THE HONBLE SRI JUSTICE DILIP B.BHOSALE AND THE HONBLE SRI JUSTICE A.RAMALINGESWARA RAO

I.T.T.A. No. 316 OF 2003

11-03-2015

The Commissioner of Income Tax Appellant

M/s. Sileman Khan Mahaboob Khan Respondent

Counsel for Appellant :Ms.M.Kiranmai for
Sri J.V.Prasad

Counsel for Respondent : Sri Challa Gunaranjan

<GIST:

>HEAD NOTE:

?Cases referred : 1) [(1964) I.T.R. 353]
2) [(1961) 42 I.T.R. 49 (S.C.)]
3) (1999) 237 I.T.R. 454
4) (2004) 270 I.T.R. 275
5) (1986) 158 I.T.R. 773 (A.P.)
6) [(1999) 240 I.T.R. 5 (A.P.)]
7) AIR 1968 SC 70
8) (2013) 218 Taxman 88
9) (2014) 369 ITR 460 (Karn)
10) Judgment of Madras High Court, dated 01.12.2014

THE HONBLE SRI JUSTICE DILIP B.BHOSALE
AND
THE HONBLE SRI JUSTICE A.RAMALINGESWARA RAO

I.T.T.A. NO. 316 OF 2003

JUDGMENT: (per the Honble Sri Justice Dilip B.Bhosale)

This Income Tax Appeal by the Revenue under Section 260-A of the Income Tax Act, 1961 (for short the Act) is directed against the order of the Income Tax Appellate Tribunal, Visakhapatnam Bench in I.T.A. No. 78/H/96 for the assessment year 1992-1993.

02. The respondent-assessee is a partnership Firm engaged in export of Tobacco. The respondent- assessee filed return of income on 27-08-1992 admitting the net income of Rs. 4,78,520/-. During the previous year relating to the assessment year 1992-93, the assessee had let out his godowns. He offered the rental income for taxation under the head income from business. It is the case of the assessee, as argued by his learned counsel, that the godowns, which he had let out, were being used by him for the business of export of tobacco, and whenever they were not in use, he had given them on lease to third parties and received rent therefrom. He, therefore, claimed before the authorities below, on the basis of Clause.3 of the partnership deed, that the godowns of the firm were let out, as provided for in the said deed and that being a part of their business, the rent received from the lessee should be treated as income from business. It has come on record that such income of the assessee for the earlier years i.e. 1990-91, 1991-92 was assessed as income from property on the ground that no business as such was carried on by the assessee during those years. The assessee had carried that order in appeal before the Commissioner of Income Tax (Appeals), who decided the matter in favour of the assessee treating the entire income as income from business. That order of the appellate authority was challenged by the Revenue before the Income Tax Appellate Tribunal (ITAT). Based on the order of the Appellate Tribunal, passed for the year 1991-92, the assessment for the year 1992-93, impugned in this appeal, was completed, treating the rental income as income from property.

2.1 The CIT(Appeals), in the appeal filed by the assessee, however, held that the income from letting out of the godowns should be treated as income from business and directed the Assessing Officer to grant renewal of registration as a firm. Feeling aggrieved and dissatisfied by the order of the CIT(Appeals), the Revenue filed appeal before the Appellate

Tribunal. The Tribunal confirmed the order of the CIT(Appeals) holding that so long character of the godown is retained as a godown, it should be treated as a commercial asset and its rental income must be treated as an exploitation of commercial asset in the nature of trade. In short, the order of the CIT(Appeals) was confirmed by the Appellate Tribunal, which is the subject matter of the instant appeal.

03. In this backdrop, though at the stage of admitting the appeal on 04-02-2004 no substantial question of law was formulated, in our opinion, the following questions fall for our consideration:

1. Whether on the facts and in the circumstances of the case, the Tribunal was justified in law in holding the income from letting out of the godowns as income from business?

2. Whether on the facts and in the circumstances of the case, the Tribunal was justified in not recording any finding as to entitlement of the assessee for continuation of Registration as a firm?

04. We have heard learned counsel for the parties and with their assistance gone through the judgments relied upon by the parties in support of their contentions. It would be relevant at this stage to make brief reference to the judgments relied upon by learned counsel in support of their contentions.

4.1 In Sultan Brothers Private Limited V. Commissioner of Income-Tax, Bombay City II( ) the five Judge bench of the Supreme Court considered the question, how the income received as rent and hire is to be assessed, that is, under which section of Income Tax Act, 1922, (for short 1922 Act) is it assessable? According to the assessee in that case, the entire income ought to have been assessed under Section 10 as the income of a business or, in the alternative, under Section 12 as the income from residuary source, that is, a source not specified in the preceding Sections 7 to 11, with the allowances respectively specified in Sub-sections (3) and (4) of that Section. The appellant was a limited Company, which was owner of a certain building constructed on Plot No.

7 on the Church Gate Reclamation in Bombay which it had fitted up with furniture and fixtures for being run as a hotel. By a lease dated August 30, 1949, the assessee had let out the building fully equipped and furnished to one Voyantzis for a term of six years from 09-12-1946 for running a hotel and for certain other ancillary purposes. The lease provided for a monthly rent of Rs. 5,950/- for the building and hire of Rs. 5,000/- for the furniture and fixtures. In this backdrop, the aforementioned question fell for consideration of the Supreme Court. One of the objects of the assessee- Company in Sultan Brothers Case (supra) was to acquire land and building and to turn the same into account by construction and reconstruction, decoration, furnishing and maintenance of them and by leasing and selling the same. The Supreme Court observed that the activity contemplated in the aforesaid object of the Company, assuming it to be a business activity, would not by itself turn the lease in the present case into a business deal. It also referred its judgment in East India Housing and Land Development Trust Ltd. V. Commissioner of Income-tax, West Bengal( ) and observed that the income derived by the company from shops and stalls is income received from property and falls under the specific head described in Section 9. The character of that income is not altered because it is received by a company formed with the object of developing and setting up markets. Then the Supreme Court considered the question and observed that it is true, the rent for the building and the hire for furniture were separately reserved in the lease but that does not make the two lettings separable. Then after referring to the Clauses in the lease, further observed that the building and fixtures were to be used for one purpose, namely, for the purpose of running a hotel with them all together. The lessee was not to remove any article or things from the premises except for the purposes of and in the course of hotel business which latter would be for effecting repair to them or for replacing them where it was duty of the lessee to do so under the lease. In the light of these Clauses, the Supreme Court held that the lease clearly established the parties intention that the furniture and fixtures and the building should be enjoyed altogether and not one separately from other.

4.2 In the result the Supreme Court held that the rent from the building will be computed separately from the income from the furniture and fixtures and in the case of rent from the building the appellant would be entitled to the allowances mentioned in Sub-section (4) of Section 12 and in the case of income from the furniture and fixtures, to those mentioned in Sub-section (3) and that no part of the income can be assessed under Section 9 or under Section 10 of the 1922 Act. The Sections 22, 28 and 56 of the Income Tax Act, 1961 are corresponding to Sections 9, 10 and 12 of 1922 Act.

4.3 In Universal Plast Ltd. V. Commissioner of Income-Tax( ), the Supreme Court was dealing with the case where Tribunal found that the leasing of the factory was not a sequel to the assessees decision to go out of the business in respect of the subject factory and that it was just a make-shift transient alternative means of commercial exploitation of the commercial assets. Against this finding, the Calcutta High Court after referring to various Clauses in lease agreement, held that the assessee decided to go out of the business as far as this particular factory was concerned, the lease agreement was in fact a veiled agreement for lease-cum-sale and it could not be in the contemplation of the assessee, at the time of it entering into the license agreement, to retain the assets, any more as a commercial asset. In this backdrop, the High Court had framed the question Whether, on the facts and in the circumstances of the case, the Tribunal was correct in law in holding that the income received by the assessee by leasing out the factory was business income? This question was answered by the High Court in the negative-in favour of the Revenue and against the assessee. The Supreme Court while dealing with the case affirmed the decision of Calcutta High Court and held that the income of the assessee was not assessable as business income.

4.4 This Court in Commissioner of Income-Tax. v. Y.Narayana Murthy( ) considered the question whether, on the facts and in the circumstances of the case and in law, the Appellate Tribunal was justified in holding that letting out the godowns would amount to carrying on of business within the meaning of the Partnership Act disregarding the decision of the High Court in R.C. No. 118 of 1980, dated November 29,

1984 in the case of CIT V. Phabiomal and Sons( ). In this case the assessee had derived income from letting out the godowns to the Food Corporation of India (F.C.I.) for the assessment years 1979-80 and 1980-81. The Commissioner had taken a view that income derived from the letting out of godowns was assessable as income from the property and not from business and further held that the assessee was not entitled to the registration for assessment year 1979-80 and continuation of registration for the assessment year 1980-81. Accordingly, directions were issued to take the status of the assessee as an association of persons for the relevant assessment years 1979-80 and 1980-81. Consequently, the Assessing Officer passed the order for the assessment year 1979-80 which was upheld by the Appellate Assistant Commissioner. The assessing authority assessed the rental income as income from house property for the assessment years 1981-82 and it was upheld by the Commissioner of Income-Tax (Appeals). The Tribunal upheld the order of the Commissioner for the assessment years 1981-82 that the income derived from letting out the godowns was assessable as income from property. It, however, took the view that the letting out of the godowns to the F.C.I. would amount to exploiting the commercial asset and to carrying on of a business within the meaning of the Partnership Act. The Tribunal, therefore, held that the assessee was entitled to registration for assessment years 1979-80 and continuation of registration for the assessment year 1980-81. On a reference, this Court held that the expression business contemplates continuous activity from year to year. It was not the case of the assessee that it was in the business of construction of godowns and letting them out from year to year either to the F.C.I. or to any other interested person or persons, as the case may be. Therefore, the assessee was not continuing the activity of construction of godowns and letting them out from year to year. There was no evidence to suggest that the assessee had undertaken any such systematic business activity of construction of godowns and letting them out as business property. Thus, it was held that the Assessing Officer rightly assessed the income derived by the assessee as that of the income from the property and not from business. Consequently, it was held that the assessee

was not entitled to registration or continuation of the same in terms of Section 185 (1)(a) of the Act.

4.5 In Commissioner of Income-Tax v. Veerabhadra Industries( ), this Court had taken the similar view, as was taken in Y.Narayana Murthy (supra) holding the single act of constructing godowns and letting it out cannot be treated as a business. The expression business contemplates continuous activity from year to year. There was no evidence that the assessee was continuing the activity of constructing godowns and letting them out from year to year. There was no material that it had constructed a godown in the relevant year. Therefore, the income from a simple letting out of the godown would not be treated as a business income for the purpose of Income-Tax Act. When once it was not business income, the question of availing of benefit under Section 185(1)(a) would not arise.

4.6 In East India Housing and Land Development Trust Ltd. (supra), the Supreme Court dealt with a case of a Company which was incorporated with the objects of buying and developing landed properties and promoting and developing markets. It had purchased 10 bighas of land in the town of Calcutta and had set up a market therein. The question was whether the income realized from the tenants of the shops and stalls was liable to be taxed as business income under Section 10 of 1922 Act or as income from property under Section 9. In this case, it was contended that income from letting out of the godowns is business income and, therefore, the assessee was entitled for registration under Section 185 (1) (a) of 1922 Act. While dealing with the contention, the Supreme Court observed thus:

. It is difficult to accept the contention of learned counsel for the assessee because a single act of constructing a godown and letting it out cannot be treated as a business. The expression business contemplates continuous activity from year to year. There is no evidence that the assessee is continuing the activity of constructing godowns and letting them out from year to year. There is no material that he has constructed a godown in this year. Therefore, the income from a simple letting out of the godown cannot be treated as

business income for the purpose of the Income-tax Act. When once it is not business income the question of availing of benefit under section 185 (1) (a) of the Act does not arise. The income has to be assessed as income from property in accordance with sections 22 to 27 of the Income-tax Act. We are fortified in our view by a judgment of this court in Phabiomal and Sons case [1986] 158 ITR 773, wherein it was held that letting out a building and realising rents therefrom did not amount to carrying on of business. It is true that the Punjab and Haryana High Court in Nauharcahnd Chananrams case [1971] 82 ITR 189, took the view that letting out of a factory amounts to carrying on business. With respect we disagree with the view expressed by the Punjab and Haryana High Court. The judgment in Lakshmi Companys case [1982] 133 ITR 904 (Mad), is distinguishable from the facts of the case. It is a case where the assessee went on putting up additional constructions and letting it out to various tenants which was in the nature of business activity, because, as pointed out in the earlier paragraph, it is a case where there is continuous activity and therefore that judgment is distinguishable on facts.

(emphasis supplied)

05. Learned counsel for the assessee, in support of his case, placed reliance on the following judgments: Commissioner of Income Tax v. National Storage Pvt. Ltd. Bombay, Commissioner of Income Tax-III v. Velankani Information Systems (P.) Ltd., Commissioner of Income Tax v. Information Technology Park Ltd. and Commissioner of Income Tax III v. M/s.NDR Warehousing Pvt. Ltd., and submitted that the income arising from letting out of the godowns is an income from business and not from property.

5.1 In National Storage Pvt. Ltd. Bombay (supra), the Supreme Court was considering the case of the distributors, who were required to store films only in godowns constructed strictly in conformity with the specifications laid down in the Film Rules and in a place to be approved by the Chief Inspector of Explosives, Government of India. The assessee, after purchasing a plot of land, constructed 13 units thereon. Each unit was divided into four vaults, having a ground floor

for rewinding of films and an upper floor for storage of films. 12 units were meant for the Members of the Indian Motion Picture Distributors Association, who had floated the Company. The Income Tax Officer took the view that the assessee should be assessed under Section 9 of the Income Tax Act, 1922, and not under Section 10 thereof. The Appellate Assistant Commissioner confirmed the said view. The Tribunal held that the income was taxable under Section 10 of the said Act. When the matter came up before the High Court, it was held that where the letting was only incidental and subservient to the main business of the assessee, the income derived from the letting will not be the income from property falling under Section 9 and the exception to Section 9 may also come into operation in such cases. The appeal was dismissed by the Supreme Court. In the instant case before us, the letting out of the godowns is not the main business of the assessee and therefore, income cannot be held to be from the business activity. Thus, this judgment is of no avail to the assessee.

5.2 Similarly, in Velankani Information Systems (P.) Ltd., (supra) the assessee was a real estate developer and was in the business of providing comprehensive facilities to IT industries. The case in Information Technology Park Ltd., (supra) to which one of us is a party (DBB, J), was also a case relating to the letting out buildings along with other amenities in software technology park. In M/s.NDR Warehousing Pvt. Ltd., (supra) the assessee was engaged in the business of warehousing, handling and transport business. Thus, the facts in these cases are different and, hence, these judgments also are of no avail to the assessee.

6. In the present case, the main business of the assessee was the export of tobacco and for that purpose they had constructed godowns. As submitted by the learned counsel for the assessee, the assessee would let out the godowns when they would not require the same and earn rental income therefrom. Apart from letting out the godowns, no other services/amenities, admittedly were extended by the assessee to the lessees. Merely because one of the objectives, in the partnership deed, was to let out the godowns would not mean that the assessee had undertaken the activity of

construction of godowns and letting them out as business activity. Moreover, it is not the case of assessee that letting out of the godowns was continuous activity from year to year. Therefore, in our opinion, the income received by the assessee, by way of rent, was the income received from property and it would not fall under the head income from business. The character of the income would not stand altered because it was received by the firm with one of the objects of the partnership deed to let out their godowns. The income derived from letting out the property, in the facts of the present case, would not amount to profits or gains from the business. In other words, the income earned by letting out the godowns cannot be termed or treated as income from business. From the facts of the present case, it is clear that the assessee could let out their godowns only because those were not in use at the relevant time. Therefore, the rent received by the assessee would have to be computed as income from property. Thus, the first question framed by us is answered against the assessee and in favour of the Revenue, and in view thereof, the second question, as submitted by learned counsel for the parties, does not survive consideration.

07. Accordingly, the Appeal is allowed. No order as to costs.

08. Miscellaneous Petitions, if any, pending in the appeal also stand disposed of.

_____

Dilip B.Bhosale, J

_____

A.Ramalingeswara Rao, J
11th March, 2015.