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IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATE : 15.06.2015

CORAM

THE HONOURABLE MR. JUSTICE R.SUDHAKAR
AND
THE HONOURABLE MS. JUSTICE K.B.K.VASUKI

T.C.A. NO. 9 OF 2015

Sri Kanniah Photo Studio
No.18A, Nageswaran North Street
Kumbakonam.

.. Appellant

- Vs -

The Income Tax Officer Ward-I (1)
31, Krishnaswamy Road
Gandhi Nagar
Kumbakonam.

.. Respondent

Appeal filed against the order dated 16.4.2013 passed by the Income Tax Appellate Tribunal, Chennai 'A' Bench, made in ITA No.28/Mds/2011 against the order of the Commissioner of Income Tax (Appeals) in ITA.No.213/07-08 dated 19.10.2010.

against the order of the Deputy Commissioner of Income Tax Circle 1, Kumbakonam dated 31.12.2007 in GI.NO.8324K AA AFK7401E.

For Appellant : Mr.R.Sivaraman

For Respondents: Mr.J.Narayanasamy

JUDGMENT

(DELIVERED BY R.SUDHAKAR, J.)

Mr.Narayanasamy, learned standing counsel for the respondent is directed to take notice for the respondent/Department.

2. Aggrieved by the order of the Tribunal in allowing the appeal filed by the Revenue, the appellant/assessee is before this Court by filing the present appeal raising the following question of law :-

"Whether on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in holding that the amount of Rs.22,51,220/= paid by the appellant to the Bank for discharge of the mortgage has to be taken as expenses relating to transfer and it is wholly and exclusively incurred



for the transfer u/s 50 of the Income Tax Act, 1961?"

3. The facts, in a nutshell, are as hereunder :-

For the assessment year 2005-2006, the appellant/assessee filed return of income on 1.2.06 admitting loss of Rs.7,42,240/=. During the assessment year in question, the appellant sold land along with building at Nageswaran Koil Street, Kumbakonam for Rs.75 Lakhs. The appellant had taken mortgage loan on the said property with City Union Bank. For clearing the mortgage, the appellant made a one-time settlement with the bank in respect of the aforesaid loan and paid a sum of Rs.22,51,220/= to the bank. While computing the capital gain, this amount of Rs.22,51,220/= was claimed as expenses by the appellant under Section 48 (1) (i) of the Act. The Assessing Officer, in the course of assessment, however, held that the loan in question had been obtained by mortgaging the property long time after acquiring the same and, therefore, the same is not covered under Section 48 (1) (i) of the Act and, therefore, disallowed the assessee's claim for the purpose of computing the capital gains.

4. Aggrieved by the said disallowance, the assessee preferred appeal before the CIT (Appeals), who, relying upon the judgment of the Calcutta High Court in the case of Gopee Nath Paul & Sons - Vs - Dy. Commissioner of Income Tax (2005 (278) ITR 240) allowed the appeal and directed the assessing officer to add the capital gains in accordance with Section 50 and deleted the amount paid by the appellant to the Bank for removal of the encumbrances.

5. Aggrieved by the abovesaid order, the Department pursued appeal before the Tribunal and the Tribunal, relying on the decision of the jurisdictional High Court in the case of CIT - Vs - Vajrapani Naidu (2000 (241) ITR 560), came to hold that the decision of the jurisdictional court insofar as the plea under Section 48 (1)(i) would directly cover the issue and allowed the appeal against which the assessee is before this Court by filing the present appeal.

6. Mr.Sivaraman, learned counsel appearing for the appellant/assessee heavily relied on the judgment of the Calcutta High Court in Gopee Nath Paul's case (supra) to drive home the point that the Tribunal erred in disallowing the claim in computing capital gains with regard to the sum paid by the appellant to the Bank for discharging the mortgage under Section 48 (1) (i) r/w Section 50 of the Income Tax Act. The fact that the appellant firm constructed superstructure with the help of bank loan and due to its inability to repay the loan, on the basis of the one time settlement arrived at with the bank, the sale of the property had taken place and, therefore, the entire amount paid towards the discharge of the loan should be construed as expenditure incurred wholly and exclusively in connection with the said transfer, which fact has not been appreciated by the Tribunal in proper perspective. It is further submitted that the Tribunal erred in not appreciating the fact that the entire amount in question was used for the purpose of removing the encumbrances of mortgage and, therefore, the said



amount has to be deducted while computing capital gains. It is further submitted by the learned counsel for the appellant/assessee that in case of divergent views by two different High Courts on a similar issue, as in this case, the Tribunal should have taken the view that is more favourable to the assessee, which has not been done in this case. For the reasons aforesaid, learned counsel for the assessee/appellant sought for setting aside the order passed by the Tribunal.

7. Per contra, Mr. Narayanasamy, learned standing counsel appearing for the respondent/Department vehemently contended that in spite of divergent views of two different High Courts, the Tribunal having considered the facts of the case in depth, by normal rule of precedence, followed the decision of the jurisdictional High Court in Vajrapani Naidu's case (supra), and allowed the appeal and, therefore, no interference is warranted with the well considered findings recorded by the Tribunal.

8. Heard the learned counsel for the appellant/assessee and the learned standing counsel appearing for the respondent/Department and perused the materials available on record as also the judgments relied on by the different authorities to arrive at their respective conclusions.

9. This Court has carefully considered the facts in the present case as also the judgment of this Court as well as the Calcutta High Court. We find, on facts, there is a sale by the present appellant/assessee of land and building for Rs.75 Lakhs, which is not in dispute. Insofar as the one time settlement of Rs.22,51,220/= paid to City Union Bank to satisfy the mortgage over the property, the assessee claimed the same as expenses incurred in connection with the transfer for the purpose of computing capital gains under Section 48 (1) (i) of the Act, which was rejected by the Department and upheld by the Tribunal. In the above backdrop, the core issue before this Court is "whether such a discharge of claim to the bank could be considered as expenses in terms of Section 48 (1) (i) of the Act?"

10. For better clarity, Rule 48 (1) (i) of the Act, on which reliance is placed for claiming the disallowance, is quoted hereinbelow :-

"Mode of computation.

48. The income chargeable under the head "Capital gains" shall be computed, by deducting from the full value of the consideration received or accruing as a result of the transfer of the capital asset the following amounts, namely :-

(i) expenditure incurred wholly and exclusively in connection with such transfer;

(ii) the cost of acquisition of the asset and the cost of any improvement thereto.

* * * * *



11. On a careful reading of the above provision, it is evident that Section 48 provides that income chargeable under capital gains shall be computed by deducting from the full value of the consideration received or accruing as a result of the transfer of the capital asset such amounts, viz., expenses, incurred wholly and exclusively in connection with such transfer. The object behind such a provision is mainly for excluding those expenses incurred wholly or exclusively in connection with the transfer of the property.

The facts in the present case reveal that for further development of the property, loan had been obtained by the appellant/assessee from City Union Bank and for the purpose of clearing the mortgage loan, the appellant/assessee had sold the property and effect the one-time settlement with the bank. The Assessing Officer had held that since the mortgage loan had been long time after the acquisition of the property, the same would not stand covered under Section 48 (1) of the Act. That being the case, it does not appeal to us that the explanation relating to discharge of the mortgage to the bank, as submitted by the assessee, can be termed as expenditure, as the property had been acquired long time before taking the mortgage loan from the bank.

12. The Tribunal, to come to the finding that the said discharge of mortgage to the bank cannot be termed as expenditure, has placed reliance on the jurisdictional Court's decision in Vajrapani Naidu's case (supra). In that case, the assessee sold immovable property under 13 sale deeds and bona fide paid certain amounts to the creditors of the vendor assessee, including mortgages on the property, which was the subject matter of sale. The Income Tax Officer and the Commissioner rejected the claim for deduction in terms of Section 48 (1). While the Tribunal reversed the view, this Court rejected the view of the Tribunal, in the following manner :-

"That view of the Tribunal is wholly unsustainable. The burden had been created by the vendor on the property sold by him. As the burden had been created for his own benefit by offering the property as security to his lenders, the amounts spent for discharging that burden of the vendor whether prior to sale, or at the time of sale, by payment to such creditors including the mortgagees, directly by the vendee cannot be regarded as expenditure wholly and exclusively in connection with the transfer.

When the mortgaged property is sold, if the consideration for the sale comprises the consideration for the sale of equity of redemption, and the amount required for the discharge of mortgage, it is the aggregate of both these sums that constitutes the consideration for the sale. The fact that the vendee makes the payment directly to the mortgagee, instead of the vendor doing so, after receiving the money from the vendee, does not make any difference for the purpose of determining



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consideration for the sale and the extent of capital gain.

The Supreme Court in the case of RM. Arunachalam v. CIT [1997] 227 ITR 222, had an occasion to consider the question as to whether the sum paid by the assessee for discharging the mortgage by the assessee is a sum which would go to reduce the cost of acquisition. The court held that such payment would go to reduce the cost of acquisition only where the mortgage had not been created by the assessee, but was created by the person from whom the assessee had acquired the title and the mortgage was subsisting at the time title was acquired by the assessee. The court further observed in that case as under (page 239) :

"The position is, however, different where the mortgage is created by the owner after he has acquired the property, the clearing off of the mortgage debt by him prior to transfer of the property would not entitle him to claim deduction under section 48 of the Act because in such a case he did not acquire any interest in the property subsequent to his acquiring the same."

It is undisputed that in this case, a mortgage had been created by the vendor-assessee and the amounts paid to the other creditors by the vendee was for the discharge of the debts which had been incurred by the assessee. The amount was paid as part of the consideration to the sale. The distinction that was sought to be made by the Tribunal between the case where the mortgage is discharged by the vendor prior to the sale and the case where the discharge of the mortgage is effected at the time of the sale by payment of the outstanding amount to the mortgagee by the vendor and the sale free from encumbrances, is untenable. The only point of relevance is whether the mortgage was created by the vendor or whether it subsisted at the time of acquisition of title thereto by the vendor and was burdened with the same at the time of such acquisition of title."

13. We find no reason to depart from this finding of this Court in Vajrapani Naidu's case (supra). In the present case, mortgage has been created by the present appellant/assessee and consequent to the sale, the assessee has discharged the mortgage to City Union Bank. As the burden had been created for his own benefit by offering the property as security to City Union Bank, the amount spent for discharging that burden whether prior to sale, or at the time of sale, by way of one-time settlement to the Bank, cannot be regarded as expenditure wholly and exclusively in connection with the transfer. In the present case, the discharge was in the course of sale. We find that the payment of the outstanding amount in



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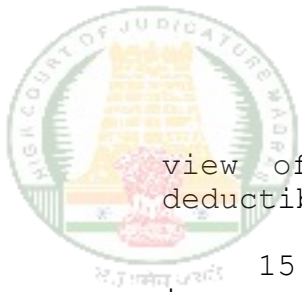
discharge of mortgage by the vendor, viz., appellant herein, cannot partake the character of an expenditure. It is not a case where the assessee had discharged the mortgage created at the time of acquisition of the property by the present appellant/assessee, to make a distinction otherwise.

14. The decision of the Calcutta High Court in Gopee Nath Paul's case (supra), on facts, is distinguishable and will not apply to the facts of the present case. In the said case, there were two firms and there were common partners. One of the firm was suffering a suit claim by Allahabad Bank. Simultaneously, another suit was filed between the partners of the two firms and based on arbitration agreement, the suit between the partners was concluded on the basis of compromise and the firms stood dissolved. A Receiver was appointed for the purpose of selling the two firms as a going concern. However, the same could not be sold as a going concern on account of liability of one of the firms to the bank and, thereafter, based on several orders of court, a deposit of Rs.25 Lakhs was made with the Court Registry as a Fixed Deposit with Allahabad Bank free from loan and attachment until further orders of court. This was done for the purpose of effecting the transfer of the assets of the two firms for securing the payment of the liabilities towards Allahabad Bank by one of the firms. The property was sold and amount was received and the capital gains was assessed in the hands of the other firm, which claimed the expenditure relatable to the sum paid to Allahabad Bank under Section 48 (1) and in such circumstances, the Calcutta High Court came to hold that based on court orders, sale of assets of the two firms having taken place and the liability of Allahabad Bank was settled consequent to that, therefore, the expenditure was incurred wholly and exclusively in connection with the transfer and in order to comply with the orders of the Court. For better clarity, the relevant portion of the decision is extracted hereunder :-

"13. We are supported in our above view by the decision in the case of CIT v. Shakuntala Kantilal [1991] 190 ITR 56 (Bom) and we are in agreement with the view taken in the said decision. Reference was also made to the case of CIT v. Abrar Alvi [2001] 247 ITR 312 (Bom), wherein, relying on Shakuntala Kantilal [1991] 190 ITR 56 (Bom), it was held that an expenditure in removing encumbrance would be deductible in the computation of capital gains. However, the discharge of mortgage created by the assessee after he acquired the property would not be deductible."

(Emphasis supplied)

The above observation squarely supports the view of this Court that where the discharge of mortgage created by the assessee after acquiring the property, the same would not be deductible. The abovesaid decision is clearly distinguishable on facts and the observation as quoted above in said decision further strengthens the



view of this Court in regard to the amounts which are to be deductible as expenditure.

15. In the light of the decisions as quoted above, this Court is persuaded to follow the reasoning of this Court in Vajrapani Naidu's case (supra), which is squarely applicable to the facts of the present case and, therefore, we have no hesitation to accept the view of this Court in the case of Vajrapani Naidu's case (supra). No question of law, much less substantial questions of law arise for consideration in this appeal.

16. Accordingly, for the reasons aforesaid, this appeal fails and the same is dismissed confirming the order passed by the Tribunal. However, in the circumstances of the case, there shall be no order as to costs.

Sd/-
Assistant Registrar(J)

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Sub Assistant Registrar

GLN

To

1. The Income Tax Officer Ward-I (1)
31, Krishnaswamy Road
Gandhi Nagar
Kumbakonam.
 2. The Income Tax Appellate Tribunal
Chennai 'A' Bench
Chennai.
 3. The Commissioner
Income Tax (Appeals)
No.44 Williams Road
Cantonment Tiruchirappalli 620 001
 4. The Deputy Commissioner of Income Tax
Circle I, Kumbakonam
- 1 cc to Mr.R. Sivaraman, Advocate, Sr. 29750

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