IN THE INCOME TAX APPELLATE TRIBUNAL
'C' BENCH, CHENNAI

BEFORE Dr. O.K.NARAYANAN, VICE-PRESIDENT
AND SHRI CHALLA NAGENDRA PRASAD, JUDICIAL MEMBER

I.T.A. No.937/Mds/2012
Assessment Year : 2008-09
AND
S.P.No.62/Mds/2012

M/s. Coimbatore Hitech Infrastructure (P) Ltd., No.365, K G 1st Campus, Thudiyalur Road, Saravanampatti, Coimbatore – 641 035. PAN-AACCC5201G (Appellant)	Vs.	The Additional Commissioner of Income-tax, Range-I, Coimbatore. (Respondent)

Appellant by : Shri S. Sridhar, Advocate
Respondent by : Dr. Yogesh Kamat, IRS, JCIT

Date of hearing : 11th May, 2012
Date of pronouncement : 12thJune, 2012

O R D E R

PER Dr. O.K.NARAYANAN, VICE PRESIDENT

This appeal is filed by the assessee. The relevant assessment year is 2008-09. The appeal is directed against the

order of the Commissioner of Income-tax (Appeals)-I at Coimbatore dated 16.3.2012 and arises out of the assessment completed under sec.143(3) of the Income-tax Act, 1961.

2. The assessee is a company engaged in the business of developing Special Economic Zone(SEZ) at Keeranatham Village, Coimbatore. The assessee company has set up a sector specific SEZ for Information Technology and Information Technology Enabled Services. A SEZ is set up, approved and governed under the provisions of The Special Economic Zones Act(SEZ Act), 2005 and The Special Economic Zones Rules(SEZ Rules), 2006 made thereunder. The administration of the scheme is vested with the SEZ authority functioning under the Rules promulgated in 2009.

3. The assessee company has satisfied the conditions to be complied with for obtaining approval from the competent authority notified under the SEZ Act. The Department of Commerce in the Ministry of Commerce and Industry, Government of India has granted the approval to the assessee company for setting up the sector specific SEZ through their proceedings dated 20.8.2006.

The SEZ set up by the assessee company has been notified by the concerned authority in Official Gazette as required under the SEZ Act, 2005. In short, the assessee company is fully approved to develop SEZ under the SEZ Act, 2005.

4. In view of the approval granted by the competent authority, the assessee company carried out its activities to set up the SEZ. As per the SEZ Act, 2005, the assessee is in the status of a Developer, who shall develop, operate and maintain the SEZ in terms of the SEZ Act, 2005 and the Rules made thereunder. A Developer for the purpose of the SEZ Act, 2005 also includes a Co-Developer. After having developed SEZ as per the conditions laid down in the approval granted by the competent authority, the assessee has let out the developed lands to three parties in the previous year relevant to the assessment year under appeal. The three parties are M/s. Robert Bosch India Ltd., M/s. Cognizant Technology Solutions India (P) Ltd. and M/s. KGISL IT Parks (P) Ltd. The assessee has leased out 21.88 acres, 23.68 acres and 11.74 acres respectively.

5. The developed lands have been leased out to the above three parties on the strength of lease agreements. The lease agreements were executed for a period of 99 years. The total lease amount agreed by M/s. Robert Bosch India Ltd. was ₹18,59,80,000/-. This is at the rate of ₹ 85 lakhs per acre. The lease amount has to be paid as one time lease premium. M/s. Robert Bosch paid 95% of the lease premium at the time of execution of agreement and 5% after the assessee carried out the shifting of High Tension Cable lines as required under the agreement. Likewise in the case of M/s. Cognizant Technology Solutions (P) Ltd. and M/s. KGISL IT Parks (P) Ltd. also, the lease rentals were paid in this manner but in instalments. It is also a common condition in the lease agreements that on expiry of lease period of 99 years, the lessees will have the option to renew the lease agreement further.

6. The assessee had applied for certificate under sec.197 of the Income-tax Act, 1961 for exemption from deduction of tax at source against payment of lease premia, in its status of a SEZ developer entitled for exemption under sec.80-IAB of the Act. The certificate was granted by the assessing authority and in the

light of that certificate, no deduction of tax was made at source at the time of paying the lease premia.

7. As the assessee company is an approved and notified SEZ, it claimed deduction in respect of its income, being profits and gains arising from development of SEZ as provided under sec.80-IAB. The deduction provided under sec.80-IAB is 100% of the profits and gains by an undertaking or entrepreneur engaged in the development of SEZ. Accordingly, the assessee filed a 'NIL' return of income.

8. Sec.80-IAB provides that any profits and gains derived by an undertaking or entrepreneur being a developer from the business of developing a SEZ are fully exempt for a period of 10 consecutive years, out of 15 assessment years. The Assessing Officer referred to the statutory conditions, that should be satisfied for claiming deduction under sec.80-IAB. Those conditions are that the assessee is to be a developer and the income is to be derived from the business of developing a SEZ. The Assessing Officer found that the assessee company has been granted approval as "a developer" within the meaning of the SEZ Act,

2005 by the competent authority. The Assessing Officer through his discussion has agreed with the facts as explained by the assessee that the assessee company is setting up a SEZ for which the assessee has been granted approval by the competent authority as a developer and, therefore, the assessee is a SEZ under sec.80-IAB of the Income-tax Act, 1961.

9. The Assessing Officer, in the course of assessment proceedings examined the case in detail. He found that the assessee has developed a SEZ as provided under the SEZ Act, 2005 in the specific sector of Information Technology and Information Technology Enabled Services. He examined the conditions laid down in the approval given by the competent authority. One of the conditions is that the assessee shall develop a minimum area of one lakh square meters. The Assessing Officer found that the assessee has not completed that minimum built up area by the end of the previous year relevant to the assessment year under appeal. The Assessing Officer accordingly, pointed out a case of breach of one condition stipulated in the approval granted to the assessee as a SEZ. The assessing authority has observed in page 10 of his order that “It is

apparent from the details filed that this condition has not been fulfilled by the assessee in order to qualify for the deduction".

10. The Assessing Officer further observed that the assessee company has derived income only in the form of lease premium on leasing out the lands to three different companies and the assessee company has not derived any profits and gains as a developer of the SEZ. According to the Assessing Officer, the income declared by the assessee company has not been derived from the business of developing SEZ. The reason to come to the above conclusion is that the assessee company has given the land on a perennial lease of 99 years with further scope of renewal, which in effect is nothing but a sale. Relying on the decision of the Hon'ble Supreme Court in the case of R. Palshikar(HUF) vs. CIT (172 ITR 311), the Assessing Officer held that the long term lease of 99 years granted by the assessee company is nothing but sale of land. He, therefore, held that the income of the assessee company was in the nature of capital gains arising on sale of land. He accordingly, declined assessee's claim of deduction under sec.80-IAB.

11. Once the Assessing Officer denied the exemption to the assessee company under sec.80-IAB, he also made certain other additions to the taxable income of the assessee company. The assessee company has created a provision for project development cost on the basis of estimates for different works to the extent of ₹ 24,60,28,194/-. The assessee has treated an amount of ₹ 7,88,47,215/- as proportionate project development cost for the unleased area, from the above total provision. It was accordingly, taken as stock inventory. The balance provision of ₹16,71,80,979/- has been claimed by the assessee as pertaining to leased out lands. According to the Assessing Officer, only an amount of ₹ 3,89,84,177/- was actually spent on the project in the previous year and even that amount was not taken as part of the closing stock. On the other hand, it was written off as expenses. The Assessing Officer therefore, held that the provision should be treated as relating to the development expenditure of land and, therefore, to be disallowed. Accordingly, the amount of ₹16,71,80,979/- was added to the income. The assessee has made a donation of ₹ 2 crores in the previous year and debited the profit and loss account. This amount was also disallowed by

the Assessing Officer and added back to the income. Thus, finally, the Assessing Officer has determined a total income of ₹89,89,01,282/- in the hands of the assessee company.

12. The assessment was taken in first appeal. The Commissioner of Income-tax(Appeals) examined the case in detail. On going through the lease agreements entered into between the assessee company and the three lessees, the Commissioner of Income-tax(Appeals) found that the lease agreements were executed and lease rentals were received by the assessee company even before starting the business of developing a sector specific SEZ. Otherwise, it is the case of the Commissioner of Income-tax(Appeals) that the assessee has not started the business of developing a SEZ before entering into lease agreements. The reason for the Commissioner of Income-tax(Appeals) to come to the above finding is that the assessee company had entered into lease agreement with M/s. Robert Bosch India Ltd. even before completing the development of SEZ as required under the Rules and also M/s.Cognizant Technology Solutions India (P) Ltd. and M/s. KGISL IT Parks (P) Ltd. had entered into lease agreements even before those companies

getting approval from the competent authority to occupy specific areas in the SEZ. Therefore, the Commissioner of Income-tax(Appeals) held that the income of the assessee company could not be held to be derived from the business of developing a SEZ. He, therefore, held that the assessee is not entitled for deduction under section 80-IAB.

13. Having arrived at the above finding, the Commissioner of Income-tax(Appeals) further examined the nature of income reported by the assessee company and held that the assessing authority is justified in treating the income as capital gains taxable in the hands of the assessee company. So also in all other aspects, the assessment was upheld. The appeal filed by the assessee was dismissed.

14. The assessee is aggrieved and therefore, the second appeal before the Tribunal. The detailed grounds raised by the assessee company read as below :

> "1.1 The learned Commissioner of Income-tax(Appeals)-I, Coimbatore has erred in passing the order in the manner passed by him. The order passed being bad in law is liable to be quashed.

2.1 The learned Commissioner of Income-tax(Appeals)-I, Coimbatore has erred in concluding that the appellant is not eligible for deduction under section 80-IAB.

2.2 The learned Commissioner of Income-tax(Appeals)-I, Coimbatore has erred in concluding that (i) the appellant has not started the business of developing a special economic zone (SEZ) and (ii) the appellant has not derived any profits and gains from the business of developing the SEZ.

2.3 The learned Commissioner of Income-tax(Appeals)-I, Coimbatore has erred in concluding that the lease premium received by the appellant for lease of SEZ land is chargeable to tax under the head 'Capital gains'.

2.4 The learned Commissioner of Income-tax(Appeals)-I, Coimbatore has erred

(i) in not appreciating that the Assessing Officer in the income tax computation form had assessed the income of the appellant under the head 'profits and gains of business'.

(ii) in upholding that the income is to be assessed as capital gains as appears to have been concluded by the

learned Assessing Officer, which conclusion of the Assessing Officer is not borne on records;

(iii) in concluding that the appellant is not eligible for deduction under section 80-IAB even if the lease premium is treated as chargeable to tax under the head 'Capital gains'.

2.5 The learned CIT(A) and the learned Assessing Officer has erred in not appreciating that having accepted that the appellant is eligible to claim deduction under section 80-IAB while issuing certificate under section 197, it is impermissible to take a contrary view subsequently.

2.6 The learned CIT(A) and the learned Assessing Officer has erred in not appreciating that having accepted that the appellant is not liable to pay tax under section 115O, it is impermissible to take a contrary view subsequently.

2.7 The various conclusions, findings and the averments of the learned Commissioner of Income-tax(Appeals)-I, Coimbatore in denying the deduction claimed under section 80-IAB are incorrect, contrary to facts and law, bad in law and liable to be quashed.

2.8 On facts and in the circumstances of the case and law applicable, the appellant is eligible for

deduction under section 80IAB and the same is to be allowed as claimed by the appellant.

2.9 Assuming without admitting that the appellant is not eligible to claim deduction under section 80-IAB, the income authorities have erred in assessing the entire lease premium without allowing deduction towards expenditure incurred and expenditure to be incurred by the appellant.

2.10 Without prejudice, the learned Commissioner of Income-tax(Appeals)-I, Coimbatore has erred in not appreciating that the lease premium receipts received by the appellant has to be spread over the lease period or the period of tax holiday in terms of section 80IAB as the case may be.

3.1 The learned Commissioner of Income-tax(Appeals)-I, Coimbatore has erred in confirming the levy of interest under section 234B of the Income-tax Act, 1961. On facts and in the circumstances of the case and law applicable, the appellant is not liable for interest under section 234B. The appellant denies its liability to pay interest under section 234B.

4.1 In view of the above and other ground to be adduced at the time of hearing, the appellant prays that the order passed by the learned Commissioner of Income tax (Appeals)-I, Coimbatore be quashed

or in the alternative

(i) Appellant be held as engaged in the business of developing the Special Economic Zone;

(ii) (a) Lease premium receipts be held as profits and gains derived from the business of developing the Special Economic Zone;

(b) Lease premium receipts be held as not chargeable to tax under the head 'Capital gains';

(c) alternatively and without prejudice, deduction under section 80-IAB be allowed even if the lease premium receipts are held to be chargeable to tax under the head 'Capital gains'

(iii) Deduction under section 80-IAB be allowed as claimed by the appellant;

(iv) Interest under section 234B be deleted."

15. We heard Shri S. Sridhar, the learned counsel appearing for the assessee company. The learned counsel explained that the scheme of SEZ is governed by the provisions of law contained in the SEZ Act, 2005. He contended that sec.80-IAB of the Income-tax Act, 1961 provides deductions in respect of profits and gains

by an undertaking or enterprise engaged in development of SEZ. In the Explanation provided thereunder, the Income-tax Act has accepted the definitions of “Developer” and “Special Economic Zone” as provided in the SEZ Act, 2005. As per sec.2(f) and (g) of the SEZ Act, 2005, ‘Developer’ means a person who, or a State Government which, has been granted by the Central Government a letter of approval under sub-sec.(12) of sec.3. The learned counsel explained that the SEZ Act, 2005 overrides other law including the Income-tax Law. He referred to sec.51 of the SEZ Act, 2005, where it is provided that the SEZ Act shall have overriding effect notwithstanding anything inconsistent therewith contained in any other law for the time being in force or in any instrument having effect by virtue of law other than this Act.

16. The learned counsel further explained that the assessee company has obtained the approval of the competent authority to engage in the business of developing SEZ as required under the provisions of the SEZ Act, 2005. Necessary notifications have been made in the Official Gazette by the competent authority. It is on the basis of the approval granted by the competent authority that the assessee has been declared as a Developer of SEZ. The

approval has been granted on the ground that the assessee company has satisfied the necessary conditions. The assessee company has complied with the conditions laid down in the Rules and in the letter of approval. The assessee has to develop and operate processing areas fit for instant accommodation of the entrepreneurs occupying SEZ. The conditions to be satisfied are that the assessee should provide infrastructure facilities like roads with street lighting, providing office spaces, food services including cafeteria or restaurant, recreation facilities, swimming pool, telephone and communication facilities including inter connectivity, medical service centre, supply of uninterrupted power, ample parking facilities, provision for water, warehousing and other services. The assessee has complied with all these stipulations as required by the Rules. The assessee has developed land into processing area. As the assessee has developed a sector specific SEZ, in the field of Information Technology and Information Technology Enabled Services, the assessee had to ensure the parameters like uninterrupted power supply of stable frequency at all times, reliable connectivity for

secure data transmission, central air conditioning and ready to use finished plug and play facility for end users.

17. The learned counsel further explained that the assessee being a Developer of SEZ can assign the lease hold right to the entrepreneurs only if those entrepreneurs hold valid letter of approval from the competent authorities.

18. In the light of the above, the learned counsel rebutted the objections raised by the assessing authority and the Commissioner of Income-tax(Appeals) in the following manner :

(i) There is no rule that a Developer of SEZ must develop the entire approved area at one stretch and only after the development of the entire area that he can lease out the processing area to eligible entrepreneurs. As and when areas are developed into operational and processing areas, the developed part and parcel of the land can be leased out to approved entrepreneurs who show interest to occupy space inside the SEZ. Therefore, there is no reason or rhyme in the finding of the Commissioner of Income-

tax(Appeals) that the assessee has leased the land to M/s. Robert Bosch India Ltd. before completing the stipulated development in the property.

(ii) Rule 11(6) of the SEZ Rules, 2006, provides that a developer holding land shall assign lease hold right to the entrepreneur holding valid letter of approval. The assessee has assigned lease hold right to M/s. Robert Bosch India Ltd., M/s. Cognizant Solutions and M/s. KGISL. The finding of the Commissioner of Income-tax(Appeals) is that the land was assigned to those parties even before those parties obtaining the approval. Those parties have obtained approval from the competent authorities as qualified entrepreneurs to occupy lease hold right inside the SEZ developed by the assessee. Once those entrepreneurs applied for the approval from the competent authorities, it is quite natural that they will proceed with further formalities for obtaining the approval. It is not practically feasible to do all the activities necessary to take possession of the lease hold land only after the formal receipt of the approval. Where the entrepreneurs have been granted approval, those approval

relates back to the date of applications put in by them. Therefore, the reasons pointed out by the Commissioner of Income-tax(Appeals) are without any basis.

19. Therefore, in the facts and circumstances of the case, the learned counsel submitted that the findings arrived at by the Commissioner of Income-tax(Appeals) are without any basis and contrary to the facts. The first objection of the Commissioner of Income-tax(Appeals) is that the assessee company has assigned the lease hold right even before developing the lease hold land as required in the letter of approval. This is not correct. The assessee has leased out land to the entrepreneurs to the extent developed, which is permissible. The assessee has clearly demarcated between the developed area leased out to entrepreneurs and the land under development as unleased area. He also explained that the finding of the Commissioner of Income-tax(Appeals) regarding the letter of approval to the entrepreneurs is not sustainable in law.

20. Now coming to the basic objection of the Assessing Officer that the perennial lease granted by the assessee to lessees

amounts to sale of land, the learned counsel invited our attention to Rule 11(9) of the SEZ Rules, 2006. The Rule says that the Developer shall not sell the land in a SEZ. He explained that while the SEZ Act and Rules specifically prohibit the sale of land in a SEZ, it is not possible for the assessing authority to hold that there was a transfer of assets by way of sale. When a direct sale is not permitted under the SEZ Rules, a deemed sale under lease cannot be presumed. The Hon'ble Supreme Court in the case of R.K.Palshikar (HUF) (172 ITR 311), relied on by the Assessing Officer was rendered in an extremely different situation. The court was examining the scope of sec.12B of the Income-tax Act, 1922. The said decision cannot come in the way of rejection of claim of deduction of the assessee under sec.80-IAB. Under the provisions of the SEZ Act, 2005, the land in SEZ cannot be sold by the Developer. When that is the legal position, a lease agreement even if for a period of 99 years cannot held to be a sale. The SEZ Rules provide that the lease period should not be less than 5 years. The Rules do not specify the maximum period of lease. The learned counsel submitted that the reasoning relied on by the Assessing Officer is unlawful.

21. The learned counsel further relied on the certificate issued by the assessing authority under sec.197 of the Income-tax Act, 1961. Sec.197(1) provides that a certificate shall be issued by the Assessing Officer if he is satisfied that the circumstances of the case justify a lower rate or no deduction of tax at source. He further explained that the assessing authority has issued the certificate of non-deduction of tax after satisfying that the assessee was entitled for deduction under sec.80-IAB. There is no material to take an altogether different view at the time of assessment.

22. The learned counsel has further relied on the decision of the Hon'ble Supreme Court in the case of Maharaja Chinthamani Saran Nath Sah Deo v. CIT (82 ITR 464) to show that the lease rent received by the assessee in lump sum does not amount to any 'salami' but the payments were in the nature of lease rent alone. He explained that the assessee has received premium for lease. Those receipts are in the nature of consideration for leasing of SEZ premises. There is no transfer or parting of right by the SEZ Developer. The learned counsel stated that the intention of the parties are apparent in the lease agreements and

the intention is to be upheld, in view of the decision of the Hon'ble Supreme Court in the case of CIT v. Motors & General Stores (66 ITR 692). He has also placed reliance on the decision of the Hon'ble Andhra Pradesh High Court in the case of Nagasuri Raghaveswara Rao v. CIT (66 ITR 496) to support his argument that the intentions of the parties are to be gathered from documents and surrounding circumstances to decide the nature of transactions. He has also relied on the decisions of the Hon'ble Supreme Court in the cases of Durga Das Khanna v. CIT (72 ITR 796) and Continental Construction Ltd. v. CIT (195 ITR 81).

23. The learned counsel concluded that the assessee is entitled for deduction under sec.80-IAB of the I.T. Act, 1961.

24. Dr. Yogesh Kamat, the learned Jt. Commissioner of Income-tax appeared for the Revenue and argued the case.

25. The learned Commissioner contended that even though the assessee is engaged in the business of developing a SEZ, the assessee company has not derived any income in that capacity for the assessment year under appeal. The assessee was

carrying on activities to develop the land into a SEZ for Information Technology and Information Technology Enabled Services. It is true that the assessee company has obtained the letter of approval from the competent authority. These facts are not objected to.

26. The learned Commissioner explained that the crucial question is whether the income reported by the assessee company for the assessment year under appeal, in fact, is derived by way of profits and gains from the business of developing a SEZ. One of the conditions required in the letter of approval was that the assessee company shall develop one lakh sq. mtrs. of processing/operational area. From the details furnished by the assessee, it is seen that the stipulated area was not developed by the assessee company by the end of the previous year relevant to the assessment year under appeal. This violates one of the important stipulations contained in the approval. On this ground itself, the assessee is not entitled for deduction claimed under sec.80-IAB.

27. When the assessee company has assigned lease hold right over the land to three parties, the development of SEZ was not complete. In the case of M/s. Robert Bosch India Ltd., the lease agreement was executed before completing the required development of the property. In the case of remaining two lessees, they did not have the approval of the competent authority at the time of executing the agreements. From the above, it is clear that the lease agreements have been entered into between the assessee company and the three parties before satisfying the necessary conditions of developing the SEZ. Therefore, it is not possible to hold that the income reported by the assessee company is by way of profits and gains derived by carrying on the business of developing SEZ.

28. It is, in these circumstances, that the Assessing Officer has examined the true nature of income disclosed by the assessee in its return. The assessee company has derived the income from giving lease hold right over the land on the basis of the perennial lease agreement for a long period of 99 years. The Hon'ble Supreme Court in the case of R.K.Palshikar (HUF) v. CIT (172 ITR 311) has held that de facto speaking such lease is in fact,

nothing else but sale. The learned Commissioner contended that the Assessing Officer has rightly relied on the said judgment of the Hon'ble Supreme Court. When the perennial lease of 99 years is examined, it is very clear, that in reality, it was only a sale. That means, the assessee company has transferred its property and therefore, the income arising on such sale is in the nature of capital gains.

29. In the matter of other additions also, the learned Commissioner supported the orders passed by the lower authorities. He concluded that the appeal filed by the assessee may be dismissed.

30. We heard both sides in detail.

31. Sec.80-IAB of the I.T .Act, 1961 provides for deductions in respect of profits and gains by an undertaking or enterprise engaged in development of SEZ. The section provides that where the gross total income of an assessee, being a Developer, includes any profits and gains derived by an undertaking or an enterprise from any business of developing a SEZ, notified on or after the 1st day of April, 2005 under the SEZ Act, 2005, there

shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of the assessee, a deduction of an amount equal to one hundred per cent of the profits and gains derived from such business for ten consecutive assessment years, out of 15 years beginning from the year in which a SEZ has been notified by the Central Government of India. The Explanation provided under sec.80-IAB adopts the SEZ Act, 2005 for the purposes of the definitions "Developer", "Special Economic Zone" etc.

32. For the purposes of our discussion, it is also necessary to go through some of the provisions of SEZ Act, 2005 and SEZ Rules, 2006.

33. The approval and notification necessary for recognizing a Developer under the SEZ Act, 2005 is vested with the Government of India, in the Ministry of Commerce and Industry, Department of Commerce. The administration of the scheme of SEZ is vested with the authorities appointed under the SEZ Authority Rules, 2009. Sec.2(f) and (g) of the SEZ Act, 2005 defines "Developer" as a person among other things who has

been granted by the Central Government a letter of approval under sub-sections (10) & (12) of sec.3. SEZ means each SEZ notified and also includes existing SEZ. Board means Board of approval under sub-sec.(1) of sec.8. It is the Board which grants an approval. Sub-sec.(10) of sec.3 provides that the Central Government shall grant a letter of approval on such terms and conditions and obligations and entitlements as may be approved by the Board, to the Developer.

34. Sec.51 of the SEZ Act, 2005 declares that the provisions of the SEZ Act, 2005, shall have overriding effect notwithstanding anything inconsistent therewith contained in any other law for the time being in force or in any instrument having effect by virtue of any law other than this Act. This overriding effect is reiterated in sec.27 of the SEZ Act, 2005, where it is provided that the provisions of the Income-tax Act, 1961 are to apply with certain modifications in relation to Developers and entrepreneurs. Such modifications are provided in Second Schedule to the Act. The overriding effect is again emphasized in sec.52 of the SEZ Act, 2005, with certain provisions of the Customs Act, 1962 not to apply to the SEZ.

35. Rule 6 of the SEZ Rules, 2006, deals with the letter of approval to the Developer. Sub-rule (2) thereof provides that the letter of approval of a Developer shall be valid for a period of three years within which time at least one unit commenced production and the SEZ becomes operational from the date of commencement of such production. Rule 11 provides the procedure for demarcating processing area and non-processing area in a SEZ. Sub-rule (5) thereof stipulates that the land or built up space in the processing area or Free Trade and Warehousing Zone shall be given on lease only to the entrepreneurs holding a valid letter of approval issued under Rule 19 and the lease period shall not be less than five years but notwithstanding any other condition in the lease deed, the lease rights would cease to exist in case of the expiry or cancellation of the letter approval. Sub-rule (6) of Rule 11 provides that the Developer holding land on lease basis shall assign lease hold right to the entrepreneur holding valid letter of approval. Sub-rule (8) thereof provides that the Developer may allot land in the processing area on lease basis to a person desiring to create infrastructure facilities for use by the prospective units.

36. One of the most important restrictions provided in sub-rule(9) of Rule 11 is that the Developer shall not sell the land in a SEZ.

37. We may consider the eligibility of the claim of the assessee for deduction under sec.80-IAB, keeping in view the provisions of sec.80-IAB and the above mentioned provisions of the SEZ Act, 2005 and Rules under the SEZ Rules, 2006.

38. The assessee is a company engaged in the business of developing sector specific SEZ for Information Technology and Information Technology Enabled Services at Coimbatore. There is no dispute regarding the character of the business carried on by the assessee company. The assessee company has been granted approval by Government of India through their letter dated 20.8.2006. The approval still continues in force. By virtue of overriding effect of the SEZ Act, 2005, it is an established fact that the company is a Developer who is engaged in the business of developing SEZ.

39. Having confirmed the above fact, it is necessary to examine what would be the nature of income earned by the assessee.

Sec.80-IAB provides that where the gross total income of an assessee, being a Developer includes any profits and gains derived by an undertaking or an enterprise from any business of developing a SEZ, there shall be allowed one hundred percent of the profits and gains derived from such business as deduction. It is clear from the facts of the case that the assessee company is engaged in the business of developing a SEZ. The activity carried on by the assessee is developing a SEZ. It amounts to the business of developing a SEZ explained in sec.80-IAB.

40. What is contemplated in sec.80-IAB of the Income-tax Act, 1961 is the business of developing a SEZ. It is not the business of running eligible units approved by the competent authority. In the present case assessee is the developer. It need not do any other business to claim the benefit of deduction under sec.80-IAB. Assessee's SEZ is sector specific for Information Technology and Information Technology Enabled Services. Assessee is not required to run operating units in the sector of Information Technology and Information Technology Enabled Services. That business is to be carried on by approved entrepreneurs like M/s.

Robert Bosch, M/s. Cognizant Technology, KGISL IT Parks etc. to whom assessee has leased out developed area within the SEZ.

41. Therefore, the only income derived in the hands of the assessee developer will be the lease rent and other service charges if any. The assessee is not expected to derive income from operating business units engaged in the sector of Information Technology and Information Technology Enabled Services. The profits and gains of business of a developer contemplated in sec.80-IAB for the purpose of deduction thereunder, is nothing but lease/rental income. Therefore, it is an anti-thesis of the law stated in sec.80-IAB to hold that lease rental income is not “profits and gains” of business in the hands of assessee developer.

42. The law provides in sec.80-IAB that having approved by the Government of India, developing a SEZ, by itself is the business contemplated under sec.80-IAB for providing deduction in respect of a Developer. The statute itself has made it clear that the lease rental income generated in the hands of a Developer engaged in

setting up of the SEZ, is the profits and gains derived from the business of developing a SEZ.

43. The lower authorities have tried to ignore the above statutory provision by raising certain objections. The first objection is that the assessee has not satisfied one of the conditions of the approval that the assessee should have developed a minimum built up area of one lakh sq. mtrs. It is the case of the lower authorities that the assessee has granted lease hold right of property to three parties before setting up of SEZ itself. In other words, the objection of the lower authorities is that the assessee could have granted lease hold right to approved entrepreneurs only after the completion of the entire development of project. It is the case of the lower authorities that the developed portion of the SEZ cannot be given on lease before completing the development of entire approved land. This presumption is against the law stated in the SEZ Act, 2005. Rule 6(2) of the SEZ Rules, 2006 provides that the letter of approval of a Developer granted shall be valid for a period of three years within which time at lease one unit has commenced production and the SEZ become operational from the date of

commencement of such production. It is clear from the above Rule that the SEZ Act, 2005 does not contemplate that a Developer can assign the land to the entrepreneurs only after completing the development of the entire approved land. The condition specified in the Rule to sustain the validity of the approval is that at least one unit should commence production and to that extent, the SEZ should become operational. Therefore, the objection of the lower authorities that the assessee has leased out a portion of its property before completing the development of entire project is not sustainable in law. The objection of not having developed land of one lakh sq. mtrs. thus fails.

44. The other objection raised by the lower authorities is that the developed portion of the property has been allotted to the entrepreneurs before those parties obtaining the approval from the competent authority. It is to be seen that the competent authority has granted approval to the entrepreneurs, M/s. Robert Bosch India Ltd., M/s. Cognizant Technology Solutions India (P) Ltd. and M/s, KGISL IT Parks (P) Ltd. to whom the assessee has granted lease hold right. The approval granted by the

competent authority dates back to the application put in by them. It is not possible to hold a view that lease hold right has been assigned to the entrepreneurs before obtaining the approval only for the technical reason that the assessee and the concerned parties have commenced negotiations for allotment of lease hold right prior to the formal receipt of the approval from the competent authority. It is to be seen that business activities are carried on in a comprehensive manner so as to make the business operational at the earliest point of time. The lower authorities are not justified in holding such a view against the assessee company.

45. The finding of the lower authorities is that the income earned by the assessee is in the nature of capital gains because 99 years of lease agreement executed by the assessee company amounted to sale of the property. It is already mentioned that the SEZ Act, 2005 overrides all other Laws. This is made specific in sec.51 of the SEZ Act, 2005. It is also clear that Rule 11(9) of the SEZ Rules, 2006 provides that a Developer shall not sell the land in the SEZ. The legal consequence of the above statute is that the assessee as a Developer of SEZ is prohibited from selling

the land developed by him in the SEZ. When the law does not approve the sale, there cannot be a transfer of property. It is not possible to hold a view that the lease amounted to sale of the property for the reason that the lease is perennial in nature extending over a period of 99 years. This is against Rule 11(9) of SEZ Rules, 2006 which overrides all other laws by virtue of Sec.51 of SEZ Act, 2005.

46. The Assessing Officer has relied on the decision of the Hon'ble Supreme Court in the case of R.K.Palshkar (HUF) (172 ITR 311). That case was considered by the Hon'ble Apex Court in the light of sec.12B of the I.T. Act, 1922. The assessee therein had developed its ancestral agricultural land into building plots. Thereafter those plots were assigned to various parties on the basis of lease agreements for a period of 99 years. While examining the liability of the assessee for capital gains tax, the Hon'ble Supreme Court held that even though the relevant agreement was characterised as a lease agreement, de facto speaking, the transaction was a sale as the lease agreement covered a period of 99 years. The Hon'ble Supreme Court has

gone through all the aspects of the case and the colourful device deployed by the assessee to evade the payment of capital gains tax. The Hon'ble Apex Court has looked into the pith and substance of the transaction and came to the view that for all practical purposes, those building plots were sold. That was a decision arrived at by the Hon'ble Supreme Court under the provisions of the Income-tax Act, 1922. In the present case, the SEZ Act, 2005 overrides the provisions of the Income-tax Act, 1961 for deciding the basic character of transactions entered into by the Developer and the approved entrepreneurs. Sec.51 of the SEZ Act, 2005 declares the overriding character of that Act. Rule 11(9) prohibits a Developer from selling the land to entrepreneurs. Therefore, the concept of transfer in the present case has to be examined in the overriding light of the SEZ Act, 2005. When the SEZ Act, 2005 provides that it is not permissible for a Developer to sell the land in a SEZ, it is not conceivable in law that the assessee can transfer the ownership of the property to the approved entrepreneurs through any other means. Therefore, there cannot be a case of capital gains arising in the hands of the assessee.

47. Rule 11(6) of SEZ Rules, 2006 states that the Developer shall assign lease hold right to the entrepreneur holding valid letter of approval. It is also seen in Rule 11(5) of SEZ Rules. 2006 that the land or built up space in the processing area or Free Trade and Warehousing Zone shall be given on lease only to the entrepreneurs holding a valid letter of approval and the minimum period of lease shall be 5 years. The SEZ Act, 2005 does not allow a Developer to sell the land in the SEZ. The Developer can only lease out the land to the entrepreneurs holding a valid letter of approval. Minimum period of lease is 5 years. The maximum period is not specified.

48. Therefore, it is clear that the assessee-Developer has proceeded with the allotment of developed area on lease hold basis to the approved entrepreneurs, viz., M/s. Robert Bosch India Ltd., M/s. Cognizant Technology Solutions India (P) Ltd. and M/s, KGISL IT Parks (P) Ltd. in accordance with SEZ Act, 2005 and SEZ Rules, 2006. The period of lease is 99 years which is permissible under the SEZ Act, 2005. Where there is no right of sale, the possible way is only lease. It may be a perennial lease but that does not change the character of the lease. The

length of lease period is usually determined by business, technological, financial and other operational considerations. Where the approved entrepreneurs set up units in SEZ with investments of billions of rupees, it is not possible to absorb the capital cost within a short period. Therefore, it is necessary in the interest of the developer and the approved entrepreneur to extend the lease period to such a longer period so that both the developer and the entrepreneur will be in a position to absorb their capital investments. This is also in tune with the policy declared by the Government of India. With reference to the set up of SEZ, the Government is encouraging SEZ development on a long term basis as part of its economic policy. It is in the public interest that the lease period is always longer so that the developed asset is exploited for sustained economic growth.

49. The assessee is an approved Developer of SEZ. The only activity carried on by the assessee is developing a sector specific SEZ. It has leased out the developed plots to the entrepreneurs who had obtained the letter of approval from the competent authority. Sec.80-IAB provides that setting up of a SEZ is the business of developing SEZ. Therefore, the assessee is not

expected to perform any other activity than developing of a SEZ to qualify for deduction.

50. In the facts and circumstances of the case, we find that the lower authorities are not justified in refusing deduction under sec.80-IAB. The claim of deduction made by the assessee under sec.80-IAB is in accordance with law. The assessing authority is directed to give the deduction.

51. Other issues raised in this appeal relating to different additions are only academic for the reason that those items, even if added to the total income of the assessee, are still part of 100% deduction available under sec.80-IAB; so also is the ground raised by the assessee on taxing of dividend income. This principle has been upheld by the Hon'ble Bombay High Court in CIT vs Punit Commercial Ltd. (245 ITR 550).

52. The assessing authority is therefore, directed to re-do the assessment after giving the assessee deduction under sec.80-IAB.

53. In result, this appeal filed by the assessee is allowed.

54. As the appeal itself is decided, the Stay Petition filed by the assessee is dismissed as infructuous.

Order pronounced on Tuesday, the 12th of June, 2012 at Chennai.

Sd/-	Sd/-
(Challa Nagendra Prasad)	**(Dr. O.K.Narayanan)**
Judicial Member	Vice-President

Chennai,
Dated the 12th June, 2012

mpo*

Copy to:

1. Appellant
2. Respondent
3. CIT(A)
4. CIT
5. DR