IN THE INCOME TAX APPELLATE TRIBUNAL

'A' BENCH, CHENNAI

BEFORE Dr. O.K.NARAYANAN, VICE-PRESIDENT
AND SHRI VIKAS AWASTHY, JUDICIAL MEMBER

ITA Nos.1614 & 1615(Mds)/2011
Assessment Years : 2006-07 & 2007-08

M/s.Mahindra Holidays & Resorts India Ltd., Mahindra Towers, II Floor, 17-18, Patullos Road, Chennai-600 002. PAN AAACM6469L. (Appellant)	Vs.	The Deputy Commissioner of Income-tax, Large Tax Payer Unit, Chennai. (Respondent)

AND

ITA Nos.1762 & 1763(Mds)/2011
Assessment Years : 2006-07 & 2007-08

The Deputy Commissioner of Income-tax, Large Tax Payer Unit, Chennai. (Appellant)	Vs.	M/s.Mahindra Holidays & Resorts India Ltd., Chennai. (Respondent)

Assessee by : Shri R.Vijayaraghavan, Advocate
Department by : Shri Shaji PJacob, IRS, Addl.CIT

Date of Hearing : 9th October, 2012
Date of Pronouncement : 17thOctober, 2012

O R D E R

PER Dr.O.K.NARAYANAN, VICE PRESIDENT

This is a set of cross appeals filed by the assessee and the Revenue for the two assessment years 2006-07 and 2007-08. These appeals are directed against the orders passed by the Commissioner of Income-tax(Appeals), Large Tax Payer Unit at Chennai on 25-8-2011. The appeals arise out of the assessments completed under section 143(3) of the Income-tax Act, 1961.

2. We will first consider the cross appeals filed for the assessment year 2006-07.

3. The appeal filed by the assessee is in ITA No.1614(Mds)/2011.

3.1. The first ground raised by the assessee is that the Commissioner of Income-tax(Appeals) has erred in confirming the addition of ₹ 61,78,71,246/- to the income of the assessee. It is the case of the assessee that the said sum was not chargeable to tax as income of the assessee for the assessment year under appeal.

3.2. The assessee is engaged in the business of running holiday homes on time share basis. Members are admitted as time shareholders and they are provided stay in the holiday homes maintained by the assessee for a specified number of days in a year. Whenever new members/customers subscribe to the membership of the assessee's holiday home plan, the assessee is collecting membership fees from them. The assessee provides holiday home facility for its members for a period of 25 years. A member is entitled to come and stay in the holiday home for a specified number of days in a particular year. While collecting membership fees from time shareholders, the assessee company offers 60% of such membership collection as income of the year of collection. The balance 40% of the membership fees is treated as deferred income to be spread over the remaining period of holiday share owned by a member. In a 25 year plan, the 60% membership fees is treated as income of the assessee for the first year and the balance 40% is to be treated as income of the remaining 24 years on a pro rata basis.

3.3. This method of recognizing the income was not accepted by the Assessing Officer. The Assessing Officer found that even if a time shareholder is entitled to enjoy the privilege of staying in the holiday homes of the assessee for a period of 25 years, the assessee company is not incurring any expenditure in the subsequent years for providing such facilities to the members. In addition to the membership fees collected by the assessee company, the assessee is also collecting upkeep and maintenance charges from the members as annual charges. These annual charges will take care of the expenses, if any, required in connection with providing the facilities to the members for the subsequent years of the holiday plan. The Assessing Officer has further pointed out that the assessee claims the entire expenses incurred in a particular year as deduction in that year itself, but at the same time defers a portion of its income to be spread over the subsequent years, which is not in conformity with the matching principle of accountancy. The Assessing Officer also pointed out that the expenditure not incurred or loss not suffered in a particular assessment year

cannot be deducted against the actual receipts of that particular year.

3.4. The Assessing Officer relied on the decision of the Income-tax Appellate Tribunal, Chennai Bench, rendered in the case of Sterling Holiday Resorts(India) Ltd. vs. ACIT, 295 ITR (AT) 162, wherein the Tribunal has held that the entire fee collected in a particular year in similar circumstances is the income liable for taxation in the year of receipt.

3.5. Accordingly, the Assessing Officer treated the entire hundred per cent of the membership collection as income liable for taxation for the impugned assessment year 2006-07. It is how the addition of ₹ 61,78,71,246/- has been made by the Assessing Officer.

3.6. In first appeal, the Commissioner of Income-tax(Appeals) also concurred with the findings of fact recorded by the Assessing Officer. He found that in addition to the membership fees, the assessee is also collecting annual maintenance charges or annual subscription fees. These annual charges are collected from the members irrespective of whether a member has occupied the resort or not and, when a member

occupies the facility, he makes further payment towards electricity, water, air-conditioning, etc. The Commissioner of Income-tax(Appeals) further observed that when the assessee company is collecting such annual subscription charges as well as actual utilization charges so as to meet the recurring expenses in connection with maintenance and management of the resort, the assessee is not offering the entire membership fees as its income for taxation. Only 60% of the membership fees is recognized as the income of the year and the balance 40% is spread over the remaining period of membership. The Commissioner of Income-tax(Appeals) has agreed with the assessing authority that the matching principle of accountancy is not observed and, therefore, the division of membership fee made by the assessee between 60% and 40%, is not acceptable for the purposes of income-tax.

3.7. The assessee, on the other hand, relied on the decision of the Income-tax Appellate Tribunal, Chennai 'B' Special Bench rendered in assessee's own case in ACIT vs. Mahindra Holidays & Resorts(India) Ltd., 131 TTJ (Chennai) (SB) 1. In the said Special Bench decision, the Tribunal has held

that two conditions are necessary to say that income has accrued to or earned by the assessee. They are: (i) it is necessary that the assessee must have contributed to its accruing or arising by rendering services or otherwise, and (ii) a debt must have come into existence and he must have acquired a right to receive the payment. In the present case, a debt is created in favour of the assessee immediately on execution of the agreement. However, it cannot be said that the assessee has fully contributed to its accruing by rendering services. The assessee is bound to provide accommodation to the members for one week every year till the currency of the membership. Till the assessee fulfils its promise, the parenthood cannot be traced to it. If the assessee confirms the reservation but is not able to provide the allotment or the alternate accommodation, assessee is liable to pay liquidated damages to the member. The Special Bench continued to observe that the assessee is liable to pay liquidated damages only if it is not in a position to provide accommodation as per confirmed reservation. But it is not liable to pay any damages if it is not able to provide an accommodation on account of non availability. Thus, the matter does not end on

signing of the agreement and on a person becoming a member. There is a continuing liability on the part of the assessee not only to provide accommodation but also to provide other incidental services attached with the accommodation. Relying on the judgment of the Hon'ble Supreme Court in the case of E.D.Sassoon & Co. Ltd. vs. CIT 26 ITR 27, the Special Bench held that for a liability to qualify for recognition, there must be not only present obligation but also the probability of an outflow of resources to settle that obligation. In the present case, the past event is admitting a person as a member with a promise to fulfil the obligation of providing him accommodation for one week every year for the next 25 years, which is not an ordinary obligation. The Special Bench held accordingly that the assessee is justified in treating 60% of membership fees collection as income of the year of collection and the balance 40% as the income of the remaining 24 years.

3.8. The above Special Bench decision delivered in assessee's own case has not been followed by the Commissioner of Income-tax(Appeals) in the present case. According to the Commissioner of Income-tax(Appeals), the

correct law on this issue has been laid down by the Hon'ble Supreme Court in the case of CIT vs. Calcutta Stock Exchange Association Ltd., 36 ITR 222 and in the case of Delhi Stock Exchange Association Ltd. vs. CIT, 41 ITR 495. The Commissioner of Income-tax(Appeals) observed that the above two judgments of the Hon'ble Supreme Court were not placed before the Special Bench of the Tribunal when the matter was heard. Ultimately, the Commissioner of Income-tax(Appeals) followed the above stated judgments of the Hon'ble Supreme Court and held that the assessee is not justified in treating 40% of the membership collection as deferred to be spread over the currency of membership enjoyed by a time shareholder. The Commissioner of Income-tax(Appeals) upheld the finding of the assessing authority that the entire hundred per cent of the membership fees is in the nature of income of the year of collection.

3.9. Shri R.Vijayaraghavan, the learned counsel appearing for the assessee submitted that the issue stands covered by the decision of the Income-tax Appellate Tribunal, Special Bench, in assessee's own case as reported in 131 TTJ 1

and, therefore, the Commissioner of Income-tax(Appeals) has erred in upholding the decision of the assessing authority on this issue. He contended that the decision of the Special Bench passed in assessee's own case is binding on the Commissioner of Income-tax(Appeals) and he ought to have allowed the contention of the assessee by following the said decision of the Special Bench.

3.10. Shri Shaji P Jacob, the learned Commissioner of Income-tax appearing for the Revenue, supported the detailed order passed by the Commissioner of Income-tax(Appeals) and contended that the Commissioner of Income-tax(Appeals) was constrained not to follow the Special Bench decision, as decisions of the Hon'ble Supreme Court on the issue are very much available and the Commissioner of Income-tax(Appeals) was bound to follow the judgments of the Hon'ble Supreme Court alone and in these circumstances he is justified in rejecting the contention of the assessee.

3.11. We heard both sides in detail. The decisions of the Hon'ble Supreme Court, relied on by the Commissioner of Income-tax(Appeals), in the case of CIT vs. Calcutta Stock

Exchange Association Ltd., 36 ITR 222 and in the case of Delhi Stock Exchange Association Ltd. vs. CIT, 41 ITR 495, are rendered in the context of collection of membership fees made from stock exchange members. Even though the nature of the services rendered by the stock exchange to the members and the nature of services rendered by the assessee as a holiday home provider are different, still certain basic principles have been pronounced by the Hon'ble Supreme Court in the case of Delhi Stock Exchange Association Ltd. vs. CIT, 41 ITR 495. The Hon'ble Supreme Court has observed that it was not how the assessee treated any monies received, but what was the nature of the receipts in question that was decisive of their taxability and, therefore, the fact that the assessee showed the admission fees as capital in its books was not decisive on the question of their taxability.

3.12. When coming to the minute examination of the facts of the case, we find that membership fee alone is not the obligation collected by the assessee company from its members. The assessee company levies annual charges for the upkeep and maintenance of the resorts and their equipments. Whenever

a member occupies his holiday home portion, he is charged for utilities like power, water, etc. The funds necessary for the annual services rendered by the assessee company to its members are thus annually collected from the members themselves. Therefore, such expenses need not be reserved from the membership fee collected from the members at the time of admission.

3.13. Further, the holiday home property owned by the assessee company is not maintained for a particular member. The property remains that of the assessee and the assessee has to maintain the property as its business asset irrespective of the number of new members admitted and the number of members remaining in the list for their unexpired period. There is no nexus between a particular member and the maintenance of the holiday home owned by the assessee.

3.14. Further, it is the explanation of the assessee that whenever a member is not provided with accommodation as reserved for, the assessee company is liable to pay liquidated damages to the member and it is necessary for the assessee company to provide for such liabilities as well. But it should be

seen that those liabilities are not in the nature of ascertained liabilities. They are only contingent liabilities. Such situation may or may not arise. The liability is to be settled only if such situation arises. The connected expenses also can be recognized only at that point of time. Therefore, there is no much force in the argument of the assessee that some portion of the membership fee collection should be reserved for meeting such future contingent liabilities.

3.15. From the accountancy point of view also, the 60% and 40% division made by the assessee is very cumbersome and perpetually indefinite. The final recognition of income from these compounding transactions is indefinitely postponed by the assessee. The result is that the future liability stated by the assessee is unmeasurable and unascertainable. In a particular year the assessee admits certain number of members and 60% of their membership fees is treated as income of that particular year and 40% is carried forward to the subsequent 24 assessment years to be spread over evenly. This carry forward adjustment is made year after year. This adds complexity even to the accounting comprehensiveness.

3.16. One of the basic postulates of accountancy is the "going concern" concept. The income and expenditure of an assessee is ascertained on the presumption that the assessee will carry on the business for a long time. If this 'going concern' concept is applied in assessee's case, it is easy to find that the nominal expenditure that may be required for the assessee to meet the expenditure on members for the subsequent years of admission is well compensated by the collection made in those subsequent years of admission. In that manner, the expenses apprehended by the assessee to be incurred in future for the existing members are compensated by the contributions made by the incoming members year after year. Therefore, it is compensating and, practically speaking, there is no need to preserve any portion of the membership fees to meet future liabilities.

3.17. This is mainly for the reason that, as already stated above, the liability of the assessee is to maintain the assets and properties as a whole for carrying on its business and not for a particular member. The assessee is apportioning the membership fees between 60% and 40% on the principle of

individual liability existing between the assessee and its members. The concept of individual liability is hypertechnical.

3.18. Therefore, it is very difficult to agree with the contention of the assessee company that the Revenue Model of apportioning the membership collection between 60% and 40% is justified. We find that the Revenue Model adopted by the assessee is based on hypothesis and not on facts. On the other hand, the Revenue Model of treating the entire membership fee collection as income of the year of collection proposed by the Assessing Officer is more justified.

3.19. It may be in the above context that another Bench of the Income-tax Appellate Tribunal, Chennai has held in the case of Sterling Holiday Resorts (India) Ltd. vs. ACIT, 295 ITR (AT) 162 that the concept of deferred income is alien to the Income-tax Act. Income on its coming into existence attracts tax. The obligation to use the income in a particular manner does not remove it from the category of income even if the obligation is part of the original contract giving rise to the income. The income that is received or deemed to be received in the previous year is exigible to tax.

4. But, inspite of the views expressed above, we find that we are bound to follow the judgment of the Income-tax Appellate Tribunal, Chennai 'B' Special Bench rendered in assessee's own case for the assessment years 1998-99 to 2002-03. In the said decision rendered in the case of ACIT vs. Mahindra Holidays & Resorts (India) Ltd., 131 TTJ (Chennai) (SB) 1, the Special Bench has held that 40% of deferment of membership fee resorted to by the assessee is justified. The said decision of the Special Bench is rendered in assessee's own case in exactly similar circumstances. Therefore, the rule of precedence demands that the decision of the Special Bench must prevail.

5. Accordingly, with due respect, we follow the Special Bench decision rendered in assessee's own case and hold that the assessee is justified in treating only 60% of its membership fee collection as its income of the impugned assessment year.

6. Accordingly, this issue is decided in favour of the assessee and the addition of ₹ 61,78,71,246/- is deleted.

7. The next ground raised by the assessee is that the Commissioner of Income-tax(Appeals) has erred in directing the

Assessing Officer to verify the expenditure of ₹ 3,12,77,264/- and allow it, if the same was incurred on salaries, rent, interest, repairs and furniture. It is the case of the assessee that the entire of such expenditure was allowed by the Tribunal in assessee's own case for the earlier assessment year 1998-99, through their order dated 19-10-2005 passed in ITA No.337(Mds)/2002. In fact, the Commissioner of Income-tax(Appeals) has followed the order of the Income-tax Appellate Tribunal, A-Bench, Chennai, in assessee's own case rendered for the assessment year 1998-99 in ITA No.337(Mds)/2002. It is in the light of the above order of the Tribunal that the Commissioner of Income-tax(Appeals) has directed the Assessing Officer to verify the expenditure and allow those items relating to salaries, rent, interest, repairs and furniture. The Tribunal also had given similar direction for the assessment year 2005-06. The Commissioner of Income-tax(Appeals) has strictly followed the order of the Tribunal. Therefore, we find no merit in this ground raised by the assessee. It fails.

8. The third ground raised by the assessee is that the Commissioner of Income-tax(Appeals) has erred in confirming

the disallowance of set off for loss of ₹ 2,35,60,140/- of M/s. Mahindra Entertainment Ltd. (amalgamating company) in the hands of the assessee (amalgamated company). This ground is dismissed as not pressed.

9. The assessee is partly successful in its appeal filed for the assessment year 2006-07.

10. Next we will consider the appeal filed by the Revenue for the assessment year 2006-07 in ITA No.1762(Mds)/2011.

11. The first issue raised in this appeal filed by the Revenue is that the Commissioner of Income-tax(Appeals) has erred in directing the Assessing Officer to verify the expenditure incurred by the assessee during construction and allow the same if it was incurred on furniture. It is the case of the Revenue that the Commissioner of Income-tax(Appeals) has failed to appreciate that the expenditure on furniture is clearly a capital expenditure, which would not be allowable as revenue expenditure. It is the further case of Revenue that the furniture procured during the construction period were not put to use and not even eligible for depreciation.

11.1. In fact, this issue was decided in assessee's appeal considered for the very same assessment year. The Commissioner of Income-tax(Appeals) has in fact remitted the issue to the Assessing Officer to verify whether the expenditure totaling to ₹ 3,12,77,264/- was incurred on salaries, rent, interest, repairs and furniture and if so proved, deduction to be allowed thereon. In this context the Revenue is aggrieved on the direction pertaining to that of furniture. Expenses relating to salaries, rent, interest and repairs are revenue in nature. But it is the case of the Revenue that the expenditure for the purpose of procuring furniture cannot be revenue expenditure.

11.2. We agree with the argument of the Revenue. Furniture is a capital asset. Rules have provided separate rate of depreciation in the case of furniture and fixtures. They are distinct block of assets. Therefore, the expenses incurred for procuring furniture cannot be allowed as a deduction in the nature of revenue expenditure. As the furniture was not used for the purpose of the business, depreciation also cannot be granted. Therefore, the direction of the Commissioner of Income-tax(Appeals), as far as it related to furniture is

concerned, we vacate the same and hold that the expenditure incurred for procuring furniture needs to be disallowed. This issue is decided in favour of the Revenue.

12. The next ground raised by the Revenue is that the Commissioner of Income-tax(Appeals) has erred in deleting the disallowance of software expenses of ₹ 66,97,954/-. The assessee had acquired licence to use the software for a period of three years. Every year the assessee is making payment as licence fees. As rightly pointed out by the Commissioner of Income-tax(Appeals), it is only a payment of licence fees and the assessee has not acquired any rights. The assessee was having only a permissive right to use the software. The assessee is not enjoying any copyright. In other words, it has not become the asset of the assessee company. Therefore, the Commissioner of Income-tax(Appeals) is justified in treating the amount of ₹ 66,97,954/- as revenue expenditure deductible in computing the income of the assessee company. This issue is decided against the Revenue.

13. The appeal filed by the Revenue for the assessment year 2006-07 is partly successful.

14. Next we will consider the appeal filed by the assessee for the assessment year 2007-08, in ITA No.1615(Mds)/2011.

15. The first ground raised in the appeal is that the Commissioner of Income-tax(Appeals) has erred in confirming the addition of ₹ 98,21,25,733/-. This relates to the 40% of the membership fees deferred by the assessee for future assessment years. In the light of our order for the earlier assessment year 2006-07, this issue is decided in favour of the assessee and the ground is allowed. Accordingly, the addition of ₹ 98,21,25,733/- is deleted.

16. The second ground raised by the assessee is that the Commissioner of Income-tax(Appeals) has erred in directing the Assessing Officer to verify the expenditure of ₹ 72,72,750/- and allow it if the same was incurred on salaries, rent, repairs, interest and furniture. As held for the earlier assessment year 2006-07, this ground raised by the assessee is dismissed.

17. The third ground raised by the assessee is that the Commissioner of Income-tax(Appeals) has erred in confirming the disallowance of market research expenditure of ₹ 85,28,395/- holding it to be capital in nature. The assessee had incurred ₹ 85,28,395/- towards market research expenses for launching a new holiday concept called “zest”. The expenditure was incurred in making payment to M/s.IDEO, which provides design, conceptualization and market research to help the assessee to launch the new business concept. The Commissioner of Income-tax(Appeals), in agreement with the Assessing Officer, found that these expenses related to setting up of another business, different from the business of selling time share units carried on by the assessee company. Therefore, he relied on the judgment of the Hon’ble Bombay High Court in the case of CIT vs. J.K.Chemicals Ltd., 207 ITR 985 and held that those expenses were in fact capital in nature. He accordingly confirmed the disallowance.

17.1. We agree with the lower authorities that the expenses were incurred by the assessee for setting up a new

project. The project did not take place and it was abandoned. But that does not mean that the said expenditure was incurred by the assessee for the purpose of carrying on the business regularly run by the assessee. The expenses were incurred in experimenting a new venture. Therefore, the expenses were capital in nature. If the assessee had successfully implemented the new project, the relevant expenses would have been capitalized by the assessee. Therefore, this ground of the assessee is rejected.

18. The assessee's appeal for the assessment year 2007-08 is partly allowed.

19. Next we will consider the appeal filed by the Revenue for the assessment year 2007-08 in ITA No.1763(Mds)/2011.

20. The first ground raised by the Revenue is in respect of the expenditure relating to furniture. This issue has been considered by us in the appeal filed by the assessee for the earlier assessment year 2006-07. Following the said order, the ground raised by the Revenue is allowed. The assessing

authority is directed to exclude the cost of furniture from the ambit of revenue expenditure, remitted back by the Commissioner of Income-tax(Appeals) for verification of the Assessing Officer.

21. The second ground raised by the Revenue is that the Commissioner of Income-tax(Appeals) has erred in deleting the disallowance of software expenditure of ₹ 39,59,287/-. This issue has been considered by us in the appeal filed by the Revenue for the assessment year 2006-07 and has held that it is only an annual licence payment. In tune with the earlier finding for the assessment year 2006-07, this ground raised by the Revenue is dismissed.

22. The appeal filed by the Revenue for the assessment year 2007-08 is partly allowed.

23. In result, the appeals filed by the assessee as well as the appeals filed by the Revenue are partly allowed.

Orders pronounced on Wednesday, the 17th of October, 2012 at Chennai.

Sd/-	Sd/-
(Vikas Awasthy)	(Dr. O.K.Narayanan)
Judicial Member	Vice-President

Chennai,
Dated, the 17th October, 2012.
V.A.P.

Copy to: 1. Assessee
2. Department
3. CIT
4. CIT(A)
5. DR
6. GF.