



Re: MBMC it Return for fy 21-22.

From Pranay Mehta <pranay@kgmco.in>

Date Wed 10-May-23 4:43 PM

To Soham Modi <sohammodi@modiproperties.com>

Cc sambasivarao . <sambasivarao@modiproperties.com>

Dear Soham Bhai,

I have gone through the financials based on our discussion.

1. Prima facie if we retire the partner by writing off his debit balance in capital account it would attract capital gains tax in the hand of the firm. Section 45(4) provides in brief as under :

(4) Notwithstanding anything contained in sub-section (1), where a specified person **receives during the previous year any money or capital asset or both from a specified entity in connection with the reconstitution of such specified entity**, then any profits or gains arising from such receipt by the specified person shall be chargeable to income-tax as income of such specified entity under the head "Capital gains" and shall be deemed to be the income of such specified entity of the previous year in which such money or capital asset or both were received by the specified person, and notwithstanding anything to the contrary contained in this Act, such profits or gains shall be determined in accordance with the following formula, namely:—

$$A = B + C - D$$

Where,

A = income chargeable to income-tax under this subsection as income of the specified entity under the head "Capital gains";

B = value of any money received by the specified person from the specified entity on the date of such receipt;

C = the amount of fair market value of the capital asset received by the specified person from the specified entity on the date of such receipt; and

D = the amount of balance in the capital account (represented in any manner) of the specified person in the books of account of the specified entity at the time of its reconstitution:

Provided that if the value of "A" in the above formula is negative, its value shall be deemed to be zero:

Provided further that the balance in the capital account of the specified person in the books of account of the specified entity is to be calculated without taking into account the increase in the capital account of the specified person due to revaluation of any asset or due to self-generated goodwill or any other self-generated asset.

In our context calculation would be as under

$A = 0 \text{ (money paid)} + 0 \text{ (value of asset transferred)} - (2 \text{ cr debit balance in capital account representing negative } 2\text{cr})$

$$A = 0 + 0 + 2\text{cr} = 2\text{cr}$$

Based on above department may ask to the firm to pay capital gain tax on 2cr.

2. However, on a careful reading we can take a stand that no tax is payable and litigate on the basis of following:
 - a. **There is no receipt of money during the previous year** - The debit balance in the capital account is on account of payments/withdrawals made in earlier year and not the previous year .
 - b. **There is no receipt of money or transfer of asset** - all that we are doing is passing a JV to write off the balance. Mere accounting entry cannot be treated as receipt of money
 - c. Such receipt of money or transfer of money **should be in connection with the reconstitution** - In the case on hand the money was paid in earlier years and it cannot be constructed to be in connection with the reconstitution.
 - d. The provisions of section 45(4) got introduced only w.e.f 01/04/2021. If at all the provisions were to apply it would apply prospectively for payments made after such date and it cannot apply retrospectively for any payments made prior to such date.
3. The other option available is transfer the amount to a unsecured loan account before the date of retirement. So the calculation of $A = B + C - D$ does not impact us. Rotate and close the loan over a period of time. This would be a safer option.

Regards

CA Pranay Mehta
Managing Partner
KGM & Co.
Chartered Accountants

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From: sambasivarao . <sambasivarao@modiproperties.com>
Sent: 08 May 2023 11:27
To: Pranay Mehta <pranay@kgmco.in>
Cc: Soham Modi <sohammodi@modiproperties.com>
Subject: MBMC it Return for fy 21-22.

Pranay sir,

PFA of Modi Builders Methodist Complex Income Financials for fy 21-22.

Regards,

A Sambasiva Rao
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