



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

+ **ITA No.791/2011**

% *Reserved on: 6th March, 2012*
Date of Decision: 29th March, 2012

COMMISSIONER OF INCOME TAX-IV Appellant
Through: Mr. N. P. Sahni, Sr. Standing
Counsel.

versus

M/S. I. K. INTERNATIONAL PVT. LTD. Respondent
Through: Mr. Ajay Vohra with Ms. Kavita
Jha & Mr. Somnath Shukla,
Advocates.

CORAM:

HON'BLE MR. JUSTICE SANJIV KHANNA

HON'BLE MR. JUSTICE R.V. EASWAR

1. Whether Reporters of local papers may be allowed to see the judgment?
2. To be referred to the Reporters or not ? Yes.
3. Whether the judgment should be reported in the Digest? Yes.

R.V. EASWAR, J.:

1. On 11.11.2011 the following substantial questions of law were framed: -



“(1) Whether the Income Tax Appellate Tribunal was right in holding that Assessing Officer was not justified in invoking Section 50(2) of the Income Tax Act, 1961?

In case the first question is answered against the Revenue;

(2) Whether the assessee is entitled to exemption under Section 54EC of the Income Tax Act, 1961 in respect of Rs.4,30,40,600/-?”

2. The appeal relates to the assessment year 2006-07. The assessee, who is the respondent herein, is a private limited company engaged in the business of publishing and trading of educational books.

3. The brief facts giving rise to the present appeal may now be noticed. In the return of income filed on 29.11.2006, the assessee declared long term capital gains of ₹ 2,83,99,571/- on sale of property at S-7 & 8, Green Park, New Delhi. The capital gains were invested in eligible REC bonds and exemption was claimed under Section 54EC of the Income Tax Act (hereinafter referred to as the “Act”). In addition to the long term capital gains, the assessee also declared short term capital gains of Rs.86,28,216/-. While examining the return in the course of the assessment proceedings under Section 143(3) of the Act, the Assessing Officer called upon the assessee to explain the long term capital gains and the basis on



which exemption was claimed. The assessee, in response thereto, submitted the photocopy of the purchase and sale deeds in respect of the property and explained as follows: -

“We have purchased the property S-7, 8, Green Park for ₹ 2,16,00,000/- including stamp duty ₹ 16,00,000/- on 30.03.2001, 25.04.2001 and 03.07.2001 shown under the head Fixed Assets Land ₹ 1,48,00,000/- Building ₹ 68,00,000/-. We have made further construction/alteration during the year as per requirement and charged depreciation accordingly year to year. We have never charged depreciation on Land. We have sold this property for ₹ 5,75,00,000/- under the bifurcation Land ₹ 4,72,00,000/- and Building ₹ 1,03,00,000/-. The capital Gain raised from sale of assets was invested in the Bonds ‘Rural Electrification Corporation Limited’ under section 54EC.”

4. The Assessing Officer noticed that according to the agreement of sale, the assessee was to receive ₹ 7,25,00,000/- as consideration for the property which consisted of basement, ground, first and second floors with terrace rights. The building was found to have been sold with the furniture and fixtures installed therein. The Assessing Officer further found that the assessee had purchased the property on two dates i.e. 30.03.2001 and 25.04.2001 for a consideration of ₹ 2,16,00,000/- including stamp duty of ₹ 16,00,000/-. The assessee had bifurcated the total purchase price of



₹ 2,16,00,000/- (including stamp duty) as ₹ 1,48,00,000/- for the land and ₹ 68,00,000/- for the building. In the financial years 2001-02 and 2002-03 the assessee had made additions to the building in the amounts of ₹ 92,62,242/- and ₹ 62,54,181/-. The aggregate amount of additions came to be ₹ 1,58,16,423/-. In the income tax assessments for the assessment years 2002-03 and 2003-04 the assessee had claimed depreciation at the rate of 10% on the building which was allowed in the assessments. On 29.08.2005 the assessee sold the land and building comprised in the property, namely, S-7 & 8, Green Park, New Delhi for a consideration of ₹ 7,25,00,000/-. This price included ₹ 1,50,00,000/- for the fixtures and furniture in the building. Excluding the same, the sale consideration for the land and building came to ₹ 5,75,00,000/-. Out of the consolidated sale price of ₹ 5,75,00,000/-, ₹ 4,72,00,000/- was for the land and ₹ 1,03,00,000/- was received in respect of the building.

5. In computing the capital gains on transfer of the property in terms of Section 45 of the Act, the assessee declared long term capital gains of ₹ 2,83,99,571/- in the following manner: -

Particulars	Amount (₹)	Amount (₹)
Sales Consideration of Land S-7 & S-8, Green		4,72,00,000/-



Park, New Delhi		
Less:		
- Transfer Expenses		
- Index Cost of Acquisition		
F.Y.		
2000-02 90,00,000 X (497/406)		
2001-02 58,00,000 x (497/426)	1,10,17,241	
	67,66,667	1,88,00,429
Long-term Capital Gain		2,83,99,571

6. It may be seen from the computation that the assessee computed the capital gains on the sale of land as long term capital gains and having invested the gains in REC Bonds which were eligible bonds, claimed the entire long term capital gains as exempt under Section 54 EC of the Act.

7. After noticing the aforesaid facts the Assessing Officer observed that it was not correct to say that the land, building and other assets in the building were separately sold by the assessee, that the land was not a long term capital asset as it was purchased together with the building for a consolidated price of ₹ 2,16,00,000/-, that it was, therefore, not proper for the assessee to bifurcate the value between the land and the building as was shown in the balance



sheet or in the computation of the capital gains and, therefore, the claim of the assessee to treat the land as a long term capital asset cannot be accepted. He held that the provisions of Section 50(2) of the Act were applicable since the assets sold were part of the block of assets on which depreciation was allowable and, therefore, took the view that the capital gains can only be treated as short term capital gains as provided in the aforesaid Section. He then proceeded to compute the short term capital gains. He first adopted the Written Down Value (WDV) of the assets included in the block of assets and having ascertained the same as per the depreciation chart which was part of the assessment record, he computed the WDV of the assets sold as under: -

“Total WDV as per the depreciation chart ₹ 3,06,97,710/-

Less: WDV of assets not sold:

(i)	Computer:	242799	
(ii)	Vehicles:	<u>995511</u>	<u>₹ 12,38,310/-</u>
	WDV of assets sold out:		<u>₹ 2,94,59,400/-”</u>

8. It needs to be clarified here that there were 19 items of assets in the depreciation chart in respect of which the aggregate WDV was ₹ 3,06,97,710/-. These 19 items included land as well as the building in Serial Nos.1 & 2 respectively. Out of the 19 items of



assets the Assessing Officer has excluded only the computer and softwares having WDV of ₹ 2,42,799/- and vehicles having WDV of ₹ 9,95,511/-. It follows that all the other 17 items were taken into account by the Assessing Officer while arriving at the WDV of the assets sold and these included the land and the building comprised in the property transferred. The WDV of the land was shown in the depreciation chart at ₹ 1,48,00,000/- and WDV of the building on the said land was shown as ₹ 1,06,93,049/-. The WDV of the other 15 items of assets comprised in the block of assets need not be separately noticed since the controversy does not centre around them.

9. Having arrived at the WDV of the assets sold at ₹ 2,94,59,400/-, the Assessing Officer proceeded to compute the capital gain on the sale of the building along with the furniture and fixtures as follows: -

“Sale price of the assets:	₹ 7,25,00,000/-
Less: WDV of the assets sold:	<u>₹ 2,94,59,400/-</u>
	<u>₹ 4,30,40,600/-”</u>

10. The aforesaid amount of ₹ 4,30,40,600/- was brought to tax as short term capital gains computed under Section 50(2) of the Act. The Assessing Officer also negatived the assessee's claim for deduction under Section 54EC of the Act on the ground that the said



deduction was not allowable because the depreciable asset, namely, the building was purchased and additions were made up to the end of the financial year 2002-03 and since the building along with furniture and fixtures were sold on 29.08.2005, within a period of 3 years, the same cannot be said to be a long term capital asset as defined in Section 2 (29A) read with Section 2 (42A) of the Act, which require that the capital asset must be held by the assessee for more than 36 months immediately preceding the date of transfer in order that the same can be held to be a long term capital asset. The benefit of Section 54EC is available only in respect of capital gains arising on sale of a long term capital asset. Since the building was held to be a short term capital asset by the Assessing Officer, the benefit of deduction under Section 54EC of the Act was not allowed.

11. The assessee appealed against the assessment order and challenged the computation of short term capital gains under Section 50(2) of the Act and the refusal to allow deduction under Section 54EC of the Act before the CIT (Appeals). It would appear that before the CIT (Appeals) the assessee submitted valuation reports from an approved valuer in support of the bifurcation of the purchase price between the land and building at ₹ 1,48,00,000/- and ₹ 68,00,000/- respectively. These valuation reports were sought to be admitted as additional evidence under Rule 46A of the Income Tax



Rules. The CIT (Appeals) called for the objections, if any, of the Assessing Officer. After considering them, he held that in the course of the assessment proceedings the Assessing Officer never asked the assessee to produce any valuation report in support of the bifurcation of the purchase price and in fact no notice had been given to the assessee to explain the basis of the valuation of the property or the intention to treat the sale of land and building as a composite sale. In this view of the matter he admitted the additional evidence.

12. As regards the computation of the capital gains under Section 50(2) of the Act, the CIT (Appeals) agreed with the assessee that the section was not applicable and that the Assessing Officer was not right in treating the building as a short term capital asset and in consequently rejecting the claim for relief under Section 54EC. He found that in the books of account of the assessee, the cost of the land and the superstructure were separately shown on the basis of registered valuer's report dated 30.06.2001. He further found that the assessee had claimed and was allowed depreciation only on the super structure/ building and no depreciation had been allowed in respect of the land. The depreciation had been allowed on the building year after year from the assessment year 2002-03 till the assessment year 2005-06. The CIT (Appeals) agreed with the assessee that long term capital gains had to be computed on the sale



of the land since no depreciation had been claimed or allowed thereon. If no rate of depreciation is prescribed in respect of an asset, the said asset does not form part of the block of assets as provided in Section 32 of the Act. On this line of reasoning, the CIT (Appeals) directed the Assessing Officer to compute the long term capital gains on sale of land as it was held for more than 36 months and consequently directed the Assessing Officer to allow deduction under Section 54EC.

12. It is against the aforesaid decision of the Tribunal that the Revenue is in appeal before this Court. Section 50 of the Act makes “special provision for computation of capital gains in case of depreciable asset”. The provisions of this section apply notwithstanding anything contained in Section 2(42A) of the Act. In other words, even if a depreciable capital asset was held by the assessee for a period exceeding 36 months and would have normally been considered as a long term capital asset, it will not be so considered, but would be considered only as a short term capital asset. The section, however, is applicable only in respect of sale of a capital assets forming part of a block of asset in respect of which depreciation has been allowed. If these conditions are satisfied then any surplus arising on the sale of the depreciable asset would be treated only as short term capital gains. Sub-section (2) provides for



a situation where all the assets in the block of assets are transferred thus bringing about cessation of the block itself. In such case also the surplus arising on account of the transfer of the entire block of assets will be deemed to be capital gains arising from the transfer of short term capital assets, irrespective of the period of holding. The primary condition for the applicability of Section 50 of the Act is that the asset transferred should be a depreciable asset on which depreciation was actually allowed under the Act. It is necessary in this connection to also read Section 2(11) which defines a “block of assets” and Section 32 which provides for allowance of depreciation. A “block of assets” is defined under Section 2(11) as follows: -

“block of assets” means a group of assets falling within a class of assets comprising –

- (a) tangible assets, being buildings, machinery, plant or furniture;*
- (b) intangible assets, being know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature,*

in respect of which the same percentage of depreciation is prescribed;”



13. Section 32 provides for the allowance of depreciation in respect of certain assets. Sub-section (1), so far as it is relevant for our purpose, is re-produced below: -

- “32. (1) *In respect of depreciation of –*
- (i) *buildings, machinery, plant or furniture, being tangible assets;*
 - (ii) *know-how, patents, copyrights, trade marks, licences, franchises or any other business or commercial rights of similar nature, being intangible assets acquired on or after the 1st day of April, 1998,*

Owned, wholly or partly, by the assessee and used for the purposes of the business or profession, the following deductions shall be allowed –

- (i) *in the case of assets of an undertaking engaged in generation or generation and distribution of power, such percentage on the actual cost thereof to the assessee as may be prescribed;*
- (ii) *in the case of any block of assets, such percentage on the written down value thereof as may be prescribed;”*

14. A combined reading of Section 2(11), Section 32(1) and Section 50(2) of the Act shows that (i) a block of assets is one in respect of which the same percentage of depreciation is prescribed in



respect of the assets falling in the same class; (ii) no depreciation is allowable in respect of land as it is not specifically mentioned as an asset eligible for depreciation either in Section 2(11) or in Section 32(1) and (iii) the provisions of Section 50 are applicable only when the asset transferred forms part of a block of assets and in addition it was also allowed depreciation under the Act.

15. The Assessing Officer in our opinion was in error in invoking the provisions of Section 50(2) of the Act to the sale of the land and building comprised in S-7 & 8, Green Park, New Delhi on 29.08.2005. As the depreciation charts and the schedule of fixed assets forming part of the balance sheets show, the cost of the land has been taken at ₹ 1,48,00,000/- as on 31.03.2002 to 31.03.2005. No depreciation has been allowed on the land in any of the assessment years. In fact, as we have already found, no rate of depreciation has ever been prescribed for land. That land is not a depreciable asset is no longer *res integra* after the judgment of the Supreme Court in ***CIT, Punjab, Jammu & Kashmir and Himachal Pradesh v. Alps Theatre***, (1987) 65 ITR 377. If land is not a depreciable asset and cannot form part of the block of assets in the absence of a rate of depreciation having been prescribed therefor, we do not see how the provisions of Section 50 of the Act can be invoked to the present case. The Assessing Officer was clearly acted



contrary to law when he invoked Section 50(2) of the Act on the footing that the land formed part of the block of assets.

16. The assessee has sold the land and building. The land as an asset was held from April, 2001 to August, 2005 for a period of more than 36 months. The land, having been held for a period of more than 36 months, the surplus of the sale price over the indexed cost of acquisition was rightly shown as long term capital gains by the assessee. Since, the assessee has invested ₹ 2,90,00,000/- in REC Bonds the entire long term capital gains are exempt under Section 54EC of the Act.

17. We are fortified in our conclusion by the judgment of the Madras High Court in **CIT v. Dr. D. L. Ramachandra Rao**, (1999) 236 ITR 1 and that of the Bombay High Court in **CIT v. Citibank N.A.**, (2003) 261 ITR 570. We may also notice the judgment of the Privy Council in **Narayan Das Ketty v. Jatindra Nath Roy Chowdhry**, AIR 1927 PC 135 in which it has been held that having regard to the law in India it is possible to have separation of ownership of building from the ownership of the land. This view of the Privy Council was approved by the Supreme Court in **Bishan Das v. State of Punjab**, AIR 1961 SC 1570. We may also notice a very early judgment of the Full Bench of Madras High Court in **CIT**



v. *The Madras Cricket Club*, (1934) 2 ITR 209 wherein the difference between the legal position in this regard obtaining in England and in India was noticed and highlighted and it was observed by Owen Beasley, C.J. as under: -

“....The first contention put forward by the assesseees is that they are not the owners of the buildings which are now upon the land. The rule in India which is different from that in England, is that a person who builds a superstructure upon the land of another man remains the owner of the superstructure and can at the end of his term remove that superstructure from the land, whereas in England a person who erects a building on the land of another cannot do so as the building at the end of the lease becomes the property of the lessor.”

We felt the need to refer to the legal position because of the arguments addressed before us on behalf of the Revenue that the cost attributed to the building when it was purchased was only ₹ 68,00,000/- divided as ₹ 49,32,000/- for S-7, Green Park, New Delhi and ₹ 18,68,000/- for S-8, Green Park, New Delhi, whereas the assessee had incurred expenditure on additions to the building in the amount of ₹ 1,58,16,423/- up to 31.03.2003 and reckoned from this date, the assessee did not hold the property for more than 3 years and, therefore, the sale of land cannot be considered as a sale of a long term capital asset. From this it was sought to be argued, as was observed in para 3.3 of the assessment order, that the land is not a



long term capital asset because the assessee never really purchased the land but it actually purchased the ready built building. The Assessing Officer as well as the learned Sr. Standing Counsel perhaps intend to convey that what attracted the assessee to the property was the fact that there was a building on the land and not the land itself, since a substantial amount of ₹ 1,54,16,423/- was invested in putting up additions to the building to which the assessee had only ascribed a cost of ₹ 68,00,000/- when it purchased the property. Apart from the fact that this line of reasoning appears to us, with respect, to be somewhat convoluted, it also does not appear to take note of considerations that drive people to purchase landed property. What attracts them, as is common knowledge, is the land which appreciates phenomenally, depending upon the location and not the building which is on the land. The fact that the assessee incurred substantial expenditure on additions to the building could well have been because of the compulsions of its business and not because it considered the land to be of considerably low worth compared to the worth of the building. We are unable to appreciate or accept the line of argument adopted by the Assessing Officer as well as the learned Sr. Standing Counsel.

19. In view of the above discussion, we answer both the substantial questions of law in the affirmative and in favour of the assessee. The



appeal filed by the Revenue is accordingly dismissed with no order as to costs.

(R.V. EASWAR)
JUDGE

(SANJIV KHANNA)
JUDGE

MARCH 29, 2012
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