आयकर अपीलीय अधिकरण] पुणे न्यायपीठ "बी" पुणे में
IN THE INCOME TAX APPELLATE TRIBUNAL
PUNE BENCH "B", PUNE

BEFORE MS. SUSHMA CHOWLA, JM AND
SHRI ANIL CHATURVEDI, AM

आयकर अपील स / ITA No.2206/PUN/2016
निर्धारण वर्ष / Assessment Year : 2012-13

M/s. Kolte Patil Developers Limited,
2nd Floor, City Point, Dhole Patil Road,
Pune – 411 001.

..... अपीलार्थी / Appellant

PAN : AAACK7310G.

बनाम v/s

The Dy.Commissioner of Income-Tax,
Central Circle – 1(1), Pune.

..... प्रत्यर्थी / Respondent

Assessee by : Shri Nikhil Pathak.

Revenue by : Shri Sudhendu Das.

सुनवाई की तारीख / Date of Hearing : 04.02.2019		घोषणा की तारीख / Date of Pronouncement: 03.05.2019

आदेश / ORDER

PER ANIL CHATURVEDI, AM :

1. This appeal filed by the assessee is emanating out of the order of Commissioner of Income Tax (A) – Pune – 11 dated 29.07.2016 for the assessment year 2012-13.

2. The relevant facts as culled out from the material on record are as under :-

Assessee is a company stated to be engaged in the business of real estate development. Assessee electronically filed its return of income for A.Y. 2012-13 on 29.09.2012 declaring total income of Rs.32,74,69,918/-. The case was selected for scrutiny and thereafter

assessment was framed u/s 143(3) of the Act vide order dt.27.03.2015 and the total income was determined at Rs.37,66,84,050/-. Aggrieved by the order of AO, assessee carried the matter before Ld.CIT(A), who vide order dt.29.07.2016 (in appeal No.Pn/CIT(A)-11/DCIT, Cen. Cir.1(1), Pune/101/2015-16) granted partial relief to the assessee. Aggrieved by the order of Ld.CIT(A), assessee is now in appeal before us and has raised the following grounds :

"1. The learned CIT(A) erred in confirming the disallowance of Rs.1.40 Crs. on account of indirect expenditure u/s 14A r.w.r. 8D(2)(iii) as against Rs.5,00,000/- made by the appellant company.

2. The learned CIT(A) failed to appreciate that the disallowance made by the A.O. on account of indirect expenditure was not justified since the learned A.O. had not recorded any objective satisfaction to demonstrate that the disallowance made of Rs.5,00,000/- by the appellant company was not correct and accordingly, the disallowance confirmed by CIT(A) should be deleted.

3. The learned CIT(A) failed to appreciate that the assessee had not incurred any indirect expenditure of Rs.1.40 Crs. for earning exempt income and hence, the disallowance of Rs.5,00,000/- offered by the assessee was more than sufficient to cover the indirect expenditure incurred, if any, for earning exempt income and hence, the disallowance confirmed by the CIT(A) should be deleted.

4. Without prejudice to the above grounds, the learned CIT(A) erred in not appreciating that the investments made by the appellant company in partnership firms and group companies were out of commercial expediency and the same was not made with an intention to earn tax free income an hence, if at all, any disallowance u/s 14A r.w.r 8D is to be made, then the amount of investments made in group concerns should be excluded of computing the disallowance.

5. Without prejudice to the above grounds, the learned CIT(A) failed t appreciate that the investments on which no tax free income was earned b the assessee in this year should have been excluded while determining the disallowance u/s 14A r.w.r. 8D.

6. Without prejudice to the above grounds, the assessee submits that the investment made in partnership firms is not a tax free investment since the income earned by the firm is subjected to income tax and hence, the investment in partnership firm may be excluded from the amount of 'tax free investments' while computing the disallowance u/s 14A as per Rule 8D(ii).

7. Without prejudice to the above grounds, the assessee submits that the disallowance made u/s 14A is very high and may be reduced substantially.

8. The learned CIT(A) erred in confirming the addition of Rs.14,10,590/-- u/s 22 r.w.s. 23(4) on account of deemed rent in respect of unsold unit held as stock in trade by the appellant company in various projects.

9. The learned CIT(A) failed to appreciate that the appellant company had held these unsold unit as stock in trade and hence, as these units were occupied by the assessee for its business purpose, there was no reason to tax the annual value of such unsold units u/s 22 of the Act.

10. Without prejudice to the above grounds, the assessee submits that assuming without admitting that the income of such unsold units was taxable as income from house property u/s 22, it is submitted that the unsold units were vacant for the entire year and accordingly, the income thereon was to be considered at Rs. NIL in view of the provisions of Section 23(1) (c) and hence, the entire addition made by the learned CIT(A) may kindly be deleted.

11. Without prejudice to the above grounds, the assessee submits that the net annual retable value adopted by the A.O. is on an adhoc basis and the same should be substituted by the municipal retable value determined for the various units by the local authorities.

12. Without prejudice to the above grounds, assuming without admitting that the addition made towards income from house property is justified, the assessee submits that the deduction u/s 24 and municipal taxes may be allowed to the assessee while computing the annual value of the various units."

3. Before us, at the outset, Ld.A.R. submitted that ground Nos.1 to 7 are inter-connected and are with respect to disallowance u/s 14A of the Act and ground Nos.8 to 12 are inter-connected and are with respect to addition made on account of deemed rent in respect of unsold units. Ground No.13 is general in nature and requires no adjudication. In view of the aforesaid submission of Ld.A.R. we first proceed to decide the issue with respect to disallowance u/s 14A of the Act.

4. During the course of assessment proceedings, on perusing the computation of income, AO noticed that assessee had earned exempt income in the form of dividend and share of profits to the extent of 13.20 crores (rounded off). It was the claim of the assessee that no

expenditure was incurred for earning exempt income but however Rs.5 lakhs was suo moto disallowed u/s 14A of the Act by the assessee on adhoc basis. Assessee was asked to explain as to why disallowance u/s 14A of the Act not be made u/s 14A r.w.r. 8D of Income Tax Rules, to which assessee inter-alia stated that it has not incurred any expenditure for earning exempt income, the investments are out of own funds and no borrowed funds have been used for making the investments. The submissions of the assessee were not found acceptable to the AO. AO thereafter concluded that the provisions of Sec.14A of the Act are applicable to assessee. He thereafter, on the basis of method prescribed under Rule 8D of I.T. Rules, worked out the disallowance at Rs.4,82,14,704/- and after giving credit of Rs.5,00,000/- being the suo moto disallowance made by the assessee, disallowed the balance amount of Rs.4,77,14,704/-. Aggrieved by the order of AO, assessee carried the matter before Ld.CIT(A), who after relying on the decision of Tribunal in assessee's own case in A.Ys. 2008-09 & 2009-10 held that in view of the assessee's own funds being more than the tax free investments, no disallowance of interest under Rule 8D(2)(ii) of I.T. Rules is called for. However, with respect to the disallowance of indirect expenses under Rule 8D(2)(iii), he granted partial relief to the assessee :

> *4.15 Coming to the disallowance of the indirect expenditure under Rule 8D, the honorable Tribunal in the above mentioned decision held as under:*
>
> > *"So far as the disallowance of indirect expenditure for earning tax free dividend income is concerned we find there is no objective satisfaction recorded by the AO which is one of the mandates of section 14A(2) of the I.T. Act. Neither there is any discussion by the AO nor any specific query raised by the AO to the assessee on this issue. At the same time, there is no suo moto disallowance made by the assessee on account of the expenditure attributable*

to earning of the exempt income other than the expenditure on account of IPO. Although the assessee has neither disallowed any expenditure on this account in the computation statement presumably on the ground that no expenditure has been incurred and although the AO has also not specifically discussed this issue in the body of the assessment order, however, it cannot be said that no expenditure has been incurred by the assessee for earning the tax free income. Considering the totality of the facts of the case, we are of the considered opinion that disallowance of Rs.10 lakhs on adhoc basis on account of expenditure attributes for earning tax free income will meet the ends of justice. We hold and direct accordingly."

4.16 Thus the honourable Tribunal in principle upheld the disallowance of the indirect expenditure thought on an ad hoc basis, notwithstanding the fact that the AO had not recorded his satisfaction in this regard.

4.17. In the present case, the AO has recorded his satisfaction at para 3.3 of the asst order, Further I find that as per the appellant total investment in tax free equities were Rs.281.07 cr. excluding the investment in debentures of the group companies, which the AO appear to have included, The appellant claims that as per the ITAT decision only those investments should be considered from which the appellant had actually received income/dividend. However I find that the honourable ITAT had confirmed the disallowance of Rs.10 lakh on an ad hoc basic. Further, the CBDT circular no 5/2014 was not brought to the notice of the honourable ITAT. The circular makes it very clear that even if no income is actually earned during the year, disallowance u/s 14A should be considered.

4.18 I cannot indulge in disallowance on an ad-hoc basis. Therefore I hold that it will be proper to apply Rule 8D (2)(iii) to work out the disallowance out of the indirect expenditure, The working is as under:

281.17 cr X .5% = 1.40 Cr.

Accordingly disallowance of Rs.1.40 Cr. is confirmed as against the disallowance of Rs.4.82 cr made by the AO u/s 14A."

Aggrieved by the order of Ld.CIT(A), assessee is now in appeal before us.

5. Before us, Ld.A.R. reiterated the submissions made before AO and Ld.CIT(A) and further submitted that in the present case, assessee had suo moto disallowed the expenses under Sec.14A of the Act at Rs.5 lakhs. He submitted that AO has not recorded necessary satisfaction as to how the working of the disallowance made by the

assessee is incorrect. He submitted that once the assessee made suo moto disallowance of the expenses incurred to earn exempt income then it was incumbent upon the AO to examine such claim and to record his dis-satisfaction with the claim made before proceeding to disallow the expenses under Rule 8D of I.T. Rules and in support of his contention he relied on the decision of Hon'ble Apex Court in the case of Godrej & Boyce Manufacturing Co. Ltd., Vs. DCIT reported in (2017) 394 ITR 449 (SC). In the present case, he submitted that satisfaction with respect to suo moto disallowance of expenditure was not recorded by the AO and therefore the application of Rule 8D of I.T. Rules was not appropriate. He therefore submitted that the disallowance made by AO be deleted. Ld.D.R. on the other hand submitted that AO has clearly recorded his non-satisfaction and therefore AO was fully justified in invoking the provisions of Sec.14A r.w.r 8D. He thus supported the order of AO and Ld.CIT(A).

6. We have heard the rival submissions and perused the material on record. The issue in the present ground is with respect to the disallowance of expenses made u/s 14A r.w.r 8D of the Income Tax Rules. It is an undisputed fact that assessee has earned exempt income during the year and had suo moto disallowed Rs.5,00,000/- u/s 14A of the Act. It is also an undisputed fact that AO rejected the suo moto disallowance made by assessee on the ground that the disallowance was not worked out as per mandate of Rule 8D of IT Rules. He thereafter computed the disallowance under Sec.14A r.w.r 8D. On the issue of necessity of recording the satisfaction before proceeding to work out disallowance under Rule 8D of IT Rules, we find

that Hon'ble Bombay High Court in the case of CIT Vs. Asian Paints Limited (ITA No.1564 of 2016 order dated 06.02.2019) and after considering the decision of Hon'ble Apex Court in the case of Godrej and Boyce Manufacturing Co., Ltd., Vs. DCIT reported in 394 ITR 449 (SC) has held that Rule 8D of the rules cannot be invoked where suo moto disallowance made by the assessee is not found to be satisfactory by the AO having regard to the account of the assessee. It has further held that in the absence of recording of non-satisfaction in terms of Sec.14A(2) of the Act, invocation of Rule 8D is not permissible. The relevant question before the Hon'ble High Court and its observation are as under :

> *"2. The Revenue urges the following questions of law for our consideration :-*
>
> *(a).....*
>
> *(b).....*
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> *(c) Whether on the facts and in the circumstances of the case and in law, the Tribunal was right in deleting addition of Rs.1,10,72,191/- being disallowance made u/s 14A r/w Rule 8D, without giving the AO opportunity to remove any defect, if at all caused by non-mention of the satisfaction. Any such requirement was wrongly read by the Tribunal ?*
>
> 3....
>
> *4. Regarding question no.(c):-*
>
> *(a) In its return of income, the respondent made a suo-moto disallowance of Rs.15.21 lakhs being the expenditure incurred to earn exempt income under Section 14A of the Act. The Assessing Officer disregarded the same and proceeded to disallow an amount of Rs.1.10 crores under Section 14A of the Act read with Rule 8D of the Rules as expenditure incurred to earn exempt income. Thus, adding Rs.1.10 crores to the income of the respondent.*
>
> *(b) Being aggrieved, the respondent filed an appeal to the CIT(A) but without success.*
>
> *(c) On further appeal, the impugned order of the Tribunal while allowing the appeal held that before invoking the provisions of Rule 8D of the*

Income Tax Rules, the Assessing Officer has to record his non-satisfaction with the suo moto disallowance of expenditure made towards earning exempt income by the respondent. This exercise not having been carried out by the Assessing Officer before applying Rule 8D of the Income Tax Rules, the disallowance of expenditure to earn exempt income cannot be sustained.

(d) This issue is no longer res integra as the Apex Court in Godrej & Boyce Mfg. Co. Ltd. Vs. Dy. CIT, 394 ITR 449 decided the issue in favour of the respondent. In the above case, the Supreme Court has while considering the issue of disallowing of expenditure incurred to earn exempt income observed as under :-

> *"Whether such determination is to be made on application of the formula prescribed under rule 8D or in the best judgment of the Assessing Officer, what the law postulates is the requirement of a satisfaction in the Assessing Officer that having regard to the accounts of the assessee, as placed before him, it is not possible to generate the requisite satisfaction with regard to the correctness of the claim of the assessee. It is only thereafter that the provisions of section 14A (2) and (3) read with rule 8D of the Rules or a best judgment determination, as earlier prevailing, would become applicable."*

Thus, Rule 8D of the Rules cannot be invoked where the suo moto disallowance made by the respondent assessee is not found to be satisfactory by the Assessing Officer having regard to the accounts of the assessee. In the absence of recording the aforesaid fact of non-satisfaction in terms of Section 14A(2) of the Act, invocation of Rule 8D is not permissible.

(e) Therefore, in view of the above decision of the Apex Court, this question also does not give rise to any substantial question of law. Thus, not entertained.

7. In view of the aforesaid facts and relying on the decision of Hon'ble Bombay High Court cited supra and in view of the absence of recording of necessary satisfaction in terms of Sec.14A(2) of the Act, we are of the view that in the present case, no disallowance of expenses under Sec.14A r.w.r 8D is called for. We therefore direct the deletion of addition made by AO and upheld by Ld.CIT(A). **Thus, the ground of the assessee is allowed.**

8. Now, we take other issue of deemed rent in respect of unsold units.

8.1. During the course of assessment proceedings, AO noticed that assessee was holding closing stock of 32 unsold flats/shops. AO was of the view that since assessee was owner of two or more house properties, provision of Sec.23(4) of the Act would be attracted and as per which assessee should have offered deemed rental income from the aforesaid properties. The assessee was therefore asked as to why the deemed rent in respect of closing stock not be brought to tax. The submission of the assessee made before AO was not found acceptable to AO. AO thereafter relying on the decision of Hon'ble High Court in the case of CIT Vs. Ansal Housing and Construction reported in [2013] 29 taxmann.com 303 was of the view that deemed rent as per the provisions of Sec.23(4) of the Act is chargeable. AO thereafter on the basis of Annual Letting Value (ALV) as per PMC worked out the aggregate value for 32 unsold flats/shops at Rs.14,10,590/- and made its addition. Aggrieved by the order of AO, assessee carried the matter before Ld.CIT(A), who upheld the order of AO. Aggrieved by the order of Ld.CIT(A), assessee is now in appeal before us.

9. Before us, Ld.A.R. reiterated the submissions made before AO and Ld.CIT(A) and further submitted that the issue of deemed rent is covered in assessee's favour by various decisions of Pune Tribunal and more specifically, the decision in the case of M/s. Cosmopolis Construction (in ITA Nos.230 and 231/PUN/2018 dt.12.09.2018). He also placed on record the copy of the aforesaid decision. He therefore submitted that the addition made by AO and confirmed by Ld.CIT(A) be

deleted. Ld.D.R. on the other hand, supported the order of lower authorities.

10. We have heard the rival submissions and perused the material on record. The issue in the present case is with respect to addition under the head 'income from house property' on the 32 unsold flats/shops by the assessee. It is an undisputed fact that assessee is in the business of Civil Engineers, Builders and Developers and had in the closing stock of 32 unsold flats. It is also an undisputed fact that these 32 flats were vacant and no rental income was derived by the assessee during the year under consideration. We find that Hon'ble Gujarat High Court in the case of CIT Vs. Neha Builders Pvt. Ltd., reported in [2007] 164 Taxmann 342 has held that when the business of the assessee is to construct the property and sell it or to construct or let out then that would be the "business" and the business stocks which may include movable and immovable properties would be taken to be "stock-in-trade" and any income derived from such stocks cannot be termed as "income from house property". We further find that the Co-ordinate Bench of the Mumbai Tribunal in the case of C.R. Developments Pvt. Ltd., Vs. CIT in ITA No.4277/2012 order dt.13.05.2015, after considering the decision of Hon'ble Apex Court in the case of Chennai Properties and Investment Vs. CIT (2015) 373 ITR 673 (SC) has held that on the flats which were unsold, which were neither given on rent nor the assessee had intention to let out the flats, no deemed rental income could be considered in assessee's hands. We further find that the Co-ordinate Bench of Pune Tribunal in the case of M/s. Cosmopolis Construction (in ITA Nos.230 and 231/PUN/2018 dt.12.09.2018) after

considering the decision of Hon'ble Gujarat High Court in the case of CIT Vs. Neha Builders (P) Ltd., (supra), the decision of Mumbai Tribunal in the case of C.R. Developments Pvt. Ltd., (supra) after also considering the decision in the case of CIT Vs. Ansal Housing and Construction reported in [2013] 29 taxmann.com 303 has held that no notional annual rental value on unsold flats held in stock-in-trade can be made in assessee's hands. The relevant findings of the Co-ordinate Bench of the Tribunal is as under :

> *7. The issue before us for adjudication is whether the notional annual rental value on unsold flats held as stock-in-trade by the assessee is to be assessed under the head „Business Income" or under the head „Income from House Property". The Hon"ble Gujarat High Court in the case of Commissioner of Income Tax Vs. Neha Builders (P.) Ltd. (supra) has held that where the property is held as stock-in-trade any income derived rom stock would be „income from business" and not „income from house property". The relevant extract of the findings of Hon"ble High Court are as under :*
>
> > *"7. From the order passed by the learned CIT(A), it would clearly appear that the case of the assessee was that the company was incorporated with the main object of purchase, take on lease, or acquire by sale, or let out the buildings constructed by the assessee. Development of land or property would also be one of the businesses for which the company was incorporated.*
> >
> > *8. True it is, that income derived from the property would always be termed as 'income' from the property, but if the property is used as 'stock-in-trade', then the said property would become or partake the character of the stock, and any income derived from the stock, would be 'income' from the business, and not income from the property. If the business of the assessee is to construct the property and sell it or to construct and let out the same, then that would be the 'business' and the business stocks, which may include movable and immovable, would be taken to be 'stock-in-trade', and any income derived from such stocks cannot be termed as 'income from property'. Even otherwise, it is to be seen that there was distinction between the 'income from business' and 'income from property' on one side, and 'any income from other sources'. The Tribunal, in our considered opinion, was absolutely unjustified in comparing the rental income with the dividend income on the shares or interest income on the deposits. Even otherwise, this question was not raised before the subordinate Tribunals and, all of sudden, the Tribunal started applying the analogy.*
> >
> > *9. From the statement of the assessee, it would clearly appear that it was treating the property as 'stock-in-trade'. Not only this, it*

will also be clear from the records that, except for the ground floor, which has been let out by the assessee, all other portions of the property constructed have been sold out. If that be so, the property, right from the beginning was a 'stock-intrade'."

8. In the case of Commissioner of Income Tax Vs. Ansal Housing Finance And Leasing Co. Ltd. (supra) the Hon''ble Delhi High Court taking a contrary view has held that annual rental value on unsold flats built by assessee engaged in construction business is assessable as income from house property. It is a well settled law that when two divergent views of non-jurisdictional High Courts are available and there is no decision on the issue from the Jurisdictional High Court, the view in favour of the assessee has to be adopted [Commissioner of Income Tax Vs. Vegetable Products Ltd.(supra)].

9. In so far as the decision of Hon''ble Bombay High Court in the case of Commissioner of Income Tax Vs. Sane & Doshi Enterprises (supra) is concerned we find that the facts in the said case are at variance. In the said case the assessee was engaged in construction business. The assessee rented out unsold flats and suo-motu offered rental income from the flats under the head „Income from House Property''. On the contrary the Revenue wanted to tax rental income under the head „Business Income''. The matter travelled to the Tribunal. The Tribunal held that the income earned by the assessee from renting of flats is to be assessed under the head „Income from House Property''. The Department carried the matter in appeal before the Hon''ble High Court. The Hon''ble High Court confirmed the findings of Tribunal and held that rental income received from unsold portion of property constructed by the assessee, is assessable as income from house property. The core difference between the case of the assessee and in the case of Commissioner of Income Tax Vs. Sane & Doshi Enterprises (supra) is that in the case of assessee, it is notional annual rental income on flats held as stock which is sought to be taxed, whereas in the case of Commissioner of Income Tax Vs. Sane & Doshi Enterprises (supra) it was the case of actual rental income earned by the assessee from renting of flats constructed by it. Hence, the decision rendered in the case of Commissioner of Income Tax Vs. Sane & Doshi Enterprises (supra) would not apply in the facts of the present case.

10. We further find that Mumbai Bench of the Tribunal in M/s. C.R. Developments Pvt. Ltd. Vs. JCIT (supra), M/s. Runwal Constructions Vs. ACIT (supra) and Shri Girdharilal K. Lulla Vs. DCIT (supra) under similar set of facts have taken a consistent view in holding notional annual rental value on unsold flats held as stock-in-trade by the assessee engaged in construction and development activities as "Business Income''.

11. Before us, no distinguishing feature in the facts of the present case and the case decided by Pune ITAT noted herein above has been pointed out by Revenue. In view of the aforesaid facts, we following the decision of Co-ordinate Bench of the Pune Tribunal in the case of M/s. Cosmopolis Construction Vs. ITO (supra) hold that in the present case,

no addition on account of deemed rent of 32 unsold flats can be made in hands of the assessee. We therefore set aside the addition made by AO. **Thus, the ground of the assessee is allowed.**

12. **In the result, the appeal of the assessee is allowed.**

Order pronounced on the 3rd day of May, 2019.

Sd/-	**Sd/-**
(**SUSHMA CHOWLA**)	(**ANIL CHATURVEDI**)
न्यायिक सदस्य / JUDICIAL MEMBER	**लेखा सदस्य / ACCOUNTANT MEMBER**

पुणे Pune; दिनांक Dated : 3rd May, 2019.
Yamini

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent
3. CIT(A)-11, Pune.
4. Pr. CIT(Central), Pune.
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, "बी" / DR, ITAT, "बी" Pune;
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER

// True Copy //

वरिष्ठ निजी सचिव / Sr. Private Secretary
आयकर अपीलीय अधिकरण ,पुणे / ITAT, Pune.