

(1994) 11 BOM CK 0066

In the Bombay High Court

Case No : Income-tax Reference No. 174 of 1983

Commissioner of Income Tax

APPELLANT

Vs

Arvindkumar Odhavji

RESPONDENT

Date of Decision : 16-11-1994

Acts Referred:

Income Tax Act, 1961 — Section 14, 28, 56

Citation : (1995) 213 ITR 551

Hon'ble Judges : S.M. Jhunjhunwala, J; B.P Saraf, J

Bench : Division Bench

Advocate : G.S. Jetley, for the Appellant; Y.P. Trivedi, for the Respondent

Judgement

S.M. Jhunjhunwala J.

1. By this reference filed u/s 256(1) of the Income Tax Act, 1961, at the instance of the Revenue, the following question has been referred :

"Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the rent income received from the Vijaya Bank as per lease agreement for 15 years was liable to be assessed as "business" income and not as income from "other sources" for the assessment year 1976-77 ?"

2. The assessee is an individual who had income from property as well as business. The assessee carried on business in partnership with others in rented premises. According to the assessee, the assessee was not doing well in the business carried on in partnership as a result whereof, the assessee suffered substantial losses and in order to save the losses and reduce the indebtedness, the assessee thought of letting out the premises where the business was carried on, on sub-lease. The assessee entered into an agreement dated October 17, 1973, with the Vijaya Bank Ltd. for leasing out the said premises to the Vijaya Bank Ltd. for a period of 15 years on lease amount of Rs. 6,000 per month. The said agreement also contained a clause for renewal of the lease for a period of five years. The Vijaya Bank Ltd. (for short, "the said bank") had agreed to

advance a loan of Rs. 5 lakhs to the partnership firm on interest at the rate of ten per cent. per annum and the lease rent payable by the said bank was to be adjusted against the interest payable by the partnership firm on the loan amount. Clause 11 of the said agreement which is relevant for the purpose of the controversy involved, reads as under :

"11. The licensees have as agreed advanced a loan to the licensors of a sum of Rs. 5,00,000 with ten per cent. as interest thereon, which amount is paid on the following terms :

(a) The loan amount will be debited in the "Messrs. Odhavji Lavji and Co."s loan account in the licensees" books of account.

(b) The loan and interest will be repaid by adjustment by crediting the monthly licence fees amount of Rs. 6,000 payable by the licensees to the licensors at the end of each current month.

(c) Interest at the rate of ten per cent. per annum as provided above will be payable with six months" rests on the loan amount or the balances thereof remaining due each month."

3. In the assessment year 1976-77, the Income Tax Officer assessed the lease rent income from the said bank as "income from other sources" instead of an "income from business". In the appeal before the Appellate Assistant Commissioner, the assessee contended that the Income Tax Officer grossly erred in treating the lease rent realised in respect of the said premises as "income from other sources" since the said premises were a commercial asset of the partnership firm, the assessee was free to exploit the same in any manner as the assessee desired so as to yield better returns and as such, should have been treated as "income from business". The Appellate Assistant Commissioner held that the income realised by letting out the said premises was required to be treated as "income from business" and directed the Income Tax Officer to modify the computation of income accordingly treated it as business income. Against the said order of the Appellate Assistant Commissioner, the Department filed an appeal before the Income Tax Appellate Tribunal (for short, "the Tribunal"). The Tribunal held that by letting out the said premises on lease for 15 years it could not be said that the said premises had ceased to be part of the assessee's commercial assets and that the loan taken by the said partnership firm was closely connected with the business of the assessee and that the income by way of rental received for the period of 15 years was to be treated as business income. In view of the said findings of the Tribunal, the present reference has been filed at the instance of the Revenue.

4. The rental income received in respect of the said premises was assessable as part of the assessee's total income. The question, however, was under which head of income the rent amount was to be assessed for purpose of computation of total income of the assessee. Originally, for some period, the assessee showed the income received by way of rent in respect of the said premises as "income

from other sources". Later on, the assessee claimed such income as "income from business". The Income Tax Officer assessed such income as "income from other sources". The Appellate Assistant Commissioner treated it as business income. The Tribunal accepted the assessee's contention and directed the assessment of rental income as business income. Mr. Jetley, learned counsel for the Revenue, has submitted that the Tribunal's decision is erroneous in law. In his submission, sub-letting or giving of the said premises on licence basis was not the business of the assessee as the said partnership firm carried on business in aerated water and as such, the rental income received by the assessee during the previous year relevant to the assessment year was not "income from business". In support of his submission, Mr. Jetley has relied upon the judgment of this court in the case of *Baijnath Brijmohan and Sons P. Ltd. Vs. Commissioner of Income Tax*, . Mr. Trivedi, learned counsel for the assessee, has submitted that sub-letting of the said premises by the assessee to the said bank was an integral part of the said agreement under which the said bank had advanced a loan of Rs. 5 lakhs to the said partnership firm at the concessional rate of ten per cent. per annum and that it being a case of exploitation of a commercial asset by the assessee, the rental income derived therefrom was to be treated as "income from business". In support of his submissions, Mr. Trivedi has relied upon judgments in *Commissioner of Income Tax, Delhi (Central) Vs. Northern India Theatres P. Ltd.*, , *Commissioner of Income Tax, Tamil Nadu-I Vs. B. Nagi Reddy*, , *Commissioner of Income Tax, Lucknow Vs. Vikram Cotton Mills Ltd.*, and *Commissioner of Income Tax Vs. Anand Rubber and Plastics (P.) Ltd.*, .

5. The assessee is an individual. The assessee has been a partner in the said partnership firm of Messrs. Odhavji Lavji and Co., who carried on business in aerated water material. The said business was carried on at the said rental premises. The said partnership firm had sub-let or given on licence the said premises to the said bank on the terms and conditions mentioned in the said agreement dated October 17, 1973. In the facts of the case, the question which arises for determination is as to whether the rental income received by the said partnership firm from the said bank was required to be treated as "income from business" as contended by the assessee or "income from other sources". No general principle can be laid down in this regard. Whether a particular letting is business has to be decided in the circumstances of each case and each case must be decided in the setting and background of its own facts. In each case what has to be seen is whether the asset is being exploited commercially by the letting out or whether it is being let out for the purpose of enjoying the rent. Whether a particular income received by the assessee as a result of activities carried on by the assessee is business income or rental income depends upon the manner of exploitation of the asset by the assessee.

6. The Income Tax is only one tax, levied on the sum total of the income classified and chargeable under the various heads. Section 14 of the Income Tax Act, 1961, classifies profits and gains under different heads according to the character of the source, for the purpose of providing for each head appropriate

rules for computing the amount of income. The heads of income enumerated u/s 14 are mutually exclusive. Income which is specifically made chargeable under a distinct head cannot be brought to charge under a different head.

7. As per the assessee, the business in aerated water material carried on by the said partnership firm was not doing very well and the assessee had suffered substantial losses and in order to save the losses and reduce the indebtedness, the assessee thought of letting out the said premises on sub-lease and entered into the said agreement dated October 17, 1973, with the said bank for leasing out the said premises for period of 15 years on a lease rent of Rs. 6,000 per month with an option to renew the same for a period of five years. The Appellate Assistant Commissioner had held that as the assessee temporarily let out the business premises to the said bank and decided to carry on its business activities from other places near by and since the said bank had provided substantial amount of loan at favourable interest and agreed to pay lease rent of Rs. 6,000 per month, the arrangement was beneficial to the assessee's business and the income realised by the said partnership firm by letting out the said premises temporarily was to be considered as income from business. The Department in appeal contended before the Tribunal that the assessee was a tenant in respect of the said premises and that the tenancy right was not part of the business assets of the said partnership firm. It was further contended that in any event the said premises leased out to the said bank had ceased to be part of the assessee's business premises and it had severed its connection with the firm since the lease for a period of 15 years was for substantially a long period of sever its connection with the business of the said partnership firm. On the facts of the case, the Tribunal held as under :

"We do not find any material to show that the Department has accepted that tenancy right is a commercial asset. Reliance had been placed on the finding that the leasing out is closely connected with the loan which will be given by the bank to the assessee. In other words, the premises leased out is something like security for the loan. Now, all securities on which loans are granted for business are not necessarily commercial assets. Whether they are commercial assets or not is to be decided by the nexus with the business."

8. Although Mr. Trivedi has submitted that it being the case of exploitation of a commercial asset by the assessee, the rental income derived therefrom should have been treated as "income from business", in the facts of the case, it is not possible even to accept that the tenancy in respect of the said premises was a commercial asset of the said partnership firm or that the rental income received therefrom was "income from business". The assessee, in individual, was a tenant in respect of the said premises where the said partnership firm carried on business in aerated water material. The said partnership firm had sub-let the said premises in favour of the said bank for a substantial long period of 15 years on the terms mentioned in the said agreement dated October 17, 1973. There is nothing to show that the said partnership firm or the assessee at any time

carried on business of letting out their office premises. The facts found clearly show that the only business which the said partnership firm or the assessee had been carrying on was in aerated water material. The activity of sub-letting the said premises to the said bank, in our opinion, cannot be said to be a business activity of the assessee or of the said partnership firm but merely a way of exploiting the property of the assessee, namely, the tenancy rights in the said premises to derive income therefrom. The rental income derived by the assessee from sub-letting the said premises was not business income. We find considerable support for the view which we are taking from the judgment of a Division Bench of this court in *Parekh Traders Vs. Commissioner of Income Tax, Poona*, :

"..... In that case, the assessee-firm which carried on business in the manufacture and sale of manure mixtures in the City of Poona constructed a godown outside the limits of the Poona Municipality. From July, 1968, till the middle of November, 1968, it used the godown for storing its raw materials, etc. Thereafter the godown was let out up to January, 1971. In the assessment year 1970-71, the assessee had in its return disclosed a sum of Rs. 80,092 as "income from house property" against the godown rent of Rs. 1,08,300. The Income Tax Officer held that the rent received from the letting out of the godown had to be assessed as "income from other sources". The Appellate Assistant Commissioner held that the rent had to be assessed as income from house property and that the annual value of the godown was Rs. 1,08,300. The Tribunal held that the income derived by the assessee by letting out the godown was to be assessed under the head "Income from house property"."

9. It has been pointed out by the Division Bench that the heads of income enumerated in section 14 of the Income Tax Act, 1961, are mutually exclusive and each specific head covers items of income arising from the specific source. Income derived as rent from property must be computed under the specific head regardless of the fact that property had at one time been utilised by the assessee for business purposes. Such property cannot be treated as a business asset and the rent therefrom as income from business. The Division Bench took the view that although the godown at one time had been used for business purposes by the assessee, since in the relevant previous year the godown had been let out for purposes other than business, it could not be held that the income from (letting) the godown was business income. It was really income from house property. In coming to this conclusion, the Division Bench has placed reliance on the decision of the Supreme Court in *East India Housing and Land Development Trust Ltd. Vs. Commissioner of Income Tax, West Bengal*, . In that case, the Supreme Court has taken that if the income from a source falls within a specific head set out in section 6 of the Indian Income Tax Act, 1922, the fact that it may indirectly be covered by another head will not make the income taxable under the latter head.

10. Even in the case of *Baijnath Brijmohan and Sons P. Ltd. Vs. Commissioner of Income Tax*, relied upon by Mr. Jetly, a Division Bench of this court, while relying

upon the judgment of this court in *Parekh Traders Vs. Commissioner of Income Tax, Poona*, , took a similar view. In that case, the assessee was a private limited company incorporated in 1959 primarily with the object of dealing in mill-made cloth on commission basis. It took certain office premises on hire and also took a godown on hire. It let out part of the office premises and the godown on leave and licence basis against the payment of compensation. It was held by this court that the facts found clearly showed that the only business which the assessee therein had been carrying on was dealing in mill-made cloth on commission basis and there was nothing to show that warehousing business was carried on by the assessee and the letting out of the office premises and godown was merely a way of exploiting the property of the assessee. The income derived therefrom was held not assessable as income from business.

11. The judgments relied upon by Mr. Trivedi have no applicability to the facts of the instant case. In the case of *Commissioner of Income Tax, Delhi (Central) Vs. Northern India Theatres P. Ltd.*, , the assessee, a private company incorporated to carry on the business of cinema and allied businesses, constructed a cinema house on a plot taken on sub-lease. Subsequently, one Hari Singh had given an interest-free loan to the assessee therein to meet the cost of construction of the cinema house which amount was to be refunded in monthly instalments. A lease agreement was entered into with the said Hari Singh under which the premises together with the equipment were let out to him at a monthly rent for a period of ten years. Licence to run the cinema was granted to the assessee and it continued in the name of the assessee. It was a case of exploitation of commercial asset by the assessee in a commercial manner. Even in the case of *Commissioner of Income Tax, Tamil Nadu-I Vs. B. Nagi Reddy*, , the assessee, who was the owner of two cinematograph studios, leased them on rental income was included for assessment in the assessee's total income. The assessee had been utilising these studios in making films of his own. The facts in that case were considered in association with the assessee's own many-sided career in the film business as a producer, as a distributor, as an exhibitor, as a studio owner and the like and the rental income received by the assessee from the lease of the studios was assessed under the head "Business". The Supreme Court in *Commissioner of Income Tax, Lucknow Vs. Vikram Cotton Mills Ltd.*, , was considering the case of a company which carried on the business of manufacture of textiles. In a creditor's petition, the High Court had evolved a scheme u/s 153 of the Indian Companies Act, 1913, whereunder the business assets were let on rental and the management of the company was transferred to a board of trustees approved by the High Court. On the reference, the High Court had affirmed the decision of the Tribunal holding that the income derived by the company by way of lease rent from letting out of its assets was assessable under the head "Profits and gains of business". On appeal to the Supreme Court, the Supreme Court affirmed the decision of the High Court. This was also a case of exploiting commercial assets of the assessee-company in a commercial manner. In the case of *Commissioner of Income Tax Vs. Anand Rubber and Plastics (P.)*

Ltd., , on which also reliance has been placed by Mr. Trivedi, the Punjab and Haryana High Court was considering a case where the main part of the factory building continued to be used by the assessee-company for its own business activities and only that part of the building which could not be exploited by the assessee-company was let out for a short while by it to some other manufacturing concern. On a peculiar facts of that case, the court held that the Tribunal was right in considering the rental income as business income. In the case before the Punjab and Haryana High Court, the concerned asset was a commercial asset. Moreover, a portion of the factory premises was exploited in a commercial manner and a large portion thereof was retained by the assessee-company for carrying on its own business. In the instant case, though the said agreement dated October 17, 1973, mentions retention of a small portion of the said premises/by the assessee, as held by the Appellate Assistant Commissioner on finding of facts, the entire said premises were let out to the said bank and the assessee decided to carry on the business activities from another place near about.

12. In the facts of the case, merely because advancement of loan by the said bank to the said partnership-firm is also mentioned in the said agreement dated October 17, 1973, it cannot be said that leasing out of the said premises to the said bank was closely connected with the loan advanced by the said bank. Moreover, all securities on which loans are granted for business are not necessarily commercial assets of the person or persons to whom loans are advanced. The letting out of the said premises to the said bank being merely for enjoyment of rental income derived could not be treated as "income from business". In this view of the matter, we hold that the Tribunal was in error in assessing the rental income as business income.

13. Accordingly, we answer the question in the negative, that is, in favour of the Revenue and against the assessee.

14. In the facts of the case, there shall be no order as to costs.