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IN THE HIGH COURT OF DELHI AT NEW DELHI

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ITA 602/2015

PARAS BUILDTECH INDIA PRIVATE LIMITED Appellant
Through Mr Salil Aggarwal and Mr Ravi Pratap
Mall, Advocates.

versus

COMMISSIONER OF INCOME TAX Respondent
Through Mr Rohit Madan, Advocate.

AND

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ITA 603/2015

PARAS BUILDTECH INDIA PRIVATE LIMITED Appellant
Through Mr Salil Aggarwal and Mr Ravi Pratap
Mall, Advocates.

versus

COMMISSIONER OF INCOME TAX , Respondent
Through Mr Rohit Madan, Advocate.

CORAM:
JUSTICE S. MURALIDHAR
JUSTICE VIBHU BAKHRU

ORDER

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18.11.2015

S. Muralidhar, J.:

1. These two appeals by the Assessee under Section 260A (1) of the Income Tax Act, 1961 ('the Act') are directed against the orders dated 17th February,

2015 of the Income Tax Appellate Tribunal ('ITAT') in ITA No. 4316/Del/2010 [for the Assessment Year ('AY') 2005-06] and ITA No. 235/Del/2010 [for AY 2006-07].

2. Admit.

3. The following questions of law are framed for consideration:

(a) For AY 2005-06, whether the ITAT was justified in setting aside the order of the CIT (A) and holding in the facts and circumstances of the case the advance amount received by the Assessee should be treated as income in its hands in the year in which the advance amounts were received and in applying AS-7 (revised) i.e. the percentage completion method to the Assessee?

(b) For AY 2006-07, whether the ITAT was justified in setting aside the order of the CIT (A) deleting the addition of the sum received by the Assessee on account of advance from bookings and restoring the case to the file of the AO for a fresh decision?

4. The background to the filing of the present appeals is that the Appellant Assessee is engaged in the business of real estate as a developer. The Assessee either purchases land in its own name or gets the power of attorney from the land owner in case the property is owned by another party so as to carry out activities of development on the land in terms of a collaboration agreement. The Assessee enters into agreements to develop and sell overall projects in terms of sharing with the owner. It enters into contracts with various buyers and receives sums by way advance for booking or reserving flats/shops/areas. On completion of the project, the Assessee hands over the possession of the flats booked to the respective customers/buyers along with the execution of the sale/conveyance deed.

5. It is stated that the Assessee regularly follows Accounting Standard (AS) 9 issued by the Institute of Chartered Accountants of India (ICAI). In this method, revenue is recognized as and when significant risk and reward of ownership/title is transferred. All sums received for the construction project till such time are treated as advances and shown as liability. All expenses incurred in the construction are accounted for in the stock in trade and/or block of buildings and are reflected as such in the balance sheet of the Assessee.

6. The Assessee started construction of a nine floor commercial complex, viz., 'Paras Down Town Centre' at Sector-53, Gurgaon in the financial year (FY) 2003-04. The said project was completed during FY 2004-05. As per the P & L Account and Balance Sheet, for financial year 2004-05, the Appellant had received Rs.15,39,84,824/- of which Rs.11,11,03,624/- was on account of advance bookings and Rs.4,28,81,200/- on account of actual sale. The Assessee incurred Rs.11,91,40,472 as total expenditure shown as total cost for construction of the commercial complex. However, the Assessee only showed the costs of Rs. 3.47 crores, corresponding to the recognised sales of Rs 4.28 crores, as costs in its balance sheet. The remaining receipts of Rs. 11.11 crore were shown as a current liability.

7. The Assessee filed a return of income along with an audited financial statement on 13th October 2005 for AY 2005-06 by declaring an income of Rs.57,75,159. A question arose during the assessment proceedings whether the percentage completion method (encapsulated in AS 7 issued by the

ICAI) should be applied to the Assessee? The Assessing Officer (AO) called upon the Assessee to submit whether the working of the profit was done as per the project completion method or the percentage completion method as provided in AS-7 issued by ICAI. In reply thereto, the Assessee took the categorical stand that AS-7 was not applicable since it was a developer and not a contractor. It further took the stand that it had booked sales on signing of title deeds in AYs 2005-06 and 2006-07.

8. The AO however rejected this contention and held that AS-7 is applicable to the Assessee. The AO held that the Assessee was acting as a contractor. It was held that significant risks and rewards of ownership had been transferred by the Assessee to buyers when the agreements to sell were entered into with them. The books of account of the Assessee were rejected under Section 145 of the Act and its profits were computed by applying the AS-7. The AO added a sum of Rs.1,56,88,100 to the Assessee's declared income by applying the percentage completion method. Apart from this the AO disallowed certain other sums including the sums on account of depreciation and under Section 14A of the Act. The income of the Assessee was determined at Rs.2,28,68,559/- as against the declared income of Rs.57,75,159/-.

9. Aggrieved by the order dated 28th December, 2007 passed by the AO, the Assessee file an Appeal before the Commissioner of Income Tax (Appeals) [CIT (A)]. By the order dated 2nd July, 2010 the CIT (A) held that the Assessee was only a developer and not a contractor and that AS-7 would not apply to it. It was held that the action of rejecting the books of account of the

Assessee under Section 145 of the Act could not be upheld. The AO was directed to compute the income of the Assessee in terms of the Revenue recognition method followed by the Assessee. The addition made by the AO in the sum of Rs. 5,23,00,137/- was directed to be deleted. Significantly, the CIT (A) also noted that the entire exercise was revenue neutral as the AO had only advanced the accrual of income from AY 2006-07 to AYs 2004-05 and 2005-06.

10. As far as AY 2006-07 is concerned, the AO by the assessment order dated 31st December, 2007 again applied the percentage completion method and made an addition of Rs.10,76,70,521 (constituting the advance booking amounts received) to the income of the Assessee. It was urged by the Assessee before the AO in respect of the aforementioned advance booking amount, that the civil work/construction activities had not even started and no amount could therefore be booked either under the project completion or the percentage completion methods. It was further pointed out that a sum of Rs.53.5 lakhs had been refunded in the immediate next year since the transaction could not materialise. The AO, however, negated the above pleas.

11. The appeal filed by the Assessee for AY 2006-07 was allowed by the CIT (A) by a separate order dated 12th November, 2009 accepting the plea of the Assessee that the advances received against two of the projects could not be treated as income since construction had not started. No expenses had been booked by the Assessee against the said advances. Therefore, even on the basis of AS -7 the said sum could not be assessed as income of the

Assessee.

12. Aggrieved by the above orders of the CIT (A) in relation to AYs 2005-06 and 2006-07, the Revenue filed appeals before the ITAT.

13. It may be mentioned that the ITAT passed two sets of orders. By one order dated 17th February, 2015 the ITAT disposed of the Revenue's appeals pertaining to AY 2004-05 (ITA Nos. 234/Del/2010) and AY 2005-06 (ITA No. 4316/Del/2016). As far as the appeal concerning AY 2004-05 is concerned, it was held by the ITAT that since the AO had bifurcated the income from the Paras Down Town Centre, Sector-53 into two years i.e., AY 2004-05 and 2005-06, the addition made by the AO for AY 2004-05 had to be deleted. To this extent, therefore, the Assessee is not aggrieved by the said order and has, therefore, not filed any appeal as far as AY 2004-05 is concerned.

14. As far as AY 2005-06 is concerned, the ITAT reversed the order dated 2nd July 2010 of the CIT (A) and accepted the plea of the Revenue that the percentage completion method would apply since the Assessee had transferred risks and rewards to the buyers even prior to commencement of construction activities. The further factor which weighed with the ITAT was that some of the buyers had transferred their rights in construction to third parties during the currency of the construction.

15. A separate order was passed by the ITAT in ITA No. 235/Del/2010 being the Revenue's Appeal for AY 2006-07. The ITAT recorded the

submission that the parties were agreement that there was not much discussion on the factual aspects either in the order of the AO or the order of the CIT (A). The ITAT proceeded to set aside the order of the CIT (A) and remand the matter to the AO for deciding it afresh in conformity with the ITAT's order for AYs 2004-05 and 2005-06.

16. At the outset, it is required to be noticed that the ITAT has in the impugned order dated 17th February, 2015 in ITA No. 4316/Del/2010 upheld the finding rendered by the CIT (A) that the Assessee was only a developer and not a contractor. This finding is significant because, as noticed hereinbefore, the agreements entered into by the Assessee are only on the basis that it is a developer. The Assessee has throughout been contending that it is not a contractor. This finding has been accepted by the Revenue inasmuch as it has not filed any appeal against the impugned order of the ITAT.

17. The other significant aspect is that the Assessee has been able to make good its plea regarding treatment of the sum received by it as advance in its books of accounts. The balance sheets filed by the Assessee, copies of which are enclosed with the memorandum of Appeal, do bear out the fact that the cost of construction is capitalized as regards the flats the construction of which is yet to be completed, and no conveyance deed has been executed or possession has not been handed over. The Assessee's balance sheet dated 31st March, 2005 discloses under the sub-head 'Inventory' under the head 'Current loans and advances' a sum of Rs.7,09,93,957. The explanatory Schedule 4 describes the said figure as 'Stock and inventory'. It is also

stated in Item No. 1 (b) of Schedule 19 in the Notes to the Accounts forming part of the final audit statement as under:

“b) Revenue Recognition

Sale of building:

- i) When building is ready to be delivered –
Sale is booked in the books of accounts on the date of possession agreed upon or on the date of sale if the sale deed is executed before the date of possession agreed.
- ii) When the building is not ready to be delivered-
Sale is booked on the date of the building transferred and possession handed over.

The income and expenditure are accounted for on accrual basis revenue of sale of offices/shops etc is recognized on signing of title deeds. All sums received till then for the construction project are treated as advances and shown as liability.”

18. Section 145 (1) of the Act states that the income chargeable under the heads ‘Profits and gains of business or profession’ shall be computed in accordance with either cash or mercantile system of accounting "regularly employed by the Assessee". It is only with effect from 1st April 2015 that a change has been brought about in Section 145 (2) which permits the central government to notify in the Official Gazette from time to time the income computation and disclosure standards to be followed by any class of Assesses or in respect of any class of income. That change is prospective and in any event does not apply to the case on hand.

19. The settled legal position as far as Section 145 of the Act is concerned is that it is not open to an AO to reject the accounts of an Assessee unless he

comes to a determination that notified accounting standards have not been regularly followed by the Assessee. As pointed out by the CIT (A) in the order dated 2nd July, 2010, the AS of the ICAI did not have any statutory recognition under the Act although it was binding under the Companies Act, 1956. The method of accounting followed by the Assessee in the present case i.e. project completion method was certainly one of the recognized methods and has been consistently followed by it.

20. In *Commissioner of Income Tax v. Bilahari Investment P Ltd. (2008) 299 ITR 1 (SC)* it was observed as under:

“Recognition/identification of income under the 1961 Act is attainable by several methods of accounting. It may be noted that the same result could be attained by any one of the accounting methods. The completed contract method is one such method. Similarly, the percentage of completion method is another such method.

Under the completed contract method, the revenue is not recognized until the contract is complete. Under the said method, costs are accumulated during the course of the contract. The profit and loss is established in the last accounting period and transferred to the profit and loss account. The said method determines results only when the contract is completed. This method leads to objective assessment of the results of the contract.

On the other hand, the percentage of completion method tries to attain periodic recognition of income in order to reflect current performance. The amount of revenue recognized under the method determined by reference to the stage of completion of the contract. The stage of completion can be looked at under this method by taking into consideration the proportion that costs incurred to date bears to the estimated total costs of contract.

The above indicates the difference between the completed contract method and the percentage of completion method.”

21. In the present case, there was therefore no good reason for the ITAT to have reversed the finding of the CIT (A). The only reason given in the impugned order of the ITAT is that ‘risks and rewards’ of ownership were transferred to the buyers who had paid the booking advance amounts and in some cases these rights were transferred to third parties. However, this does not in any manner affect the treatment of the said amounts in the books of the Assessee. As noted hereinbefore, the expenses of construction were not debited to the P & L account of the Assessee. It was shown as cost of construction or block of buildings. It is only as and when a conveyance deed was executed or possession delivered that the receipt was shown as income. The explanation added by way of Notes to the Accounts was not taken note of by the ITAT when it came to the conclusion that the percentage completion method should apply to the Assessee.

22. The other aspect that appears to have escaped the attention of the ITAT is that the Assessee offered to tax in the subsequent FY the amounts received and therefore there was no actual loss to the revenue. In similar circumstances, the Supreme Court in **CIT v. Excel Industries Limited 2013 ITR 295 (SC)** observed that the dispute if any raised at the instance of the Revenue would be at best academic. The stand of the Assessee in the present case also finds support in the decision of the Gujarat High Court in **CIT-IV v. Shivalik Buildwell (P) Ltd. (2013) 40 taxmann.com 219 (Gujarat)**. It was held that the Assessee in that case, who was a developer, was entitled to

book the amount received as booking advance as income on transfer of the property. Till then the advance booking amounts could not be treated as his trading receipt. The High Court recognized that the Assessee in that case was entitled to apply the project completion method in terms of the applicable AS.

23. This Court too has by order dated 7th January 2015 in ITA 111/2014 (*CIT v. SABH Infrastructure Ltd.*) held likewise, after noticing the decisions of the Supreme Court in *CIT v. Bilahari Investment P. Ltd.* (*supra*) and the order dated 15th November 2011 in ITA No. 928 of 2011 (*CIT v. Manish Buildwell Pvt. Ltd.*).

24. For the aforementioned reasons this Court answers question (a) as far as AY 2005-06 is concerned in the negative, i.e. favour of the Assessee and against the Revenue.

25. As far as AY 2006-07 is concerned, it is apparent that the ITAT in the impugned order lost sight of the fact that the advances received by the Assessee were in respect of a project that never took off. A part of the advance amount was returned in the following FY since the transaction itself fell through. In the circumstances the question of treating the amounts as income in the hands of the Assessee did not arise. No purpose was going to be served in remanding the matter to the AO for a fresh determination. Consequently, as far as AY 2006-07 is concerned, question (b) is answered in the negative i.e. in favour of the Assessee and against the Revenue.

26. The impugned orders dated 17th February 2015 of the ITAT to the above extent are hereby set aside.

27. The appeals are allowed in the above terms. No order as to costs.

S.MURALIDHAR, J

VIBHU BAKHRU, J

NOVEMBER 18, 2015

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