

Comecon Overseas (P) Ltd. Vs. Dy. Cit, Spl. Range 1

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Court : Income Tax Appellate Tribunal ITAT Delhi

Decided On : Feb-10-2006

Reported in : (2006)8SOT82(Delhi)

Appellant : Comecon Overseas (P) Ltd.

Respondent : Dy. Cit, Spl. Range 1

Judgement :

This appeal of the assessee-company is directed against the order dated 17-12-1998 passed by Commissioner (Appeals), New Delhi for assessment year 1992-93. In substance, all the grounds of appeal relate to the disallowance of depreciation on the assets given on lease by the assessee.

2. Briefly stated, the facts are that during the year the assessee had entered into purchase and leased back agreements as follows: In June, 1991 SIL approached the assessee for leasing of five sugar mills rollers. These were purchased by SIL from BHEL in February, 1990 for a sum of Rs. 6,08,400 + Rs. 9,12,600. Subsequently, SIL got some machining work done by M/s. United Engineering Works who charged Rs. 20,000 per shaft. Thus the total cost of SIL came to Rs. 16,21,000.

Against this assessee had shown the cost at Rs. 41.25 lakhs. The assessing officer found that lease with SIL had expired in September, 1994 but the assessee had not taken possession of leased asset in accordance with the lease agreement. The assessee stated that there was a litigation with SIL. The assessing officer,

however, was not satisfied with the explanation as the litigation was only for recovery of dues and not for securing the custody of assets. It was stated before the assessing officer that the assessee had filed suit against SIL for recovery of outstanding dues as also for repossession of the assets and another suit for winding up of SIL before the Lucknow High Court. The assessing officer observed that the assessee was basically an exporter and the business of leasing was not its main business. The leasing transaction had been entered into to derive 100 per cent depreciation and to reduce its tax liability. The assessing officer worked out the Internal Rate of Return (IRR) with respect to the lease transaction at 13.76 per cent whereas in a pure finance transaction the market rate was around 20 per cent. She found that SIL had unabsorbed losses and did not require the benefit of depreciation. She therefore held the leasing transaction to be a colourable device aimed at reducing the tax liability. Hence, she treated the transaction with SIL as a purely finance transaction and the claim of 100 per cent depreciation was disallowed.

The assessee purchased second-hand gas cylinders SIGL & GAPL and leased back to them. These were purchased by GAPL and SIGL at the rate of Rs. 1,400 per cylinder on 21-3-1992 whereas these were sold to the assessee on 24-3-1992 at the rate of Rs. 22,000 per gas cylinder. The assessee received a security deposit of Rs. 72,000 from SIGL. At the end of lease period of three years these gas cylinders were finally sold off for a sum of Rs. 532 per gas cylinder to M/s. Shah Enterprises. The assessing officer asked the assessee to show cause as to why this case would not come under the purview of Explanation 3 to section 43(1). The assessee submitted that the provision of Explanation 3 to section 41 (1) could not be attracted as the asset had not been used by SIGL or GAPL and the transaction was not entered into with the object of reducing the assessee's income tax liability. The assessing officer held that had the lease been a genuine one the assessee would have attempted at procuring the second-hand asset at the prevailing market price. She was of the opinion that the assessee was not interested in the asset per se but it was the benefit of 100 per cent depreciation claim that motivated the assessee to enter into the agreement. The IRR in this case was worked to 14 per cent only, In this case SIGL and GAPL had no use of 100 per cent depreciation because they had unabsorbed losses. Hence, she

treated the transaction entered into with SIGL and GAPL as financing transaction and the claim of 100 per cent depreciation was disallowed.

The assessee purchased 520 glass bottles moulds from M/s. Mohan Crystal Glass Works (MCGW) for Rs. 14,01,400 and leased back to them and at the end of the lease period of 3 years were sold for Rs. 15,415 only to M/s. National Serial Ltd., a sister concern of the assessee. The IRR in this case was worked out at 14.10 per cent. MCGW was a loss-making concern during the relevant previous year. Therefore, the assessing officer treated this transaction as a mere financing transaction and the claim of 100 per cent depreciation was disallowed.

The assessee purchased pusher type furnace from M/s. Punjab Potteries (PP) for a sum of Rs. 10,57,500 and leased back to them. The furnace was said to be erected by Associated Furnaces (P) Ltd. The assessing officer found that the period of lease in this case had expired on 31-3-1997 but the assessee had not taken re-possession of the asset.

She found that M/s. Punjab Potteries was not in operation for the last 3-4 years and there was no rational as to why Punjab Potteries Ltd. should pay lease rent for an asset which was not being used. It could have gone for premature termination of lease. Lessee had book profits of Rs. 1, 17,129 only and could easily forego the depreciation in favour of the assessee. On local enquiry it was revealed that a Director of the assessee-company was interested in M/s, Punjab Potteries. She treated the transaction as financial transaction and disallowed the claim of 100 per cent depreciation, Thus, the assessing officer held that all the five transactions entered into by the assessee with SIL, SIGL, GAPL, MCGW and PP were aimed at avoiding the payment of tax, She was of the view that the assessee had resorted to a colourable devices in the form of purchase and leased back transactions and relying upon decision in the case of McDowell & Co. Ltd. v. CTO (1985) 154 ITR 148 (SC) she held the transaction not genuine and disallowed the entire claim of depreciation.

Being aggrieved the assessee preferred appeal before the Commissioner (Appeals). The learned counsel for the assessee submitted that assessing officer was not correct in observing that the assessee was basically an exporter. He

explained that the exports constituted a very small percentage of the assessee's business. The assessee-company was duly authorized to enter into leasing transactions and the same was stated in the Memorandum of Association. The assessing officer therefore should not have drawn adverse inference on this account. It was also not correct to say that all these lessees were suffering losses. It was submitted that the profits of the five concerns namely SIL, SIGL, GAPL, PP and MCGW were at Rs. 59.25 lakhs, 0.87 lakhs, 0.21 lakhs, 1.07 lakhs and 116.74 lakhs respectively. Therefore, the contention that the lessee and the lessor mutually stood to gain by entering into these transactions was not vallearned With regard to IRR of the lessee transaction it was submitted that the revenue cannot draw adverse inference by comparing IRR rates of leasing transactions with that of a finance transaction as these were not similar transactions.

The assessing officer had acted purely on suspicion without any evidence. All the five lease transactions were with regard to specific items on goods and they were properly evidenced by an invoice. They have effectively delivered to the owner and any payment in excess of limits laid down by section 40A(3) were made by way of crossed cheque or crossed demand draft. In the case of SIL the payment of Rs. 41.25 lakhs had been as cost of the assets. The assessee filed a comprehensive suit against SIL for winding up as also for recovery of rental and of leased assets. He pointed out that assessing officer was not correct in working out cost of five Sugar Mill Rollers at Rs. 16,2 1,000 only. It was stated that the sugar mill rollers had two shafts and each shaft was purchased for a sum of Rs. 3,23,942 from BHEL. The cost of 10 shafts were therefore Rs. 32,39,420 over and above the matching over of Rs. 20,000 was done through M/s. United Engineering Works. Certain bills of Central Foundry Forge Plan, showing sale of sugar mills roller to SIL dated 27-2-1990 and 3-3-1990 had also been filed.

In the case of gas cylinder it was stated that though the assessing officer had issued show cause for invoking Explanation 3 to section 43(1), the assessing officer did not invoke the section finally. These assets after expiry of lease period recovered from the lessee and sold to a third party. He mentioned that continuous pusher type furnace had not been recovered from M/s. Punjab Potteries as the assessee was arranging for a buyer of the equipment and till such time it had been

agreed the asset remain with the lessee. The learned counsel explained that due to the Supreme Court order the lessor was not able to locate the buyer in the National Capital Territory of Delhi as this item causes environmental pollution. In the case of glass bottle moulds the assessee-company had received back a sum of Rs. 17,37,732 as lease rental and at the termination of the lease the asset had been sold for Rs. 15,415. Thus, in all the cases of lease the assets were purchased by the assessee and their existence had not been doubted by the revenue. The learned Commissioner (Appeals) has held thus :- "1 All the five transactions are sale and lease back transactions. The assessee has purchased the equipment as per invoice, the equipment had been in the ownership and custody of the lessee before its purchase by the assessee and the same were leased back to the assessee on payment of lease rentals. In the case of SIL the lease agreements for five sugar mill rollers. The assessing officer has computed its value in the hands of SIL at Rs. 16,21,000 whereas the appellant has stated the total cost in the hands of SIL at Rs. 33.39 lakhs. On comparison of the items purchased by the SIL from M/s. Central Foundry Forge Plant the copies of bill of which have been filed before me it is seen that these purchases were for Mill roller shaft DRG No. 550 X 4650. Forge No. and Heat No. in these items is indicated in the bills. As against this the invoice of SIL of its sale to the appellant-company is only with respect to Sugar Mill Rollers Sl. No. 1 to 5 at the rate of 7,50,000 total amount Rs. 37,50,000 + CST. I am, therefore, unable to accept the contention of the appellant that the Sugar Mill rollers bought by the assessee-company from SIL and then leased out to them were the same items which were purchased by SIL from Central Foundry Forge Plant vide their bills dated 6-3-1990, 3-3-1990 and 27-2-1990. It is also not clear as what use the lessee company had put its equipment to in the intervening period between its purchase and its sale to the appellant-company vide invoice dated 11-9-1991. Beside whereas the appellant-company has claimed depreciation of Rs. 41.25 lakhs in the year under appeal it had shown corresponding profits of Rs. 2.79 lakhs + 5.58 lakhs + 10 lakhs only on the ground that further rentals were not received from the lessee. The appellant, however, had received a sum of Rs. 14.25 lakhs from lessee by way of security deposit which is not liable to tax. The asset continuous to remain with the lessee till date on the ground of litigation before the Lucknow High Court. The appellant, however, has

not submitted any paper or proof indicating that the Lucknow Bench of the Allahabad High Court has ordered the status quo for which reason the delivery of the leased asset cannot be taken. In the absence of such directions from the High Court the assessee remains free to recover the leased asset for which clearly no efforts have been made. With regard to gas cylinders it is not disputed that whereas the market price of per gas cylinder was Rs. 1400 the assessee procure the same at enhanced rate of Rs. 2,200 per gas cylinder. On perusal of the sale bills of these cylinders it is seen that no details regarding the make or even the capacity of these cylinders is mentioned. In the case of glass bottle moulds these were sold for a nominal amount after expiry of the lease period to a sister concern of the lessee. In the case Continuous Pusher Type Furnace against the cost of Rs. 10,57,500 the lease rental worked out to 3.5 lakhs and the asset continues to remain with the lessee till date.

On perusal of the lease agreement it is seen that the agreement stipulates that the property will be delivered by the supplier of the equipments to the lessee and the lessee shall pay all charges in respect of its delivery. Article 8 of the lease agreement states that the lessee shall maintain on the equipment/property insignia, identification or maker's marks, numbers or plates, etc. Article 24 provides that on the termination of the lessee shall on its risks and costs return the equipment in good condition and perfect working order at the place designated by the lessor. In the present case the stipulation for delivery of the asset is paper clause only. In all the five cases the equipments was with the lessee prior to the lease agreement. The stipulation regarding identification of the leased asset also remains on paper only as no identification of the leased asset has been made either in the schedule of description of leased asset to the leased agreement or even in the invoice of sale to the appellant-company. None of the invoices mentioned the make, the number, design of the asset purchased by the assessee. Thus the basic criteria of identifying the asset which belongs to the assessee-company has not been fulfilled. Besides, in two cases i.e., five Sugar Mill Rollers and the Continuous Pusher Type Furnace the leased out asset continuous to remain with the lessee much after the expiry of the lease. In the third case i.e., Glass Bottle Moulds the asset has been disposed of for a nominal price to a sister concern of the lessee. In all these cases the basic ingredients of ownership of a

defined asset leasing. The essential difference between the finance transactions and leased transaction is ownership of the asset. The assessee having failed to pass the criteria on this account cannot be stated to be an ownership of the asset. The ownership has not been conclusively proved in the absence of failure to retrieve the asset and complete lapse of identification on the leased asset. It is also not irrelevant that the actual cost as shown by the assessee does not compare to the market cost of the asset as has been shown in the case of Gas cylinders and Sugar Mills Rollers. 1, therefore, uphold the order of the assessing officer treating the transactions as a finance transaction. The appeal on this ground is dismissed." Before us, the learned counsel for the assessee has submitted that the assessee-company has been carrying on the business of trading, exports, imports, financing and leasing. In this connection he has referred to the extract of Memorandum of Association of the assessee-company placed at page 181 of the paper book, which clearly indicates that leasing of asset is one of the objects incidental or ancillary to the attainment of main objects. In original assessment made the assessing officer disallowed 25 per cent of the depreciation claimed on the machinery leased out i.e., Rs. 1,82,745 (25 per cent of Rs. 73,09,900). The original assessment was however set aside to the assessing officer with the specific direction to the assessing officer, which directions have not been complied with by the assessing officer, hence failure to follow the direction of appellate authority is denial of justice. In this connection he has referred to the following directions given by the Commissioner (Appeals) in the order dated 22-3-1996 :- "18. I have considered the facts and circumstances of the case and rival submissions. No doubt leasing of assets which are fully depreciated has been one of the modes recently employed by certain companies. However, the issue to be examined is the intention behind these transactions and whether it is done with a view to claim depreciation a second time on fully or substantially depreciated assets. The assessing officer has not even examined as to whether all these assets were fully or substantially depreciated assets when these were purchased and whether the main purpose was only to claim depreciation on these assets and set it off against the interests income. For this purpose, the assessing officer should examine the assessment records of the sellers of the assets to find out whether these were in fact fully or substantially depreciated assets. The assessing

officer should also have made enquiries (as mentioned in para 16 above) to find out whether appellant had purchased fully or substantially depreciated assets from loss-making concerns. No proper enquiries were made in this regard before making the disallowance under section 32 for depreciation. The assessing officer will examine this issue in detail and afford a proper opportunity to the appellant before he comes to any conclusion in the matter. Assessing officer will also examine whether the case of appellant falls under Explanation 3 below section 43(1) of the Income Tax Act and afford a specific opportunity to appellant before reaching any conclusion in the matter.

19. In the result the assessment is set aside to be made de novo in the light of the above directions." The learned counsel has further submitted that in all these cases the assets were purchased by the assessee-company and they were distinctively identifiable. The physical delivery had been taken by the assessee-company in all the cases. A confirmation from each of the supplier/seller was duly furnished. These assets were acquired by the assessee-company having regard to the business requirements of the assessee. The regular rentals had been shown and accounted for in the relevant years. During the year the assessee had purchased five sugar mill rollers from SIL, a company engaged in manufacturing and fabrication and commissioning of machinery for sugar plants. The copy of invoice for a sum of Rs. 41,25,000 issued by SIL for a sale of five sugar mill rollers is placed at page 133 of the paper book. The learned counsel has mentioned that the said company acquired a sick sugar unit known as Khalilabad Sugar Pvt. Ltd., and thereafter undertaken a major expansion and modernization programme of the said sugar mill. In June, 1991, M/s. SIL approached the assessee-company for leasing of sugar mill rolls. Accordingly, a lease agreement dated 10-9-1991 was entered into between the assessee-company and M/s. SIL, a copy of which is placed at page 185 of the paper book. These assets were purchased by M/s. SIL from Bharat Heavy Electricals Ltd. (a unit of Central Foundry Forge Plant) in February, 1990. In this regard, the learned counsel has referred to the purchase order placed by M/s. SIL on M/s. BHEL which is available at page 99 of the paper book. A copy of invoice of BHEL is available at pages 103-105 of the paper book. The learned counsel further submitted that thereafter SIL sent the said rolls to M/s.

United Engineering Works, Ghaziabad for further processing and machining. In this connection he has referred to bill dated 11-9-1991 of the United Engineering Works placed at page 98 of the paper book.

M/s. United Engineering Works thereafter dispatched the said rollers to Khalilabad Sugar Mills a unit of M/s. SIL at the request of the lessee.

The assessee duly paid for acquisition of sugar mill rollers. The aforesaid sugar mill rollers had a specific S1. No. embossed on them which could be evident from the copy of invoice raised by M/s. BHEL.

Thus, he has urged that the property in the said specific case of sugar mill rollers had passed on the assessee-company. M/s. SIL has confirmed that five sugar mill rollers were taken on lease from the assessee and the same were put to use, as per copy of letter at page 96 of paper book. The learned counsel has pointed out that the assessing officer was not correct in working out the cost of five sugar mill rollers at Rs. 16,21,000. It was stated that sugar mill roller had two shafts and each shaft was purchased for a sum of Rs. 3,23,942 from M/s. BHEL. The cost of 10 shafts was, therefore, Rs. 32,39,420 plus CST and over and above this machinery work of Rs. 20,000 per shaft was done through M/s.

United Engineering Works. As regards the observation of the assessing officer that the lease with SIL had expired in September, 1994, but the assessee had not taken possession of the leased asset in accordance with the lease agreement, the learned counsel has pointed out that there was litigation with M/s. SIL and in view of the order of the status quo the possession of the said assets could not be obtained by the assessee.

With regard to the gas cylinder the learned counsel has submitted that the assessee-company had purchased empty gas cylinders from M/s. Sethi Industrial Gases Pvt. Ltd. (SIGL) and M/s. Gujarat Acetylene Pvt. Ltd. (GAPL), Ahmedabad and leased back the same to them. The copy of invoice raised by the above supplier along with the challans were duly furnished before the assessing officer. The said supplier had purchased the gas cylinder from M/s. Sirhind Steel Ltd. the copy of invoice raised by M/s. Sirhind Steel Ltd. would show the identification

number of each of the cylinders. In this connection, the learned counsel has referred to the delivery challans and invoices placed at page 89 of the paper book. He has further submitted that these empty oxygen gas cylinders were used by the lessee. However, it has been confirmed by the lessee that no depreciation has been claimed on the leased assets.

in this connection, he has referred to the copies of the letter received from the lessees at pages 139 and 140 of the paper book. He has further stated that these assets, after the expiry of the lease periods were recovered from the lessee and sold to the third party. He has further mentioned that though the assessing officer had issued show-cause notice for invoking Explanation 3 to section 43(1), however, he did not invoke the said section finally. As regards the 520 glass bottle moulds the learned counsel has submitted that the assessee purchased 520 glass bottle moulds from M/s. Mohan Crystal Glass Works, a unit engaged in the manufacture of glass bottle moulds and leased over the same to M/s. Mohan Meacon Ltd. In this connection, he has referred to the invoice dated 28-3-1999 issued by Mohan Crystal Glass Works Prop. Mohan Meacon Ltd.) placed at page.88. A reference has also been made to page 87 wherein it has been confirmed that 520 glass bottles were taken on lease from the assessee and the same were put to use in the business of manufacturing of glass bottles. He has further pointed out that M/s. Mohan Meacon Ltd. vide their letter dated 20-1-1988 placed at page 135 of the paper book have further confirmed that they had taken on lease the glass moulds from the assessee-firm and the assets were duly identifiable. The learned counsel has further pointed out that after the expiry of the -lease period the glass bottle moulds were sold by the assessee-company to M/s. National Cereals Ltd. at Mohan Nagar for Rs. 15,415 on.31-7-1996.

As regards the continuous pusher job furnace, learned counsel has submitted that the assessee had purchased the above furnaces from M/s.

Associated Furnaces Pvt. Ltd. and the same were delivered to the assessee-company. The copy of invoices and the challans, site gate pass and transporters GR were duly furnished to the assessing officer. The supplier of the said furnace had also confirmed the same. The furnace was thereafter given on lease by the

assessee-company to M/s. Punjab Potteries. In this connection, the has referred to the Punjab Potteries letter placed at page 138 of the paper book wherein they have confirmed about the taking of lease of the aforesaid assets. They have also confirmed that no depreciation have been claimed by them on such assets leased by the assessee and the assets when purchased was new. He has further pointed out that the said assets could not be recovered from M/s. Punjab Potteries as the assessee was arranging for a buyer of the equipment and till such time it has been agreed that the asset would remain with the assessee. learned counsel has explained that due to the Supreme Court order the lessor was not able to locate a buyer in the National Capital Territory of Delhi as these items causes environmental pollution. Thus, the learned counsel has contended that in all the cases of lease the assets were purchased by the assessee and their existence had neither been doubted by the revenue. Thus, he has urged that the lower authorities were not justified in denying the claim of depreciation on the aforesaid assets leased to the above named parties.

The learned Department Representative, on the other hand, has submitted that it is incorrect to say that the assessing officer has not followed the directions given by the Commissioner (Appeals) in his order dated 22-3-1996 inasmuch as the assessing officer has examined the matter in great details on the lines of directions given by the Commissioner (Appeals). The Learned DR has further argued in support of the impugned order on the line of reasoning assigned by the lower authorities.

We have heard the parties and have perused the material to which our attention was drawn during the course of hearing of the appeal. The transaction of sale and lease back are well known transactions. It is a common knowledge that several banks and institutions are carrying out the leasing business by financing purchase of equipment taken back and used by them on lease. Explanation 4A to section 43(1) which came in the statute with effect from 1-10-1996 also recognizes the sale and lease back transactions. However, in all such transactions it has to be proved that the transactions were entered into bona fidely and there is material to show that these are given effect to. The transactions are to be proved by the person relying upon them to claim deductions.

Whether a particular transaction is a genuine business transaction or not has to be gathered from the facts of each case. In the case of sale and lease back transactions the same is generally to be treated as a sham if there is finding that the assessee shown to have leased out the asset not exist or where it is found that the same asset is leased out to more than one lessee at the same time. If these findings are not there and if other related facts are not found to be abnormal then there is little scope to apply the ratio of the decision in the case of McDowell & Co. Ltd. v. CTO (1985) 154 ITR 148 (SC). It may be mentioned that the decision in the case of McDowell & Co. Ltd. (supra) has been considered recently by the Hon'ble Supreme Court in the case of Union of India v. Azadi Bachao Andolan (2003) 263 ITR 706 where Their Lordships at page 758 have held as under : 'We may in this connection usefully refer to the judgment of the Madras High Court in M.V. Valliapan v. ITO (1988) 170 ITR 238 (Mad), which has rightly concluded that the decision in McDowell (1985) 154 ITR 148 (SC) cannot be read as laying down that every attempt at tax planning is illegitimate and must be ignored, or that every transaction or arrangement which is perfectly permissible under law, which has the effect of reducing the tax burden of the assessee, must be looked upon the disfavour. Though the Madras High Court had occasion to refer to the judgment of the Privy Council in IRC v. Challenge Corporation Ltd. (1987) 2 WLR 24, and did not have the benefit of the House of Lord's pronouncement in Craven's case (1988) 3 All ER 495 (HL)/(1990) 183 ITR 216 (HL), the view taken by the Madras High Court appears to be correct and we are inclined to agree with it.

We may also refer to the judgment of the Gujarat High Court in Banyan and Berry v. CIT (1996) 222 ITR 831 (Guj) at 850 where referring to McDowell's case (1985) 154 ITR 148 (SC), the court observed : 'The court nowhere said that every action or inaction on the part of the taxpayer which results in reduction of tax liability to which he may be subjected in future, is to be viewed with suspicion and be treated as a device for avoidance of tax irrespective of legitimacy or genuineness of the act; an inference which unfortunately, in our opinion, the Tribunal apparently appears to have drawn from the enunciation made in McDowell's case (1985) 154 ITR 148 (SC). The ratio of any decision has to be understood in the context it has been made.

The facts and circumstances which lead to McDowels decision leave us in no doubt that the principle enunciated in the above case has not affected the freedom of the citizen to act in a manner according to his requirements, his wishes in the manner of doing any trade, activity or planning his affairs with circumspection, within the framework of law, unless the same fall in the category of colourable device which may properly be called a device or a dubious method or a subterfuge clothed with apparent dignity.' The assessee is engaged in the business of import and export, financing and leasing. During the year under consideration the assessee has entered into a purchase and lease back agreement with the above named parties.

The assessee purchased five sugar mill rollers from M/s. Sumec International Ltd. (SIL), leased back the same to M/s. SIL on 10-9-1991. The assessing officer held that this transaction with M/s.

SIL as a colourable device to reduce the tax liability. She noticed that M/s. SIL purchased these assets from BHEL (Unit : Central Foundry Forge Plant) at Rs. 16,21,000 including the cost of machining work done to those assets whereas the assessee had claimed to have purchased from M/s. SIL at Rs. 41.25 lakhs. Moreover, after the expiry of lease period the assessee had not got possession of assets leased out to them. The case of the assessee, however, is that one sugar mill roller had two shafts and each shaft was purchased for a sum of Rs. 3,23,942 from BHEL. Thus, the cost of 10 shafts came to Rs. 32,39,420 plus CST and over and above the machinery work of Rs. 20,000 per shaft was done. In this connection, the learned counsel for the assessee referred to pages 99 to 105 of the paper book. learned counsel further explained that the assets continued to be remained with the lessee on account of litigation pending before the Hon'ble High Court of Allahabad (Lucknow Bench). In this connection, he has referred to pages 111 to 132 of the Paper Book. The perusal of these papers would show that these papers relate to the company petition filed under section 433(e) read with section 439(b) of the Companies Act, 1956 before the Lucknow Bench of the Allahabad High Court for winding up of the lessee company (M/s.

SIL) on account of dishonouring of cheque No. 151229 dated 1-10-1993 of Rs. 22,79,000 and cheque No. 151230 dated 1-1-1994 for the same amount being quarterly rental for the respective quarters drawn on bank of India in favour of the complainant i.e., the assessee-company herein. It is also mentioned in the company petition that M/s. SIL entered into a lease agreement with the complainant (assessee) on 10-9-1991 and took on lease five sugar mills rollers for a period of 3 years on a rental stipulated in the said deed. Thus, the fact that the assessee-company moved the Hon'ble High Court for winding up of the lessee company as aforesaid would establish that there was a purchase and lease agreement for five sugar mill rollers between the assessee and the lessee company and not merely a paper agreement. The payment made by cheque to the lessee company for purchase of the said sugar mill rollers has not been disputed. The invoice dated 11-9-1991 issued by Sumec International Ltd. for sugar mill rollers 1 to 5 in favour of the assessee is for a sum of Rs. 41.25 lakhs. The lessee has also given a certificate that it received the delivery of five sugar mill rollers on lease from the assessee-company as per lease agreement dated 10-9-1991. The Explanation 3 to section 43(1) reads as under :- "Where, before the date of acquisition by the assessee, the assets were at anytime used by any other person for the purposes of his business or profession and the assessing officer is satisfied that the main purpose of the transfer of such assets, directly or indirectly to the assessee, was the reduction of a liability to income tax (by claiming depreciation with reference to an enhanced cost), the actual cost to the assessee shall be such an amount as the assessing officer may, with the previous approval of the Joint Commissioner, determine having regard to all the circumstances of the case." It is one of the essential conditions for invoking Explanation 3 to section 43(1) that before the date of acquisition of the asset by the assessee the asset was used by other person for the purposes of his business. The second condition is that the assessing officer is satisfied that the main purpose of the transfer of such assets directly or indirectly to the assessee was for reduction of liability to income tax by claiming depreciation with reference to the enhanced cost. If these two conditions are satisfied, then the actual cost to the assessee shall be determined by the assessing officer with the previous approval of JCIT. It may be mentioned that the actual cost to the assessee is entirely a question of fact to be determined with

reference to the evidence and the material. The mere production of documentary evidence showing that a contract was made for the purchase of the asset at a certain price does not conclusively establish the correctness of the claim made by the assessee specially where the assessing officer is of the opinion that in the deal the assessee has taken resort to a subterfuge or device in order to avoid tax which he is liable to pay or otherwise has acted fraudulently or the transaction is illusory or colourable. In such cases the assessing officer can go behind the contract and ascertain the actual cost for the purpose of correct ascertainment of income tax liability of the assessee - *Guzdar Kajora Coal Mines Ltd. v. CIT* (1972) 85 ITR 599 (SC), *CIT v. Jogta Coal Co. Ltd.* (1965) 55 ITR 89 (Cal.) refers. Where an asset was already in use in the hands of one person and its written value has been ascertained by assessing officer and that person transfers the asset to another person for a price exceeding the WDV in the depreciation chart of the file of assessing officer, it is open to the assessing officer to refuse to accept the sale price as the actual cost to the purchaser in the purchaser's assessment. It may however be mentioned that there may be genuine case where asset has appreciated in value since its original purchase and consequently the market value on the date of the sale is greater than its WDV in the assessing officer's chart. It is all a matter to be considered on the facts and circumstances of each case.

There is no material on record to show that the assets were used by M/s. SIL prior to the impugned purchase and lease agreement nor the assessing officer has found out whether these assets were fully or substantially depreciated when these assets were purchased by the assessee-company despite the direction given by Commissioner (Appeals) in its order dated 22-2-1996. The assessing officer merely mentioned that M/s. SIL had unabsorbed loss and did not require the benefit of depreciation. Nor the assessing officer has examined as to whether the case of the assessee fall under Explanation 3 to section 43(1) of the Act as directed by Commissioner (Appeals) in the said order. Therefore, in the absence of such findings no doubt can be cast on cost of assets shown by the assessee.

The essential characteristic of sale is that the property or the goods passes to the buyer. It is not necessary that the assets should physically move to the buyer in order to constitute a valid sale. It is essential that the property in the goods passes

to the buyer, risk and reward attached to the goods also passes to the buyer. The buyer in the instant case has earned the reward in the form of lease rental by leasing it back to the seller. The profit earned on the sale by lessee is also subject to short-term capital gain. The lease agreement contains a clause that on the expiry of the lease period the lessee shall deliver the assets to the lessor/assessee. It is seen that but for the litigation between the assessee and M/s. SIL as aforesaid, the asset would have been returned to the assessee on the expiry of lease period. It is not the case of the revenue that the agreement in question is not entered into at arm's length inasmuch as both the parties are not of same group of company or otherwise related to each other. In the circumstances, we are of the view that in the instant case assessee has satisfied the conditions for the purpose of claiming depreciation under section 32 that the depreciable assets are owned by the assessee and the same were used for the purpose of assessee's business. We, therefore, direct to allow claim of depreciation in respect of these assets of five sugar mill rollers.

The second purchase and lease back transaction relates to gas cylinder.

These gas cylinders were purchased by GAPL and SIGL at the rate of Rs. 1,400 per gas cylinder on 21-3-1992 and the same were sold to the assessee at the rate of Rs. 2,200 per gas cylinder on 24-3-1992. These were used by the lessee. However, they stated to have claimed no depreciation on these assets. In respect of these transactions there is no finding as to whether lessee had claimed and was allowed any depreciation on these assets prior to the impugned transaction of purchase and lease back nor assessing officer has examined whether the case of the assessee falls under Explanation 3 to section 43(1). For the reasons mentioned in respect of the first transaction of purchase and lease back, we direct to allow the claim of depreciation in respect of this transaction.

The third transaction of purchase and lease back relate to 510 glass bottle mould purchased for Rs. 14,01,400 from M/s. Mohan Crystal Glass Works, a unit engaged in the manufacture of glass mould and lease back the same to said concern. The copy of invoice issued by Mohan Crystal Glass Works (Prop. Mohan Meacon Ltd.) is placed at page 88/PB. At the end of lease period the assets were

sold to M/s. National Serial Ltd. a sister concern of the assessee. The grievance of the revenue appears to be that asset purchased at Rs. 14,01,400 were at the end of lease of period were sold at a paltry sum of Rs. 15,415. Hence, this was not a genuine transaction. It seems that revenue is not disputing the purchase price nor the fact that these assets were leased back to the same party nor that the lessee used the assets during the lease period or rental fixed under the agreement was abnormally low. In the absence of these facts, mere fact that the assets sold at the end of lease period at meagre price to sister concerns cannot be said to be material fact which may tilt the issue in favour of the revenue. Further, for the reasons mentioned in respect of first transaction above, we direct to allow the claim of depreciation to the assessee in respect of this transaction.

The last transaction of purchase and lease back relates to continuous pusher type furnace. It is seen that assessee purchased continuous pusher type furnace from M/s. Associated Industrial Furnace (P.) Ltd. for a sum of Rs. 10,57,500, the copies of challan and invoices giving details of various items are placed at pages 67 to 80/PB. The Associated Ind. Furnaces (P.) Ltd. has also confirmed that they have sold /delivered the machinery to its client, M/s. Comecon Overseas (P.) Ltd., the assessee herein vide invoice No. 53 dated 26-3-1992, invoice No. 54 dated 21-3-1992 and invoice No. 55 dated 28-3-1992. They have further confirmed that the said machinery was delivered at Punjab Potteries Premises at Gurgaon Road, New Delhi at the request of M/s.

Comecon Overseas vide their letter placed at page 81/PB addressed to Dy. Commissioner of Income Tax, Spl. Range, New Delhi. M/s. Punjab Potteries vide letter dated page 83 /PB addressed to Dy. CIT has also confirmed that one continuous pusher type furnace has been taken on lease by them from the assessee and this furnace has been fabricated and supplied by M/s. Associated Ind. Furnaces (P) Ltd. M/s. Punjab Potteries have further confirmed that they have not sold this furnace to M/s. Comecon Overseas (P) Ltd. Therefore, in view of above facts, this is incorrect to say that this is purchase and lease back transaction entered into by the assessee and M/s. Punjab Potteries. The fact that the assessee has purchased this furnace at the cost of Rs. 10,57,500 is not in dispute nor the fact that the same was leased out to M/s. Punjab Potteries. The

reason for not recovering the furnace from M/ section Punjab Potteries after the expiry of lease period has been explained by the learned counsel which appears to be justified.

The leasing of the asset being the business of the assessee. We, therefore, hold that the assessee-company has satisfied the conditions for the purpose of claiming depreciation under section 32 that depreciable assets are owned by the assessee and the same were used for the purpose of assessee's business. We, therefore, direct to allow the depreciation to the assessee.

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