

Acit and Another Vs. M/S. True Zone Buildwell Pvt. Ltd. and Another

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Court : Income Tax Appellate Tribunal ITAT Delhi

Decided On : Jan-24-2013

Judge : The Honourable Mr. R.P. Tolani, Judicial Member & the Honourable Mr. B.C. Meena, Accountant Member

Appeal No. : ITA Nos. 1696 & 2094/Del./2012 & CO No. 249/Del/2012

Appellant : Acit and Another

Respondent : M/S. True Zone Buildwell Pvt. Ltd. and Another

Judgement :

B.C. Meena, Accountant Member

The revenue has filed ITA No.1696/Del/2012 and the assessee has preferred Cross Objection No.249/Del/2012 against this appeal. The assessee has also filed ITA No.2094/Del/2012 on certain issues against the order of CIT (A) dated 31.01.2012. The grounds of appeal taken in these three matters are as under :-

ITA No.1696/Del/2012

"1. The order of Ld. CIT(A) is not correct in law and facts.

2. On the facts and in the circumstances of the case, the Ld CIT(A) has erred in law and facts in deleting the addition of Rs.6,26,860/- in respect of M/s. Uttaranchal Realtors Pvt. Ltd. out of the total addition of Rs.14,85,009/- made by

the Assessing officer in respect of disallowance of commission.

3. On the facts and in the circumstances of the case, the Ld CIT(A) has erred in holding that the estimation of profit amounting to Rs.4,17,12,850/- by the Assessing Officer in place of profit declared by the assessee of Rs.3,89,49,700/- on percentage completion method is not accepted.

4. The order of Ld CIT(A) is perverse in law and on facts.

5. The appellant craves leave to add, alter or amend any/all of the grounds of appeal before or during the course of hearing of the appeal."

CO No.249/Del/2012

"1. That Ld. ACIT has erred in law as well as on facts in raising ground no.3 in deleting the addition of Rs.41712850/- made by the AO on account of estimating the profit under percentage completion method because CIT(A) has appreciated which AO ignored that:

a) The AO has not made any addition but estimated the profits.

b) The AO has rejected the books of accounts u/s 145(3) without any valid reasons.

c) The AO has applied method of accounting not relevant to the assessee's business while assessee has adopted and opted standard method of accounting approved by Accounting Standards of ICAI and held to be standard method by the Hon'ble Supreme Court and recently Delhi High Court in Manish Buildwell's case.

d) The AO has failed to appreciate that assessee is not engaged in the business of construction of building or structures but engaged in the business of development of land/selling of plots of land.

e) The AO has also failed to appreciate that sale of plot of land is made by registered documents by handing over the plot and no ownership vest in the property before final payment is made while in construction activities building is made by the buyer by making part payments on construction basis.

2. The respondent craves leave for addition, modification, alteration, amendment of any of the cross objection.

ITA No.2094/Del/2012

"1. Whether on the facts and circumstances of the case, the Ld. CIT(A)-XXXI is correct in upholding the assessment framed outside the search material and after the change of opinion?

2. That on the facts and circumstance of the case, the Ld. CIT(A)- XXXI erred in confirming the addition of Rs.8,58,149/- being the amount of out of books commission paid by the assessee company u/s 69C of the Income Tax Act, 1961.

3. The assessee craves for the addition, modification and deletion of the grounds of appeal."

2. A search and seizure operation was carried out u/s 132 of the Income-tax Act, 1961 along with other group cases on 31.07.2008. The search was also carried out at the residence of the Director, Shri Rakesh Kumar Garg where certain documents relating to the assessee were found and seized.

3. Ground Nos.1, 4 and 5 of revenue's appeal (ITA No.1696/Del/2012), ground no.2 of cross objection and ground no.3 of assessee's appeal (ITA No.2094/Del/2012) are general in nature and do not require any adjudication, hence the same are dismissed.

4. First of all, we consider ground no.1 of assessee's appeal where the assessee has raised the issue that the assessment has been framed outside the search material and after the change of opinion.

5. We have heard both the sides on the issue. We have already upheld the assessment on the basis of similar facts and circumstances in assessee's own case in ITA No.2092/Del/2012 for Assessment Year 2007-08 vide order dated 04.01.2013. The relevant para of the said order is reproduced as under:-

"5. We have heard both the sides on the issue. We have upheld the assessment on the basis of similar facts and circumstances in assessee's own case in ITA

No.2091/Del/2012 for Assessment Year 2006-07 vide order dated 31.12.2012. The relevant para of the said order is reproduced as under:- "6. We have considered rival submissions on the issue and has gone through the material on record and relevant pages of the paper book. In our considered view, there was a seized material found at the residence of the Director which has to be considered for making the assessment u/s 153A in the case of assessee company and on the basis of such seized material as far as it relates to the undisclosed income of the assessee the addition is required to be made. It is not the material, whether the seized material was found at the premises of the assessee or at the residence of the Director. The company is represented through its Directors, therefore, material found at the residence of the Director is relevant and has to be considered for making the assessments u/s 153A. As far as the scope of the assessment is concerned, we hold that wherever the issues have been considered u/s 143(3) and the assessment has been concluded prior to the initiation of the search the scope of assessment remains limited to the search material and other issues not considered at the time of making the assessment u/s 143(3) of the Act. Considering the totality of the facts and circumstances, we are unable to agree with the contention of the assessee that assessment u/s 153A has been made on the basis of outside the search material and after the change of opinion."

Moreover, in this year, the assessment was made u/s 144 of the Income-tax Act, 1961 on 09.12.2009. The same was held invalid as there was a search operation at the premises of the assessee on 31.07.2008. In view of the provisions of section 153A, the pending assessments abate. The order passed u/s 144 was against the law. Considering all the relevant facts, we dismiss this ground of assessee's appeal."

Considering all these facts, we dismiss this ground.

6. Ground No.2 in the revenue's appeal and ground no.2 in assessee's appeal are against the deleting/sustaining of addition on the issue of disallowance of commission.

7. The total addition made by the Assessing Officer was Rs.14,85,009/-. CIT (A) deleted the addition of Rs.6,26,860/- related to M/s. Uttaranchal Realtors P. Ltd.

against which the revenue is in appeal and CIT (A) sustained the addition of Rs.8,58,149/- against which the assessee is in appeal.

8. We have heard both the sides on the issue. The bills found at the time of search was as under:-

Period 01.04.2008 to 31.03.2009				PARY A-7
S.No.	Ann./Pg.no.	DATE	Name of the Party	Amount
1	A-9/24	19.06.2008	Basera Properties	8,58,149
2	A-2/25	19.06.2008	Uttranchal Realtors P. Ltd.	6,26,860
	Total			14,85,009

The CIT (A) deleted the addition by holding as under :-

"6.3 I have carefully considered the submission, perused the order of assessment and evidence on record. The dispute, as raised by the appellant, pertains to the additions of Rs.14,85,009/- made by the A.O. on account of commission paid out of books u/s 69C of the Income Tax Act. As per the AO, amount paid for commission during the year is less than the amount of bills of commission seized by the department at the time of search and therefore an addition of difference amount was made by the AO. In contention to that AR has submitted detailed explanation party wise and also submitted the reconciliation for the difference amount. After considering the submissions made and documents submitted, I am of the considered opinion that in case of M/s Basera addition of Rs.8,58,149/- is confirmed. Concerning an addition of Rs.6,26,860/- of M/s. Uttranchal Realtors Pvt. Ltd. it is required to be deleted as the same has been added in the preceding Assessment Year 2008-09. IN result out of addition o Rs.14,85,000/- and an addition of Rs.8,58,149 is retained and confirmed. Therefore, the ground raised by the appellant is partly allowed."

We have also perused the material available on record and we find that the CIT (A) has rightly deleted the addition of Rs.6,26,860/- related to Uttranchal Realtors Pvt. Ltd. and the same has been accounted for in the preceding Assessment Year

2008-09. We also find that assessee has failed to explain the reasonable explanation with regard to the commission of Basera Properties, therefore, we find no fault in the order of the CIT (A) and we sustain the same. Thus, ground no.2 of revenue's appeal and ground no.2 of assessee's appeal are dismissed.

9. In the ground no.3, the revenue has raised the issue of estimation of the profit amounting to Rs.4,17,12,850/- instead of the profit declared by the assessee of Rs.3,89,49,700/- on percentage completion method. In the cross objection, the assessee has supported the order of CIT (A) on the basis that Assessing Officer has not made any addition but estimated the profits. The Assessing Officer has rejected the books of accounts of the assessee without any reason. The Assessing Officer has applied the method of accounting not relevant to the assessee's business. The assessee has adopted and opted standard method of accounting approved by Accounting Standards of ICAI and also by Hon'ble Supreme Court and Hon'ble jurisdictional High Court in the case of Manish Buildwell. The assessee has also pleaded that Assessing Officer has failed to appreciate that assessee is not engaged in the business of building or structures but engaged in the business of development of land and selling of plots of land. The assessee has also pleaded that Assessing Officer has failed to appreciate the fact that sale of plot of land is made by registered documents by handing over the plot and no ownership is transferred prior to the final payment received in respect of the sale of the plot of land. While in construction activities the payments are made on the construction basis. Therefore, the percentage completion method is not applicable to the facts of assessee's case.

10. We have heard both the sides on the issue. The assessee has recognized the sales of the plot when the possession of the plot is transferred to the customer and full consideration for the plot had been received. The assessee was following the project completion method which has been accepted by the department in the earlier years. The CIT (A) has granted the relief to the assessee by holding as under :-

"7.1.1 The AO has noticed from the note mentioned with the balance sheet, that the assessee has recognized the sales, when possession of plot has been

transferred to the customers and full consideration of that Plot has been received. As the assessee was not following the percentage completion method, therefore, the assessee was asked to show cause as to why the profit for the assessment year should not be computed by following the percentage completion method.

7.1.2 The AR of the Appellant has submitted that the assessee has been following the project completion method of accounting and the same has been accepted by the department also while making assessment u/s 143(3) of the Act for the assessment year 2005-06. the department has accepted the method of accounting and not only they held it the right and appropriate method but also were convinced as not having deferred the tax liability and were pleased to follow the same for the A.Y 2006-2007. The AR also submitted the copy of assessment orders and submitted that if same has been accepted by the department earlier also, then how the same can be held as an inappropriate method to compute the income as per project completion method which the assessee has followed.

Again, AR has brought the attention that even the Income Tax Act, 1961 has not made it mandatory to follow as section 145 and 145A of the Act, which is Inscribed as under :-

"Section 145:- (1) Income chargeable under the head "Profits and Gains of business or profession" or "Income from Other Sources", subject to the provisions of sub-section (2), be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee.

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

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

Section 145A Notwithstanding anything to the contrary contained in section 145.-

(a) The valuation of purchase or sale of goods and inventory for the purposes of determining the income chargeable under the head "Profits and gains of business or profession" shall be-

(i) In accordance with the method of accounting regularly employed by the assessee; and

(ii) Further adjusted to include the amount of any tax, duty, cess or fee (by whatever name called} actually paid or incurred by the assessee to bring the goods to the place of its location and condition as on the date of valuation.

Explanation.- For the purpose of this section, any tax, duty, cess or fee (by whatever name called) under any law for the time being in force, shall include all such payments notwithstanding any right arising as a consequence to such payment;

(b) Interest received by an assessee on compensation or enhanced compensation, as the case may be, shall be deemed of be the income of the year in which it is received.

As per Income Tax Act provisions, only two accounting standards are mandatory in nature which are elaborated below and other standards are recommendatory.

Official Gazette: As per Notification No. SO 69(E), dated 25-1- 1996 for Notified Accounting Standards, Notified standards is as under:

a. Accounting standard I relating to discloser of accounting Policies.

b. Accounting standard II relating to discloser of prior period items and extra ordinary items and changes in accounting policies.

In accordance to that the assessee is not following percentage completion method which falls under accounting standard -7, i.e. accounting for construction contracts. They are following project completion method. Moreover, this standard deals with the accounting for the construction contracts and not with the taxation

matters.

However, Accounting standard-7 states that there are two methods of accounting for contracts commonly followed by contractors are the percentage of completion method and the completed contract method.

a) Under the percentage of completion method, revenue is recognized as the contract activity progresses based on the stage of completion reached. The costs incurred in reaching the stage of completion are matched with this revenue, resulting in the reporting of results which can be attributed to the proportion of work completed. Although (as per the principle of 'prudence') revenue is recognized only when realized, under this method, the revenue is recognized as the activity progresses even though in certain circumstances it may not be realized.

b) Under the completed contract method, revenue is recognized only when the contract is completed or substantially completed; that is, when only minor work is expected other than warranty obligation. Costs and progress payments received are accumulated during the course of the contract but revenue is not recognized until the contract activity is substantially completed.

The principal advantage of the completed contract method is that it is based on results as determined when the contract is completed or substantially completed rather than on estimates which may require subsequent adjustment as a result of unforeseen costs and possible losses. The risk of recognizing profits that may not have been earned is therefore minimized.

The AR of the appellant inferred that the Income Tax Act has not prescribed any method of accounting as per section 145 or 145A of the Act, for the builders and real estate; therefore, the observation of the AO is erroneous.

The AR has inscribed that assessee has the choice on method, but such method should be shown as regularly followed. Department cannot compel to choose a particular method and in support of that has placed the following case laws to defend his contention.

- a) CIT v. McMillan and CO. [1958] 33 ITR 182 (SC).
- b) Investments Ltd v. CIT [1970] 77 ITR 533 (SC)
- c) MKB Asia (P) Ltd. v. CIT [2008] 167 Taxman 256 (Gau.).
- d) CIT VS. Hyundai Heavy Industries Co. Ltd. (2007) 210 CTR (SC) 178 . (2007) 291 ITR 482 (SC)
- e) CIT Vs. Bilahari Investment (P) Ltd. (2008) 215 CTR (SC) 201 : (2008) 3 DTR (SC) 329 : (2008) 299 ITR 1 (SC)
- f) Juggilal Kamlapat Bankers v. CIT [1975] 101 ITR 40 (All.)
- g) CIT v. Smt. Vimla O. Son wane [1994] 75 Taxman 335 (Bom.)
- h) Awadhesh Builders vs. ITO (2010) 37 SOT 122
- i) Vastukar vs ITO (ITAT Cuttak)
- j) Fort Projects (P) Ltd. V. Deputy Commissioner of Income Tax (2011) 63 DTR (Kol)(Trib) 145

7.2.1 The AO has discussed the legal position of the accounting principles to be followed In the case of the Real Estate Developers. As per the AO the project takes normally 4-5 years before it is completed. The developer receives advances right from the beginning rather prior to work of construction commences and continues taking installments regularly from the buyers as the construction progresses. Therefore, question arises that when income becomes taxable in such cases. Is it the year of completion of the project or should the income be offered on a year to year basis. If the income is to be offered on a year to year basis should it be computed on percentage of completion method or should it be estimated?

7.2.2 The AR has submitted that the assessee has carried out the business of real estate developers by developing land and then plotting it. The land has been developed in the earlier year and the plots are being sold on payment basis which

is varying from 45 days to 6 Months. There is no period of 4-5 years is involved as has been envisaged by the AO in his assessment order. The observation of the AO is his own observation and has got nothing to do with the business of the assessee as the assessee have not carried out the construction works and has received installments as the construction progresses. AR stated that the observation of AO is not related with the business of the assessee, as such, the same cannot be the basis for converting the project completion method to percentage completion method. The assessee has accounted for its income on the basis of the sale of the plots as and when the full payment of the plot has been received. The income has been recognized in that very year and no deferment has been made as alleged by the AO.

7.3.1 The AO has inferred that it is a well settled principle that for the purpose of income tax, income has to be determined on a year to year basis. This was so decided by the Supreme Court in the case of P.M. Mohammed Vs. CIT (1969) 73 ITR 735. Therefore, in the case of Real Estate Developers also, the income is to be offered on a year to year basis.

7.3.2 The AR in his reply submitted that the facts of the case as quoted by the AO are totally different with the facts of the appellant and the distinguishment of the facts is as under:

Differentiation and distinguishment:-

The facts of the case are altogether different than the facts of the assessee. In the case cited by the Ld AO, it has been held:-

Business-Adventure in the nature of trade-Agreement for purchase of vast areas of land - Division of area into 23 Plots-Sale of 22 plots to others and 23rd retained by the assessee-Whether transactions in the nature of trade- Profits from transaction how ascertained- Value of plot retained by assessee, whether to be taken into account.

In the case of the assessee, no such situation for purchase of vast area of land, division of the area into 23 plots and one plot retained by the assessee himself,

and whether the value of plot retained by the assessee is to be taken into account was present. Rather there has been a substantial question of law as has been raised by the AO that whether, the method of accounting followed by the assessee from the past so many years and accepted by the department as the correct method of deducing profits is liable to be converted into project completion method to percentage completion method. The facts of the case and the substantial question raised by the AO are nowhere covered, as such, the same is not applicable in the case of the assessee company and is not to be relied upon.

7.4.1 The AO has observed that it is a well settled principle as to if no specific method of recognizing revenue has been prescribed in the Income Tax Act, in that case the usually accepted methods or principles should be adopted. In this connection it is stated that the Council of the Institute of Chartered Accountants of India had issued a guidance note in the year 2006, recommending the principles for recognition of revenues arising from real estate sales by the enterprises engaged in such activities (commonly referred to as 'real estate developers', 'builders' or 'property developers'). As per the Guidance Note Revenue in the case of real estate sales should be recognized when the following conditions are satisfied:

1. The seller has transferred to the buyer all significant risks and rewards of ownership and the seller retains no effective control of the real estate to a degree usually associated with ownership;
2. No significant uncertainty exists regarding the amount of the consideration that will be derived from the real estate sale; and
3. It is not unreasonable to expect ultimate collection.

It is also provided in the guidance note that in the case of real estate sale, all significant risks and rewards of ownership are normally considered to be transferred when legal title passes to the buyer (e.g., at the time of the registration, with the relevant authorities, of the real estate in the name of the buyer) or when the seller enters into an agreement for sale. All significant risks and rewards of ownership are also considered to be transferred, if the seller has entered into a

legally enforceable agreement for sale with the buyer even though the legal title is not passed or the possession of the real estate is not given to the buyer.

When the seller has transferred to the buyer all the significant risks and rewards of ownership, it would be appropriate to recognize revenue at that stage. However, In case the seller is obliged to perform any substantial acts after the transfer of all significant risks and rewards of the ownership, revenue should be recognized on the proportionate basis as the acts are performed, i.e., by applying the percentage of completion method in the manner explained in Accounting Standard (AS) 7, Construction Contracts. Therefore, in the case of Real Estate Developers also, the income is to be offered on a year to year basis.

7.4.2 The AR has submitted that the guidance notes issued by the ICAI in 2006 has been withdrawn and is not applicable. As per accounting standard prescribed what has been held as mandatory is reproduced below:-

In accounting for constructions contracts in financial statements, either the percentage of completion method or the completed contract method may be used. When a contractor uses a particular method of accounting for a contract then the same method should be adopted for all other contracts which meet similar criteria.

Therefore, the observation made by the AO are nothing but a distorted inference made by him. Therefore, the same are not liable to be considered and the consequent additions made, based thereon is liable to be deleted. The AR has provide the recent Judgment of Hon'ble Delhi High Court CIT Vs. Manish Build Well (P) Ltd. (Del.) (HC) (2011) 63 DTR 369 which has endorsed the submission of the appellant.

7.5 I have carefully considered the submission, perused the order of assessment and evidence on record. The dispute, as raised by the appellant, pertains to the estimation of the profit by the AO on percentage completion method instead of project completion method. The AO has the contention that project of the appellant takes normally 4-5 years before it is completed. The assessee receives advances prior to commencement of the construction work and continues taking installments regularly from the buyers as the construction progresses. Therefore, income

should be taxable on year to year basis on percentage of completion of the project. Against the contention of the AO, AR has submitted that plots are being sold on payment basis which is varying from 45 days to 6 Months. The AR has also stated that department cannot compel the appellant to follow any particular method. Income Tax Act does not force anyone to follow any particular accounting standard. The appellant was following project completion method which is in accordance of the existing law and the same has also been accepted by the Income Tax department during assessment done earlier u/s 143(3) and it is the settled law that if one method is employed, it should regularly be employed. After considering the argument of both and in view of the judgement announced by the Hon'ble Delhi High Court in case of CIT Vs. Manish Build Well (P) Ltd. (Del.) (HC) (2011) 63 DTR 369, I am of the considered opinion that no evidences was found during the course of search to show that the books of account are not properly maintained by the appellant. The main thrust of the AO while making the addition is that the appellant is deferring the payment of taxes. However, this allegation of the AO is devoid of merits and cannot be accepted because the appellant is consistently following a method of accounting which is recognized in real estate development business. It cannot be said that the Project Completion Method could result in deferment of payment of taxes. It has been held by the Hon'ble High Court, Delhi in above case that AS-7 issued by ICAI also recognizes the position that in case of construction contracts the assessee can follow either of the two methods. This Project Completion Method has been accepted by the A.O in earlier years, hence, arguments of the AR of the appellant has a strong acceptance Thus, estimation of profit amounting to Rs.4,17,12,850/- in place of profit declared by the appellant of Rs.3,89,49,700/- on percentage completion method is not accepted.

This ground of appeal is thus allowed."

We have carefully gone through the facts of the case and considered submissions of the case and has also considered the evidences on record. The only dispute is regarding the estimation of profit. The Assessing Officer adopted percentage completion method while assessee is adopting project completion method. As per Assessing Officer, the project takes 4 - 5 years to be completed, therefore, the income should be taxed year to year basis on percentage completion method of

the project. In assessee's case, the plots are being sold and the payment is being received within a period of 45 days to six months. The assessee is adopting project completion method regularly. The only presumption of the Assessing Officer is differing the payment of taxes and on that basis, the Assessing Officer has adopted the percentage completion method. In our considered view, there was no sufficient material with the Assessing Officer which could establish that the assessee was differing the payment of taxes by adopting the project completion method. He assessee was consistently following this method which is a recognized method of accounting income in the business of real estate development.

Considering totality of these facts, we find no fault in the order of CIT (A) and we dismiss this ground of revenue's appeal and allow the cross objection filed by the assessee.

11. In the result, the appeal of the revenue and appeal of the assessee are dismissed and the cross objection filed by the assessee is allowed.

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