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

RESERVED ON : 30.10.2012
PRONOUNCED ON: 05.11.2012

\+ **ITA 956/2011 AND ITA 957/2011**

M/S. GAIL INDIA LIMITED ..... Appellant
Through: Sh. Ajay Vohra, Ms. Kavita Jha, Sh. Amit Sachdeva and Sh. Vaibhav Kulkarni, Advocates.

versus

THE JOINT COMMISSIONER OF INCOME TAX ..... Respondent
Through: Sh. Sanjeev Sabharwal, Sr. Standing Counsel with Ms. Gayatri Verma and Sh. Puneet Gupta, Advocates.

CORAM:

MR. JUSTICE S. RAVINDRA BHAT
MR. JUSTICE R.V. EASWAR

MR. JUSTICE S.RAVINDRA BHAT

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1. The assessee in these appeals questions an order of the Income Tax Appellate Tribunal (ITAT) dated 22.01.2010 in ITA Nos.1372/Del/2001 and 1724/Del/2002 in respect of two assessment years. The questions of law were framed by Court in its order dated 11.08.2011 :

Questions of law from order dated 11.08.2011

"(i) Whether in view of the fact that in the earlier year the Tribunal had restored the issue relating to deduction of amortization of lease premium to the Assessing Officer, they ought to have done the same for the year under consideration?

(ii) Whether the premium/lumpsum amount paid in lieu of payment of annual rent for taking land on a long lease would be deductible as rent under Section 30 of the Income Tax Act, 1961?

(iii) whether the premium/lumpsum advance lease rentals paid in consideration for the grant of lease of land is deductible as revenue expenditure under Section 37 of the Income Tax Act, 1961.?"

2. At the outset it was urged on behalf of the assessee that the only question of law which arises is correctness of disallowance directed by the Income Tax authorities, on account of the assessee's amortization cost of land which according to the Revenue constituted capital expenditure.

3. The relevant facts are that the assessee, which is engaged in the manufacture of Hydrocarbon and distribution of natural gas, entered into a lease arrangements with local municipalities, in respect of land. The lease agreements contained certain standard terms. The lease arrangements were for a long period ranging between 60-95 years. The various clauses in the lease agreements in question permitted the appellant to construct buildings upon the lease hands which were to ultimately vest with the landlord upon expiry of term of the lease. These leases were granted on payment of heavy premia upfront and down payment basis. Lease agreements also contained stipulation reserving nominal rent ranging between ₹.1 to ₹.100/- P.A. and in some cases worked out to 2.5% of the premium paid. It is urged that the appellant had claimed deduction of ₹.30,94,464/- towards amortizing of such premia paid for use of land on long term lease. The assessee had contended that the premium paid on lumpsum basis indicated the captalised value or a consolidated lumpsum payment of rent, which would otherwise have been payable annually. The Assessing Officer in respect of both the assessment years in question disallowed the claim for amortized value of lease rentals which was

sought to be on the ground that the lumpsum premium was capital expenditure. The CIT (Appeals) for both the assessment orders rejected the assessee's claim. The Appellate Commissioner rejected the assessee's contention for the assessment years 1999-2000 on the basis of the following reasonings :

> *"6.1 The appellant has submitted before me that various pieces of land have been taken on lease by the company at different places and in all such agreements, the appellant does not have any ownership rights over the land and the lease hold rights are available only for specified periods. In all cases, the land will revert back to its original owner at the end of the lease period. Relying on the decision of the Supreme Court in the case of Empire Jute Company Limited -124-ITR-1 as well as other decisions, it is submitted that since the premium paid in respect of the lease agreements does not result in the acquisition of the capital assets, the payments are in the nature of revenue expenses and the amortization claimed should be allowed. The appellant has also cited a decision of the Karnataka High Court in the case of HMT Limited-203-ITR-820, where it was held that the premium paid for acquiring lease hold rights was only in the nature of advance rent and was, therefore, allowable as revenue expense. In that case, the Court had considered a lease obtained from the Maharashtra Industrial Development Corporation for a period of 95 years on a payment of annual rent of Rs.1 per annum. After the expiry of the lease period, the land along with the building constructed by the assessee, was required to be surrendered to the MIDC. On the facts of the case, the Court held that there was no annual lease rental being paid by the assessee and the premium paid at the time of entering into the agreement was nothing but rent paid in advance, and was hence allowable as revenue expense. In the present case the appellant has furnished a lease agreement in respect of one such land at Usar in Maharashtra where the lease is obtained by the appellant from the MIDC on terms which are almost identical to the terms of the lease considered in the case of HMT Limited. On the basis of these facts and the decision of the Karnataka High Court, the appellant has submitted that the amortization of lease premium claimed should be allowed.*
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> *6.2 On going through the decision cited by the appellant of the Karnataka High Court and respectfully following the same, I hold that the premium paid by the appellant on all such lease agreements as are similar to the agreement entered into with MIDC for land at Usar, constitutes revenue expenses. In view of the Supreme Court decision in the case of Madras Industrial Investment Corporation Limited- 225 ITR 802 (SC) the total amount of lease premium paid in respect of such agreements should be amortized over the period of lease and only the amount pertaining to the relevant previous year should be allowed as a deduction. The AO is, therefore, directed to verify all the lease agreements in respect of which the amortization is claimed and allow the pro-rata lease*

premium in respect of such agreements as are similar to the above mentioned agreement with MIDC in respect of the land at Usar. Such agreements would be those under which no annual lease rental, or a nominal lease rental of Rs.1/- per month/annum is payable and a premium is paid on entering into the agreement which can be taken to be advance rent paid, as found by Karnataka High Court in the above mentioned decision. However, in case of an agreement in which an annual payment of rent, other than a nominal rent, is required, the amount of lease premium cannot be said to be payment of rent in advance and in such cases the premium will be in the nature of capital expenditure incurred for obtaining lease hold rights and no amortization will be allowable."

4. In respect of the succeeding assessment year the CIT (Appeals) followed his reasoning for the previous year, for the rejection of a similar claim by the assessee. The ITAT by its common order dismissed the appellant's claim stating as follows :

"9. Next grievance of the assessee relates to disallowance on account of amortizing the cost of land, by holding the same as capital expenditure. Cost incurred for land is always capital in nature unless assessee is dealing in land. No depreciation is allowable on such cost of land, therefore, there is no question for allowing amortization of such cost of land. We, therefore, confirm the decision of lower authorities on this issue."

5. The assessee argued that the nominal rent payable for each year during the subsistence of the lease arrangements is a strong indication that the heavy premium paid in all instances constituted advance rental which clearly qualifies for deduction for amortization. It has emphasized that every acquisition of each lease hold rights, contrary to the Tribunal's observation, amounts to a capital expenditure. Here, learned counsel urged that it is important to consider the nature of advantage in a commercial sense and so understood if the expenditure fall in the capital field would it not qualify as revenue expenditure. In this regard, learned counsel relied upon the judgment of the Supreme Court in *CIT Vs. Madras Auto Services* **(**1998) 233 ITR 468. He also relied upon the judgment of the Madras High Court in *CIT Vs. Gemini Arts Private Limited* (2002) 254 ITR 201. Further reliance was placed upon the judgment reported as *Deputy CIT Vs. Sun Pharmaceuticals India Limited* (2010) 329 ITR 479 and the ruling of the

Karnataka High Court in *Commissioner of Income Tax Vs. HMT Limited* 1993 203 ITR 820. It was highlighted that in all these cases almost identical lease hold arrangements have been treated as capital expenditure but Court by application of the Supreme Court's rulings in *Empire Jute Co. Ltd. Vs. CIT (1980) 124 ITR 1 & CIT Vs. Associated Cement Co. Ltd. (1988) 172 ITR 257 (SC)*, proceed to hold that the expenditure did not fall in the capital field.

6. This Court has considered these submissions and the issue which was sought to be urged has been re-visited on a number of occasions by various Courts. There is no doubt that in *Madras Auto Services case (supra)*, the Court had observed that there is no single decisive test to ascertain whether an expenditure qualifies as Revenue or that which properly falls in the capital field. Several aspects are to be applied such as nature of gain by the assessee, specially in a case of this kind, whereby constructing a building on a land which belongs to someone else, the saving in expenditure etc., a very important consideration, the Court emphasized that it should be seen from the "*Commercial point of view".* The other aspect emphasized by the Supreme Court was whatever substituted for revenue expenditure should normally be considered as revenue expenditure.

7. It is no doubt true that the decisions in *HMT (Supra), Sun Pharmaceuticals (supra) and Gemini Arts (supra)* dealt with fact situations where the assessee had obtained long lease, and where the Court found the down payment as lumpsum premium to be a real advance rental payment which therefore qualify as revenue expenditure. At the same time, this Court is also aware of the fact that in *Madras Auto services (supra)*, the leased land contained a dilapidated structure, and since it could not be used by the assessee, the parties therefore agreed that the assessee could construct upon the land at its own cost but at the same time it would have no right or title in the new construction. All this was taken into consideration by the

Court to hold that the amount paid at the commencement of the lease was the advance rent that could be amortized. At the same time, there are other rulings by the Supreme Court in (*Assam Bengal Cement Company Limited Vs. CIT* (1955) 27 ITR 34, *CIT Vs. Panbari Tea Company Limited* (1965) 57 ITR 422 and *Durga Madira Sangh Vs. Commissioner of Income Tax* (1969) 72 ITR 769. In all these cases, the Court upheld the Revenue's contention and stated that the expenditure towards acquisition of lease amounted to "brining into existence an asset or advantage for enduring benefit of the business" and was properly attributable by way of capital expenditure – cf (*Assam Bengal Cement Co Limited*). In *Panbari Tea Company Limited (Supra),* the Court underlined the fact where the party consciously chose to assign two different meanings to the expressions "P*remium" and "Rent".* The Court would not be justified in concluding that the premium paid constituted advance rent. Significantly this Court notices that in *Panbari Tea Company Limited*, the lease arrangement itself were for a period of 10 years, despite which the Supreme Court held it to constitute a capital asset. In the present case, unlike in *Madras Auto Services* or other decisions of the Supreme Court cited by the assessee, the lease arrangements are for a substantially long period i.e. 60-95 years. That the arrangements do not confer outright ownership rights to the lessee is besides the point as the enjoyment of the land as a lessee in such cases is substantially that of the owner itself. In other words, barring the right to alienate or outright sale of the property in unqualified manner, all rights of enjoyment in respect of leased properties are with the assessee. Furthermore, even though the stipulation in the deed – one of which (dated 25.07.1995 with MHIDC) was produced during the hearing by the assessee, clause 3(m) enjoins the lessee not to transfer either directly or indirectly, sell or encumber the lease benefits to any other party, the same stipulation enables transfer with "*previous consent in writing*

of the Chief Executive Officer". This Court is also further conscious of the fact that the conditions embodied in such lease deed are part of the general policies consciously adopted by the municipal and statutory authorities who manage and lease out such assets.

8. Having regard to these factors, this Court finds no infirmity with the reasoning of the Tribunal.

9. In view of the above conclusion, the questions of law are answered against the assessee and in favour of the Revenue. The appeals consequently have to fail and are accordingly dismissed without any order to costs.

(S.RAVINDRA BHAT)
JUDGE

(R.V. EASWAR)
JUDGE

5th November, 2012