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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Reserved on: 3rd September, 2015
Date of Decision: 24th September, 2015

ITA 38/2002

TELETUBE ELECTRONICS LTD. .....Petitioner
Through: Mr. Ajay Vohra, Senior Advocate with Ms. Kavita Jha and Mr. Vaibhav Kulkarni, Advocates.

Versus

COMMISSIONER OF INCOME TAX, DELHI-VI .....Respondent
Through: Mr. Raghvendra K. Singh and Mr.Kamal Sawhney, Advocates.

AND

ITA 132/2002

CIT .....Petitioner
Through: Mr. Raghvendra K. Singh and Mr.Kamal Sawhney, Advocates.

Versus

TELETUBE ELECTRONICS LTD. .....Respondent
Through: Mr. Ajay Vohra, Senior Advocate with Ms. Kavita Jha and Mr. Vaibhav Kulkarni, Advocates.

CORAM:
DR. JUSTICE S. MURALIDHAR
MR. JUSTICE VIBHU BAKHRU

JUDGMENT
24.09.2015

Dr. S. Muralidhar, J.

1. These are two appeals under Section 260A of the Income Tax Act, 1961 ('Act') by the Assessee and the Revenue against the impugned common order dated 28th September 2001 passed by the Income Tax Appellate Tribunal ('ITAT') in ITA No. 892/Del/99 for Assessment Year 1994-95.

Questions of law

2. On 25th November 2002 while admitting the appeals, the following questions of law were framed for consideration:

> "(1) Whether on the facts and circumstances of the case, the Tribunal was right in law in holding that lease for a period of ten years of plant and machinery along with land and building was a capital asset within the meaning of section 2 (14) of the Act?
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> (2) Whether on the facts and circumstances of the case and in law, the Tribunal was right in holding that lease of facilities i.e. plant and machinery along with and building amounted to transfer within the meaning of Section 2(47) of the Act?
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> (3)Whether on the facts and circumstances of the case and in law, the Tribunal was right in holding that transaction of lease of facilities was a case of sale of leasehold rights?
>
> (4) Whether in the facts and circumstances of the case the ITAT erred in holding that the transaction tantamounts to transaction of lease of land, building thereon and lease of plant and machinery and not the sale of plant and machinery itself?

(5) Whether on the facts and circumstances of the case, the ITAT erred in holding that the transaction is chargeable to capital gains under Section 45 but not u/s 50 of the Income tax Act?"

Background facts

3. The Assessee Teletube Electronics Ltd. ('TEL') had two divisions i.e. a picture tube division situated at Ghaziabad in Uttar Pradesh and a glass bulb division at Bhiwadi, Rajasthan for manufacturing glass shells/bulbs for domestic use. The said glass bulb division, which had three lines i.e. Line-I, Line-II and Line-III, became operational during the AY 1984-85. The land on which the Bhiwadi division was situated, i.e. 496/497 RIICO Industrial Area, was given on lease to the Assessee by the Rajasthan Industrial Development and Investment Corporation Limited (RIICO) under a lease deed dated 24th June 1983.

4. During the relevant AY 1994-95, all three lines of the glass bulb division were leased by the Assessee to Samcor Glass Limited, Kota ('SGL'), a joint venture of Samtel India Limited ('SIL') and Corning Inc. of USA ('Corning'). SGL was in the process of setting up manufacturing facilities for "glass panels, funnels and neck" which constitute the basic components for manufacture of black and white television picture tubes. A lease agreement was entered into on 24th February 1994 between the Assessee and the SGL whereby the 'facilities' defined as the "plant and machinery and land and buildings" of the glass bulb division at Bhiwadi, Rajasthan was leased to SGL for a period of 10 years with effect from that date.

5. For the purposes of determining the lease rental to be charged, the Assessee got the business of the glass bulb division valued by M/s. S.S. Kothari & Co., Chartered Accountants (CA). They valued the business as a going concern at Rs.20.72 crores. This formed the basis for fixing the consideration for the facilities leased out. The lease agreement noted that an advance of Rs.3.64 crores had already been paid by SGL to the Assessee on 25th January 1993. The balance sum of Rs.17.09 crores was payable in 16 equal half-yearly instalment with add on interest @14% per month. After accounting for a moratorium of two years, the payment of lease rental was to commence with effect from 1st April 1996. The payment of interest however, was to commence from the date of agreement i.e. 24th February 1994. During the moratorium period, the Assessee was under an obligation to shift the plant and machinery from Bhiwadi and instal it at the premises of SGL at Kota. The cost of shifting was to be reimbursed by SGL.

6. Pursuant to the approval of the draft lease agreement by the financial institutions, Line-II was shifted from Bhiwadi to Kota in April 1993. Lines-I and III were shifted after July 1994. In the return of income filed on 29th November 1994 by the Assessee for AY 1994-95 it disclosed 'nil' income after adjustment of brought forward business losses and allowances. The lease rental receipts from SGL were disclosed as revenue receipts. The Assessee claimed depreciation in respect of the facilities leased out to SGL.

The Assessment Order

7. The case was picked up for scrutiny and various queries were raised by the Assessing Officer ('AO'). On 13th March 1997, the AO issued a show

cause notice ('SCN') requiring the Assessee to explain why the lease agreement should not be treated as a transaction in the nature of sale of the movable/depreciable assets and capital gain not be charged under Section 45 read with Section 50 of the Act. In respect of the said SCN, the Assessee replied on 25th March 1997 contending that the lease could not be treated as 'transfer'.

8. By the order dated 27th March 1997, the AO rejected the above plea and held the lease agreement was in effect a transfer within the meaning of Section 45 read with Section 2 (47) of the Act. The reasons given in the order of the AO for the said conclusion were as under:

(i) The definition of 'transfer' in Section 2(47) of the Act was an inclusive one. On the strength of the decision of the Supreme Court in ***CIT v. Narang Dairy Products 219 ITR 478*** it was held that the term 'transfer' could not be restricted to the kinds of transfer enumerated therein and would include every possible transaction which results in destruction, annihilation, extinction, termination, cessation or cancellation by satisfaction or otherwise of all or any of bundle of rights which the Assessee has in capital assets whether such asset is corporeal or incorporeal. The essence of the lease did not exclude the contextual or ordinary meaning of the word 'transfer'.

(ii) A survey carried out by the Income Tax Department (ITD) on 28th January 1997 showed that the Assessee had not parted with possession of either the land or the building and had only shifted the plant and machinery (barring a few items) to the plant of SGL at Kota. There was no evidence of

any use of the land and building by the SGL. The use by it of the land and building in Bhiwadi on a few occasions was like the use by any other group company of SGL. This made it appear that the land and building was in fact not leased. The survey revealed that a training centre called Samtel Training Centre was in operation in the premises; the front portion of the factory building was being used for theoretical as well as practical teaching; the Administrative Block is converted into a dormitory type accommodation for the trainees and there was a canteen as well as a volley ball and cricket ground. The middle and rear portion of the factory building had a lot of old machinery scrap belonging to SIL, a sister concern of the Assessee. Some plant and machinery like DG Sets, two Compressors, one Transformer, two Diesel Tanks and two LPG Tanks still remained in the factory premises. This made it appear that the premises was still being utilised by the Assessee and its sister concern for their own purposes.

(iii) SGL was to provide plant and machinery for manufacturing the glass component and SIL was to provide sealing facility which in the context could only be plant and machinery. The valuation report of the CA showed that the residual life of the plant and equipment was not more than 8 to 10 years and, therefore, their useful life would come to an end by 2004 and by that time the Black & White Television market would also disappear. The inevitable conclusion was that the sealing facility had been in effect sold for a handsome payment.

(iv) In respect of the lease agreement, the Assessee had itself applied under Section 230A of the Act for a 'no objection certificate' (NOC) in

anticipation of the transfer of the leasehold rights in respect of the land which had been leased to the Assessee by RIICO along with the building and the ownership rights of the plant and machinery. In column 7 (2) of the application the Assessee had stated that its rights, interests, title in the property were "proposed to be transferred" and the nature of the rights is described as the "lease/ownership rights" in the land at Bhiwadi and the ownership rights over the plant and machinery. The name of the transferee/assignee was shown as SGL. Thus even if the transaction was made to appear as an agreement of a lease, it was indeed a transfer of capital asset within the meaning of Section 2 (47) read with Section 45 of the Act.

(v) The routine management of the SGL was in the hands of Samtel Group and the Assessee only had equity participation which had been pledged to RIICO as an additional security. Given the above relationship between the TEL and SGL, it was plain that the SGL was also part of the Samtel Group. From the joint venture (JV) agreement between Corning and SIL, particularly in view of the 'non-compete clause', it was plain that the intention was to get rid of the sealing facility of the Assessee so that the Assessee could not become a competitor. This was also necessitated since the black and white television market was in decline and, therefore, the Assessee ruled itself out from the use of these assets in future. The conclusion, therefore, was that a transfer had taken place of the plant and machinery.

(vi) The basis of valuation of the Assessee as a going concern at Rs.20.729 crores was unreliable since despite the Assessee getting substantial lease

rentals in AY 1995-96 and 1996-97 it had been incurring losses. By resorting to the said device, SGL was shown to be incurring expenditure and Assessee as earning income which was getting absorbed by its losses and carried forward losses. Lines-I and II would have completed their life terms much before the expiry of the lease period and Line-III would have zero life by 2004. Therefore, in terms of the lease agreement, the assets to be reverted to the Assessee would only have scrap value. Consequently, the lease was a transfer attracting capital gains but only in relation to transfer of movable assets. Thus short term capital gains were attracted under Section 50 of the Act.

Order of the CIT (A)

9. The appeal filed by the Assessee was dismissed by the CIT (A) by an order dated 23rd February 1999. The CIT (A) affirmed the factual findings of the AO and concluded that the fact of the use of the Bhiwadi premises by other parties; the shifting of Line-II before the date of the lease; the prohibition on the Appellant carrying on a competing business and other terms of the lease made the transaction of the lease a colourable device.

10. The CIT (A) too held that the application made by the Assessee under Section 230A of the Act revealed that the Assessee's real intention to treat the transaction as one of transfer of plant and machinery by way of sale. The lessee had no use of land and building and whatever use was there was at the behest of the lessee and its sister concern. In terms of Clause 3.1(c) of the lease agreement, the lessee had to take prior written consent from the Assessee for sub-letting or parting with possession of the premises at

Bhiwadi. No such consent had been taken. The questions raised by the AO remained to be satisfactorily answered and, therefore, it is concluded that these were "collusive and shady transactions".

11. The CIT (A) also referred to the statements recorded during the course of the assessment proceedings and the survey in great detail and agreed with the conclusion reached by the AO that the accounting treatment given by SGL revealed that it had started treating the plant and machinery as its own. The total lease value was Rs.20.73 crores and after adjusting the down payment of Rs.3.46 crores, the lessee was due to pay 14% interest on the balance of Rs.17.09 crores. The treatment of Rs.20.73 crores was as if it was due to the lessor in the relevant previous year. This was a case of accrual during a previous year as per the mercantile method of book keeping. Therefore, this was a case of a sham transaction entered into between the lessor and lessee to postpone the liability of taxes. Addition made by the AO under Section 50 of the Act in the sum of Rs.20,30,61,973 was upheld.

Order of the ITAT

12. The Assessee then filed ITA No. 892/Del/99 before the ITAT. The ITAT found that there was no material or evidence on the basis of which the conclusions of the AO could be stated to be justified. The fact that after expiry of the lease the plant and machinery would have very little value since the black and white television market was in a decline was not relevant for coming to the conclusion that there was a sale of plant and machinery. It was not the case of the Revenue that the plant and machinery would continue to remain in possession with the lessee since on expiry of the

period of the lease, the lessee was bound to restore it to the lessor. The Revenue had failed to prove that there was in fact a sale of plant and machinery. There was nothing in the lease deed to show to the contrary. On the other hand the lessee was prohibited from assigning any right on the property to third party and bound to display that the ownership of the plant machinery was with the lessor. Therefore, the ITAT vacated the finding of the AO that there was a sale of plant and machinery and held that there was only a lease thereof.

13. As far as the land and building was concerned, the ITAT observed that the contents of the lease deed clearly showed that there was a grant of lease of the land with building thereon as well as the plant and machinery against huge consideration. The finding of the AO that the Assessee was not dispossessed of the land and building "was based on suspicion and conjectures". The AO had not given any concrete material to prove whether the lease was a sham transaction. Therefore, the conclusion reached by the ITAT was that there was a package deal for lease of the building and plant and machinery. It could not be held to be a colourable device as contended by the Revenue.

14. The ITAT referred to the decisions of the Supreme Court in ***A.R. Krishnamurthy v. CIT (1989) 176 ITR 417 (SC)*** as well as in ***Palshikhar HUF v. CIT 172 ITR 311(SC)*** and held that the transaction of lease would fall within the general meaning of transfer of a capital asset. Therefore, it would be futile to examine whether Section 269UA was applicable. The ITAT held that the Explanation to Section 2(47) could be invoked only

where the transaction did not fall either in the general meaning of the word 'transfer' or within any of the sub-clauses in Section 2 (47) of the Act. The meaning of transfer in Section 269UA(f) has to be restricted for the purposes of Chapter XXC. The ITAT also held that merely because the payment of instalment was shown as lease rental, it could not be said that the instalments paid did not form part of the price. Once the price of the asset was fixed it was between the parties to decide about the terms of payments which unless prohibited in the statute cannot be gone behind.

15. On an examination of the lease deed, the ITAT held that the leasehold rights in the business assets were sold for Rs.20.729 crore which was undoubtedly agreed to be paid in instalments with interest @ 14 per cent. Consequently, Section 45 was applicable. However, it was held that Section 50 is not applicable since the asset itself was not transferred.

16. As regards the land and building, the ITAT held that their ownership continued to remain with the Assessee. The order of the CIT(A) was modified and the AO was directed to re-compute the capital gain in accordance with law. The AO was also directed to re-adjudicate the consequential issues like depreciation, investment allowance, terminal allowance, etc. in accordance with law.

ITAT's order on the Assessee's application under Section 254 (2)

17. The Assessee moved an application under Section 254(2) of the Act before the ITAT praying for some directions to the AO while computing capital gains as directed in the judgement of the ITAT. In the application,

the Assessee contended that the value of the business was determined by M/s. S.S. Kothari & Company prior to it being given on lease by the Assessee and that in adopting the value the fact that the Assessee was also to go out of business of manufacture of television picture tubes as per the JV Agreement was duly considered. The loss of earning capacity of the Assessee was given weightage in determining the value. According to the Assessee 66.67 % of the value was towards loss of profit earning capacity and, therefore, to that extent the sale consideration was to be split between lease consideration for lease of assets and sum received for the Assessee not indulging in a competing business. A direction was sought to clarify the said position.

18. In the said application, the Tribunal *inter alia* ordered as under:

> "4. After considering the submissions of the parties, we find substance in the submissions of Id counsel of assessee that Tribunal has inherent power to clarify its order, however, subject to the condition that it does not affect or alter the findings recorded by the Tribunal. We are also in agreement with Mr. Sahu that total consideration for sale of leasehold business assets has been determined by the Tribunal and, therefore, the same cannot be altered by any means. However, it is also true that such sale consideration relates to total business assets comprising of various assets such as non depreciable land, buildings, plant and machinery (etc.). There may be different period of holding in respect of such assets and different computation will be required for computing capital gains. It is, therefore, necessary to apportion the sale consideration in respect of various assets which together form the leasehold business assets. Therefore, in the interest of justice and in order to avoid multiplicity of litigation, the AO is directed to bifurcate the sale consideration in respect of different categories of assets and then compute the capital gains

in accordance with the directions given in our order."

Proceedings pursuant to the remand

19. It requires to be noticed that pursuant to the remand of the matter to the AO by the ITAT by its impugned order dated 28th September 2001, the AO by an order dated 11th March 2003 re-determined the long term capital gain at Rs.19,70,66,665 and the short term capital gain at Rs.55,62,066. The Assessee then took up that order in appeal before the CIT(A). The appeal was dismissed by the CIT (A) by order dated 10th November 2003. Against that order the Assessee filed ITA No.59/Del/2004 before the ITAT. By the order dated 18th August 2004, the appeal of the Assessee was partly allowed by the ITAT. That order forms subject matter of ITA No.240/2005 in this Court. Although the said appeal was originally listed together with the present appeals, it has been directed to be listed separately since the outcome of the present appeals will determine the fate of the said appeal.

Subsequent developments

20. Mr. Ajay Vohra, learned Senior Counsel appearing for the Assessee at the outset pointed out that an important subsequent development was that after the 10 year period of the lease agreement dated 24th February 1994 expired, the land and building reverted to the Assessee and was sold by it to three unrelated parties. The Assessee had sought to bring the above facts on record by filing CM No.19803/2014. However, the said application was dismissed by the Court on 4th February, 2015, on the ground that "the facts urged do not reflect on the merits of the case as they relate to assessment of later years." Mr. Vohra nevertheless sought to rely on the assessment orders

and orders in appeal pertaining to the subsequent AYs which record the above transactions.

21. With the leave of the Court, Mr. Vohra placed on record the following documents:

i. Copy of the computation of income of the Appellant for the previous year ended 31st March, 2005.

ii. Copy of the assessment order dated 29th December, 2008 passed under Section 143(3) of the Act for the AY 2005-2006, in the case of the Appellant.

iii. Copy of the order dated 29th July, 2011 passed by the CIT(A) under Section 143(3) of the Act for the AY 2005-2006 in the case of the Appellant.

iv. Copy of the order dated 30th August, 2011 passed by the CIT(A) under Section 143(3) of the Act for the AY 2006-2007 in the case of the Petitioner.

Submissions of counsel for the Revenue

22. In the appeal filed by the Revenue, it was submitted by Mr. Raghvendra Singh, learned Junior Standing Counsel for the Revenue, that the lease agreement was an exercise in tax -avoidance and, therefore, both the AO and the CIT(A) rightly held that the real transaction was one of sale of the assets constituting transfer and attracting capital gains under Section 45 read with Section 50 of the Act. He submitted that the ITAT ignored the facts revealed in the survey that was undertaken in the premises of the Assessee on 28th January 1997. The survey made it plain that only the possession of plant and

machinery was given to SGL whereas the land and building were retained by the Assessee for the purposes of running a training centre. No goods belonging to the lessee SGL were found in the premises. Further it was revealed that the Line 2 of the plant and machinery at Bhiwadi had been shifted from April 1993 itself, i.e. prior to the date of the lease agreement.

23. Mr. Singh further submitted that it is unlikely that there would be a lease for a value of Rs.20.729 crore which was the entire value of the Assessee as a going concern if indeed what was being transferred was only the leasehold rights. Mr. Singh placed considerable reliance upon the application made by the Assessee under Section 230A of the Act seeking permission for transfer of the leasehold rights in the land at Bhiwadi together with the building and plant and machinery. He submitted that had such transaction not amounted to a transfer, there was no need for the Assessee to have made any such application in the first place.

24. Mr. Singh submitted that the findings of the ITAT were contradictory as effectively it made it impossible to tax the amount as short term capital gain or to tax the lease rentals as income. He submitted that the parties to the lease agreement had entered into a colourable device by resorting to dubious methods and subterfuges and that the Assessee could not seek to take shelter behind a draft agreement not recognised by law.

25. Mr. Singh submitted that there was no answer to the Revenue's contention that the residual value of the plant and machinery after termination of the lease would be negligible and this when seen in light of

the consideration of the transfer, i.e. Rs.20.729 crore, it was evident that the intention was to sell the plant and machinery to the lessee. Mr. Singh referred to the decisions in ***Vodafone International Holdings BV v. Union of India (2012) 341 ITR 1*** and ***CIT v. Shivraj Gupta(2015) 372 ITR 337 (Del.)***.

Submissions of counsel for the Assessee

26. In reply Mr. Vohra submitted that it was not possible to dissect the lease agreement and hold that while the giving on lease the plant and machinery was valid, the lease of the land and building was a sham transaction. It is inconceivable that the mere plant and machinery would be leased for Rs.20.729 crore. According to Mr. Vohra the terms of the lease agreement clearly indicated that the lessee had no right to title and interest and the leased property which had to revert to the lessor at the end of the period of lease.

27. Mr. Vohra referred to Section 2 (47) (vi) read with Explanation 1 thereto of the Act which defines 'transfer' and read it along with the definition of 'immovable property' under 269 UA (d) (i) and (ii) of the Act and the word 'transfer' in Section 269 UA (f) (i). He submitted that inasmuch as the lease was for a period of less than twelve years, there was no 'transfer' of a capital asset as defined under Section 2 (14) of the Act. Mr. Vohra pointed out that Section 50B was a special provision for computation of capital gains in case of a slump sale which is inserted with effect from 1st April 2000. Under Section 50B (1) profits or gains arising from a slump sale would be chargeable to income tax as capital gains arising from the transfer of long

term capital assets and which shall be deemed to be the income of the previous year in which the transfer took place. The proviso stated that where the undertaking was held to be for not more than 36 months immediately preceding the date of transfer it would be deemed to be the capital gains arising from the transfer of short-term capital assets. If it was the case of the Revenue that there was in fact any such slump sale the treatment itself would be very different and the question of any disallowance as a revenue expenditure would not even arise. He pointed out that the Revenue was unclear whether the transaction was a lease or a sale.

28. Emphasising that the substance of the transaction was only a lease, Mr. Vohra submitted that the actual terms of the lease deed have to be looked into to determine what the intention of the parties was. He contrasted the transaction in the present case with the kind of transaction envisaged by Explanation 4A to Section 43(1) of the Act which is a sale-cum-lease transaction. He also referred to the decisions in ***Commissioner of Income Tax v. Cosmo Films Ltd. [2011] 12 taxmann.com 217 (Del)*** and ***Commissioner of Income Tax v. George Willamson (Assam) Limited [2004] 136 Taxmann 52 (Gau.)***. He submitted that the lease agreement was not intended as a tax avoidance device. The consideration was fixed on the basis of the value of the entire going concern because of the opportunity loss of the lessor.

29. Mr. Vohra distinguished the decisions in ***Traders and Miners Ltd. v. CIT (1955) 27 ITR 341 (Patna)*** and ***A.R. Krishnamurthy*** (*supra*) where the context was the grant of lease of mining rights and which therefore was of a

very different character. In this context he also referred to the decisions in ***Sun Engineering 198 ITR 227 (SC)*** and ***R.K. Palshikhar HUF*** (*supra*).

Rejoinder submissions of the Revenue

30. In rejoinder Mr. Raghvendra Singh, learned counsel for the Revenue referred to the decision in ***Shin Satellite Public Co. Ltd. v. Jain Studios Ltd. (2006) 2 SCC 628*** in support of his submission that the lease of the plant and machinery was capable of being severed from the lease of the land and building. He submitted that the consistent position taken by the Revenue throughout was that the lease of land and building was sham and it was in fact the Assessee who has, by making an application under Section 230A of the Act, been taking contradictory stands. He submitted that the fact that the lessee continued to be possession of the land and building could not be ignored. The transaction as a whole had to be examined for determining what in fact was sought to be brought out by the parties. He referred to the internal evidence rule explained in ***Goyal Gases (P) Ltd. v. CIT 227 ITR 536 (Del)*** and submitted that it was open to the Revenue to go behind the words used in the lease agreement.

31. According to Mr. Singh, the wording of Section 2 (47) (vi) of the Act was wide enough to include the transaction in question and, therefore, it amounted to 'transfer' of a capital asset. According to him, Section 269UA(d)(ii) read with Section 269UA(f)(ii) expanded the scope of the definition rather than narrowing it. He also referred to Sections 105 and 108 of the Transfer of Property Act, 1882 (‘TP Act’).

Is the leasehold right a capital asset under Section 2 (14)?

32. The first issue that is required to be considered is whether the leasehold rights in the plant and machinery, land and buildings is a 'capital asset' within the meaning of Section 2 (14) of the Act.

33. Section 2 (14) (a) of the Act defines 'capital asset' to mean "property of any kind held by an Assessee, whether or not connected with his business or profession." The exceptions are set out in sub-clauses (i) to (vi). It is not the case of even the Assessee that the property in question falls within any of those exceptions. The words "any kind" which follow the word "property' in Section 2 (47) (a) reflects the legislative intent to bring within its fold even a lease of immovable property. However, the duration of the lease would be a critical factor in determining whether the property in question, viz., leasehold rights would be a capital asset.

34. For a lease of an immovable property defined as such in Section 105 of the TP Act to be a capital asset within the meaning of Section 2 (14) (a) of the Act, the nature of the leasehold right granted to the lessee under the lease deed will have to be examined. For e.g., the Patna High Court in ***Traders and Miners Ltd.*** (*supra*) held that lease of land for a period of 99 years was a transfer of interest in the land and creates a right in *rem.* It was held that there is a transfer of interest in favour of the lessee notwithstanding that the property leased reverts to the lessor. This decision was approved by the Supreme Court in ***A.R. Krishnamurthy*** (*supra*). The grant of leasehold rights in a mining lease grants the lessee not only the right to possess and enjoy the property but also exploit it for the minerals. The lessee in a mining

lease can, therefore, exploit the property and change its essential features and substratum with the permission of the lessor. This right, which is more than a mere right to possess a property to the exclusion of everyone else for a limited period, could partake the character of a capital asset.

35. However, in the present case, where the question arises in the context of the next question whether the lease deed results in a transfer of a 'capital asset', the answer will have to be found from a careful reading of the causes of the lease agreement itself. While *de hors* the context, it might be possible in theory for a leasehold right to be construed as a capital asset since the words used in Section 2 (14) (a) are indeed of a wide amplitude, in the context of the present case, where under the lease agreement dated 24th February 1994 what is given to SGL is a limited right to hold and possess the facilities leased to it for a limited period of ten years, with further restriction on sub-letting it or transferring any right or interest therein to anyone without the permission of the lessor and with the lease agreement making it explicit that at the end of the lease period the facilities leased it SGL would revert to the Assessee, it is difficult to hold that the leasehold rights given to the Assessee under the lease agreement is a 'capital asset'.

36. Consequently, question (1) is answered by holding that the leasehold right, given to SGL for a period of ten years, of the plant and machinery along with land and building, is not a 'capital asset' within the meaning of Section 2 (14) (a) of the Act.

Was there a 'transfer' of a capital asset?

37. Assuming that that the leasehold rights under the lease agreement dated 24th February 1994 is a capital asset, the next question, which is by far the most crucial as far as the present appeals are concerned, is whether in the facts and circumstances the lease of the plant and machinery along with the land and building would amount to a 'transfer in relation to a capital asset' within the meaning of Section 2 (47) of the Act?

38. Section 2 (47) (vi) of the Act defines transfer to mean any transaction, whether "by way of any agreement or any arrangement or in any other manner whatsoever", which has the effect of "transferring, or enabling the enjoyment of, any immovable property." Explanation 1 to Section 2 (47) states that for the purposes of sub-clause (vi), "immovable property" shall have the same meaning as in clause (d) of Section 269UA. This insertion is given retrospective effect from 1st April, 1962.

39. Section 269UA (d) has, therefore, been incorporated by reference into Section 2 (47) (vi). It defines "immovable property" to mean:

> "269UA.
> (d) "immovable property" means-
>
> (i) any land or any building or part of a building, and includes, where any land or any building or part of a building is to be transferred together with any machinery, plant, furniture, fittings or other things, such machinery, plant, furniture, fittings or other things also.
>
> Explanation.- For the purposes of this sub- clause," land, building, part of a building, machinery, plant, furniture, fittings

and other things" **include any rights therein**;

(ii) any rights in or with respect to any land or any building or a part of a building (whether or not including any machinery, plant, furniture, fittings or other things, therein) which has been constructed or which is to be constructed, accruing or arising from any transaction (whether by way of becoming a member of, or acquiring shares in, a co- operative society, company or other association of persons or by way of any agreement or any arrangement of whatever nature), **not being a transaction by way of sale, exchange or lease of such land, building or part of a building**;" (emphasis supplied)

40. The combined reading of both the above sub-clauses makes it clear that the kind of right which is transferred under the lease agreement in question viz., leasehold right, can be relatable to sub-clause (i) of Section 269 UA (d) and not sub-clause (ii). That is not the end of the matter. The word 'transfer' for the purposes of Section 269UA (d) (i) has been defined under Section 269UA(f)(i) which states that:

"269UA.
(*f*) "transfer"

(i) in relation to any immovable property referred to in sub-clause (*i*) of clause (*d*), means transfer of such property by way of sale or exchange or lease for a term of **not less than twelve years**, and includes allowing the possession of such property to be taken or retained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882 (4 of 1882).
Explanation.—For the purposes of this sub-clause, a lease which provides for the extension of the term thereof by a further term or terms shall be deemed to be a lease for a term of not less than twelve years, if the aggregate of the term for which such lease is to be granted and the further term or terms for which it can be so extended is not less than twelve years;"

(emphasis supplied)

41. The case of the Assessee is that by virtue of Explanation (1) to Section 2 (47), Section 269UA (d) (i) is attracted. Section 269UA(f)(i) describes 'transfer' for the purposes of Section 269 UA (d) (i) to mean the transfer of property, including by way of lease, "for a term not less than twelve years." Therefore, in the present case the Assessee is right in contending that since the lease is for a period of ten years, there is no 'transfer' of a capital asset within the meaning of Section 2 (47) (vi) of the Act read with Explanation 1 thereto.

42. The ITAT rejected the above contention since according to it the transaction of lease fell within the general meaning of 'transfer'. According to the ITAT Explanation 1 could be invoked only where the transaction did not fall under the general meaning of the word 'transfer' or the items listed at sub-clauses (i) to (v). It further pointed out that while the legislature had incorporated Section 269UA(d) "it would be illegal to further incorporate the meaning of the words 'transfer' as defined in Section 269UA(f)." It was held that the meaning of transfer in Section 269UA(f) had to be restricted only for the purposes of Chapter XXC.

43. The Court is unable to agree with the above approach of the ITAT to interpreting what appear to be plain and unambiguous provisions of the Act. It is useful to recall that this entire discussion is in the backdrop of what constitutes 'transfer' in relation to a capital asset. Further, the entire exercise is for ultimately determining if there has been any capital gains arising from

the transaction. Under Section 45(1) 'capital gains' are any profits or gains arising from the transfer of a capital asset effected in the previous year. When the word ‘transfer’ itself has been defined under Section 2(47) (vi) and by virtue of Explanation 1 "shall" have the same meaning as Section 269UA(d) then it is not possible to 'restrict' Explanation 1 to only those transactions described in Chapter XXC. Explanation 1 is a deeming fiction and incorporates by way of reference the provisions of Section 269 UA (d) in order to understand the meaning of the word 'transfer' for the purposes of Section 2 (47) (vi). Therefore, that entire scheme has to be given effect to. In other words, it is not possible to omit the reference to Section 269UA(d) (i) which in turn brings in Section 269UA(f) (i). The ITAT has therefore erred in conveniently choosing to not apply the Explanation 1 to Section 2 (47) in order to arrive at the conclusion there was indeed a 'transfer' of a capital asset brought about by the lease agreement in question.

44. The AO, the CIT (A) and the ITAT have relied on the decisions in ***Traders and Miners Ltd.*** (*supra*), ***A.R. Krishnamurthy*** (*supra*) and ***CIT v. Narang Diary Products (1996) 219 ITR 478 (SC)***. Reference has also been made to Section 2 (47) (ii) which talks of the "extinguishment of rights".

45. If the lease agreement dated 24th February 1994 is read carefully it is clear that no proprietary right is created in favour of SGL thereunder. Clause 3.1(c) which provides that the lessee, i.e. SGL, during the term of the lease shall not assign, sublet or part with possession of the facilities or any part thereof without the written consent of the lessor. Clause 3.1(n) prohibits the lessee from transferring or assigning or otherwise disposing of its rights

and obligations whether by way of mortgage, charge, sub-lease, sale or assignment. Clause 3.1(i) states that the lessee would not claim any right, title or interest over the facilities other than the rights granted by the lessor.

46. The decisions relied upon by the ITAT pertained to mining leases which stand on an entirely different footing. In ***Traders and Miners Ltd.*** (*supra*), the lease was for 99 years. The subject matter of the lease was not merely the right to hold the land but also exploit the valuable interest in the land, i.e. right to extract minerals therefrom. The consideration for the lease was the combination of a *salami* and a yearly reserve rent. Capital gain was charged with reference to the *salami* and not the yearly reserve rent.

47. In ***A.R. Krishnamurthy*** (*supra*) the mining rights were leased for a period of ten years. The consideration was a premium of Rs. 5 lakhs plus a royalty of Rs.12 per sq. cubic ft of clay extracted subject to a minimum of Rs. 60,000 per year. Interestingly, the fact that there was a transfer of a capital asset was not contested by the Assessee in that case. The right transferred by the lease deed was the right to exploit the land and extract the clay which flowed from the ownership of the land. This was therefore more than a mere right to possess the property without any other right to alter the nature or structure of the land or extract anything therefrom which is what has been transferred under the lease agreement in the present case. No premium has been paid by the lessee and SGL has not been granted any proprietary right in the land or the building.

48. In ***R.K. Palshikhar*** (*supra*), the Assessee had obtained permission to

develop agricultural land to make it suitable for a housing colony. Thereafter he sub-divided the land into plots and gave them on 99 year lease. This was held to be a transfer in relation to a capital asset within the meaning of Section 12 B of the Income Tax Act 1922. One more fact distinguishing that case from the present one was that the consideration for the 99 year lease was *salami* and not the yearly rent. The capital gain was charged with reference to the *salami*. Here again, no dispute was raised that the land itself constituted a capital asset.

49. In ***CIT v. Narang Diary*** (*supra*), the issue concerned the interpretation of the words "otherwise transferred" in Section 33 of the Act. The context was the provision of rebate in respect of a new machinery and plant owned by an assessee and wholly used for the purpose of business. In that context it was held that not only ownership but also the exclusive use of the assets by the assessee was essential for claiming rebate. Under Section 45 there is no requirement of exclusive use by the owner of the asset.

50. The mere fact that the Assessee may have applied under Section 230A of the Act to seek permission of the Department cannot be held against it as far as the correct legal position is concerned. In other words the fact that certain columns in the concerned form were filled by the Assessee to imply that there was a transfer of leasehold/ownership rights cannot be read to constitute a waiver by the Assessee of the legal defences that flow from a correct interpretation of the clauses of the lease agreement and from a correct reading of Section 2 (47) with Section 45 of the Act.

51. The ITAT has itself observed that the mere fact that the land and building may not have been used by the lessee or that after expiry of the lease the plant and machinery would have very little value since the black and white television market was in a decline were by themselves not relevant for coming to the conclusion that there was a sale of plant and machinery or of the leasehold rights in the land and building. The lease agreement had to form the fundamental basis for understanding what the transaction in effect was. The relationship between the parties could not have been re-configured on the basis of surmises and conjectures. The AO and CIT (A) appeared to have proceeded on the basic suspicion that the lease agreement was a tax avoidance device and this prevented them from objectively viewing the transaction for what it in effect was. The decision in ***CIT v. Cosmo Films Ltd.*** (*supra*) reiterated the settled legal position that the court would have to find out as to what was the real intention of the parties in entering into the agreement and that "such intention has to be gathered from the words in the said agreement in a tangible and in an objective manner and not upon a hypothetical assessment of the supposed motive of the Assessee to avoid tax." In ***CIT v. George Willamson (Assam) Limited*** (*supra*) the Court citing the decision of the Supreme Court in ***Union of India v. Azadi Bachao Andolan [2003] 132 Taxman 373 (SC)*** observed: "It is open for Assessees to arrange their affairs in such a manner that it would not attract the tax liabilities, so far as it can be managed within the permissible limit of the law. Tax management is permissible, if the law authorises so."

52. Recently, in ***Vodafone International Holdings BV*** (*supra*) the Supreme

Court explained the legal position regarding tax avoidance as under:

> "68. .....In the application of a judicial anti-avoidance rule, the Revenue may invoke the "substance over form" principle or "piercing the corporate veil" test only after it is able to establish on the basis of the facts and circumstances surrounding the transaction that the impugned transaction is a sham or tax avoidant. To give an example, if a structure is used for circular trading or round tripping or to pay bribes then such transactions, though having a legal form, should be discarded by applying the test of fiscal nullity. Similarly, in a case where the Revenue finds that in a Holding Structure an entity which has no commercial/business substance has been interposed only to avoid tax then in such cases applying the test of fiscal nullity it would be open to the Revenue to discard such interpositioning of that entity. However, this has to be done at the threshold. In this connection, we may reiterate the "look at" principle enunciated in *Ramsay* (supra) in which it was held that the Revenue or the Court must look at a document or a transaction in a context to which it properly belongs to. It is the task of the Revenue/Court to ascertain the legal nature of the transaction and while doing so it has to look at the entire transaction as a whole and not to adopt a dissecting approach. The Revenue cannot start with the question as to whether the impugned transaction is a tax deferment/saving device but that it should apply the "look at" test to ascertain its true legal nature [See *Craven v. White* (supra) which further observed that genuine strategic tax planning has not been abandoned by any decision of the English Courts till date]."

53. This Court is also unable to agree with the contention of the learned counsel for the Revenue that the lease of the plant and machinery can be separated from the lease of the land and buildings and the former transaction held to be valid and the latter a sham transaction. The Court is of the view that the context in which the decision in ***Shin Satellite Public Co. Ltd. v. Jain Studios Ltd.*** (*supra*) was rendered was entirely different from the

present case and that decision is of no assistance to the Revenue here.

Was there a 'sale' of leasehold rights?

54. This brings us to question Nos.3 and 4, i.e. whether a transaction pertaining to land and building or of plant and machinery could be treated as sale of either the leasehold rights in respect of the land or the sale of the plant and machinery itself?

55. There seems to be a contradiction in the order of the ITAT where in para 46 it states that in the present case the land is not a depreciable asset and that as far as the building and plant and machinery were concerned, the ownership thereof remained in the Assessee and, therefore, it could not be said that either the asset itself have been sold or the block of assets ceased to be in existence." The ITAT appears to acknowledge that the ownership of the assets continued with the Assessee. However, the ITAT proceeded to hold that the "leasehold rights" and "not the asset itself" was sold. It is not understood how the ITAT has arrived at the concept of sale of leasehold rights because a sale connotes absolute transfer of rights with no reversion of any part thereof to the original owner. There has to be an extinguishment of ownership rights in order that a transaction can be said to be a 'sale'. Here, as noted earlier, the lessee does not even have the right of sub-letting the facilities. The leasehold right is only for a period of ten years and at the end of that period the leased facilities revert to the owner. Consequently, the Court is unable to agree with the conclusion of the ITAT that in the present case there was a "sale" of leasehold rights by virtue of the lease agreement in question.

56. What appears to have weighed with the ITAT is the valuation of the business as a going concern and the said valuation forming the basis for determining the consideration for the grant of the lease and fixing of the yearly lease rentals. The explanation offered by the Assessee that the fact that it was not going to be in control of the assets or use them for its business, that there was going to be a loss of business opportunity which, therefore, had to be compensated and this weighed with the CAs in fixing the valuation appears to be a plausible one. While there is a non-compete in the agreement between the TEL and SGL, that by itself does not lead to the conclusion that the transaction of lease was in fact one of sale.

57. In any event this whole hypothesis stands disproved by the fact that on the expiry of the lease period, the land, building and plant and machinery reverted to the Assessee. The land and the building were sold by the Assessee to an unrelated third party. The said transactions formed the subject matter of the Assessment order for the AY 2006-07. The order of the CIT (A) dated 30th August 2011 has been perused by the Court. It holds that the sale of the land by the Assessee to an unrelated third party, M/s. Blossom Automotives, for a consideration of Rs. 4.01 crores took place on 8th September 2005 and after accepting the Assessee's valuation of the said land the CIT (A) has directed that the Assessee be taxed on long term capital gains arising out of the said sale of the land. The said order also shows that for the building, which was also sold as part of the sale of land, the Assessee has continued to claim depreciation till the date of such sale. The fact that the Assessee continued to claim depreciation on the plant and machinery and building is another indication that the Assessee continued to assert

ownership of the assets in question during the relevant AYs. The above order of the CIT (A) forms part of the records of the Department and has naturally not been disputed by it. Although this development could not have been anticipated at the time the AO or the CIT (A) decided the issue in the present case, it completely vindicates the Assessee's stand in relation to the nature of the transaction forming the subject matter of the lease agreement.

58. Consequently, there are several factors in favour of the Assessee that persuade the Court to hold, with reference to question Nos. 3 and 4 that the ITAT was not right in holding that the transaction of lease of the facilities was a sale of leasehold rights and that there was in any event a sale of the plant and machinery. The Court answers question Nos.3 and 4 in favour of the Assessee and against the Revenue.

Was there a capital gain under Section 45?

59. The last question that requires to be addressed whether there could be said to be any capital gains under Section 45 of the Act? In light of the above discussion, the question will have to be answered in favour of the Assessee and against the Revenue. The Court is of the view that the transaction in question was nothing more than a transaction of lease and has been acted upon by the parties as such. This was not a device adopted by the Assessee for tax avoidance.

60. The question No.5 is accordingly answered in favour of the Assessee and against the Revenue. It is held that the ITAT erred in holding that the transaction in question was chargeable to capital gain under Section 45 of

the Act. There was no occasion for the ITAT to remand the matter to the AO for re-computation of the capital gains.

Conclusion

61. The impugned order of the ITAT to the above extent is set aside and the appeal of the Assessee is allowed. The Revenue's appeal is dismissed.

S. MURALIDHAR, J

VIBHU BAKHRU, J

SEPTEMBER 24, 2015
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