Ker) and CIT v C.R. Subramanian (2000) 242 ITR 342 (Kar)****.*

Agreeing with the above Rajasthan High Court view, it has been held that land can be considered a separate capital asset even if a building is constructed thereon. Thus, where the land is held for more than a prescribed period, the gains arising from the sale of the land can be considered as long-term capital gains even though the building thereon, being a new construction, is held for a period less than the prescribed one

CIT v Dr. D.L. Ramachandra Rao (1999) 236 ITR 51 (Mad)

CIT v Citibank N.A. (2004) 260 ITR 570 (Bom)

In the above cases, the burden will be on the assessee to satisfy how much of the sale proceeds should be apportioned for the land and how much of the sale proceeds pertained to the structure.

CIT v Estate of Omprakash Jhunjhunwala (2002) 254 ITR 152 (Cal)

Period of holding of share in the co-operative housing society: While computing the capital gain tax in case of transfer of his shares by a person who is a member of co-operative housing society, the relevant date would be date on which the member acquires the shares in the co-operative housing society and the date on which member had sold his shares therein. Thus, where the assessee acquired shares in the society on 6-9-1979 and was allotted flat on 15-11-1979. He was given possession of flat in October 1981, and sold the shares of the society along with the flat, on 4-12-1982, the capital gains arising from the sale were long-term capital gains, shares having been held for more than 36 months.

CIT v Anilben Upendra Shah (2003) 262 ITR 657 (Guj)

Similarly, the assessee became a member in Venus Apartments (Galaxy Co-operative Housing Society). He was allotted a flat in

the building of the society by resolution dated 4-11-1980, passed by the managing committee of the society. On the date of allotment, i.e., 4-11-1980, the property was under construction and came to be completed on 12-9-1983. Physical possession was handed over to the assessee on 12-9-1983. On 30-4-1984, the flat was sold by the assessee for a consideration of Rs. 3,75,000. The assessee worked out long-term capital gains at Rs. 1,59,395. The Assessing Officer did not accept the stand of the assessee that the assessee had become the owner of the property as per resolution dated 4-11-1980.

According to the Assessing Officer the assessee had held the property for a period of less than 36 months and as such was liable to short-term capital gains tax, it was held that the assessee in the present case was allotted a share by the co-operative housing society on 4-11-1980, and the sale of the same took place on 30-4-1984, i.e., after a period of 36 months. The Tribunal was therefore justified in holding that the capital gains arising were long-term capital gains and the assessee was entitled to deduction from such gains as per law.

CIT v Jindas Panchand Gandhi (2005) 279 ITR 552 (Guj)

***Right to acquire any house property*:** **Where a flat is booked with a builder under a letter of allotment or an agreement for sale, this would represent only a right to acquire a flat and if such right is acquired more than 36 months back, it becomes a long-term asset. However, when the possession of the flat is taken, the period of holding would once again commence from the date of the possession of the flat as the small right to acquire a flat merged into larger right and small right upon a merger would lose its existence.**

12.7 COST OF ACQUISITION

Cost of acquisition of an asset is the value for which it was acquired by the assessee. Expenses of capital nature for completing or acquiring the title of the property are includable in the cost of acquisition.

Judicial decision on cost of acquisition:

Cost of acquisition of an asset acquired from the previous owner in any mode given u/s 49(1): In this case, the cost of acquisition is taken as the cost to the previous owner and it is this cost which will have to be indexed. For the purpose of indexation the year in which the asset was *first held* by the assessee (not the previous owner) is to be considered. The indexation will be done as under:

Cost of acquisition to the previous owner ´ CII of the year of transferCII of the year in which the asset is first held by the assessee

However, in the case of *Mrs**. Pushpa Sofat*** **(2002) 81 ITD 1 (Chd)(SMC),** the indexation of cost was allowed from the date of acquisition of the asset by the previous owner and not the date when the asset was acquired by the assessee from the previous owner under any mode given under section 49(1).

12.8 VALUATION AS ON 1.4.1981

Reference to the DVO can be made u/s 55A only when the AO is of the opinion that the value of the capital asset claimed by the assessee is less than the fair market value and not when he was of the opinion that the fair market value of the property as on 01.04.1981 as shown by the assessee was more than its actual fair market value.

CIT V. Daulat Mohta HUF ITA No. 1031 Of 2008 Dt. 22.09.2008 (Bombay High Court)

ITO V. Smt. Lalitaben B. Kapadia (2008) 115 TTJ 938 (Mum)

Patel India (P) Ltd. V. Dy. CIT (1999) 63 TTJ 19 (Mum)

12.9 NO REGISTRATION – 50C NOT APPLICABLE upto 30/09/2009

In **NAVNEET KUMAR THAKKAR VS. ITO (2007) 112 TTJ 76 (JD)**, it was held that section 50C embodies the legal fiction by which the value assessed by the stamp duty authorities is considered as the full value of consideration for the property transferred. It does not go beyond the cases in which the subject transferred property has not become the subject–matter of registration and the question of valuation for stamp duty purposes has not arisen.

Amendment w.e.f. 01/10/2009

Law is amended w.e.f. 01/10/2009 to include all the cases whether registered or unregistered

12.10 EXEMPTION OF CAPITAL GAINS UNDER VARIOUS SUB-CLAUSES OF SECTION 10, SECTION 11(1A) AND SECTION 13A

Exemption of capital gains on compensation received on compulsory acquisition of agricultural land situated within specified urban limits:

With a view to mitigate the hardship faced by the farmers whose agricultural land is situated in specified urban limits has been *compulsorily acquired,* the Finance (No. 2) Act, 2004 has inserted a new clause (37) in section 10 so as to exempt the capital gains (whether short-term or long-term) arising to an *individual or a Hindu undivided family* from transfer of agricultural land by way of *compulsory acquisition* where the compensation or the enhanced compensation or consideration, as the case may be, is received *on or after 1-4-2004*.

The exemption is available only when such land has been used for agricultural purposes during the preceding two years *by such individual* or a *parent of his* or by *such* Hindu undivided family.

Where the compulsory acquisition has taken place before 1-4-2004, but the compensation is received after 31-3-2004, it shall be exempt. But if part of the original compensation in the above case has already been received before 1-4-2004, then exemption shall not be available even though balance original compensation is received after 31-3-2004.

However, enhanced compensation received on or after 1-4-2004 against agricultural land compulsorily acquired before 1-4-2004 shall be exempt.

12.11 EXEMPTION OF CAPITAL GAINS U/s. 54, 54B, 54EC & 54F

a) *Profit on transfer of house property used for residence [Section 54]:*

Benefit of section 54 is confined to sale of a residential house after 36 months and reinvestment in a residential house. Reinvestment benefits are available both for purchase and construction of the house. Purchase has to be either one year before or two years later. Construction has to be completed within three years of the sale of the asset in respect of which benefit of reinvestment is claimed. There have been many decisions on purchase/ construction of the house. Further, certain clarifications have also been issued in this regard. These have been summarized as under:

i. *House includes part of the house*: House property does not mean a complete independent house. It includes independent residential units also, like flats in a multi-storied complex. The emphasis is not on the type of the property, but on the head under which the rental income is assessed. [***CIT (Addl.)* v *Vidya Prakash Talwar* (1981) 132 ITR 661 (Del)**].

ii. *Release deed may also be treated as purchase*: Where a property is owned by more than one person and the other co-owner or co-owners release his or their respective share or interest in the property in favour of one of the co-owners, it can be said that the property has been purchased by the releasee. Such release also fulfils the condition of section 54 as to purchase so far as releasee-assessee is concerned [***CIT* v *T.N. Aravinda Reddy* (1979) 120 ITR 46 (SC)**]

iii. *Addition of floor to the existing house eligible for exemption under section 54*: The assessee sold his residential property and invested the capital gain within the stipulated time in the construction of a new floor on another house owned by him by demolishing the existing floor; it was held that he was entitled to exemption under section 54. [***CIT* v *Narasimhan (PV)* (1990) 181 ITR 101 (Mad)**].

iv. <u>*No exemption under section 54 if land only is sold*</u>: The house property concerned must be building or land appurtenant to building. The basic test was whether the land appurtenant to building could be used independent of the user of the building. If so, it cannot be said to be land appurtenant to building. Further, the basic requirement is that the capital gain should arise from the transfer of building or land, the income of which is chargeable under the head income from house property. If the land alone is sold, the provisions of section 54 will have no application inasmuch as the income from land is not chargeable under the head income from house property. [***CIT* v *Zaibunnisa Begum* (1985) 151 ITR 320 (AP)**].

v. <u>*Successor is entitled to benefit of exemption in case of death of the assessee*</u>: In case of assessee's death during the stipulated period, benefit of exemption under section 54(1) is available to legal representative, if the required conditions are satisfied by the legal representative. [***Ramanathan* (*CV*) v *CIT* (1980) 155 ITR 191 (Mad)**].

vi. <u>*Purchase of limited interest in the house eligible for exemption under section 54*</u>: Where an assessee had sold the residential house and acquired only 15% interest in another house and such other house was already used for residence prior to purchase, it was held that the benefit should be available to the assessee. [***CIT* v *Chandaben Maganlal* (2000) 245 ITR 182 (Guj)**]. In coming to the conclusion, the High Court followed its own earlier decision in ***CIT* v *Tikyomal Jasanmal* (1971) 82 ITR 95 (Guj)**. In that case, what was purchased was a unit of house property, while in the present case before the High Court; it was a limited interest in the property.

vii. <u>*Construction in another property not eligible for exemption*</u>: An assessee gifted some land to his wife. He, thereafter, constructed a building on the said land. The Government acquired the land and building and paid compensation for land to the wife and for the building to the assessee (husband). It was held that capital gain on land was assessable in the hands of the husband by virtue of section 64 but he was not entitled to exemption under section 54 in respect of capital gain on the acquisition of the land of the wife as the capital gain to the wife did not arise on transfer of a residential house. [***T.N. Vasavan* v *CIT* (1992) 197 ITR 163 (Ker)**].

viii. <u>*House of the firm used by partners*</u>: Where a firm's property is used for residence of partners and thereafter distributed to the partners upon dissolution of the firm and the partner sells the same, exemption can be claimed by the partner under section 54. For this purpose, period for which this property was held by the firm shall also be taken into account for determining the question whether the house property was a long-term capital asset or not. [***CIT* v *M.K. Chandrakanth* (2002) 258 ITR 14 (Mad)**].

ix. <u>*There can be both purchase and construction*</u>: Where the assessee had partly invested the capital gains on the purchase of another house and partly on the construction of additional floor to the house so purchased within the prescribed time limit, it was held that the Income-tax Officer was not justified in restricting exemption to investment on purchase only, holding that the exemption under section 54 was admissible either for purchase or for construction but not for both. [***Sarkar* (*B.B.*) v *CIT* (1981) 132 ITR 661 (Del)**].

x. <u>*Construction can start before the sale of asset*:</u> The construction of the new house may start before the date of transfer, but it should be completed after the date of transfer of the original house. [***CIT* v *J.R. Subramanya Bhat* (1987) 165 ITR 571 (Karn)**]. The very fact that purchase of another house as also the construction can take place before the sale means that cost of purchase or new construction need not flow from the sale proceeds of the old property. [***CIT* v *H.K. Kapoor* (*Decd*) 1998 234 ITR 753 (All)** and ***CIT* v *M. Vasudevan Chettiar* (1998) 234 ITR 705 (Mad)**].

xi. <u>Allotment of a flat by DDA under the Self-Financing Scheme shall be treated as construction of the house [Circular No. 471, dated 15-10-1986]. Similarly, allotment of a flat or a house by a co-operative society, of which the assessee is the member, is also treated as construction of the house</u>

[Circular No. 672, dated 16-12-1993]

Further, in these cases, the assessee shall be entitled to claim exemption in respect of capital gains even though the construction is not completed within the statutory time limit. [***Sashi Varma* v *CIT* (1997) 224 ITR 106 (MP)**].

Delhi High Court has applied the same analogy where the assessee made substantial payment within the prescribed time and thus acquired substantial domain over the property, although the builder failed to hand over the possession within the stipulated period. [***CIT* v *R.C. Sood* (2000) 108 Taxman 227 (Del)**].

xii. As per a circular of CBDT, the cost of the land is an integral part of the cost of the residential house, whether purchased or constructed. [Circular No. 667, dated 18-10-1993]

xiii. Where an assessee who owned a house property, sold the same and purchased another property in the name of his wife, exemption under section 54 shall be allowable. **[*CIT* v *V. Natarajan* (2006) 154 Taxman 399 (Mad)]**.

xiv. Where the assessee utilised the sale consideration for other purposes and borrowed the money for the purpose of purchasing the residential house property to claim exemption under section 54, it was held that the contention that the same amount should have been utilised for the acquisition of new asset could not be accepted. [***Bombay Housing Corporation* v *Asst. CIT* (2002) 81 ITD 454 (Bom)**. **Also** followed in ***Mrs. Prema P. Shah, Sanjiv P. Shah* v *ITO* (2006) 282 ITR (AT) 211 (Mumbai)**].

xv. Where non-resident Indian sold property in India and purchased residential property in U.K. and claimed deduction under section 54, it was held that it was not necessary that residential property should be purchased in India itself. **[*Mrs. Prema P. Shah, Sanjiv P.***

Shah **v *ITO* (2006) 282 ITR (AT) 211 (Mumbai)]**.

However, in another case, the Tribunal held that the words purchase/ construction of a residential house, in section 54F on plain and simple reading, mean that the purchase/construction of a residential house must be in India and not outside India.

Therefore, the benefit under section 54F is not allowable for a residential house purchased/constructed outside India. ***Leena J. Shah*** **v *Asstt. CIT* (2006) 6 SOT 721 (Ahd)**

b) *Capital gain on transfer of land used for agricultural purposes [Section 54B]*:

Any capital gain (short-term or long-term), arising to an assessee (only individuals), from the transfer of any agricultural land which has been used by the assessee or his parents for at least a period of 2 years immediately preceding the date of transfer, for agricultural purposes, shall be exempt to the extent such capital gain is invested in the purchase of another agricultural land within a period of 2 years after the date of transfer to be used for agricultural purpose, provided the new agricultural land purchased, is not transferred within a period of 3 years from the date of its acquisition.

Section 54B is applicable only to individuals and not to any other assessee this is because the section uses the expression used by "his or a parent of his" which clearly indicate that the "assessee" refers to an individual. [***CIT* v *Devarajalu* (*G.K.*) (1991) 191 ITR 211 (Mad)**].

However, Finance Act, 2012 has amended the section so as to grant the benefit to Hindu undivided family also.

c) *Capital gain on transfer of long-term capital assets not to be charged on investment in certain bonds [Section 54EC]*:

Any long-term capital gain, arising to any assessee, from the transfer of any capital asset on or after 1-4-2000 shall be exempt to the extent such capital gain is invested within a period of 6 months after the date of such transfer in the long-term specified asset provided such specified asset is not transferred or converted into money within a period of 3 years from the date of its acquisition.

Exemption under section 54EC is not available in respect of deemed capital gains on amount received on liquidation of a company: Section 54E (now section 54EC) permits reinvestment benefit, if the sale proceeds/capital gains on sale of long-term capital assets are invested in the manner required by the section. Where a shareholder is made liable for deemed capital gains on amount received on liquidation of a company, is he eligible for reinvestment benefit under section 54E (now 54EC)? It was held that section 54E (now 54EC) would have application only where there is an actual transfer and not in a case, where there is only a deemed transfer. [***CIT* v *Ruby Trading Co. Pvt. Ltd.* (2003) 259 ITR 54 (Raj)**]

Benefit under section 54EC, etc. available even on transfer of depreciable assets: Although as per section 50 the profit arising from the transfer of depreciable asset shall be a gain arising from the transfer of short-term capital asset, hence short-term capital gain but section 50 nowhere says that depreciable asset shall be treated as short-term capital asset. Section 54E [or say 54EC or 54F, etc.] is an independent provision which is not controlled by section 50. If the conditions necessary under section 54E are complied with by the assessee, he will be entitled to the benefit envisaged in section 54E, even on transfer of depreciable assets held for more than 36 months. [***CIT* v *Assam Petroleum Industries* (*P.*) *Ltd.* (2003) 131 Taxman 699 (Gau)**. See also ***CIT* v *ACE Builders Pvt. Ltd.* (2005) 144 Taxman 855 (Bom)**]

On the same analogy benefit under section 54EC or 54F shall be available in the case of depreciate asset if these are held for more than 36 months.

d) Capital Gain on transfer of asset, other than a residential house [Section 54F]:

Any long-term capital gain, arising to an individual or HUF, from the transfer of any capital asset, *other than residential house property*, shall be exempt in full, if the entire net sales consideration is invested in purchase of one residential house within one year *before* or two years *after* the date of transfer of such an asset or in the construction of one residential house within three years after the date of such transfer. Where part of the net sales consideration is invested, it will be exempt proportionately.

The above exemption shall be available only when the assessee does not own *more than one residential* house property *on the date of transfer* of such asset exclusive of the one which he has bought for claiming exemption under section 54F.

Section 54 and 54F are comparable in many respects. Hence, the law and precedents relating to section 54 as to whether the house property on which investment is made is residential or not, the law relating to time limits, the precedent that construction could start earlier though completed within three years are all equally applicable for section 54F. Hence, for judicial decisions for section 54F, refer to the judicial decisions given under section 54.

12.12 CAPITAL GAIN ON THE TRANSFER OF LAND, FORMING PART OF BUILDING WHICH IS DEPRECIABLE, CAN BE LONG-TERM

Section 50 provides for determination of the cost of construction of superstructure and it does not apply to land as land is not a depreciable asset. Hence, if the building comprising of the land is sold, the capital gain on superstructure shall be short-term capital gain in terms of section 50 and the capital gain on land, if held for more than 36 months, shall be long-term capital gain. This is because the land is independent and identifiable capital asset and it continues to remain so even after construction of the building thereon. [***CIT v CITI Bank NA* (2003) 261 ITR 570 (Bom)**].

12.13 BLOCK OF ASSETS – SECTION 2(11)

Where land and building were used for the business, an important issue arises whether the new constructed area received can be added to the block of assets. The new constructed area will not be a building used for the purpose of the business. If it is not an asset which will be used as a "Building" for the purpose of business, it may not become a part of the Block of Assets.

For the purpose of redevelopment, the old building has to be demolished. Such building may be part of the block of asset. Issue arises as to whether indexed cost of structure can be deducted to arrive at the long term capital gains on the sale of land. Indexation u/s. 48 is allowed only in respect of cost of acquisition or cost of improvement of the capital asset transferred. Therefore, one may contend that only the land is transferred and not the building, which will be demolished to enable the development of land, hence the cost of structure cannot be taken into consideration and only index cost of land will be considered.

13. INCOME FROM HOUSE PROPERTY

The annual value of property consisting of any buildings or lands appurtenant thereto of which the assessee is the owner, other than such portions of such property as he may occupy for the purposes of any business or profession carried on by him the profits of which are chargeable to income-tax, shall be chargeable to income-tax under the head "Income from house property".

HOW TO COMPUTE INCOME FROM HOUSE PROPERTY

Gross Annual Value	**Xxxxx**
Less: Municipal Taxes	**Xxxxx**
Net Annual Value	**Xxxxx**

Less: Deduction u/s 24

- Standard Deduction @ 30%	Xxxxxx
- Interest from Borrowed Capital	Xxxxxx
Income From House Property	XXXXXX

Points to remember:

- Annual value of property is chargeable under the head '*Income from house property'*. In order that the annual value be charged under this head, it is *irrelevant* whether the actual income from such house property has accrued or has been received by the assessee.
- Property should consist of any buildings or lands *appurtenant* thereto.
- Section 22 is not confined only to house property, but extends to all buildings whether used as dwelling house or for other purposes [***CIT* v. *Chennai Properties & Investments Ltd.* (2004) 136 Taxman 202 (Mad); (2002) 266 ITR 685 (Mad)**].
- The manner in which the building is used by the assessee is not relevant. It can be used by him for letting out on rent, leasing it out, using it for his own residence, etc. However, the building should not be occupied by the assessee for his business or profession. Similarly, the person to whom the building has been let out may use it for any purpose, say, for his own residence or for his business or profession, etc. Further, building may take any form, e.g., a cinema theatre, an auditorium or even an amphitheatre (which does not have a roof).
- Annual value of a building situated *outside India* is also taxable under this head. In the case of a resident but not ordinarily resident or a non-resident, annual value of such a building is charged to tax in India only if income from such property is received or is accrued in India during the previous year.
- Land appurtenant to a building consists of such portions of land that are taken to be a part and parcel of the building in order to *enable the enjoyment* of the possession of such building. Therefore, garden attached to the building, approach roads, etc., form part of the building.
- 'Building' does not include *vacant land*. Thus, income from vacant land is charged either under the head 'Profits and gains of business or profession' or under the head 'Income from other sources', as the case may be.
- The assessee should be the owner of such property.
- The house property should not be *occupied* by the assessee for the purposes of his business or profession, the profits of which are *chargeable* under the head 'Profits and gains of business or profession'
- Income received from giving the building to other person on hire or by license *need not always* be treated under the head 'Income from house property'. Each case has to be looked at from a businessman's point of view to find out whether the letting was the *doing of a business* or the *exploitation of his property* by an owner [***Sultan Brothers (P) Ltd.* v. *CIT* (1964) 51 ITR 353 (SC)**]. If it is for doing of a business, the relevant income will be charged under the head 'Profits and gains of business or profession'.
- Interest on borrowed capital (of the current year and pre- construction period) is deductible. However, the maximum deduction available if the capital is borrowed on or after 1999 is Rs. 1,50,000 and Rs. 30,000 if capital is borrowed before 1.04.1999.
- If the actual rent being in excess of Municipal Corporation/standard rent, all the expenses and outgoings have to be excluded from the rent receivable and the net of the amount should be considered to be the income of the Assessee**.** ***(ITO V. GOPICHAND P. GODHWANI (2005) 1 SOT 374 (MUM.)****)*
- *Where assessee, co–owner of house property, claimed deduction on account of salary and bonus of sweepers, pumpman and liftman and electricity charges being expenses incurred for electric burning for pump motor and common passage, assessee was not entitled to deduction u/s. 24; however, annual value of assessee's house property should be assumed at reduced value, i.e., after deducting impugned amounts from rental, being only in relation to expenditure required to be necessarily incurred for enjoyment / user of relevant property.*

J.B. PATEL CO. V.S DY. CIT (ASSTT.) (2009) 118 ITD 556 (AHD)

· In the case of **M.V. SONAVALA V. CIT, 177 ITR 246 (BOM)**, it was held that "*the income from house property has to be computed on the basis of the sum of which the property might reasonably be let from year to year to the annual Municipal rateable value. The word "or" is disjunctive as such it is possible to take the sum for which property might reasonably let from year to year or the Municipal rateable value. It is pertinent to note that while deciding this issue the Hon'ble jurisdictional High court took into consideration the decisions of the Apex Court rendered in the case of Devan Daulat Rai Kapoor Vs. New Delhi Municipal Committee, 122 ITR 700 (SC) and in the case of Sheila Kaushik vs. CIT, 131 ITR 435 (SC).*"

14. RECENT AMENDMENTS IN THE BUDGET 2013-2014

a. Section 56(2)(vii) has been amended w.e.f. 01.04.2014 as already discussed earlier.

b. Section 43CA, a new provision has been inserted after section 43C by the Finance Act,2013, w.e.f. 01.04.2014;

<u>SECTION 43CA OF THE INCOME TAX ACT, 1961:</u>

Special provision for full value of consideration for transfer of assets other than capital assets in certain cases.

43CA (1) *Where the consideration received or accruing as a result of the transfer by an assessee of an asset (other than capital asset), being land or building or both, is less than the value adopted or assessed or assessable by any authority of a state government for the purpose of payment of stamp duty in respect of such transfer, the value so adopted or assessed or assessable shall, for the purpose of computing profits and gains from such transfer of such asset, be deemed to be the full value of the consideration received or accruing as a result of such transfer.*

(2) The provisions of sub-section (2) and sub-section (3) of section 50C shall, so far as may be, apply in relation to determination of the value adopted or assessed or assessable under sub-section (1).

(3) Where the date of agreement fixing the value of consideration for transfer of the asset and the date of registration of such transfer of asset are not the same, the value referred to in sub-section (1) may be taken as the value assessable by any authority of a state government for the purpose of payment of stamp duty in respect of such transfer on the date of agreement.

(4) The provisions of sub-section (3) shall apply only in a case where the amount of consideration or a part thereof has been received by any mode other than cash on or before the date of agreement of transfer of the asset.

<u>Existing provision in respect of the above amendment:</u>

The white paper on Black Money presented by the Government of India points out that very high levels of stamp duty (over 5%) in many states create incentives for tax evasion through under reporting of consideration in sale deed.

To combat tax evasion through under reporting of sale consideration in sale deed, section 50C was inserted in the Act by the Finance Act, 2002 w.e.f. 01.04.2003.

In cases of transfer of capital asset being land or building or both, the said section deems stamp duty value as the full value of consideration where the consideration shown in the sale deed is less than the stamp duty value.

Currently, when a capital asset, being immoveable property, is transferred for a consideration which is less than the value adopted, assessed or assessable by any authority of a state government for the purpose of payment of stamp duty in respect of such transfer, then such value (stamp duty value) is taken as full value of consideration under section 50C. These provisions do not apply to transfer of immoveable property, **held by the transferor of stock-in-trade.**

<u>Loopholes/Problems:</u>

In **CIT vs. Kan Construction and Colonizers (P) Ltd. [2012 20 taxmann.com 381]**, the Allahabad High Court held that section 50C is not applicable to sale of plots by a builder since plots are his stock-in-trade and not capital assets in view of the following:

- Section 50C uses the word "capital asset". For applicability of section 50C, one of the essential requirements is that land or buildings sold should be capital asset. Stock-in-trade has been excluded from the definition of capital asset by section 2(14).
- Investment in purchase and sale of plots by a builder who is indulged in selling buildings is ancillary and incidental to his business activity. 'Stock-in-trade' includes all such chattels as are required for the purpose of being sold or let on hire in a person's trade.

To overcome the judicial decision in Kan Construction (supra), the Finance Act, 2013 inserted new section 43CA with effect from assessment year 2014-2015.

c. SECTION 194-IA OF THE INCOME TAX ACT, 1961

Another amendment is in respect of payment on transfer of certain immoveable property other than agricultural land.

194-IA *(1) Any person, being a transferee , responsible for paying (other than the person referred to in section 194LA) to a resident transferor any sum by way of consideration for transfer of any immoveable property (other than agricultural land) shall, at the time of credit of such sum to the account of the transferor or at the time of payment of such sum in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct an amount equal to one per cent of such sum as income tax thereon.*

(2) No deduction under sub-section (1) shall be made where the consideration for the transfer of an immoveable property is less than fifty lakh rupees.

(3) The provisions of section 203A shall apply to a person required to deduct tax in accordance with the provisions of this section.

Explanation.- *For the purpose of this section,-*

(a) "agricultural land" means agricultural land in India, not being a land situated in any area referred to in items (a) and (b) of sub-clause (iii) of clause (14) of section 2;

(b) "immoveable property" means any land (other than agricultural land) or any building or part of a building.

Under section 195, on transfer of immoveable property by a non-resident, tax is required to be deducted at source by the transferee. However, there is no such requirement on transfer of immoveable property by a resident except in case of compulsory acquisition of certain immoveable properties (section 194LA).

The Finance Act, 2013 inserted new section 194-IA to introduce TDS on consideration on transfer of immoveable properties.

The objects of this have been explained by Explanatory Memorandum as under:

"*There is a statutory requirement under section 139A of the Income Tax Act read with rule 114B of the Income Tax Rules 1961 to quote Permanent Account Number (PAN) in documents pertaining to purchase or sale of immoveable property for value of Rs. 5 lakh or more. However, the information furnished to the department in Annual Information Returns by the Registrar or Sub-Registrar indicate that a majority of the purchasers or sellers of immoveable properties, valued at Rs. 30 lakhs or more, during the financial years 2011-2012 did not quote or quoted invalid PAN in the documents relating to transfer of property. In order to have a reporting mechanism of transaction in the real estate sector and also to collect tax at the earliest point of time, it is proposed to insert a new section 194-IA...*"

The Finance Minister in his speech explained the objects of the new section 194-IA as under:

"145. Transactions in immoveable properties are usually under- valued and under-reported. One-half of the transactions do not carry the PAN of the parties concerned. With a view to improve the reporting of such transactions and the taxation of capital gains, I propose to apply TDS at the rate of one percent on the value of transfer of immoveable property where the consideration exceeds Rs. 50 lakhs. However, agricultural land will be exempt."

Section 194-IA provides that every transferee (purchaser or buyer), at the time of making payment or crediting of any sum as consideration for transfer of immoveable property (other than agricultural land) to a resident transferor, shall deduct tax, at the rate of 1% of such sum. In order to reduce the compliance burden on small taxpayers, no deduction of tax shall be made where the total amount of consideration for the transfer of an immoveable property is less than Rs. 50,00,000. The provisions of section 203A [regarding obligation of deductors to obtaining tax deduction and collection account number (i.e. TAN) shall not apply in respect of tax deducted under this section. This amendment will take effect from 01.06.2013.

AMENDMENTS IN SECTION 2(14) OF THE INCOME TAX ACT, 1961 BY FINANCE BILL 2013-2014

By the provision of "Sec. 2(14) Capital Asset", rural agriculture land was exempt from capital gain. For being rural agriculture land, land must satisfy certain conditions laid down in section 2(14). The Finance Minister amended these conditions through Finance Bill, 2013-14. For simplicity, we discuss effect of this amendment in two parts.

A. Criteria for being rural agricultural land prior to 01/04/2013

B. Criteria for being rural agricultural land after 01/04/2013

v **Criteria for being rural agricultural land prior to 1-04-2013:**

<u>Prior to 01/04/2013, following section is applicable:</u>

2(14)(iii) [Agricultural land in India, not being land situate-

(a) in any area which is comprised within the jurisdiction of a municipality (whether known as a municipality, municipal corporation, notified area committee, town area committee, town committee, or by any other name) or a cantonment board and which has a population of not less than ten thousand according to the last preceding census of which the relevant figures have been published before the first day of the previous year; or

(b) in any area **within such distance**, not being more than eight kilometers, from the local limits of any municipality or cantonment board referred to in item (a), as the Central Government may, having regard to the extent of, and scope for, urbanization of that area and other relevant considerations, specify in this behalf by notification in the Official Gazette;]

Thus, if these conditions are satisfied than land will be agricultural land.

· Land is situated within the jurisdiction of a municipality or a cantonment board having population of less than 10000.

· Land is situated outside the notified distance from jurisdiction of municipality. Govt. can notify maximum distance of 8 km.

If these conditions are satisfied then land is rural agricultural land and not liable for capital gain tax.

The manner of measurement of distance was not given in the definition. Therefore, it was taken by road. And same view was followed in following judicial pronouncement.

(1) CIT V.LAL SINGH [2010] 195 TAXMAN 420 (PUNJ. & HAR.)

(2) CIT V. SANTINDER PAL SINGH [2010] 188 TAXMAN 54 (PUNJ. & HAR.)

(3) LAUKIK DEVELOPERS V. DY .CIT [2007] 105 ITD 657 (MUMBAI)

v **Criteria for being rural agricultural land after 1-04-2013:**

<u>After 01/04/2013 following sections are applicable:</u>

As per section 2(14) "capital asset" means property of any kind held by an assessee, whether or not connected with his business or profession, but does not include-

(iii) Agricultural land in India, not being a land situated-

a) In any area which is comprised within the jurisdiction of a municipality (whether known as municipality, municipal corporation, notified area committee, town area committee, town committee, or by any other name) or a cantonment board and which has a population of not less than ten thousand [according to the last preceding census of which the relevant figures have been published before the first day of the previous year]; or

b) In any area within the distance, ***measured*** ***<u>aerially.</u>***-

(I) Not being more than two kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than ten thousand but not exceeding one lakh; or

(II) Not being more than six kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than one lakh but not exceeding ten lakh; or

(III) Not being more than eight kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than ten lakh.

Explanation.—*For the purposes of this sub-clause, "population" means the population according to the last preceding census of which the relevant figures have been published before the first day of the previous year;*

Thus, if these conditions are satisfied then agricultural land will be rural agricultural and accordingly not liable for capital gain tax.

· Land is situated in any within the jurisdiction of a municipality or a cantonment board having population of less than 10000.

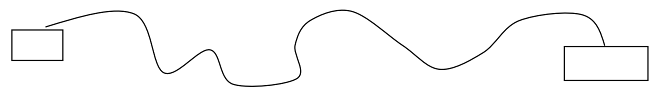
· Distance of land from municipality and population limit.

Distance	**Population**
Within 2 kilometers	10,000-1,00,000
2 kilometers – 6 kilometers	1,00,000-10,00,000
6 kilometers – 8 kilometers	More than 10,00,000

The distance from the Municipal Corporation measurement:

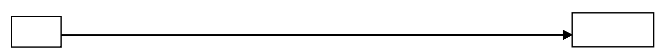
<u>Such distance is to be measured on **straight line aerially** as crow flies.</u> The shortest aerial distance has to be considered. Such shortest aerial distance is defined as "A straight line distance between two places.'' A human would travel further to get from one point to another due to obstacles or lack of roads or trails, but a crow can go in a straight line between them. Humans have to follow roads which have their twists and turns. But, a crow does not have to face the barriers that humans face. Hence, we measure the straight line distance between two places.

"The distance as the crow flies is a way to describe the distance between two locations without considering all the variable factors. As an example, traveling from California to Maine involves a rather indirect route around, over and through mountain ranges and so forth. The driving distance might be about 3,500 miles, but the distance as the crow flies is about 2,800 miles.



Human [By road]

Crow's flight straight line distance (aerial measurement)



These amendments will take effect from 1st April, 2014 and will, accordingly, apply in relation to assessment year 2014-15 and subsequent assessment years.

<u>Effect of the amendment</u>

a) Distance from jurisdiction or municipality or cantonment board within which agricultural land is to be considered as urban land has been changed from uniformly 8 km to within 8 km depending on population of municipality or cantonment board.

b) Distance to be measured straight line aerially as crow flies and not by road method which was used by courts in various decisions. This amendment overcomes above court decisions which say that distance should be measured by road.

c) More land will be covered under the urban land because aerially distance covered more area.

d) Earlier only notified area were covered under the distance criteria but from now onwards any area will be covered under the distance criteria.

e) Impact on Wealth Tax

The term agricultural land is not defined in Wealth-tax Act. However, it is defined in section 2(14) of the Income-tax Act. The definition for non-urban land and agricultural land is similar. Hence, the above analysis will also be applicable for the purpose of determination of net wealth as per the Wealth-tax Act. Thus, a person owning land will need to re-assess as to whether the land owned by him will qualify for exemption from wealth tax or not.

15. <u>CHANGES AS PER DIRECT TAX CODE:</u>

<u>CHANGES IN HOUSE PROPERTY:</u>

- Standard deduction earlier @ 30% is now changed to 20%
- Income from house property shall include income from the letting of any buildings along with any machinery, plant, furniture or any other facility if the letting of such building is inseparable from the letting of the machinery, plant, furniture or facility.
- In case of the letting out house property, the gross rent will be the amount of rent received or receivable for the F.Y.
- Gross rent will not be computed at a presumptive rate of 6 percent of the rateable value or cost of construction/ acquisition.
- In the case of house property which is not let out, the gross rent will be nil. As the gross rent will be taken as nil, no deduction for taxes or interest, etc. will be allowed. However, in the case of one house property, which has not been let out, an individual or HUF will be eligible for deduction on account of interest on capital borrowed for acquisition or construction of such house property (subject to a maximum ceiling of Rs. 1.5 lakh) from the gross total income. The overall limit of deduction for savings will be calibrated accordingly.

<u>CHANGES IN CAPITAL GAIN:</u>

- The DTC provides that gains (losses) arising from the transfer of investment assets will be treated as Capital Gain (losses). These gains (losses) will be included in the total income of the financial year in which the investment asset is transferred. The Capital Gains will be subjected to tax at the rate of 30% in the case of non-resident and in the case of residents at the applicable maximum marginal rate.
- Under the code, the current distinction between short-term investment asset and long-term investment asset on the basis of the length of holding of the asset will be eliminated
- The cost of acquisition is generally with reference to the value of the asset on the base date or, if the asset is acquired after such date, the cost at which the asset is acquired. The base date will now be shifted from 01.04.1981 to 01.04.2000. As a result, all unrealized capital gains due to appreciation during the period from 01.04.1981 to 31.03.2000 will not be liable to tax as the assessee will have an option to take the cost of acquisition of these assets at the price prevailing as on 01.04.2000.
- The capital gain arising from transfer of any investment assets held for less than one year from the end of financial year in which it is acquired will be computed without any specified deduction or indexation. It will be included in the total income and will be charged to tax at the rate applicable to the taxpayer.

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Note: **This has been presented as a paper at a conference organized by All Gujarat Federation of Tax Consultants held on 03.06.2014**

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TRANSFER PRICING ARTICLE ON SPECIFIED DOMESTIC TRANSACTIONS

CA. Akshay Dave
CA. Nisarg Trivedi

1. INTRODUCTION

The genesis of transfer pricing principle is that there are different tax rates in various tax jurisdictions and accordingly there is an opportunity of tax arbitrage for the tax payers. Hence, there is a tendency of taxpayers to take undue advantage of this tax arbitration and shift their profits overseas in a low tax jurisdiction. In order to curb this harmful tax practice, the law of transfer pricing was evolved as an anti-avoidance tax law to ensure that the controlled price between two Associated Enterprises ('AEs') is at fair price or in other words is at "arm's length". The transfer pricing regulations in India were earlier applicable only to the cross border transactions undertaken by two Associated Enterprises.

Earlier, the taxpayers were under obligation to undertake domestic transactions with related parties at fair market value [Section 40A(2)(b)]. However, while examining related party transactions between two Indian Companies in the case of *CIT v Glaxo SmithKline Asia (P) Ltd. (236 CTR 113)*, the Supreme Court suggested that the government should consider making Transfer Pricing Regulations applicable to domestic transactions as well. This recommendation was provided considering there was no objective mechanism to arrive at a fair market value as per the erstwhile provisions under the Income Tax Act.

While making this suggestion, the Supreme Court categorically referred to two situations where transfer pricing provisions could be relevant in the context of domestic transactions. The two situations being:

- Transactions between loss-making and profit-making Indian entities; and
- Transactions between two units of an Indian entity having differential tax rates.

In light of the above recommendation, Finance Minister by way of an amendment *vide* Finance Act, 2012, included certain domestic transactions (hereinafter referred as Specified Domestic Transactions or SDT) within the purview of transfer pricing provisions. A new section 92BA was inserted defining specified domestic transactions and provisions of section 92, 92C, 92D and 92E have been amended to include within its scope such SDT. Rules relating to computational & documentation aspects including Form number 3CEB dealing with international transactions have been amended to include within their scope such SDT.

2. Scope of Specified Domestic Transactions

Section 92BA has specified following transactions within the meaning of SDT provided the aggregate value of such transactions exceeds Rs. 5 crore in a previous year.

(i) any expenditure in respect of which payment has been made or is to be made to a person referred to in clause (b) of sub-section (2) of section 40A; [**Payment made to related concerns U/s. 40A(2)(b)**]

(ii) any transaction referred to in section 80A; **[Transactions relating to transfer of goods or services, between 10A/10AA/10B/10BA, units claiming deductions under Part C of Chapter VIA with another unit of the assessee**]

(iii) any transfer of goods or services referred to in sub-section (8) of section 80-IA; **[Transactions relating to transfer of goods or services, between units claiming deductions under section 80IA with another unit of the assessee]**

(iv) any business transacted between the assessee and other person as referred to in sub-section (10) of section 80IA; [**Transaction of an assessee with any party, having close connection, which in the opinion of Assessing Officers**

leading to more than the ordinary profit of units claiming deductions]

(v) any transaction, referred to in any other section under Chapter VI-A or section 10AA, to which provisions of sub-section (8) or sub-section (10) of section 80-IA are applicable; or **[Transactions between units calming deduction u/s 10AA or under Chapter VI-A as falling under the provision of section 80-IA(8) / (10)]**

(vi) any other transaction as may be prescribed,

It can be noted that the specified domestic transaction also includes transaction executed outside India with a related party as specified u/s. 40A(2)(b) of the Act, provided it is falling within the definition of "international transactions" under section 92B of the Act. E.g. payment made to non-executive foreign director.

3. Impact of introduction of SDT provisions and its non-compliance

With the introduction of these provisions, all transactions which are covered within the scope of SDT shall be required to meet the "arm's length" test. Further, this has imposed an obligation on the assesse to demonstrate that the covered transaction undertaken is at arm's length price. For the purpose of demonstrating the same, the assesse shall be required to undergo the process which was earlier required to be undertaken only in case of international transactions with AEs. A brief process has been discussed in the ensuing paragraphs.

3.1 Computing the arm's length price

While complying with the provisions of SDT, the assesse has to ensure that the controlled transactions should be at arm's length price. In order to determine that these transactions are at arm's length, the assesse should use the most appropriate method out of the six methods prescribed under section 92C of the Act. While selecting the most appropriate method, each transaction shall be separately analyzed and accordingly the best suited method considering the facts and circumstances of the case shall be selected.

3.2 Documentation requirements

Similar to the requirement of maintaining documentation for international transaction, while complying with the provisions of SDT, the assesse shall be required to maintain detailed Transfer Pricing Document to substantiate the arm's length dealing by the assesse. The Transfer Pricing Document shall be in compliance with section 92D read with rule 10D of the Income-tax Rules, 1962. The documents can be broadly classified into three categories, viz., Company & Industry overview, Function Asset & Risk ('FAR") analysis and economic analysis. The same is briefly discussed as under:

· **Company & Industry Overview:**

Under this section of TP Document, a brief background of the Company shall be provided. Further, the industry overview gives the insights / highlights of the industry in which the company is operating. This shall especially be helpful in case there are certain restrictions which have been prescribed by an industry body which may have influence on pricing of the transactions. Further, the industry overview can be of importance in case of profit based methods like Transaction Net Margin Method ('TNMM'), Cost plus Method ('CPM') or Resale Price Method ('RPM'). For example, the Fast Moving Consumer Goods ('FMCG') industry has not performed well in some financial year, which has impacted the profit margins of the assesse, then it can be presented to the tax officer that low margin of the assessee is attributable to the industry scenario in which the business operations are undertaken by the assessee.

· **FAR Analysis:**

Under this section of the Transfer Pricing Documentation, the assessee is required to bring out the actual Functions performed by the assesse and its related parties, Assets employed by them and finally the Risk borne by them while undertaking the transaction. This analysis is important as collectively these three factors have a huge influence on the price at which the transaction shall be undertaken. With the help of this analysis, the assesse would be in a position to broadly characterize the transactions in some category which can then be benchmarked with the third party information available in the public domain.

- **Economic Analysis:**

A detailed benchmarking analysis which the assessee has undertaken to arrive at arm's length price shall be provided in this section of TP Documentation. This section shall elaborate on the analysis undertaken to derive the most appropriate method to benchmark a particular transaction. Further, the section should consist of the detailed application of the most appropriate method which substantiate the arm's length test for the transaction undertaken, etc. For example, this section should cover a detailed Transfer Pricing Search analysis employed by the assessee in case the assessee has used TNMM as the most appropriate method. Further, this section may also cover, the proof of third party documents in case other price based method has been employed to determine the arm's length price. Hence, this section covers the ultimate outcome of the entire TP analysis undertaken by the assesse.

The above mentioned analysis shall be required to be carried out for each individual transaction undertaken by the assessee. However, where the different transactions undertaken by the assessee are closely linked to each other and it is not possible to benchmark the transactions individually, the assessee may aggregate such transactions and perform benchmarking analysis / economic analysis to determine the arm's length nature of the transactions.

3.3 Steep penalties on non-compliance

The Income-tax Act has prescribed penalties for non-compliance of the provisions of transfer pricing which includes the provisions of SDT. Interestingly, most of the penalties prescribed are linked to the value of transactions and accordingly the quantum of penalties becomes huge on violation of any provision. A brief table has been reproduced below which captures various sections under which penalties are levied with respect to non-compliance of Transfer Pricing provisions:

Sr. No.	Type of penalty	Section	Penalty
1	a) Failure to keep and maintain prescribed information/ documents	271AA	2% of the value of each international transaction or specified domestic transaction
	(b) Failure to report any such transaction or		
	(c) Maintain or furnish incorrect information/ document		
2	Failure to furnish information / documents during assessment u/s 92D	271G	2% of the value of each international transaction or specified domestic transaction
3	Adjustment to taxpayer's income during assessment	271(1)(c)	100% to 300% of tax on adjustment amount
4	Failure to furnish accountant's report u/s 92E	271BA	INR 100,000

4. Some Issues

4.1 Computation of threshold of Rs. 5 crore

As discussed above, the aggregate amount of transactions referred to in section 92BA shall exceed Rs. 5 crore to qualify for Specified Domestic Transactions. However, it is not specified in the definition as to what value has to be considered while computing the aggregate value of the transactions, i.e., whether it is the arm's length price or the actual price of the transactions that need to be considered. However, since monetary limit has been prescribed to determine whether the arm's length of the transactions have to be computed or not, logically, the monetary limit would have to be considered having regard to the actual recorded value of the transactions.

Cases may arise where the same transaction falls in more than one clauses of section 92BA. For example, transfer of goods and services between two units would fall both within clauses (ii) and (iii) of section 92BA. Similarly, purchase of goods from persons specified under section 40A(2)(b) for the purpose an eligible unit may fall within clause (i) as well as clause (iv) of section 92BA, which refer to transactions referred to in section 80-IA(10).

In our view, the arguments for taking the actual transaction value and to avoid of the duplication of same transaction while computing the threshold limit of Rs. 5 crore is more logical and can be advanced.

4.2 40A(2)(b) - Tax arbitrage

As discussed above, the amendment has brought all expenditure incurred with related party within Transfer Pricing net, irrespective of the fact that there is no possibility of tax arbitrage for the transactions under review. Accordingly, the tax payers are required to comply with the onerous obligation of complying with the provisions of determination of arm's length for all the related party expenditure incurred by them. Eventually, in many cases this proves to be an unfruitful exercise both for the taxpayers and tax authorities as there is no motive for the taxpayers to pay more to the related party considering the other party is in the same tax bracket.

It shall be worthwhile to note here that before introduction of Domestic Transfer Pricing, the related party transactions under section 40A(2)(b) of the Act were required to be undertaken at Fair Market Value ('FMV'). However, since it was practically difficult to arrive at FMV, the Finance Ministry adopting the suggestions of the Supreme Court incorporated the provisions of Arm's Length Price (ALP) on the related party transactions undertaken under section 40A(2)(b) of the Act. It may, however, be noted that the provisions relating to SDT are enacted in a manner which does not exclude within its scope the above transactions.

4.3 40A(2)(b) - Direct Holding v/s. Indirect Holding

As per section 40A(2)(b) of the Act, the company having substantial interest in the business or profession of other company shall be considered as related parties. However, there can be two ways of interpreting this clause. One way of interpreting could be to consider only direct holding companies as related parties for this clause. The logic for this restrictive interpretation could be that since the legislature has not employed the words "indirect" while drafting the clause, there could be no intention of the exchequer to include indirect holding companies within the purview of section 40A(2)(b) of the Act. Further, this view is also supported by Circular 6P of 1968 issued by Central Board of Direct Taxes ('CBDT') which clarified that only direct holding shall be considered for the purpose of determining related party relationship. Considering the legal position that circular issued by CBDT is binding on Assessing Officer whether it would be advisable for the taxpayers to take a stand that indirect holding companies may not be covered under section 40A(2)(b) of the Act and accordingly the same shall not be subject to Domestic Transfer Pricing provisions?

Before concluding on the above, it shall be worthwhile to also consider the Guidance Note on Report under Section 92E of the Income Tax Act, 1961 issued by Institute of Chartered Accountants of India (ICAI) in this behalf. ICAI has clarified, in its guidance note, that not only the direct holding but indirect holding by one entity into the other shall also be considered as related party for the purpose section 40A(2)(b) of the Act. It shall be interesting discussion as to whether the guidance note issued by ICAI shall be binding on tax authorities or the taxpayers and whether the mention of indirect holding in the guidance note of ICAI shall have any relevance for taxpayers while taking a stand on whether the transactions with indirect holding companies shall be reported under Transfer Pricing Report?

In this connection, one would like to go through the penal provisions in case of non-compliance of Transfer Pricing provisions according to which separate penalties at the rate of two percent of the value of transactions may be levied by Transfer Pricing Officer (TPO) on account of non-reporting of transactions covered or non-maintenance of information as required under Transfer Pricing Regulations, etc.

While discussing on the parties covered under the definition of section 40A(2)(b) of the Act, it shall also be important to observe that the legislature has brought amendment by way of Finance Act , 2012 effective from 1-4-2013 (i.e., from Assessment Year 2013-14 onwards). By way of this amendment, the scope of related party transactions has been extended to include companies having common parent company within its ambit. Hence, the Government of India is leaving no stone unturned to capture all the possible influenced / tainted domestic related party transactions within the compliance of Transfer Pricing.

4.4 How to determine arm's length price for

directors' remuneration? Since the scope of domestic transfer pricing is wide enough to cover all transactions under section 40A(2)(b) of the Act, it shall also include within its scope the remuneration paid to directors by the company. This becomes a subject matter of debate as to how to benchmark the remuneration paid to its own directors by the company. Technically one may argue that it shall not be possible to benchmark the same as there can never be uncontrolled payment towards director remuneration. The reason being the remuneration paid even by an independent company to its director shall be considered as controlled transaction and accordingly the taxpayer will not be in a position to obtain uncontrolled director remuneration payment which may be adopted as a benchmark by the company.

Further, using comparable salaries of peers in similar companies for benchmarking and proving the arm's length nature of executive pay would also be difficult. This is because such remunerations vary widely.

Further, justifying the handsome salaries given to top executives is going to be a tough call for Indian companies as assessing the contribution and potential of employees is highly subjective and would vary from company to company.

However, this being law as on date, remuneration to directors of all companies passing the humble limit of five crores for applicability of SDT would need to comply with its provisions and would accordingly need to benchmark the same.

In the first audit cycle after executive pay was brought under transfer pricing provisions in the Finance Act of 2012, it has been observed that the tax officers are preparing to go deep into the returns of managerial remuneration which companies have filed last November for Financial Year 2012-13 to verify the reasonableness of corporate salary spending.

Tax officers unimpressed by the justifications given could disallow as business expenditure what they think is the excess remuneration and add the same to the taxable income of the companies. Such re-computation of income, called transfer pricing adjustments, would lead to higher tax claims.

The idea of subjecting executive pay to transfer pricing rules is to prevent shifting of profits to related parties, eroding the tax base and jeopardizing the interests of the larger shareholder community of an enterprise.

Considering the above practical challenges, it would be much appreciated if CBDT comes out with a clarification regarding ways to benchmark directors' remuneration. By the time the required clarification comes from tax department, the taxpayer shall be required to meticulously document the method to be adopted to arrive at the arm's length price in its Transfer Pricing Study report.

The taxpayers may consider various approaches to benchmark its directors' remuneration, like shareholder approved managerial remuneration, use of external HR compensation survey reports, references to the pay received by executives prior to them becoming directors, compliance with the ceiling on total managerial remuneration as required by the Companies Act, benchmarking based on the benefits accrued to the organization from the contribution by the directors, documenting the profile of director to justify that remuneration paid to them commensurate to their experiences and qualifications, etc.

4.5 Impact on Tax Holiday undertakings

As mentioned in the introductory paragraph, the genesis of transfer pricing is to ensure that transactions having possibility of tax arbitrage shall be undertaken at arm's length price. Considering the same, CBDT had made an amendment in the Act to include not only transactions covered under section 40A(2)(b) of the Act, but also eligible tax holiday units of the assessee within the purview of Specified Domestic Transactions subject to conditions.

As per section 80-IA(8) of the Income Tax Act, any transfer of goods and services by / to eligible unit to / by non-eligible unit needs to be at arm's length price. Accordingly, the taxpayers having tax holiday undertakings and where there is transfer of goods or services within eligible and non-eligible undertaking, the taxpayer would be required to justify that such transfer within business is at arm's length.

4.6 Meaning of Close Connection?

An interesting issue arises while analyzing SDT provisions to tax holiday unit under section 80-IA(10) of the Act. The relevant extract of the same is reproduced below:-

"*...Where it appears to the Assessing Officer that, owing to the close connection between the assessee carrying on the eligible business to which this section applies and any other person, or for any other reason, the course of business between them is so arranged that the business transacted between them produces to the assessee more than the ordinary profits which might be expected to arise in such eligible business, the Assessing Officer shall, in computing the profits and gains of such eligible business for the purposes of the deduction under this section, take the amount of profits as may be reasonably deemed to have been derived therefrom:*

Provided that in case the aforesaid arrangement involves a specified domestic transaction referred to in section 92BA, the amount of profits from such transaction shall be determined having regard to arm's length price as defined in clause (ii) of section 92F...."

While reading the proviso to section 80-IA(10) of the Act, a question arises as to whether all the transactions undertaken by eligible unit under section 80-IA(10) of the Act needs to be determined at arm's length price? It may appear unusual as the taxpayers would then be required to determine arm's length price even for uncontrolled transactions. This would be against the spirit of Transfer Pricing Law. Further, the meaning of word 'close connection' has not been defined in the Act. This has created ambiguity for taxpayers while filing its return of income. In absence of any specified definition, one may contend that the definition of section 40A(2)(b) of the Act should be employed to arrive at the arm's length price. Alternatively, the taxpayer may consider the definition of section 92A of the Act, i.e., Associated Enterprise or may consider the parties to be closely connected in cases where the parties are covered as related parties as per Accounting Standard 18 issued by ICAI. The issue crops up since the definition / meaning assigned in all three different provisions provide different parties.

5. Conclusion

It can be observed that with the introduction of Specified Domestic Transactions provisions, the taxpayers are left with onerous obligation to comply with detailed transfer pricing rules, like maintenance of Transfer Pricing Documentation, determination of arm's length price, etc. It shall be much appreciated if the provisions of SDT are restricted to the circumstances in which there is a possibility of tax arbitrage like one involving tax holiday undertakings. Nevertheless, in case these provisions are continued to be extended to all classes of transactions then the government should consider bringing amendment in second proviso to section 92C(4) of the Act, which permits only single track adjustment and prohibits consequential adjustments in the hand of the other party.

Also, the finance ministry should evaluate net gain to the exchequer of these provisions considering the fact that the tax authorities would also be required to invest their significant time and resources in supervising the compliances of these provisions.

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WILLS AND ITS ADVANTAGES

K. H. Kaji, Advocate
Manish K. Kaji, Advocate
Can be contacted at: kanishkakaji@gmail.com

Considerable confusion prevails in the minds of even educated persons and some time even amongst Tax Practitioners as to the law of Wills in India.

Every person who has assets and property and a family should make a Will, whether he is young or aged. It is an erroneous impression in the minds of persons that one should make a Will only when he is aged and not in good health.

With the above back ground, we would like to deal with the topic of Wills, when and how it should be made and whether it requires witnesses or registration or stamp paper for making a Will and the advantages of making a Will.

In contrast to the complicated and legal wordings required for executing a sale deed or a deed of mortgage or a deed of gift, the drafting of a Will has a very simple formality. The following aspects are required to be kept in mind while dealing with Will and its advantages.

At the outset, it may be stated that the law of Wills is substantially governed by Indian Succession Act, 1925, hereinafter referred to as "ISA". However, many sections do not apply to Hindus, Buddhists, Sikhs, or Jains, shortly referred to hereafter as "Hindus, etc." Further, most of the provisions do not apply to Muslims.

The subject will be discussed hereinafter under different heads:-

(1) WHAT LAW GOVERNS THE TESTATOR?

So far as immovable properties are concerned, the making of Wills will be governed by the law of the place where property is situated. However, this proposition is important only if there are properties outside India.

So far as movable properties are concerned, it will be governed by the law of testator's domicile. In brief, it may be mentioned that domicile is determined on the basis of a person's residence and the intention to remain there indefinitely but not on account of service, unless some circumstances should occur to alter his intention.

(2) WHAT IS WILL?

Will is a legal declaration by a testator with respect to his property which he desires to be carried into effect after his death. Mere expression of desire is not enough in law, but there must be clear words bequeathing the property after the death of the testator. Therefore, during his life time Will is always revocable.

It is necessary to emphasize that Will need not comprise the entire property of the testator. It may be limited to a portion of it. Similarly, several Wills can be legally executed by the testator for different properties. If there is no will qua a particular property, it devolves by intestate succession. To avoid this situation, a residuary clause is generally added in the Will, bequeathing all remaining and unmentioned properties to certain legatees.

(3) WHAT IS CODICIL?

It is document executed in the same manner as a Will changing or altering or adding to the disposal made earlier in the Will. Just as a Will can be revoked by subsequent Will, a codicil can also be revoked by subsequent Will or Codicil. It may be noted that putting cross lines on the Will or codicil does not amount to cancellation or revocation of the Will/ codicil unless such cancellation follows the procedure required for making the Will and words are used to that effect.

(4) KINDS OF WILLS

Usually Will is made by a single individual for his own property. However, the following two kinds of Wills may be mentioned:-

(i) Joint Wills: - In this case a single document is executed by two or more persons disposing of their separate or joint properties to same or different legatees. Such a Will operates separately and independently as regards each testator on his death. It is revocable by each of them prior to his death and even by survivor on the death of one of them.

(ii) **Mutual Wills: -** In this case a Will is made by two testators conferring reciprocal benefits on each other. This is mostly in case of husband and wife. Such Wills are revocable so long as both the testators are alive, but if one of them dies and the other takes the advantage under it, then it becomes irrevocable by him/her.

(iii) Oral Wills are not valid in India except in the case of Muslims.

(5) CAPACITY TO MAKE WILL

All persons of sound mind not being minors are competent to make a Will. In India person attains majority at completion of 18 years, unless guardian is appointed by Court of his person or property in which case he attains majority on attaining 21 years. Insane person can also make a Will during his lucid interval.

As a Will disposes of the property after testator's death, it can be revoked or altered at any time during his life time.

There is no limitation on the person's power to deal with his property. He may exclude his near relations and give the property to total strangers in preference to his relatives. Even if the Will is unreasonable excluding his close relations, it would be valid and effective, if it is established that the person was of sound mind and not under coercion or undue influence while making the Will.

(6) EXECUTION OF A WILL

The requirements of making a Will are very simple:-

It must bear his signature (which includes even a mark or thumb impression) in presence of a two witnesses who have seen the person sign the Will or to put his mark or thumb impression. Two witnesses are essential for attesting the Will, but both need not be present at the same time.

Will is not required to be executed on any stamp paper and it is not required to be registered under any law. The language can be very simple and it need not use legal wordings.

It is optional for a person to get the Will registered so that the proof of making of the Will by testator becomes easier in case any dispute or challenge is feared by the testator or raised after his death. The attesting witnesses or the testator may sign at any place but generally and advisedly it should be put at the end of the document and also each page may be signed or initialed so as to avoid substitution of the page by someone. The normal phraseology used for Testator and attesting witnesses is as follows:-

Dated this ____ (date) day of ____________ (month) _______ (Year).

____
TESTATOR
Signed in the presence of
____
(Name of the witness)

It is important to note that attesting witness is not required to know the contents of the Will. He is only testifying that the Will is signed by the testator in his presence.

(7) REVOCATION OF WILL

The Will can be revoked in the following ways:-

(i) By another Will or Codicil.

(ii) By any writing declaring an intention to revoke the Will or Codicil and executed in the same manner as a Will.

(iii) By burning, tearing or otherwise destroying the Will by the testator.

As said above, merely cancelling by crossing two lines over it will not amount to valid revocation. It may also be noted that there is no automatic revocation of the Will by the marriage of the testator. Provision in s. 69 providing for cancellation of the Will on marriage does not apply to Hindus, etc. but applies to Christians & Parsis.

(8) **PROPERTY WHICH CAN BE DISPOSED OF BY A WILL**

It is obvious that any property which the testator can dispose of while alive can be disposed off by Will. This is so unless his interest in the property comes to an end on death, for example, in life interest.

(9) BEQUEST WITH REPUGNANT CONDITIONS

It may be noted that testator cannot bequeath the property to someone and at the same time restrict its enjoyment or disposal by such a legatee. In that case the bequest will be valid, but the condition will be invalid. This aspect requires to be made clear, because very often person making a Will will bequeath the property to his wife, but provide that after her death she will not be able to dispose of the property by Will to other persons such as her brother or parents, but the same should go to testator's children or any other person. If such is the intention of testator, he has to confer only life interest to the legatee to use the property during the life time and provide to whom it will go on death of life estate holder. Similarly, while bequeathing the property he cannot lay down a special mode of devolution of property, once he has disposed of the same in favour of the legatee.

(10) Deposit and Registration of Will

As stated above, it is optional for the testator to register his Will in which case himself and the two witnesses will have to sign in the presence of the sub-registrar under the Indian Registration Act.

This ensures the validity and the genuineness of the signature of the testator and the two witnesses.

Another alternative available to the testator is depositing the Will under provisions of the Registration Act. This deposit ensures a safety of the Will. The Will duly executed as above put in the sealed cover can be submitted to the sub-registrar by the testator or by his agent and the same can be withdrawn at any time by the testator or his authorized agent. It may be noted that Will which is registered or deposited can be revoked or cancelled at any time and another Will can be executed by the testator without registering the same.

(11) Coparcenary property

Under Hindu Succession Act, as amended in 2005, a male or female may dispose of by his/her share in the Joint family property by will. Male member can dispose of the share by Will so also a daughter, who becomes a coparcener like a son may dispose of the same by Will. Wife/mother who got the share in the joint family property at the time of deemed partition on account of death of the husband, or on actual partition between father and son or between sons can also dispose of her share in the property by Will.

(12) Probate of Will

Without going into the details of the procedure for obtaining probate to be issued by the Court, it may be stated that procedure for getting a probate is provided for in Indian Succession Act when authorities such as Banks, Companies, Revenue Authorities, etc. do not accept the Will unless the same is probated. It is nothing but certified copy of the Will under seal of the Court after issuing notice to heirs.

(13) Wills and Tax Planning

Quite often tax planning is resorted to by a testator through the medium of a Will. Also social aspects may require the testator not to give away property to one or more legatees specifically, but to create the trust of the properties or part of the properties, mentioning the beneficiaries, but providing indeterminate shares to the beneficiaries and leaving the distribution of income or corpus to the trustees of the trust considering the need or requirement of various persons mentioned in the trust deed as beneficiaries. The obvious advantage in adopting this method is to see that the income or corpus of the property settled on trust is distributed to all or some of the beneficiaries as per the requirement of those beneficiaries such as education, marriage, settlement in life, etc. The tax advantage will result if the trust created by Will does not give the income or corpus separately to one or more beneficiaries, but provides indeterminate shares in the income or property at the discretion of the trustees. In case of such a trust created by Will, it will be a separate taxable entity liable to tax at the appropriate rate and not at the maximum marginal tax rate which would be the position if such trust with indeterminate shares was created during his life time. However, only one such trust with indeterminate shares can be created for getting the benefit of being taxed at appropriate rate. The advantage would be that the income distributed by trustees will not be taxable in the hands of the beneficiaries who receive the same, but will be taxed in the hands of the trustees at the appropriate rate and not at the maximum marginal rate. If a trust is created with specific shares to the beneficiaries, income or corpus which a beneficiary is entitled to have will be added to its income or wealth. This situation will be avoided by creating a trust by Will with indeterminate shares.

(14) BEQUEST TO UNBORN PERSON

Very often the testator desires to bequeath his property to his grand children who are not in existence at the time of making of the Will or even at the time of his death. Such a bequest to an unborn person is governed by section 112 & 113 of the Indian Succession Act. Under the said section, a direct bequest in favour of persons not in existence at the time of testator's death is declared void. By way of exception to the above position, the section provides for situation one where there is a prior bequest in favour of an existing person which is to precede the bequest to the unborn person who stands in particular degree of relation to a specified individual and vesting of the bequest is otherwise deferred to such a unborn person until a time later than the death of the testator. In such situation, under the above exception, if a person answering the description is alive, either at the death of the testator or comes in to existence between that event and such later time then the bequest shall go to such person, though he may not have been in existence at the time of testator's death and if such person is dead than the bequest shall go to his legal representatives. Further, under s. 113, bequest to the unborn person has to comprise the whole of remaining interest of the testator in the property bequeathed. In both the situations, the bequest cannot remain in abeyance at any point of time. It is not possible to discuss in detail the above subject.

The rule against perpetuity is governed by section 114 of the Indian Succession Act. For the sake of clarity sections 112 & 113 as well as 114 are reproduced below to avoid any confusion.

"112. Bequest to person by particular description, who is not in existence at testator's death. - Where a bequest is made to a person by a particular description, and there is no person in existence at the testator's death who answers the description, the bequest is void.

Exception - If property is bequeathed to a person described as standing in a particular degree of kindred to a specified individual, but his possession of it is deferred until a time later than the death of the testator, by reason of a prior bequest or otherwise; and if a person answering the description is alive at the death of the testator, or comes into existence between that event and such later time, the property shall, at such later time, go to that person, or, if he is dead, to his representatives.

113. Bequest to person not in existence at testator's death subject to prior bequest. - Where a bequest is made to a person not in existence at the time of the testator' s death, subject to a prior bequest contained in the will, the later bequest shall be void, unless it comprises the whole of the remaining interest of the testator in the thing bequeathed.

114. Rule against perpetuity. - No bequest is valid whereby the vesting of the thing bequeathed may be delayed beyond the life-time of one or more persons living at the testator's death and the minority of some person who shall be in existence at the expiration of that period, and to whom, if he attains full age, the thing bequeathed is to belong."

(15) PROVISION FOR ACCUMULATION

It may be noted that under s. 117 of Indian Succession Act provision to accumulate income wholly or in part for a period longer than 18 years from the death of the testator shall be void to that extent. There are certain exceptions which are as under:

"117. Effect of direction for accumulation –

(1) Where the terms of a will direct that the income arising from any property shall be accumulated either wholly or in part during any period longer than a period of eighteen years from the death of the testator, such direction shall, save as hereinafter provided be void to the extent to which the period during which the accumulation is directed exceeds the aforesaid period, and at the end of such period of eighteen years the property

and the income thereof shall be disposed of as if the period during which the accumulation has been directed to be made had elapsed.

(2) This section shall not affect any direction for accumulation for the purpose of—

(i) the payment of the debts of the testator or any other person taking any interest under the will, or

(ii) the provision of portions for children or remoter issue of the testator or of any other person taking any interest under the will, or

(iii) the preservation or maintenance of any property bequeathed; and such direction may be made accordingly."

(16) BEQUEST TO AN EXECUTOR

It may be noted that under s. 141 of Indian Succession Act, the bequest to an executor mentioned in the Will to carry out the provisions of the Will is invalid unless he proves the will or otherwise manifests an intention to act as executor.

(17) BEQUEST TO AN ATTESTING WITNESS

Bequest is invalid under s. 67 Indian Succession Act, but the section does not apply to Hindus, etc. Hence, it would be valid for Hindus, etc.

(18) GENERAL

(1) It is also suggested that if the testator does not desire to register the Will, he and the witnesses can execute the same before a notary. It will be sufficient proof that the Will has been executed by the testator and attested by two witnesses. It may be noted that at present the notary requires passport size photograph to be affixed to the document at the end.

(2) Property which is subject to encumbrance cannot be bequeathed without liability. The liability has to be discharged either by the testator's estate or by the legatee as provided by the Will.

(3) Even if the property such as shares or house in a society contains nomination in favour of wife or son, it can be bequeathed to anyone because the nominee is not entitled to be the owner on the death of the testator, but he holds the same on behalf of the legal heirs mentioned in the Will or on interstatacy. The situation will be different, if there are joint holders (such as wife or son) on the record. Then, the second holder becomes the owner of the property.

(4) Section 118 of Indian Succession Act puts restriction on bequest to charity, in case of person having a nephew or niece or any nearer relatives, except provided by following the requirements mentioned in section 118. However, this section has been struck-down by the Supreme Court as unconstitutional in the decision in AIR 2003 SC 2902.

(5) If a person who has made the Will ceases to be a Hindu, etc. and becomes a Christian he will not be governed by Hindu Law, but will be totally governed by all provisions of Indian Succession Act.

In brief, the following are the benefits/ advantages of making a Will:

(i) Procedure is very simple.

(ii) Different Wills can be executed for different properties.

(iii) Can be easily revoked, by following the same procedure.

(iv) One discretionary trust can be created by Will for tax benefit as stated above.

(v) Capital gain on transfer of capital assets is avoided by giving the property by Will as against transferring the same during the testator's life time.

(vi) It enables the testator to give the property to anyone he desires as against mandatory provisions of section 8 (in case of male) or section 15 (in case of female) (Hindu Succession Act) under which property will go to the heirs mentioned in the above sections.

It is, therefore, very desirable for a person having property to make a Will so that the property, after his death, can go to the persons he desires.

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