* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

\+ **ITR Nos. 203-10 of 1989**
with
ITR Nos. 19-20 of 1991

% *Decision Delivered On: 06th September, 2010*

1) **ITR Nos. 203-10 of 1989**

M/s. HANSALLAYA PROPERTIES, NEW DELHI . . . Appellant

through : Mr. M.S. Syali, Sr. Advocate with Ms. Mahua Kalra, Advocate.

VERSUS

COMMISSIONER OF INCOME TAX, DELHI-VIII, NEW DELHI
. . .Respondent

through: Mr. Sanjeev Sabharwal, Advocate

2) **ITR Nos. 19-20 of 1991**

Mrs. PUSHPA VADERA ...Appellant

Through: Mr. M.S. Syali, Sr. Advocate with Ms. Mahua Kalra, Advocate.

VERSUS

COMMISSIONER OF INCOME TAX ...Respondent

Through: Mr. Sanjeev Sabharwal, Advocate

CORAM :-
HON'BLE MR. JUSTICE A.K. SIKRI
HON'BLE MS. JUSTICE REVA KHETRAPAL

1. Whether Reporters of Local newspapers may be allowed to see the Judgment?
2. To be referred to the Reporter or not?
3. Whether the Judgment should be reported in the Digest?

A.K. SIKRI, J. *(ORAL)*

1. Before we reproduce the questions of law referred for opinion of this Court by the Income Tax Appellate Tribunal (hereinafter referred to as 'the Tribunal') in compliance with the order passed by this Court under Section 256(2) of the Income Tax Act ('the Act' in short), we deem it appropriate to state the facts leading to the reference.

2. The land at 15-Barakhamba Road, New Delhi (leasehold land) was originally leased on 31.5.1932 to a partnership firm M/s. Naraindass Hansraj in which late Shri H.R. Vadera was a partner. On that land stood a building which was occupied by the two daughters of Shri H.R. Vadera, viz., Dr. Miss Lila Raj and Dr. Miss Shanti Raj. The firm M/s. Hansalaya Properties came into existence with effect from 08.8.1970 under a deed of partnership executed on the said date between late Shri H.R. Vadera and Mrs. Pushpa Vadera. Two minor children of Mrs. Pushpa Vadera were also admitted to the benefits of the said partnership. As per the said partnership, the business of the assessee was of a constructing a multi-storeyed commercial building on the land situated at 15-Barakhamba Road, New Delhi after demolishing the existing structure. The firm M/s. Naraindass Hans Raj had been dissolved and the lease-hold land was allotted, to late Shri Hansraj Vadera. On 08.8.1970 (the date on which the assessee firm was constituted) late Shri H.R. Vadera brought in the aforesaid lease-hold property and the building situated thereon as his capital contribution in the capital of the said firm. This was done in terms of Clause 3 of the said Partnership Deed. Thereafter on

31.8.1970, the capital account of late Shri H.R. Vadera w credited by ₹2,01,000 and the same amount was debited in the assessee's books as the value of the said property which had been brought in by Shri H.R. Vadera in the said new firm. The building plans for developing the aforesaid property for the purposes of constructing a multi-storeyed commercial building thereon, were approved by the New Delhi Municipal Corporation in October, 1970.

Shri H.R. Vadera expired on 09.11.1971 and under a Will executed by him his son Mr. Devraj Vadera became the partner in the said firm in his place. Thereafter, the building project commenced and got completed by 31st May, 1977. In view of the fact that the above project of the assessee went on for several years, the assessee was asked by the Income Tax Authorities in 1977 (when the assessment for the Assessment Year 1975-76 was taken up by the Income Tax Officers) to file a consolidated profit and loss account for the entire period starting from 08.08.1970 to 31.051977 with a view to determine the profit of the entire venture as all the assessments of the said firm were pending at that time. The entire profit was thereafter apportioned in each previous year. In the consolidated Profit and Loss Account for the above period (which was filed by the assessee in September, 1977) the assessee debited as one of its items of expenditure, a sum of ₹2,01,000 as the cost of the land at 15-Barakhamba Road, New Delhi on which its project was being executed. However in March, 1978, the assessee field a revised consolidated Profit and Loss Account in which the cost of the aforesaid land was debited

by ₹36,61,625. The figure of ₹ 36,61, 625 represented the mark value as per approved valuer's certificate as on 018.08.1970. The capital account of late Shir Hansraj Vadera was credited with a further sum of ₹34,60,625 (₹36,61,625 - ₹2,01,000). The value of the land in the wealth tax returns of Shri Hansraj Vadera and other partners on the respective valuation dates, viz., March 31, 1970 to 1974 were revised keeping in view the value of land at ₹36,61,625 as on 08.08.1970, at ₹31,81,410, ₹40,09,900, ₹48,02,950, ₹54,17,750 and ₹62,74,125 respectively. The revision in the value of the land aforesaid was confirmed in appeals.

3. In the Estate duty proceedings of late Shri H.R. Vadera, the value of the land was also revised by his son and heir Shri Devraj for determining the interest of late H.R. Vadera in the partnership firm wherein the value was revised to ₹45,23,800 keeping in view the revision land value as on 08.08.1970 at ₹36,61,625. The said revision of was finally accepted after appellate proceedings by valuing the said land at ₹45,23,800 as revised by the legal heir. The Income Tax Officer, in his draft order, rejected the revised figure of the cost of land at ₹36,61,625 debited by the assessee to its revised consolidated Profit and Loss Account and held that the assessee was entitled only to a deduction of ₹2,01,000 as the cost of the land in computing its profit from the venture. This was the order for Assessment Years 1972-73 and from 1974-75 to 1977-78. The assessment order was framed to the same effect after obtaining the approval of the Inspecting Assistant Commissioner.

4. The Commissioner of Income Tax (Appeals) also held that t assessee was entitled to a deduction of ₹2,01,000 only as the cost of land in computing its profit from the venture.

5. Thereafter, the matter came up before the Income Tax Appellate Tribunal (hereinafter referred to as 'the Tribunal'). It was submitted on behalf of the assessee before the Tribunal that in terms of Clause 3 of the Partnership Deed, the correct amount to be credited to the capital account of late Shri H.R. Vadera and debited in the assessee's account as the cost of the land was not ₹2,01,000 (being the amount originally declared by late Shri H.R. Vadera in his wealth tax returns for the Assessment Year 1970-71), but the fair market value for the purpose of assessment, as the return contemplates market value as determined by the wealth tax authorities. It was also said that the land which was brought in by late Shri H.R. Vadera as his capital contribution to the assessee, had been received by the assessee as a capital asset and had been subsequently converted into stock-in-trade by the assessee and therefore, the assessee was entitled to debit in its Profit and Loss Account, as the cost to it, the market value of such land on the date of its conversion by the assessee into stock-in-trade. It was also said that in any case the proper and real commercial profits of the assessee could be ascertained only after deducting the sum of ₹36,61,625 as the cost of land, being the land's market value as on the date of its introduction into the assessee firm. When the appeal was heard by the Division Bench, there was difference of opinion. The Judicial Member vide its order dated 18.06.1982 rejected all the arguments based on the

interpretation of Clause 3 of the Partnership Deed that the la was initially received by the assessee as a capital asset and was, therefore, converted by its into its stock-in-trade and that the real profits had to be ascertained by the application of commercial principles. However, the learned Accountant Member vide its order dated 12.07.1982 accepted all the arguments of the assessee and held that on the interpretation of Clause 3 of the Partnership Deed and on account of the fact that the land brought in by late Shri H.R. Vadera as his capital contribution to the assessee was received initially by the assessee as a capital asset and was thereafter converted by it into stock-in-trade, and also on account of the general principles of commercial accounting for determining the real profits of the business, the Assessee was entitled to a debit of ₹36,61,625 in its Profit and Loss Account as the cost to it of the land. On account of the above difference of opinion, the following issues were referred to the Special Bench:

1) Whether the assessee firm is entitled to deduction of ₹2,01,000 or ₹36,61,625 as cost of the land on which the multi-storeyed building was constructed on the following grounds:-

    (a) Interpretation of Clause 3 of the Partnership Agreement,

    (b) The land having been brought in by late Shri H.R. Vadera as a stock-in-trade or as a capital asset, and

    (c) If brought in as a capital asset, then on its being converted into stock-in-trade.

2) Whether there is any evidence of money being charg or so whether addition sustained by the Judicial Member is justified.

6. The Special Bench vide its order dated 15.04.1983, agreed with the view taken by the learned Judicial Member. In conformity with the decision of the Special Bench, the Bench thereafter passed an order dated 28.07.1983.

7. It is in the aforesaid background, the following two questions are formulated and referred for opinion of this Court:

1) Whether the Tribunal was right in holding that in computing the profits and gains of the firm on the sale of the properties in question, the value of the plot brought in by one the partners M/s. Vadera by way of capital contribution, should be taken as figure with which he was initially credited in respect of that plot, viz., ₹2,01,000 or should the value be taken on some other basis? If so, what basis?

2) Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that the assessee is not entitled in the computation of its profits to the deduction of ₹3 lakhs paid to (Dr. Miss) Lila Raj and Dr. (Miss) Shanti Raj by the assessee firm?"

8. Out of the above questions, question No.1 is referred for Assessment Years 1972-73 to 1979-80 and question No.2 for Assessment Year 1972-73. Now we proceed to answer these questions.

Question No. 1

9. From the facts emanated above, the following aspects clearly emerge:

(a) Mr. H.R. Vadera was partner in some other firms, vi M/s. Naraindass Hansraj and on dissolution of that firm when the accounts of the partnership was settled, he was given the leasehold land in question which came to his share.

(b) Partnership in question, i.e., the assessee firm was constituted in which Mr. Vadera also joined as one of the partners, he brought the aforesaid asset into his firm 'as his capital contribution in the capital of the said firm'.

(c) Clause (3) of the Partnership Deed executed between the partners provided the manner in which the said land was to be valued to determine the capital contributed by Mr. Vadera. This Clause reads as under:

> "the land situated at 15-Barakhamba Road, New Delhi shall be the property of the firm and as taken in the Wealth Tax return of Sh. Hansraj Vadera and shall be credited to his capital account in the books of the firm. Therefore, the respective partners may contribute such capital as they mutually agree upon."

10. On 31.08.1970, the capital account of Mr. Vadera was credited by ₹2,01,000 and the same amount was debited in the assessee's books as the value of the said property.

11. After construction of multi-storeyed commercial building on the said plot of land, which took several years, the Assessing Officer asked the assessee to file consolidated profit and loss account for the entire period from 08.08.1970 to 31.05.1977. Though initially in the consolidated profit and loss accounts in the said period, the

assessee debited a sum of ₹2,01,000 as cost of land, the revis return was filed in March, 1978 wherein this cost of land was debited by ₹36,61,625. It is not in dispute that the revised return was filed well within permissible time. The books of account of Mr. Vadera was also credited with further sum of ₹36,61,625 thereby showing his capital as ₹36,61,625.

12. In the wealth tax assessment, the property in question was finally taxed at a value of ₹36,61,625. Same was the value taken in proceedings under Gift Tax Act as well as Estate Duty assessment while leaving the duty on the estate levy by Mr. Vadera.

13. Notwithstanding the fact that for the purpose of wealth tax charge into the hands of Mr. Vadera, the value of this property was treated at ₹36,61,625, and this fact was pleaded before the AO, the AO refused to accept the same. The AO was of the opinion that when the aforesaid property was brought by the assessee in the form of his contribution as capital, value in the books of account was shown as 2,01,000 and therefore, for the purpose of the income tax that was the value which was to be taken into consideration, moreso when the capital account of Mr. Vadera was credited with this amount. He was of the opinion that the assessment under the Income Tax Act was to be framed on the basis of provisions contained in the Act and was not to be influenced by other Direct Tax. This is the view, which is accepted by the CIT(A) as well as the Tribunal and the proprietary or correctness of this view is the subject matter of dispute.

14. No doubt, the Income Tax Authorities are supposed to look into the provisions contained in the Act for the purpose of making

assessment. What we find is that even if those provisions are be applied, there is an error in the approach of the Authorities below. We have already spelt out the basic features/facts of this case. What is glossed over by the Authorities below is that the property in question was brought in by Mr. Vadera as partner of the assessee firm in the form of capital. Insofar as Mr. Vadera is concerned, it was his capital contribution to the firm. Thus, it was to be evaluated in the manner the partners agreed in the manner provided in Clause 3 of the Partnership Deed. That Clause, which has been reproduced above, clearly stipulates that it would be as per the wealth tax returns. Thus, the capital that was brought in by Mr. Vadera in the form of the aforesaid land was to be given the valuation which had to be determined as per the wealth tax returns by the Wealth Tax Authorities. Once we are clear in our mind about this approach, which was required to be taken, it hardly need to be emphasized that if the valuation of the land in question was accepted by the Wealth Tax Authorities to be ₹36,61,625, the contribution of the said land in the form of capital to the firm also had to be at par. There could not have been a different yardstick. It would be clearly an absurd position that for the purpose of payments of wealth tax it was valued at ₹36,61,625, but when it comes to his capital contribution by giving that asset to the firm, it is valued at a partly sum of ₹2,01,000. No doubt, entry in the books of account of the firm, in the beginning, was at ₹2,01,000. But it was open and permissible to the assessee to revise the same after the finalization of assessment under the Wealth Tax Act, as precisely that was the modus of

valuation provided in the Partnership Deed itself by the partne However, as already pointed out above, this revision was carried out by the assessee by filing revised return well within the permissible limits prescribed under the Income Tax Act.

15. It is not in dispute that on the revision of the value of the said asset, capital account of Mr. Vadera was also upgraded. We accordingly answer the question No. 1 in favour of the assessee and against the Revenue.

16. Insofar as second question of law is concerned, no arguments were advanced and it is implied there from that this question is not pressed. Therefore, this question is returned unanswered.

17. This Reference is answered accordingly.

(A.K. SIKRI)
JUDGE

(REVA KHETRAPAL)
JUDGE

SEPTEMBER 06, 2010.
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