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SooperKanoon Citation : sooperkanoon.com/75391

Court : Income Tax Appellate Tribunal ITAT Delhi

Decided On : Jan-12-2007

Reported in : (2007)109ITD198(Delhi)

Judge : D Singh, R Singh

Appellant : Midland International Ltd.

Respondent : Dcit

Judgement :

1. The assessee has filed this appeal against the order of CIT (Appeals)-IX, New Delhi, passed in Appeal No. 0380/2001-2002 dated December 23, 2002 on the following grounds: 1. That the learned Commissioner of Income Tax (Appeals) was not justified to uphold A.O.'s action in having held that for determining ALV of the property, addition of 15% interest on the security deposit, if any, had to be added and further erred in enhancing the ALV of the property by adding an amount of notional interest calculated at 15% on security deposit of Rs. 3,79,620/- instead of on Rs. 2,86,443/-adopted by the Assessing Officer.

2. That the learned Commissioner of Income Tax (Appeals) was further not justified to uphold action of the Assessing Authority in having allocated administrative and personnel expenses to property income whereas no such expenses were in fact incurred for the purpose.

3. That the learned Commissioner of Income Tax (Appeals) further gravely erred to have upheld the disallowance of Rs. 32,554/- out of telephone expenses and Rs. 8,018/- out of car expenses/depreciation observing that in the absence of a log book and call records disallowance out of vehicle depreciation and telephone expenses had to be confirmed. Appellant's contention was that in the case of the appellant company no such disallowance was warranted to be made.

2. First, we shall deal with Ground No. 1 relating to the issue of determination of ALV of the rented property.

3. Briefly stated the facts are that the assessee had let out a commercial space on an annual rent of Rs. 25,30,800/- and has also received an amount of Rs. 25,30,800/- as interest free security. The Assessing Officer was of the opinion that the security deposit received by the assessee was an advantage accruing to the assessee as a result of letting out of the property so it was to be taken into consideration for determining the ALV of the property in terms of Section 23 of the Income Tax Act. Thereafter, the Assessing Officer worked out the ALV of the property and enhanced the same by adding interest @ 15% on the average value of security deposit of Rs. 19,09,623/- and made the impugned addition of Rs. 2,86,443/- by relying upon the decision of ITAT Bombay Bench in the case of CIT v. Rati Agnihotri in ITA No. 6826 BOL/80A and 8824/Del/90 wherein the Tribunal held that interest on security deposit had to be added to the actual rent received in order to arrive at ALV of the property.

4. Aggrieved, the assessee filed an appeal before the CIT (A) and contended that no addition on account of notional interest on the security deposit was called for because the security deposit was obtained only in order to cover the risk arising from handing over the property for use to an unknown person and the risk associated with the failure on the part of the tenant to honour the terms of the lease. The assessee further contended before the CIT (A) that the Assessing Officer had not been able to bring on record anything to show that the rent fixed as per the base deed was in any manner less than the prevailing rent of a similar property in the same area and there was no reason to deviate from the rent as stated in the lease deed because under the provisions of Income Tax Act the

concept of taxing notional or hypothetical income, as affirmed by Supreme Court in the case of Godhra Electricity (C) Ltd. v. CIT reported in 225 ITR 746, and in the case of CIT v. Satya & Co. reported in 75 Taxman 193, was not recognized. For a similar view learned AR for the assessee relied upon J.K. Investors (Bombay) Ltd. v. DCIT 74 ITD 274.

5. After considering the submissions, the CIT (A), after giving a notice to the assessee, enhanced the ALV by adopting notional rent at 15% on a sum of Rs. 25,30,800/- and increased the annual value of the property by Rs. 3,79,620/-, against Rs. 2,86,443/- adopted by the Assessing Officer by modifying the order of the Assessing Officer. In the order the CIT (A) further observed that the interest free deposit definitely contribute to bring down the rent and, therefore, is necessary to be taken into consideration for determining the sum for which the property might reasonable expected to let from year to year.

6. Further, that the assessee has not furnished the municipal valuation of the property as admitted by the assessee in his letter. Thereafter placing reliance on the decision of ITAT Mumbai Bench in the case of ITO v. Chem Mech (P) Ltd. 83 ITD 427 and the case of Rakesh Aggarwal v. ACIT 221 ITR 492 (Del) the CIT (A) held that the annual letting value of the property under Section 22 of the Act can be worked out by taking into consideration the notional interest received by the assessee on interest free security deposit received by the assessee from the tenant and hence the CIT (A) confirmed the action of the A.O. for determining the ALV of the property by adopting 15% interest rate on the security deposit.

7. Aggrieved, the assessee is in appeal before us. Learned AR for the assessee reiterated the submissions and further relied upon the case law cited before the CIT (A) and also referred to the recent decision of Delhi Bench in the case of Kailash Enterprises, New Delhi v. DCIT, ITA No. 504/Del/2001, Assessment Year 1997-98 dt. 28.10.2005 and submitted that the element of notional income by way of interest on security deposit received by the assessee cannot be considered to determine the ALV of the property under Section 23(1)(a) so the tax authorities below were not justified in making the impugned addition under Clause (b) of Section 23 (1) of the Act.

8. On the other hand, learned DR for the revenue supporting the orders of tax authorities below submitted that the CIT (A) has rightly made the impugned addition by enhancing the ALV of the property by taking notional interest @ 15% of the interest free security deposit received by the assessee from his tenant and, therefore, the assessee's appeal is liable to be dismissed. In support of his contentions, learned DR for the revenue further placed reliance in the case of Shri Bipinbhai Vadilal Family Trust No. 1 v. Commissioner of Income Tax Guj; Rakesh Agarwal (Legal Heir of Late R.S. Agarwal) v. Assistant Commissioner of Income-Tax Del and Assistant Commissioner of Income Tax v. Shreyas K. Doshi 2006 (005) SOT 0797 TBOM.9. We have considered the rival contentions of both the parties, perused the records and carefully gone through the orders of tax authorities below.

10. The undisputed facts in this case are that the assessee has received annual rent of Rs. 25,30,800/- alongwith interest free security deposit of Rs. 25,30,800/-. The assessee has not filed any annual letting value either as determined under the Municipal Corporation Laws or as under the Rent Control Act nor the Assessing Officer has done so under the provisions of Section 23(1)(a) of the Act. It means that by not determining the ALV under Section 23(1)(a) the Assessing Officer has neither compared the ALV of the property with the actual rent declared by the assessee nor has given any finding that the rent declared by the assessee was in any way less than the ALV required to be determined under Section 23(1)(a) of the Act.

11. The relevant provisions of Section 23, after amendment w.e.f.

01.04.1976 and as applicable for assessment year, under consideration before us, are stated as under: As per Section 23 (1) of the Income Tax for the purpose 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 owner in respect thereof is in excess of the sum referred to in Clause (a), the amount so received or receivable; Thus, on giving a comprehensive reading to provisions of Section 23(1)(a) and 23(1)(b), it is inferred that the annual value of the property for

determining the income from house property is deemed to be the sum for which the property might reasonably be expected to let from year to year or where the property is let and the annual rent received or receivable is in excess of such sum, the amount so received or receivable.

It further means that the determination of the annual value is to be made of the sum for which property might be reasonably expected to let from year to year and the same is to be compared with the actual rent received and if the rent so received or receivable is higher than the amount at which it would be reasonably expected to let from year to year then the actual rent received will be adopted as an annual value.

12. Thus, we find that for the purposes of Section 22 for determining the annual value of the property, the Assessing Officer as per Section 23(1)(a) is required to determine the sum for which the property might reasonably be expected to let from year to year and which can be determined with reference to the standard rent if the same has been fixed and if not fixed then by referring to municipal ratable value of the property in case the same is fixed and if not then the same can be determined as per the guidelines laid down in the provisions of Municipal Act because in the case of CIT v. Bhaskar Mitter 73 Taxman 473 (Cal.), their Lordships have held that the annual value cannot exceed the standard rent and the fair rent under the Rent Control Act and where the standard rent is not fixed the ratable value of the property may be a good guide.

Similarly, in the cases of Mrs. Sheela Kaushik v. CIT 131 ITR 435 (SC), Dr. Balbir Singh v. MCD 152 ITR 388 and Dewan Daulat Ram Kapoor v. NDMC 122 ITR 700, their Lordships of the Apex Court have very clearly held that the sum for which the property reasonably be expected to let from year to year is a hypothetical amount which needs to be ascertained considering the applicable laws governing the place where the property is situated and must be held to be a standard rent determinable under the provisions of the Act applicable for such determination.

13. Thereafter, in case the Assessing Officer finds that such ratable value determined by him under Sub-clause (a) of Sub-section (1) of Section 23 is higher

than the actual rent received or receivable by the assessee under Sub-clause (b) of Section 23(1) then for this purpose of Section 22 the annual value of the property shall be taken as the value determined by the Assessing Officer under Section 23(1)(a) of Income Tax Act and in case it is lesser than the actual rent received or receivable by the owner then the actual rent received or receivable shall be taken as the annual value of the property for purposes of Section 22.

14. On carefully going through the order of the Assessing Officer, we find that the Assessing Officer has not adhered to the provisions of Section 23(1)(a) or 23(1)(b) of the Income Tax Act as he has neither determined the annual value of the property as per Section 23(1) of the Income Tax Act by adopting the value as determined by NDMC or in accordance with the provisions of Delhi Rent Control Act, if applicable in the case of the assessee. The Assessing Officer has neither compared the actual rent received with the ALV of the property determined under Section 23(1)(a) for the purposes of Income Tax Act under Section 22 of the Act.

15. In any case for the purposes of Clause (a) to Section 23(1), which is relevant to the instant case, what is required to be determined is the sum for which the property might reasonably be expected to let from year to year. The essential requirement is to arrive at a sum for which the property is 'reasonably be expected to let'. What is expected to be done is under Section 23(1)(a) is to decide the fair rent for which the property is expected to be let from year to year which can be done either on the basis of fair rent fixed by the local Municipal Corporation Laws or under the Delhi Rent Control Act but certainly not by considering any notional income representing the interest on security deposit received by the owner of the property. We are of the opinion that this certainly cannot be a relevant factor to evaluate the fair rent of the property because a notional income for such purposes was never contemplated under this section.

16. The cases (supra) relied upon by the learned DR for the revenue is distinguishable on facts. In the case of Shari Bipinbhai Vadilal Family Trust No. 1 v. Commissioner of Income Tax (supra) Gujarat High Court, we find that the agreed rent shown by the assessee was Rs. 500/- p.m.

and the same was much less than the ALV of the property adopted by the Assessing Officer at Rs. 18,000/- p.m. on the basis of the value of the property shown at Rs. 2,15,000/- and was adopted after taking into consideration these factors by the Assessing Officer. Similarly, in the case of Rakesh Agarwal (supra) decided by Hon'ble Delhi High Court the main question under consideration was regarding the reopening of the assessment under Section 147 whereas the determination of ALV under Section 23(1)(a) and 23(1)(b) was not under consideration. On the contrary the assessee before the High Court had not denied the income from house property declared and assessed on the basis of actual rent received and the same was admitted by the assessee to be less than the annual ratable value of Rs. 1,62,400/- determined by the Municipal Corporation for the purpose of property tax. In those facts the Hon'ble High Court dismissed the appeal of the assessee, but, those are not the facts under consideration in the instant case before us. Hence, this citation too is of no help to the revenue.

17. Lastly, the decision of Mumbai Bench in the case of Shreyas K.Doshi (supra) is also of not much help to the revenue because they have also accepted in principle that the actual rent received or receivable as per Section 23 (1)(b) excludes any other notional interest, as held in the decision of Calcutta High Court in Satya Co. Ltd. (supra) and Hon'ble Bombay High Court in J.K. Investors (Bombay) Ltd. (supra), and further according to them there was absolutely no dispute or a different view on this subject.

18. Whereas, from the ratio of the decision (supra) relied upon by Learned AR for the assessee as well as referred to and analyzed by us hereinabove in this order we have come to a conclusion that though the revenue under the provisions of Income Tax Act can tax the rental income of the property under the head 'income from house property' but the same cannot be done by the Assessing Officer by considering the element of notional income by way of interest on interest free security received by the assessee for the purposes of determining the ALV of the property under Section 23 (1)(a) because the same can only be considered on the basis of annual value either determined under the provision of Municipal Corporation Act or under the Delhi Rent Control Act. Hence, we conclude that the element of notional income by calculating the interest receivable on the interest

free security deposit received by the assessee for the purposes of determining the annual value of the property cannot be considered as the same is not contemplated under Section 23 of the Act.

19. In the instant case admittedly neither the assessee has given the annual letting value as determined under the provisions of Municipal Corporation Act or NDMC Act or under the Rent Control Act nor the Assessing Officer has determined the same under Section 23(1)(a) of the Act as observed in our order hereinabove, hence, in these facts and circumstances we set-aside the orders of tax authorities below and direct the Assessing Officer to recompute the ALV of the property in term of Section 23(1)(a) of the Act by considering the Municipal Valuation as per the MCD Act/By-Laws or NDMC Act/By-Laws or under Delhi Rent Control Act whichever is applicable in the instant case of the assessee and thereafter in case he finds the ALV of the property so determined to be higher than the actual rent declared by the assessee the rental income should be enhanced accordingly and in case he finds the rent declared by the assessee to be higher then the ALV so determined by the Assessing Officer then he should accept the same and should not make any addition in this regard. In the result the Ground No. 1 of the appeal filed by the assessee stands allowed partly for statistical purpose.

21. In brief, the facts relating to the Ground of Appeal are that the Assessing Officer noticed that the assessee had claimed repair expenses equal to 1/5th of ALV while computing net income from house property but had not reduced any expenses, which would have been incurred in relation to earning of the rental income. The assessee's argument that no expenses relating to house property let out were debited to the P&L Account was not accepted by the Assessing Officer. He was of the view that since the assessee was carrying out number of activities, indirect expenses were relatable to all the activities including the activity of letting the property on rent. He, therefore, apportioned indirect expenses representing personnel expenses, administrative expenses, and financial expenses aggregating to Rs. 25,30,800/- in proportion to the gross receipts and rental receipt and calculated indirect expenses attributable to rental income at Rs. 4,12,005/-.

22. On appeal before the CIT (A), the assessee contended that it had not incurred any interest expenditure on the amount spent for purchase of property and merely because the assessee was enjoying income from house property, it could not be concluded that part of the expenditure related to property income. The assessee furnished the details of the personnel administrative and financial expenses and stated that the Assessing Officer had not pointed out any item of expenditure not incurred for the business of the assessee. It was submitted that rent was being received from tenant and deposited in the bank account and this work was done by an employee who was otherwise engaged in the running of the business.

23. After considering the submissions, the CIT (A) restricted the proportionate disallowance to personnel and administrative expenses while making following observations: I have examined the contentions of the appellant. Letting out of the property and its maintenance etc. would involve some element of personnel and administrative expenses. The details of financial expenses showed that these represent bank interest and commission, interest on export packing credit and interest on export bill purchase and therefore no component could be attributed to house property income. In view of the failure of the appellant to specifically earmark personnel/administrative expenses relatable to the commercial property, the A.O. was justified in adopting the yardstick of proportionate allocation. A.O. is therefore directed to recalculate the disallowance by excluding the financial expenses and restrict the proportionate disallowance to personnel and administrative expenses.

24. We have considered the rival contentions of both the parties, perused the records and carefully gone through the orders of the tax authorities below.

25. In the instant case the assessee has specifically contended before the tax authorities below that it had not incurred any personal, administrative and financial expenses for managing the house property in question. In this regard the assessee furnished the details of personal and administrative and financial expenses for the business of the assessee. On the other hand, the tax authorities below without pointing any specific item of expenditure being incurred by the assessee towards the management of house property from which the assessee

has offered rental income for tax purposes have simply disallowed the ad hoc proportionate disallowance towards personal administrative expenses after excluding financial expenses shown by the assessee. In the instant case since the assessee has furnished the complete details of expenses incurred by the assessee for the business of the assessee, in our opinion, the tax authorities below were not justified in making the ad hoc proportionate disallowance of these expenses without identifying any such expenditure having been incurred by the assessee for administrative and personal purposes and more so, when according to the assessee he was simply receiving rent from the tenant, which was deposited in the bank account of the assessee for which it has not incurred any separate expenditure. For the reasons stated above, the ad hoc proportionate disallowance sustained by the CIT (A) in this regard cannot be upheld and, therefore, the order of CIT (A) in this regard is set-aside and Ground No. 2 of the assessee's appeal is allowed.

26. We shall now deal with Ground No. 3 of the appeal relating to the disallowance of telephone expenses, car expenses/depreciation.

27. In brief the facts relating to the ground of appeal are that the Assessing Officer disallowed a sum of Rs. 32,554/- out of telephone expenses and a sum of Rs. 8,018/- out of car expenses/depreciation on the reasoning that the elements of personal expenditure by the assessee could not be ruled out, so, 1/10th of the total expenses claimed by the assessee were disallowed treating the same to be of non-business nature.

28. The CIT (A) upheld the order the Assessing Officer by placing reliance on the decision of Madras High Court in the case of New Ambadi Estates (P) Ltd. v. State of Tamil Nadu 256 ITR 64, wherein in the case of a company their Lordships held that the onus was not on the authorities to prove that motor car expenses were partly for personal usage but the onus lay on the petitioner who claims that it was not used for personal usage.

29. Before us, learned Counsel for the assessee submitted that the issue whether in the case of a company any such disallowance, as involved in the instant case of the assessee, could be made, came up for consideration before the Gujarat High

Court in the case of Syaji Iron Industries 253 ITR 749 (Guj) and the Tribunal in DCIT v. Haryana Oxygen Ltd. 76 ITD 32 (Del); Perfect Pac (Ltd.) v. IAC 46 TTJ 438 (Del) and Banko Products Ltd. v. DCIT 63 ITD 370 (Ahmedabad) and the Tribunal consistently decided the issue in favour of the assessee and against the revenue by holding that no such disallowance could be made in the case of companies.

30. Learned AR for the assessee further submitted that the CIT (A) was not justified in ignoring the decisions favouring the assessee in preference to the decision of Madras High Court (supra) without assigning any specific reasons.

31. Learned DR for the revenue except placing reliance on the reasoning given in the order of the CIT (A) was not able to controvert the above specific submission of learned AR for the assessee.

32. In this view of the matter we are of the opinion that when the Gujarat High Court in the case of Syaji Iron Industries (supra) and various Tribunals in a number of decisions (supra) have consistently been deciding the issue in favour of the assessee and against the revenue after considering the various decisions of the High Courts, the CIT(A) was not justified in disallowing the claim of the assessee by merely following the decision of Madras High Court (supra) which was not of jurisdictional High Court because in the various judicial pronouncements by High Courts and the Apex Court it has been consistently held that in case there are two decisions of two different High Courts, one in favour of the assessee and the other against the assessee, the decision favourable to the assessee is to be adopted.

Hence, keeping in mind this principle and following the decision of Gujarat High Court in the case of Syaji Iron Industries (supra) and the decisions (supra) of the Tribunals we hold that the CIT (A) was not justified in upholding the order of Assessing Officer wherein a case of a company he disallowed the expenses claimed by the assessee company with regard to telephone and car/depreciation treating the same to be of personal nature. Accordingly, the order of CIT (A) in this regard is set aside and the disallowances sustained by the CIT (A) in this regard are deleted. Ground No. 3 of the assessee's appeal is allowed.