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

RESERVED ON: 28.08.2012
PRONOUNCED ON: 31.08.2012

\+ **ITA 166/2006**

THE COMMISSIONER OF INCOME TAX-VI ..... Petitioner
Through: Ms. Rashmi Chopra, Sr. Standing Counsel.

Versus

M/S. UBEROI SONS (MACHINES) LTD. ..... Respondent
Through: Sh. Satyen Sethi with Sh. Arta Trana Panda, Advocates.

ITA 168/2006

COMMISSIONER OF INCOME TAX ..... Petitioner
Through: Ms. Rashmi Chopra, Sr. Standing Counsel.

Versus

M/S. UBEROI SONS (MACHINES) LTD. ..... Respondent
Through: Sh. Satyen Sethi with Sh. Arta Trana Panda, Advocates.

ITA 243/2006

COMMISSIONER OF INCOME TAX ..... Petitioner
Through: Ms. Rashmi Chopra, Sr. Standing Counsel.

Versus

M/S. UBEROI SONS (MACHINES) LTD. ..... Respondent
Through: Sh. Satyen Sethi with Sh. Arta Trana Panda, Advocates.

ITA 778/2006

COMMISSIONER OF INCOME TAX ..... Petitioner
Through: Ms. Rashmi Chopra, Sr. Standing Counsel.

Versus

M/S. UBEROI SONS (MACHINES) LTD. ..... Respondent
Through: Sh. Satyen Sethi with Sh. Arta Trana Panda, Advocates.

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

MR. JUSTICE S.RAVINDRA BHAT

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1. The present appeals by the revenue are directed against a common order of the Income Tax Appellate Tribunal (ITAT) dated 5th April, 2005 in seven appeals (by the revenue) and cross objections preferred by the assessee. The following questions of law were framed for consideration of this Court:

(i) Whether the ITAT was, in the facts and circumstances of the case, correct in law in quashing the re-assessment order passed by the Assessing Officer under Section 147(1) of the Income Tax Act, 1961?

(ii) Whether the ITAT was correct in law in holding that the excess amount payable to the assessee towards *mesne* profits/compensation for unauthorized use and occupation of the premises accrued to the assessee only upon the passing of the decree by the Civil Court on 14.10.1998?"

2. The facts necessary for deciding the appeal are that the assessee, a private limited company is engaged in the real estate business and derived rental income from its commercial building a multi-storied complex let out to various tenants. During the financial year, relevant to assessment year 1992-93, the lease agreement of between the assessee and its tenant Oriental Bank of Commerce, was to expire on 31.03.1991. The premises were not vacated and the assessee filed a civil Suit before this Court claiming a decree

for possession by way of eviction. In the assessment proceedings, the assessee explained that this included the cost of Civil Suit and the advocate's expenses for the same. During the pendency of the suit, the tenant, Oriental Bank of Commerce, had been paying rent regularly @ ₹.45,900/- per month. This was charged to tax, on due basis. The Suit was decreed by this court in October, 1998. The assessee was paid a total amount of ₹.27,76,045/- as mesne profit towards arrears of rent. The decree for mesne profits/damages against the tenant-defendant was @ ₹.75,000/- per month from the date of filing of suit to the date of vacation, with costs.

3. The AO reopened the assessment for assessment years 1992-93 to 1998-99 alleging that the assessee knew that higher amount (than the actual rent) was payable as rent in respect of the premises and the assessment was completed on the basis of enhanced annual letting value. The addition sought to be made for the years previous to the year when the enhanced rents or mesne profits became payable was challenged by the assessee in appeals to the CIT (A). The Appellate Commissioner by his order, held that the action of the AO in including/adding the arrears of rent as the assessee's income from house property, (by taking annual value @ ₹.75,000/- per month for each of the assessment years) was not justified. The additions were deleted. The revenue's appeal to the ITAT was rejected by the impugned order.

4. The assumption of jurisdiction to re-assess the income had been upheld by the CIT (A); this was challenged by the assessee, in its cross objections. The assessee argued that there was no failure on its part to disclose fully and truly all material facts necessary for assessment and so,

the jurisdiction to re-assess the income was not validly assumed. The Tribunal upheld this contention, and held that the invocation of provisions of Section 147 was not sustainable in law.

5. It is contended on behalf of the revenue, by Ms. Rashmi Chopra that the assessee was under a duty to disclose the details of the claim it had made before the court, towards arrears of rent, because the provision (Section 23) not only contemplated declaration of actual rent, but also amounts that were "payable" or receivable. In this regard, it was stated that the assessee had not only received the rents during pendency of suit, but even enhancement, according to the contractual dates, till its claim was finally decreed. Therefore, it was in a position to reasonably declare the amount payable by the tenant, each year, during pendency of the litigation. However, details of such amounts claimed or receivable, were deliberately not mentioned in the returns for the earlier accounting years. The AO justifiably re-opened the assessments, under Section 147 of the Act, and brought the amounts which were payable (though paid later, after the decree) to tax for each relevant accounting year.

6. The revenue relies on the fact that Section 25-B was introduced much later, after the AY in question here. There was nothing in the tenor of the amendment, to clarify that it had retrospective effect, or implicated past transactions. In the circumstances, the assessee could not take shelter under the fact that the arrears were disclosed in the later year. The revenue also relied on the judgment of this Court in *Commissioner of Income Tax Vs. Ms. Sadhna Chadha*, 270 ITR 534 as well as the judgment reported as B.M. Gupta & sons (HUF) vs ACIT (2008) 299 ITR 410 (Del).

7. Counsel for the assessee, Mr. Sethi, argued that the appeal is bereft of merit, and the ITAT's order does not call for interference. It was argued that having regard to the structure and tenor of the statute, there was no occasion for declaring something that was *likely* to arise in the future, as "payable". At the time the assessee filed its suit for eviction, and claimed mesne profits, it did not and could not ever have known whether it would have succeeded, and the extent to which its claim for *mesne profits*, would succeed, if at all it did. The right it had was only one to approach the court, claiming possession, and seeking *mesne profits* for the time the tenant overstayed in the premises, after its possession was rendered unlawful. Such inchoate entitlements could not be considered as income "payable" which connoted something more concrete. Counsel relied on the judgment of the Supreme Court reported as *P. Mariappa Gounder (Dead) By LRs. vs Commissioner Of Income Tax* 1998 (232) ITR 2 (SC). It was also submitted that this proposition of law was accepted in *Hope (India) Ltd. v. CIT*, 238 ITR 740 (Cal.) which was followed by this Court in *Commissioner of Income Tax v R.J. Wood* 334 ITR 358.

8. The Tribunal, in its impugned order, had this to say about the re-opening of assessment pursuant to notice under Section 147:

> *"9. As per Section 147, the AO may, subject to the provisions of Sections 148 to 153, assess or re-assess any income chargeable to tax which he has reason to believe, has escaped assessment and any other income chargeable to tax which has escaped assessment and which has come to his notice subsequently. The proviso to Section 147 lays down that where an assessment u/s 143(3) has been made, no action shall be taken u/s 147 after the expiry of 4 years from the end of the relevant assessment year, unless any income chargeable to tax has escaped assessment for such assessment year by reason of failure on*

the part of the assessee, inter alia, to disclose fully and truly all material facts necessary for his assessment, for that assessment year. The stand of the assessee has been that in the course of original assessment proceedings u/s 143(3), it was specifically pointed out and explained to the AO by the assessee that the reason for the heavy expenditure claimed under the head of legal expenses was that this expenses was in respect of Advocate fee and cost of Civil Suit filed in the High Court for possession and eviction against its tenant/OBC. This has not been denied…..

…….. ……..

9.2 Even the learned Commissioner (A) has not directly address himself to this issue. It has been held that the AO reopened the assessment to bring to account the ALV that would have been seen to be the rental income for the particular year/years and that it was not so much for any omission or default of the assessee. In this regard, the objection of the assessee is well raised. The above discussed proviso to Section 147 clearly lays down that reassessment beyond the expiry of limitation cannot be done unless income has escaped assessment by reason of the failure on the part of the assessee to disclose fully and truly all material facts necessary for his assessment, for that assessment year. Therefore, the reasoning assigned by the learned Commissioner (A) to give the nod to the alleged validity of the reopening of assessment, is not sustainable. The AO could not, under the law, bring the account ALV that would have been seen to be the rental income for the particular year/years.

9.3 Otherwise also, till the time of passing of the decree in the Civil Suit, the right of the assessee to arrear of rent was merely a contingent inchoate right. The rent became receivable only on the passing of the decree. Therefore, the is no question of the assessee having not disclosed any material facts before the AO. So, on this basis, the AO could not have invoked or assumed jurisdiction to re-assess."

The above reasoning is unexceptionable. In *P. Mariappa Gounder (supra)* the Supreme Court described the "right" of a plaintiff/owner seeking possession and mesne profits (which were to be calculated and decreed after

an enquiry) as *"only an inchoate right"*. Such being the case, the assessee could not be faulted in not quantifying the potential *mesne profits* likely to accrue in the future. Re-opening of assessment, under these circumstances was not warranted. The decision of this Court in *R.J. Wood* fortifies this conclusion.

9. On the merits of the assessment, the Tribunal found as follows:

"12. Even on merits, the Department has no case. It alleges that the learned CIT (A) erred in deleting the addition of arrear of rent, which was added as income from house property by taking annual rate of Rs.75,000/- per month for the relevant year. It was only when the Suit filed by the assessee was decreed by the Hon'ble High Court, that a decree for mesne profits/damages @ Rs.75,000/- per month. Till such time as that of the passing of the decree, the Suit of the assessee was just a claim. It had no concluded right to the amount, pendente lite at best, it was an inchoate right which fructified into a right crystallized and vested in the assessee only when the decree was passed. It is trite that the purpose of the Act is to charge real income. Real income arose to the assessee only on the passing of the decree. Therefore, the learned CIT(A) was well justified in deleting the addition on account of arrears of rent.

13. Also, the decree was for mesne profits. Mesne profits are the amounts awarded against a person in wrongful possession of property. Such profits, in order to constitute income have also be have been actually received along with interest thereon. Mesne profits hitherto in a state of flux, in the sense that which are undecided as to whether they accrued to the claimant or not, cannot, in any manner amount to "real income" chargeable under the Act. They only accrued to the assessee on 14.10.1998, on which date, the decree for mesne profits was passed in favor of the assessee."

10. Section 23 of the Act explains "annual letting value," for purposes, of income from house property. The said provision reads as follows:

"Section 23. ANNUAL VALUE HOW DETERMINED.

(1) For the purposes of section 22, the annual value of any property shall be deemed to be -
(a) The sum for which the property might reasonably be expected to let from year to year; or
(b) Where the property is let and the annual rent received or receivable by the owner in respect thereof is in excess of the sum referred to in clause (a), the amount so received or receivable :
Provided that where the property is in the occupation of a tenant, the taxes levied by any local authority in respect of the property shall, to the extent such taxes are borne by the owner, be deducted (irrespective of the previous year in which the liability to pay such taxes was incurred by the owner according to the method of accounting regularly employed by him) in determining the annual value of the property of that previous year in which such taxes are actually paid by him ..."

The Madras High Court, in *Commissioner of Income-Tax, Tamil Nadu-V v. P. Mariappa Gounder* 1983 (147) ITR 676 (Mad) explained the precise nature of the right of a landlord seeking possession of residential premises, through a civil suit which also includes a claim for *mesne profits*:

"*We do not think it should take us long to find the correct answer. A claim for mesne profits is usually directed against one who has deprived the true owner of possession of his property and who has thereby prevented the true owner from enjoying the income or usufruct of the property. When, in such a suit or proceeding, the court awards mesne profits to the true owner, that represents a just recompense to him for the deprivation of the income which ought properly to have come into his hands but for the interference of the person in wrongful possession of the property.*

The Code of Civil Procedure defines mesne profits as that which a person in wrongful possession of property has actually received or might with ordinary diligence have received therefrom. The accent of the definition in section 2(12) of the Code concentrates more on the methodology of calculation of mesne profits rather than on what the true nature of mesne profits is. As we earlier stated, the rationale of awarding mesne profits is that the trespasser or the person in wrongful possession not only defies the

title of the true owner, but also prevents the true owner from enjoying the income or the usufruct of the property in question. When, therefore, the court decrees mesne profits, that decree is in recognition of the position that the true owner is entitled to the income from the property and the person in wrongful possession is to compensate the true owner in that regard by paying either the actual income from the property or a reasonable estimate of that income. Having regard to these characteristics of mesne profits, there can be no doubt that they are also a species of taxable income. Under the scheme of the I.T. Act, anything which can properly be regarded as income and which is not expressly exempted from taxation under a specific provision of the statute must be regarded as taxable income. We are, therefore, satisfied that the Tribunal and the other authorities were right in their view that mesne profits has to be assessed as taxable income in the hands of the present assessee.

…… …… ……

...To say that we do not know how much is the mesne profits but nevertheless assert that mesne profits have accrued at a given moment of time, out of ignorance, is very much like an Irish Bull, an example of which was found in the description of an escaped convict from an Irish prison: "Age not known but looks older than he really is". If we do not know how much the mesne profits are, how can we say, with any modicum of confidence, that the mesne profits have already accrued? The question of accrual, like the question of receipt, cannot be based on any theory but must rest on the solid rock of actualities. We cannot say that whenever the amount of mesne profits are quantified, that amount must relate back to an earlier point of time when the right to mesne profits itself was declared by a competent court. "Relation back" theory cannot work and would be quite inappropriate for settling the question of accrual of income, when both the accrual and income are unknown quantities.

…… …… ……

The assessee did not know how much was the income. The proceedings had, therefore, to go through the whole hog of a judicial inquiry before mesne profits could be ascertained. As it happened, the amount was fixed by the trial court only on December 22, 1962, during the year of account ended March 31, 1963. On principle as well as on authority, therefore, the mesne profits as an amount of income could be said to have accrued, in the income-tax sense of the term, only during the year ended March 31, 1963. Hence, we

must uphold the order of the AAC bringing to tax the entire amount in the assessment year 1963-64. The assessment of the same amount in 1964-65 relevant to the account year ended March 31, 1964, must be held to be erroneous."

This understanding was endorsed by the Supreme Court in the appeal against the decision of the Madras High Court. In *P. Mariappa Gounder vs. Commissioner of Income Tax* 1998 (232) ITR 2 (SC) the Court held that:

"In our opinion, the decision of the High Court does not call for any interference. It will be seen that under Order XX, rule 12, of the Code of Civil Procedure when the court passes a decree for possession and mesne profits by clause (ba) it may pass a decree "for mesne profits or directing an enquiry as to such mesne profits". In the present case, from the portion of the decree extracted hereinabove, it is clear that this court passed an order directing an enquiry as to the mesne profits which would be payable by the judgment-debtor to the decree-holder. As on the day when this court decreed the appellant's suit, there was only an inchoate right which arose in his favour. The trial court was directed to hold an enquiry and then to determine the amount of mesne profits which was payable.

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The aforesaid passage was quoted with approval by this court in CIT v. Hindustan Housing and Land Development Trust Ltd. [1986] 161 ITR 524, in which case also this court was called upon to deal with a question as to when the additional compensation awarded was liable to be taxed. In that case the amount of compensation awarded by the arbitrator was in dispute. On an appeal having been filed by the State Government it was held that the said amount could be taxed only when the dispute was resolved because if the appeal had been allowed in its entirety, the right of payment of enhanced compensation would have fallen altogether.

Applying the ratio of the aforesaid decisions, it appears to us that the decree dated April 22, 1958, passed by this court only created an inchoate right in favour of the appellant. It is only when the trial court determined the amount of mesne profits that the right to receive the same accrued in favour of the

appellant. In other words, the liability became ascertained only with the order of the trial court on December 22, 1962, and not earlier. Following the mercantile system of accounting, the mesne profits awarded by order dated December 22, 1962, were rightly taxed in the assessment year 1963-64 and it was wholly irrelevant as to when the amount awarded was in fact realised by the assessee. In our opinion, therefore, the High Court was right in deciding the reference in favour of the Department. We accordingly dismiss the appeals but in the circumstances of this case award no costs."

11. The revenue had relied on the judgment in *Sadhna Chadha.* However, that decision in fact favours the assessee, as can be seen from the following extract of this Court's judgment in that case:

"Clause (b), which is more explicit, clearly refers to the period of 12 months, which leaves no scope for doubt that the annual rent has to be the rent for 12 months. Therefore, a bare reading of section 23(1) with Explanation I appended thereto, makes it clear that any rent not relating to the relevant previous year cannot form part of the "annual rent" for the previous year, for determining the annual value of the property for the purposes of section 22 of the Act. A similar view has been expressed by the Calcutta High Court in Hamilton & Co. (P) Ltd.'s case (supra), with which we are in respectful agreement."

12. In one of its earlier judgments, *E. D. Sassoon and Co. Ltd. v. CIT* [1954] 26 ITR 27 (SC), the Supreme Court examined the meaning of the expressions, 'arises' 'accrue', and 'is received' while considering what is "income". The Court's observations, extracted below, are illuminating:

'Now what is income ? The term is nowhere defined in the Act. . . In the absence of a statutory definition we must take its ordinary dictionary meaning--"that which comes in as the periodical produce of one's work, business, lands or investments (considered in reference to its amount and commonly expressed in terms of money); annual or periodical receipts accruing to a person or corporation" (Oxford Dictionary). The word clearly implies the ideal of receipt, actual or constructive. The policy of the Act is to

make the amount taxable when it is paid or received either actually or constructively. "Accrue", "arises" and "is received" are three distinct terms. So far as receiving of income is concerned there can be no difficulty; it conveys a clear and definite meaning, and I can think of no expression which makes its meaning plainer than the word "receiving" itself. The words "accrue" and "arise" also are not defined in the Act. The ordinary dictionary meanings of these words have got to be taken as the meanings attaching to them. "Accruing" is synonymous with "arising" in the sense of springing as a natural growth or result. The three expressions "accrues", "arises" and "is received" having been used in the section, strictly speaking "accrues" should not be taken as synonymous with "arises" but in the distinct sense of growing up by way of addition or increase or as an accession or advantage; while the word "arises" means comes into existence or notice or presents itself. The former connotes the idea of a growth or accumulation and the latter of the growth or accumulation with a tangible shape so as to be receivable. It is difficult to say that this distinction has been throughout maintained in the Act and perhaps the two words seem to denote the same idea or ideas very similar, and the difference only lies in this that one is more appropriate than the other when applied to particular cases. It is clear, however, as pointed out by Fry L. J. in Colquhoun v. Brooks [1888] 21 QBD 52, 59, [this part of the decision not having been affected by the reversal of the decision by the House of Lords [1889] 14 AC 493] that both the words are used in contradistinction to the word "receive" and indicate a right to receive. They represent a state anterior to the point of time when the income becomes receivable and connote a character of the income which is more or less inchoate."

The Court held that:

"In the instant case, as indicated hereinbefore, the Government Departments agreed to enhance the rent with retrospective effect from 1982, and thus, the parties were not ad idem in their mind as regards the actual quantum of rent payable to the Assessee by its tenants and, thus, the actual amount was not ascertainable. Fair rent, keeping in view the provisions of the West Bengal Premises Tenancy Act, has to be determined and till such fair rent is determined, actual rent has to be paid by the tenants. Although the said provisions have no application in case the Government is the tenant the rent has to be paid on the basis of the agreement entered into by the parties. A claim made by a landlord for enhancement of rent cannot, thus, be

said to be an amount receivable within the meaning of Section 23(1) of the Act. A claim or a demand by itself does not come within the purview of the words 'income received or receivable' and keeping in view the provisions of Section 5 of the Income-tax Act there cannot be any doubt whatsoever such income either received or deemed to be received, accrued or arose or is deemed to accrue or arise to him or accrues or arises in India or accrues or arises outside India during the previous year.

An agreement entered into between the parties in terms whereof the quantum of rent is determined with retrospective effect, in our considered view, does not come within the purview of any of the provisions of Section 5 aforementioned."

13. This court had followed the above decision in its judgment in *R.J Wood*. The Court also noticed that newly introduced Section 25-B was clarificatory in nature, as it encapsulated the law existing (i.e. that receipts towards *mesne profits* should be taxed in the year of their receipt). This is evident from the following observation (in *R.J.Wood)*:

"Once we proceed on this basis, the obvious conclusion would be that the arrears of rent received in the assessment year 2000-01 would not relate to the previous years and are to be taxed in that year. For this reason, as far as these assessment years are concerned, the Tribunal was right in holding that the arrears of rent received in the assessment year 2000-01 could not be spread over the previous years, i.e., 1996-97 to 1999-2000."

The above conclusion is in conformity with the law declared by the Supreme Court in *P. Mariappa Gounder* (supra). Therefore, this Court holds that there is no infirmity in the findings of the Tribunal that even on merits, the arrears of rent received by the assessee (as mesne profits) could not be brought to tax for the previous years, when they fell due. They could be brought to tax only during the year of receipt. The revenue had further argued that during the year of receipt, the assessee had shown the amount so received as capital. Its character was clearly as that of income, as is evident

from the ruling of the Madras High Court in *P. Mariyappa Gounder* which was later affirmed by the Supreme Court – a fact recognized by this Court in *R.J. Wood*. The revenue had not however, re-opened the assessment in respect of the year of receipt of the amounts, in this case. As a result, this Court holds that though the amount received by the assessee was liable to tax, in accordance with the law declared by the Supreme Court – in the year of its receipt- there is no infirmity with the findings and conclusions of the Tribunal. The questions of law framed are accordingly answered against the revenue, and in favour of the asseseee, subject to the above observations and findings. The appeals are consequently dismissed.

S. RAVINDRA BHAT
(JUDGE)

R.V. EASWAR
(JUDGE)

AUGUST 31, 2012