

THE HON'BLE SRI JUSTICE RAMESH RANGANATHAN

AND

THE HON'BLE SRI JUSTICE S.RAVI KUMAR

I.T.T.A.Nos.433, 448 & 466 of 2015

COMMON ORDER: (per Hon'ble Sri Justice Ramesh Ranganathan)

Heard Sri A.V.Krishna Kaundinya, learned Senior Counsel appearing on behalf of the appellants, and Sri B.Narasimha Sarma, learned Special Standing Counsel for the Income Tax Department and, after hearing both the learned counsel, these appeals are being disposed of at the stage of admission.

These three appeals are preferred by the assesses under Section 260-A of the Income Tax Act, 1961 (for short "the Act") against the order of the Income Tax Appellate Tribunal, Hyderabad in I.T.A.Nos.1386, 1387 and 1388 of 2014 dated 14.01.2015.

The assessees, in these three appeals, are two brothers and their mother. They were assessed as individuals deriving income from salary, share income from M/s.Hansa Overseas Enterprises (a partnership firm) and income from other sources. Returns of income were filed by the assessees declaring certain income. While the returns were initially processed under Section 143(1) of the Act, subsequently, on the basis of the information available on record and as the Assessing Officer had reason to believe that the assessees' income had escaped assessment, the assessment was reopened and notices under Section 148 of the Act were issued. During the re-assessment proceedings, the Assessing Officer noted that, in the relevant previous year, the assessees had sold a property situated at Road No.12, Banjara Hills, Hyderabad by way of registered sale deed No.2540/05 dated 23.06.2005 for a consideration of Rs.1,09,50,000/- each received by their two brothers, and Rs.1,20,48,000/-, received by their mother, totalling to Rs.3,39,48,000/-. The assessees, however, did not offer the said sale transaction to tax under the head "capital gains". The case of the assessees, before the Assessing Authority, was that the entire sale proceeds, received on the sale of the subject property, were paid to State Bank of India, and was appropriated towards the debt due to the Bank from M/s.Hoe Leather Garments Private Limited, in which both the brothers were Directors. Likewise in M/s. Hansa Overseas Enterprises (a partnership firm), wherein both the brothers were the partners.

On verifying the material on record, the Assessing Officer noticed that, though the assessees had claimed that the entire sale consideration was appropriated by the Bank towards the dues outstanding in the name of M/s.Hoe Leather Garments Private Limited, in which the assessees (brothers) were directors, a perusal of the bank account maintained by them, with the State Bank of

Hyderabad, showed that, after receipt of the sale consideration, the amount received was kept in short term Fixed Deposits, and the interest earned thereon was also offered as income in the assessment years under consideration.

In his order, the Assessing Authority held that the claim of the assesseees that they did not receive the sale consideration, and the Bank had appropriated the entire sale consideration against the dues of the company, was not tenable; on being confronted with these facts, the assesseees had stated that they had made short term deposits with the State Bank of Hyderabad from out of the sale proceeds, thereafter, they had made payment to the bank towards the dues of the company, and since the sale proceeds were utilised for clearing the debts of the company, no capital gains arose. The Assessing Officer subjected the transaction to tax as capital gains holding that, as per the statutory provisions, loan repayment is not one of the modes which would entitle the assesseees to claim deduction from chargeability to tax on capital gains.

In the appeals, filed before the Commissioner (Appeals), the assesseees contended that both M/s.Hansa Overseas Enterprises (a partnership firm) and M/s.Hoe Leather Garments Private Limited had availed loans from the State Bank of India as security for which, their residential house, held jointly in the names of the assesseees (both the brothers and their mother), were mortgaged; due to recession in the market from 2002 onwards, the loan had become a Non Performing Asset; proceedings for recovery were initiated both against the partnership firm and the company; subsequently the proposal, for a One Time Settlement (OTS), was accepted by the Bank settling the amount payable at Rs.3.5 crores i.e., Rs.2.85 crores for M/s.Hoe Leather Garments Private Limited, and Rs.75 lacs for M/s.Hansa Overseas Enterprises, which was also accepted by these concerns; in terms of the OTS, the assesseees made payment, through their individual accounts, which were reflected in the books of M/s. Hoe Leather Garments Limited and M/s. Hansa Overseas Enterprises; these two concerns had also offered the amount, waived by the Bank on the OTS, as income from other sources; in the case of M/s.Hoe Leather Garments Private Limited, Rs.2,85,00,000/- was added to the income of the company treating the amounts, introduced in the names of the two directors through journal entries, as unexplained cash credits; and when cheques were given by the assesseees from their individual accounts, to discharge the debts of the company and the partnership firm, and when the bank had also confirmed this in the course of investigation made by the Assessing Officer, they could not be subjected to tax under the head "capital gains". The assesseees also contended that the assessment made in the hands of the company, treating the amounts paid by the directors towards OTS as an unsecured loan and, at the same time, charging the sale consideration again in the hands of the assesseees as capital gains, would amount to assessing the same income twice over; the sale consideration had been utilised for the purpose of discharging the debts of the company, that too, on a property mortgaged to the bank; and the same is allowable under Section 48(1) of the Act.

In his order, the Commissioner of Income Tax (Appeals) observed that there was no connection between repayment of the loan, mortgage of the property, and the sale transaction relating to the property; the property was sold prior to the OTS; the entire sale consideration, received by the bank, was credited to assessees' bank accounts, and was being used for repayment of the loan as per the OTS, through the books of accounts of the company; the amount was invested in fixed deposits in the name of the assesseees, on which interest was also earned; there was no indication that the sale consideration was either paid to the bank directly, or appropriated by the bank directly, so as to make the sale consideration eligible for deduction under Section 48 of the Act; the sale consideration was not paid directly to the mortgagee bank; the property was directly sold by the assessee, regardless of the OTS and the mortgage in force; and, hence, the assesseees claim, that the sale consideration received by them should be allowed as deduction under Section 48(1) of the Act, could not be accepted.

The Commissioner further observed that the amount, claimed to have been repaid as a loan, was not the liability of the assesseees but the liability of the company and the firm in which two of them were directors/partners; the amount used for repayment of the loan was credited, in the books of accounts of the company, as a loan from the directors who were shown as creditors to the company; the amount paid to the bank, through the books of accounts of these concerns credited in the name of the directors, could not be treated as expenses incurred by the assesseees in connection with the transfer of property; the assesseees were independent entities different from the concerns which had availed the loans; the properties were also sold independently by their owners, irrespective of the fact that there was a mortgage or an OTS; as the sale consideration had no connection with repayment of the loan, the consideration received, from such transactions, were chargeable to tax as capital gains in the hands of the assesseees; and treating the unsecured loans, as unexplained cash credits in the hands of those two concerns, had absolutely no effect on the chargeability of capital gains in the hands of individuals.

In the order under appeal, the Tribunal held that, during the relevant previous year, the assesseees had sold a house property in Banjara Hills for a sale consideration of Rs.3,39,48,000/-; the property sold was a capital asset as defined under Section 2(14) of the Act; the gain derived from sale of such property would normally be assessable to tax under the head "capital gains"; the sale consideration, received by the assesseees, was deposited into their personal bank accounts, and was kept in the form of short term fixed deposits; the interest earned on these short term fixed deposits was also offered to tax in the returns of income filed by the assesseees; the property was sold much prior to the sanction of OTS by the bank, which advanced the loans to M/s.Hoe Leather Garments Private Limited and M/s. Hansa Overseas Enterprises, wherein the assesseees (the two brothers) were directors and partners; the sale consideration was not directly paid to the bank towards discharge of the debt as per the OTS claimed by the assesseees; the amount claimed to have been

paid, by the company and the firm towards OTS, originated from the unsecured loan claimed to have been availed through the personal accounts of the directors/partners; the contention of the assesseees, that the bank had appropriated the sale consideration towards discharge of the debt as per the OTS, was not acceptable; there was no direct nexus between the receipt of the sale consideration, and the payment made to the bank towards discharge of the debt; the unsecured loan, of the amount claimed to have been received from the directors, was disbelieved by the Department while completing assessment in the case of M/s. Hoe Leather Garments Private Limited, and additions were made under Section 68 of the Act which also stood confirmed; the claim of unsecured loans from the directors, of the amount utilised towards discharge of the debt, had also not been accepted; and, therefore, the assesseees claim that, since the sale consideration was utilised towards discharge of the debt, the same could not be chargeable to capital gains, could not be accepted.

The Tribunal further held that, even if the property was mortgaged as security towards the debt availed by the company/firm, the same could not be charged to capital gains; the Supreme Court, in ***R.M.Arunachalam vs. Commissioner of Income Tax*** and ***VSNR Jagdish Chandran vs. Commissioner of Income Tax***, had held that the amount paid, out of the sale proceeds, to clear the mortgage debt could not be treated as the cost of acquisition or the cost of improvement, so as to reduce the same from the sale consideration, while computing capital gains under Section 48 of the Act; and there was no infirmity in the order passed by the Commissioner of Income Tax (Appeals).

Before us, Sri A.V.Krishna Kaundinya, learned Senior Counsel appearing on behalf of the appellants, would contend that the sale transaction could not be subjected to tax twice; the amounts received as sale consideration, which was kept in the form of short term fixed deposits, were in turn advanced as unsecured loans to the company/firm; the unsecured loans, given by the assesseees, were used for repayment of the debt due to the bank under the OTS; the amounts lent by the assesseees, in the form of unsecured loans, were treated as unexplained cash credits in the books of accounts of the company/firm; and, as these transactions had already been subjected to tax in the hands of the company and the firm, the same could not be subjected to tax in the hands of the individual assesseees also. Learned counsel would further submit that the very fact that the Tribunal had subsequently waived the penalty, imposed by the Assessing Authority, itself proved that the Tribunal also believed that the same transactions had been subjected to tax twice.

As noted both by the Adjudicating Authority and the Appellate Authority, the subject property was sold even before the bank had offered OTS; the property was sold despite an existing mortgage in favour of the bank; the sale proceeds were not utilised directly for repayment of the loan, but were kept in the form of short term fixed deposits in the names of the assesseees; and the interest earned thereon was also declared as income by the individual assesseees.

As has been rightly observed by the Commissioner of Income Tax (Appeals), and the Tribunal, no deduction can be claimed under Section 48 of the Act, even if the said amount had been utilised for repayment of the loan extended by the bank to the company and the firm. The assessment orders passed in the case of the company and the firm, and certain transactions of the company and the firm being treated as unexplained cash credits, are not in issue in the present appeals. The circumstances under which additions were made to the income of the company and the firm, treating certain amounts received by them as unexplained cash credits, are also not known. The mere fact that the company and the firm were subjected to tax, on additions made for unexplained cash credits, would not absolve the appellants herein of their liability to pay tax on capital gains on the consideration received on the sale of the subject property. The fact that the Tribunal took a lenient view subsequently, by its order dated 09.10.2015, would not justify setting aside the earlier order of the Tribunal dated 14.01.2015 upholding the assessment order. Viewed from any angle, we see no error in the order of the Tribunal, much less a substantial question of law, necessitating interference in these appeals.

All the three appeals fail and are, accordingly, dismissed. The miscellaneous petitions pending, if any, shall also stand dismissed. There shall be no order as to costs.

RAMESH RANGANATHAN, J

S.RAVI KUMAR, J

Date: 07.12.2015

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THE HON’BLE SRI JUSTICE RAMESH RANGANATHAN

AND

THE HON’BLE SRI JUSTICE S.RAVI KUMAR

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Date: 07.12.2015

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