

Payment made to partners for purchase of land above prevalent market rate would lead to Sec. 40A(2) disallowance

Summary – The Mumbai ITAT in a recent case of Kapil Ratan Associates., (the Assessee) held that w here assessee-firm having purchased land from its erstwhile partners, enhanced sale consideration five times subsequent to reconstitution of firm, Commissioner rightly passed revisional order had making disallowance u/s 40A(2)

Facts

- The assessee firm was constituted *vide* partnership deed dated 29-5-2006.
- Subsequently the assessee firm was reconstituted *vide* partnership deed dated 9-6-2008 in terms of which three partners were replaced.
- The assessee filed its return declaring loss. The assessment was completed under section 143(3) accepting loss declared in the return.
- The Commissioner noticed that prior to reconstitution of firm, assessee had purchased land from erstwhile partners of firm. He further found that after reconstitution of firm purchase consideration of land was substantially enhanced and as a result payments made to erstwhile partners were in excess of prevalent market rates which was liable to be disallowed under section 40A(2)(b).
- The Commissioner further noticed that the assessee had made payment through general entries to 'B' Ltd. which was hit by the provisions of section 40A(3) *i.e.* payment being made otherwise than by banking channel beyond the prescribed limit.
- The Commissioner thus passed a revisional order setting aside the assessment.
- On appeal:

Held

- In the instant case, the expenditure had been agreed to be incurred for the purchase of land by the assessee firm before the reconstitution of the firm. Even the cheques/banker cheques were drawn prior to the date of reconstitution of the firm. The sale consideration had been increased five times from that agreed at original agreement entered into prior to reconstitution of firm.
- All these facts are enough for forming an opinion by the Commissioner that certain expenditure has been made which is hit by the provisions of section 40A and hence, the opinion of the Commissioner cannot be said to be wrong to the effect that the assessment order was erroneous and prejudicial to the interest of the revenue since the Assessing Officer has not considered this aspect of the matter.
- So far the contention of the assessee that the Assessing Officer had applied his mind, it does not have force so far so the facts of the case in hand are concerned. A perusal of material on record reveals that the Assessing Officer had sought details of retiring partners along with return of

income, capital account and balance sheet of last three years. However, the said details had not been submitted by the assessee. Moreover, the issue relating to the applicability of section 40A has not been examined by the Assessing Officer. There was sufficient material available on the file which was enough for the Commissioner to form the opinion that the Assessing Officer had not applied his mind on this aspect of the matter. Hence, there is no infirmity in the order of the Commissioner while invoking provisions of section 263 on the issue of the application of provisions of section 40A(1) and (2).

- So far as the contention of the assessee regarding the application of provisions of section 40A(3) is concerned, the said issue has also not been examined by the Assessing Officer. The Commissioner has not made any addition but has only set aside the order of the Assessing Officer on the above said two issues for examination afresh after giving opportunity of hearing to the assessee. Hence, the assessee will be at liberty to present its case before the Assessing Officer.
- In view of above, there is no merit in the appeal of the assessee and the same is hereby dismissed.