IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED : 17.03.2025

CORAM

THE HONOURABLE MR. JUSTICE S.S. SUNDAR

AND

THE HONOURABLE MR. JUSTICE C.SARAVANAN

TCA.No.528/2011

The Commissioner of Income Tax
Circle III, Chennai. ... Appellant

Vs.

Shri K.Kumaran ... Respondent

Prayer : Tax Case Appeal preferred under Section 260A of the Income Tax Act, 1961, against the order of Income Tax Appellate Tribunal, 'A' Bench, Chennai dated 01.06.2011, passed in ITA.No.1452/[Mds]/2009

For Appellant : Mr.S.Rajesh
Junior Standing counsel

For Respondent : Mr.G.J.Yaswanthram

JUDGMENT

[Delivered by S.S.SUNDAR, J.,]

(1)The above Tax Case Appeal is directed against the order dated 01.06.2011 passed by the Income Tax Appellate Tribunal, 'A' Bench, Chennai in ITA.No.1452/Mds/2009 in respect of the Assessment Year 2006-07.

(2)Brief facts that are necessary for the disposal of this appeal are as follows:-

(a) The respondent herein [hereinafter referred to as 'assessee'] is an individual and has been carrying on business in real estate. The assessee therefore, earns income from business, long and short term capital gains and from other sources. The assessee filed Return of Income for Rs.3,20,12,651/- for the AY 2006-07. The assessment was completed under Section 143[3] of the Income Tax Act, 1961, on a total income of Rs.4,25,24,315/-.

(b) It is admitted that the assessee had sold lands at Egathur and Navalur Villages for a sum of Rs.45,70,00,000/- on 10.10.2005 to a third party. Stating that the lands sold by the assessee were agricultural lands at the time of sale, the assessee claimed exemption for the entire consideration from the levy of tax. Similarly, the assessee has invested a sum of Rs.10 Crores in NABARAD Bonds to claim exemption under Section 54EC of the Act. The Assessing Officer accepted the case of the assessee that the lands sold by the assessee in Egathur and Navalur Villages are agricultural lands. Similarly, the assessee's investment in NABARD bonds was also reduced from total income in favour of the assessee. Challenging the order of the Assessing Officer, the Department preferred a revision before the Commissioner of Income Tax, Chennai-6. The Commissioner of Income Tax held that the land which is capable of being used as 'other purpose', need not be an agricultural property. Relying upon a Government Order issued in 2004, the Commissioner held that the land is urbanizable in the year under consideration. Stating that the land has been sold to construct a township, the Commissioner disallowed deduction by holding that the land cannot be treated as agricultural land.

(c) The Commissioner then considered the issue whether the claim of deduction under Section 54EC of the Act to the extent of Rs.10 Crores by making investment in NABARD Bonds is permissible. The assessee declared long term capital gains at Rs.12,12,08,410/- under the following heads:-

1. Long Term Capital Gains on the sale sale of shares	*=Rs.6,14,07,430/-*
2. Long Term Capital Gains on sale of property vide sale document No. 4141 dated 27.10.2005	*=Rs.1,46,35,073/-*
3. Long Term Capital Gains on sale of property vide sale document No. 448 dated 13.02.2008	*=Rs.4,51,65,906/-*
Total of Long Term Capital Gains	*=Rs.12,12,08,410/-*

(d) Since investment in NABARD bonds to the tune of Rs.10 Crores was made by the assessee on 26.11.2005, the Commissioner found that the second property which was sold by the assessee on 13.02.2006, cannot be considered for deduction by claiming exemption under Section 54EC of the Act. Therefore, the Commissioner held that the Assessing Officer has allowed excess deduction under Section 54EC of the Act to the assessee to the tune of Rs.1,44,45,833/-. Hence, the Commissioner set aside the order of the Assessing Officer by holding that the capital gain is attracted in respect of the whole consideration for the entire lands at Egathur and Navalur Villages to the tune of

Rs.45,70,00,000/- and the assessee is entitled to get deduction of a sum of Rs.8,55,54,168/- under Section 54EC of the Act. Aggrieved by the same, the assessee preferred an appeal before the Income Tax Appellate Tribunal [hereinafter referred to as 'Tribunal']. The Tribunal, by the order impugned in this Tax Case Appeal, allowed the appeal and set aside the order passed by the Commissioner of Income Tax in the revision under Section 263 of the Act.

(e) The Tribunal justified the findings of the Assessing Officer in its order, which according to the Tribunal, is based on supporting evidence produced by the assessee to establish the agricultural nature of the land in Egathur and Navalur Villages. Since the revisional authority has relied upon G.O.No.287 dated 08.07.2004 which only suggest the land as urbanizable, the Tribunal held that the Government Order would only mean that the land is urbanizable in future and future transformation of land into urban land, cannot be a ground to treat the land as a non-agricultural land. The Tribunal also observed that the State Government classifying any village as urbanizable is only in contemplation of developmental activities and scheme and that has nothing to do with the administration of Income Tax law.

(f) On the question of exemption under Section 54EC of the Act, the Tribunal found that the assessee was having sufficient funds in hands to subscribe to NABARD bonds even without sale of shares and that the day-to-day comparison of available funds on the basis of cash book to verify whether the investments was made on exactly out of sale proceeds of the land or not is an extreme view opposed to the spirit of law. The Tribunal was of the view that once the funds available from different sources are summarised in the hands of assessee, then it is not possible to identify the source of income. Therefore, on both counts, the appeal filed by the assessee before the Tribunal was allowed and order of the Commissioner was set aside. Aggrieved by the same, the Commissioner of Income Tax, has preferred the above Tax Case Appeal.

(3)This Court, while admitting the Tax Case Appeal, framed the following substantial questions of law:-

(a) Whether on the facts and circumstances of the case, the ITAT was correct in the facts and

circumstances of the case to set aside the revision order passed by the CIT holding that the order of the Assessing Authority is not erroneous and prejudicial to the interest of the revenue?

(b) Whether on the facts and circumstances of the case, the ITAT was correct in law to hold that the investment in NABARD bonds for claim of reduction u/s.54EC need not be wholly from the sale consideration of corresponding properties which are subject to long Term Capital Gains?

(c) Whether on the facts and circumstances of the case, Tribunal was right in law and on facts in set aside the order u/s.263 by a liberal interpretation of Section 54EC though there is no authority in its language?

(4)The questions of law are not properly framed. However, the learned Standing counsel appearing for the Department submitted that the findings of the Tribunal on the issue whether the lands at Egathur and Navalur Villages are agricultural lands, is perverse. G.O.No.287, dated 08.07.2004 does not refer to any change in character of land as per the revenue records. Under the Town and Country Planning Act, the Government is rqeuired to give consent for publication of any notice either for preparation of Master Plan or for modification of any Master Plan. This Notification is for the purpose of future development. As far as city of Chennai is concerned, the CMDA is the appropriate authority for preparation of a Master Plan. The Master Plan does not change the character of land, but categorise the lands as residential, mixed residential, commercial, industrial, agricultural etc. Urban development is limited in any area classified as agricultural zone. However, if a land is used as agricultural land or treated as agricultural land or a cultivable land, the character of land as per revenue record does not change merely because the land is brought under the agricultural zone for the purpose of development.

(5)For the question to be decided for the purpose of income tax, what is relevant is Section 2[14] and Section 10[37] of the Income Tax Act, 1961. Section 2[14] of the Act defines 'Capital Asset' in the following lines:-

> "**2[14]Capital Asset"** *means – (a)property of any kind held by an assessee, whether or not connected with his business or profession;*
>
> *(b)any securities held by a Foreign Institutional Investor which has invested in such securities in accordance with the regulations made under the*

Securities and Exchange Board of India Act, 1992 (15 of 1992);

[(c) any unit linked insurance policy to which exemption under clause (10D) of section 10 does not apply on account of the applicability of the fourth and fifth provisos thereof,]but does not include –

(i)any stock-in-trade [other than the securities referred to in sub-clause (b)], consumable stores or raw materials held for the purposes of his business or profession ;

(ii)personal effects, that is to say, movable property (including wearing apparel and furniture) held for personal use by the assessee or any member of his family dependent on him, but excludes – (a)jewellery;(b)archaeological collections;(c)drawings;(d)paintings;(e)sculptures; or(f)any work of art.

***Explanation 1**. – For the purposes of this sub-clause, "jewellery" includes – (a)ornaments made of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metals, whether or not containing any precious or semi-precious stone, and whether or not worked or sewn into* *any wearing apparel;(b)precious or semi-precious stones, whether or not set in any furniture, utensil or other article or worked or sewn into any wearing apparel.*

Explanation 2. *– For the purposes of this clause – (a)the expression "Foreign Institutional Investor" shall have the meaning assigned to it in clause (a) of the Explanation to section 115AD;(b)the expression "securities" shall have the meaning assigned to it in clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956);*

(iii)agricultural land in India, not being land situate –

(a)in any area which is comprised within the jurisdiction of a municipality (whether known as a municipality, municipal corporation, notified area committee, town area committee, town committee, or by any other name) or a cantonment board and which has a population of not less than ten thousand ; or

(b)in any area within the distance, measured aerially, –

(I)not being more than two kilometres, from the local limits of any municipality or cantonment board

referred to in item (a) and which has a population of more than ten thousand but not exceeding one lakh; or

(II)not being more than six kilometres, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than one lakh but not exceeding ten lakh; or

(III)not being more than eight kilometres, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than ten lakh.

Explanation. *– For the purposes of this sub-clause, "population" means the population according to the last preceding census of which the relevant figures have been published before the first day of the previous year;*

(iv)6½ per cent Gold Bonds, 1977, or 7 per cent Gold Bonds, 1980, or National Defence Gold Bonds, 1980, issued by the Central Government;

(v)Special Bearer Bonds, 1991, issued by the Central Government ;

(vi)Gold Deposit Bonds issued under the Gold Deposit Scheme, 1999 or deposit certificates issued under the Gold Monetisation Scheme, 2015 notified by

the Central Government.

Explanation. *– For the removal of doubts, it is hereby clarified that "property" includes and shall be deemed to have always included any rights in or in relation to an Indian company, including rights of management or control or any other rights whatsoever;''*

(6)Section 10 deals with incomes which shall not be included in total income. Section 10[37] of the Act reads as follows:-

''***10[37]:-*** *In the case of an assessee, being an individual or a Hindu undivided family, any income chargeable under the head "Capital gains" arising from the transfer of agricultural land, where –*

(i)such land is situate in any area referred to in item (a) or item (b) of sub-clause (iii) of clause (14) of section 2;

(ii)such land, during the period of two years immediately preceding the date of transfer, was being used for agricultural purposes by such Hindu undivided family or individual or a parent of his;

(iii)such transfer is by way of compulsory acquisition under any law, or a transfer the consideration for which is determined or approved by

the Central Government or the Reserve Bank of India;

(iv)such income has arisen from the compensation or consideration for such transfer received by such assessee on or after the 1st day of April, 2004.Explanation. – For the purposes of this clause, the expression "compensation or consideration" includes the compensation or consideration enhanced or further enhanced by any court, Tribunal or other authority.''

(7)Section 2[14] defines 'what is capital asset'. However, any agricultural land, which is not located with 8Km from the local limits of any Municipality or Cantonment Board is exempted from being considered as capital asset. From the reading of Section 2[14] of the Act, it is seen that the term "Municipality" should be understood in the context to mean a Local Body whether known as Municipality, Municipal Corporation, Notified Area Committee, Town Area Committee, Town Committee or by any other name. Therefore, the conclusion of the Commissioner of Income Tax is contrary to the plain language of Section 2[14] of the Act. In the present case, the fact that the land is situated beyond 8Kms from the Municipality is not in dispute. Therefore, the order of the Appellate Tribunal holding that the lands in Egathur and Navalur Villages are agricultural lands, cannot be faulted.

(8)The next question is whether the Tribunal is correct in holding that the investment in NABARD bonds to claim deduction under Section 54EC of the Act is appropriate.

(9)Section 54EC of the Act reads as follows:-

> ***"54EC.Capital gain not to be charged on investment in certain bonds.* [Inserted by Act 10 of 2000, Section 27 (w.e.f. 1.4.2001).]**
>
> *(1)Where the capital gain arises from the transfer of a long-term capital asset [being land or building or both,] (the capital asset so transferred being hereafter in this section referred to as the original asset) and the assessee has, at any time within a period of six months after the date of such transfer, invested the whole or any part of capital gains in the long-term specified asset, the capital gain shall be dealt with in accordance with the following provisions of this section, that is to say,-*
>
> *(a)if the cost of the long-term specified asset is not less than the capital gain arising from the transfer of the original asset, the whole of such capital gain shall not be charged under section 45;*
>
> *(b)if the cost of the long-term specified asset is less than the capital gain arising from the transfer of*

the original asset, so much of the capital gain as bears to the whole of the capital gain the same proportion as the cost of acquisition of the long-term specified asset bears to the whole of the capital gain, shall not be charged under section 45.

Provided *that the investment made on or after the 1st day of April, 2007 in the long-term specified asset by an assessee during any financial year does not exceed fifty lakh rupees.] [Inserted by Act 22 of 2007, Section 18 (w.e.f. 1.4.2007).]*

(2)Where the long-term specified asset is transferred or converted (otherwise than by transfer) into money at any time within a period of three years from the date of its acquisition, the amount of capital gains arising from the transfer of the original asset not charged under section 45 on the basis of the cost of such long-term specified asset as provided in clause (a) or, as the case may be, clause (b) of sub-section (1) shall be deemed to be the income chargeable under the head "Capital gains" relating to long-term capital asset of the previous year in which the long-term specified asset is transferred or converted (otherwise than by transfer) into money.

Provided *that in case of long-term specified asset referred to in sub-clause(ii) of clause (ba) of the*

Explanation occurring after sub-section (3), this sub-section shall have effect as if for the words "three years", the words "five years" had been substituted.] [Inserted by Act 10 of 2000, Section 27 (w.e.f. 1.4.2001).]

Explanation. - *In a case where the original asset is transferred and the assessee invests the whole or any part of the capital gain received or accrued as a result of transfer of the original asset in any long-term specified asset and such assessee takes any loan or advance on the security of such specified asset, he shall be deemed to have converted (otherwise than by transfer) such specified asset into money on the date on which such loan or advance is taken.]*

(3) Where the cost of the long-term specified asset has been taken into account for the purposes of clause (a) or clause (b) of sub-section (1)-

(a) a deduction from the amount of income-tax with reference to such cost shall not be allowed under section 88 for any assessment year ending before 1st day of April, 2006;

(b) a deduction from the income with reference to such cost shall not be allowed under section 80-C for any assessment year beginning on air after the 1st day

of April, 2006.]

Explanation. *- For the purposes of this section,-*

(a)"cost", in relation to any long-term specified asset, means the amount invested in such specified asset out of capital gains received or accruing as a result of the transfer of the original asset;

(b)"long-term specified asset" for making any investment under this section during the period commencing from the 1st day of April, 2006 and ending with the 31st day of March, 2007, means any bond, redeemable after three years and issued on or the 1st day of April, 2006, but on or before the 31st day of March, 2007,- [Substituted by Act 22 of 2007, Section 17, for Clause (b) (w.r.e.f. 1.4.2006).]

(i)by the National Highways Authority of India constituted under section 3 of the National Highways Authority of India Act, 1988 (68 of 1988); or

(ii)by the Rural Electrification Corporation Limited, a company formed and registered under the Companies Act, 1956 (1 of 1956),

and notified by the Central Government in the Official Gazette for the purposes of this section with such conditions (including the condition for providing a limit on the amount of investment by an assessee in such *bond) as it thinks fit:]*

***Provided** that where any bond has been notified before the 1st day of April, 2007, subject to the conditions specified in the notification, by the Central Government in the Official Gazette under the provisions of clause (b) as they stood immediately before their amendment by the Finance Act, 2007, such bond shall be deemed to be a bond notified under this clause;] [Inserted by Act 22 of 2007, Section 18 (w.r.e.f. 1.4.2006).]*

(ba)["long-term specified asset" for making any investment under this section, - [Substituted by Finance Act, 2018 (Act No. 13 of 2018), dated 29.3.2018.]

(i)on or after the 1st day of April, 2007 but before the 1st day of April, 2018, means any bond, redeemable after three years and issued on or after the 1st day of April, 2007 but before the 1st day of April, 2018;

(ii)on or after the 1st day of April, 2018, means any bond, redeemable after five years and issued on or after the 1st day of April, 2018,by the National Highways Authority of India constituted under section 3 of the National Highways Authority of India Act, 1988 or by the Rural Electrification Corporation Limited, a company formed and registered under the Companies

Act, 1956 or any other bond notified in the Official Gazette by the Central Government in this behalf.] [Inserted by Act 10 of 2000, Section 27 (w.e.f. 1.4.2001).]] [Substituted by Act 18 of 2005, Section 17, for sub-Section (3) (w.e.f. 1.4.2006).]

(10)From the plain reading of Section 54EC of the Act, it is seen that seeking investment of whole or any part of capital gain within a period of six months from the date of transfer is chargeable. In this case, deduction under Section 54EC of the Act is by showing the investment of Rs.10 Crores in NABARD bonds. The investment in NABARD bonds was made by the assessee on 26.11.2005. In this case, it is admitted that the assessee had a sum of Rs.6,14,07,430/- by sale of Long Term Capital Gain. Similarly, the assessee sold another immovable property in Mylapore on 27.10.2005 for a consideration of Rs.1,46,35,073/-. It is admitted that another property was sold only on 13.02.2006 for a consideration of Rs.4,51,65,906/-. Therefore, consideration received on 13.02.2006 was not available with the assessee to make the investment in NABARD bonds on 26.11.2005. Therefore, the order of Commissioner of Income Tax is perfectly valid. Hence, the assessee is entitled to claim deduction under Section 54EC only for a sum of Rs.6,14,07,430/- by way of long term capital gain of sale of shares and a further sum of Rs.1,46,35,073/- by way of sale of property. As rightly held by the Commissioner, out of a sum of Rs.10 Crores, the assessee can claim exemption or deduction under Section 54EC only to an extent of Rs.8,55,54,167/-. The claim for deduction under Section 54EC cannot be permitted to the extent of Rs.1,44,45,833/-.

(11)Therefore, the order of the Tribunal impugned in this appeal cannot be sustained as regards the exemption claimed by the assessee to the tune of Rs.10 Crores under Section 54EC of the Act.

(12)As a result, this Tax Case Appeal is **partly allowed.** While confirming the order of the Tribunal as regards the finding that the sale of land in Egathur and Navalur Villages are agricultural lands to permit deduction under Section 10[37] read with Section 2[14] of the Act, the order of Tribunal is modified by reversing the finding in relation to the deduction under Section 54EC of the Act. In other words, while permitting a deduction upto a sum of Rs.8,55,54,167/- for making investment in NABARD bonds, the claim for deduction to the tune of Rs.1,44,45,833/- is disallowed. The appeal is allowed to the extent indicated. No costs.

[S.S.S.R., J.] [C.S.N., J.]
17.03.2025

AP
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To

The Commissioner of Income Tax
Circle III, Chennai.

S.S. SUNDAR, J.,
and
C.SARAVANAN, J.,

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