

Date : 22-11-2018

From :

Silver oak Realty
5-4-187/3 & 4, 2nd floor,
Soham Mansion, M.G Road,
Secunderabad – 500003.

To :

Income tax Officer,
Ward 10(3)/Hyd
IT Towers, A.C Guards
Hyderabad.

Sir/Madam,

Sub : Income tax assessment proceedings-own case-Asst. year 2016-17 –PAN ACXFS3783R-
submission of information-reg

Ref : Your Notice u/s 142(1) dated 20-11-2018.

In connection with the income tax assessment proceedings, certain information requested for is submitted hereunder for your kind consideration.

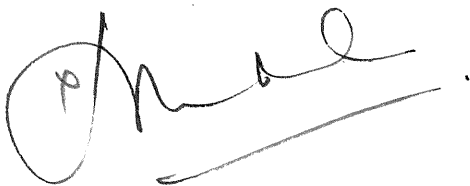
In the above referred Notice, you have requested information/explanation on the following 3(three) issues.

- i. To explain the discrepancy in the Gross Profit offered to tax and,
- ii. To bifurcate the Gross Profit offered on the sale of land and sale of houses and,
- iii. To clarify the method adopted in the computation of Gross Profit.

In reply, the following is submitted

1) In respect to the discrepancy in the Gross Profit offered to tax:

- a) In the Annexure to Notice u/s 142(1), the total Gross Profit of the firm has been worked to Rs.2,20,40,150/-
- b) The above Gross Profit of Rs.2,20,40,150/- is worked out by estimating profit of Rs.1,08,56,250/- @ 15.65% on the turnover/sale of constructed building of Rs.7,23,75,000/-. To this arrived Gross Profit of Rs.1,08,56,250/-, the Gross Profit of Rs.1,11,83,900/- on sale of land is added so as to arrive at the total Gross Profit of Rs.2,20,40,150/-



- c) For the workings of the above Gross Profit, the Gross Profit rate of Rs.15.65% is adopted stating the following in Para of the Annexure-

‘ The assessee firm recognizes its revenue on an estimate basis periodically and as per **column 40 of audit report it was certified that the Gross Profit was estimated at 15.65% for the FY 2015-16** ’ [Text in Bold is emphasized by us]

- d) At the outset, it is submitted that in column 40 of audit report, ‘**the auditors have not certified that the Gross Profit was estimated at 15.65% for the FY 2015-16**’ as stated in the Annexure to Notice. The GP of 15.65% is reported in the audit report based on the GP amount of Rs.1,32,04,690 and total turnover of Rs.8,43,87,210/- as per the Construction Account. Your understanding that the **auditors have certified that the Gross Profit was estimated at 15.65% is factually incorrect**. The GP of 15.65% reported in column 40 of the **audit report thus cannot be interpreted as ‘estimated Gross Profit certified by the auditor’**.
- e) The Gross Profit workings of Rs.1,08,56,250/- in the Annexure Notice u/s 142(1) is based on adopting GP of 15.65% as ‘**estimated Gross Profit certified by the auditor**’ on the sales turnover of Rs.7,23,75,000/- is therefore not correct. It is therefore submitted that there is no discrepancy in the Gross Profit offered to tax.
- f) Further, the firm over past many years has been following the policy for revenue recognition as is given in Schedule ‘O’ Notes to Accounts-

‘Revenue from Housing Project is recognized on an estimate basis till the Bungalows completed and are transferred/delivered to the customers.

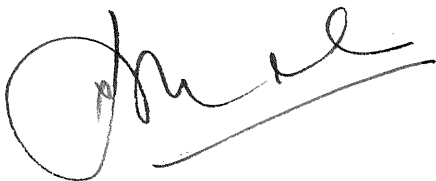
Revenue in respect of Bungalows which are completed is recognized at the point of transfer/delivery/and or is ready for delivery to the customers.

Revenue of Bungalows sold is after discount allowed.

The estimates of saleable area and costs are revised periodically by the management. The effect of such changes to estimates is recognized in the period such changes are determined’.

- g) It may be noted that there have been scrutiny assessments u/s 143(3) for the assessment years relevant to previous years between FY 2005-06 to FY 2014-15 accepting the above revenue recognition policy followed.
- h) During the year the following sale of houses, inter-alia credited to the Construction Account

Particulars	Amount
Sales II (i.e., for Phase II)	Rs. 41,00,000
Sales Phase III	Rs. 2,57,25,000
Sales Phase VII	Rs. 4,25,50,000
Total	Rs. 7,23,75,000



i) The above sales are credited to Construction Account in line with the revenue recognition policy followed.

j) Thus on the above Sales recognized, Gross Profit is not required to be estimated.

2) Bifurcation of Gross Profit offered on sale of land and sale of houses:

As requested by you the Gross Profit of Rs.20,08,580/- as per Construction Account is bifurcated as under :

Particulars	Amount
Total Gross Profit as per Construction Account	Rs. 1,31,92,480
Less : Gross Profit on sale of Land-16.5 Gts (as detailed in our submission dated 16-11-2018)	(Rs. 1,11,89,900)
Balance GP attributable towards Sale of Houses	Rs. 20,08,580

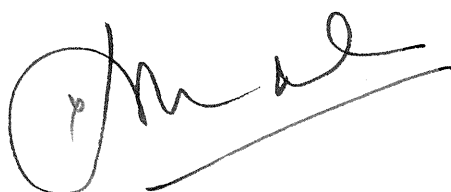
3) Clarification on method adopted in the computation of Gross Profit:

Broadly, for arriving at Gross Profit, the Construction Account is debited with opening inventories and construction expenses incurred during the year. The sale of houses, adopting revenue recognition policy, and sale of land is credited to Construction Account. The total of debits for opening stock + construction expenditure is deducted from the total of credits for sales + closing stock.

The balance amount is the Gross Profit.

The value of stocks (WIP) as at year end is computed in the following method.

Particulars	Amount
Opening Balance (WIP)	XXX
Add : Estimated Profit on installment received/receivable (Refer explanatory Note 1 below)	XXX
Add : Construction expenses during the year (Net of Misc. Income & Extra specifications received)	XXX
Sub total (A)	XXX
Less : Estimated Profit on sold flats (Refer explanatory Note 2 below)	(XXX)
Less: Sale declared flats/Houses construction expenses (Refer explanatory Note 3 below)	(XXX)
Sub total (B)	XXX
Closing Balance (WIP) (A-B)	XXX



Explanatory Note 1:

Till the construction of house is completed and delivered to the customers, no sale revenue is recognized in the Construction Account. However on advances received/ receivable from the customers, an estimated Gross Profit is added to the value of the closing stock. In this manner, the Gross Profit on advances gets offered to tax. This method is consistently followed over the years. This method also ensures that the profits are declared during the construction period and not only at the end of the project.

Explanatory Note 2:

Upon completion of the house and delivery to the customers, the sales revenue for the same is credited to Construction Account. On advances received from customers, an estimated Gross Profit are getting declared as submitted in Explanatory Note 1 above during construction period. The same is required to be deducted from the opening balance of WIP. This treatment ensures that there is no double offering of profit, one at the time of advances received and second at the time of final revenue recognition.

Explanatory Note 3:

The cost of sales (i.e., cost of construction of house completed and for which sale revenue is recognized) is deducted to arrive at the closing balance of stocks. The cost of sales is calculated on the sq.f. area sold and its cost. Out of this cost, the estimated profits declared earlier on advances received/receivable is deducted and only net cost of sales is reduced from the carrying amount of WIP. In effect, the estimated profits declared earlier which is deducted as per Explanatory Note 2 above is nullified.

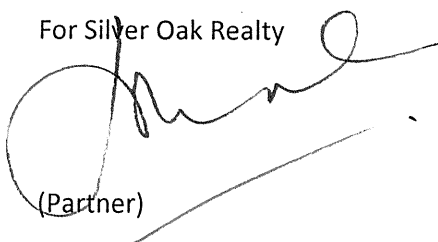
This treatment ensures that there is no double offering of profit, one at the time of advances received and second at the time of final revenue recognition.

It is reiterated that the above method and manner has been followed consistently over past years for which scrutiny assessments u/s 143(3) has been completed.

We hope you will find the above information in order.

Yours faithfully,

For Silver Oak Realty



(Partner)