**(2014) 06 AP CK 0048**

**Andhra Pradesh High Court**

**Case No:** Referred Case No. 5 of 1997

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| The Commissioner of Income Tax | | APPELLANT |
| | Vs | |
| S. Premalata | | RESPONDENT |

**Date of Decision:** June 10, 2014

**Acts Referred:**

- Income Tax Act, 1922 - Section 9
- Income Tax Act, 1961 - Section 256, 27, 32(1A)
- Transfer of Property Act, 1882 - Section 53a, 54

**Citation:** (2014) 271 CTR 249 : (2014) 367 ITR 298

**Hon'ble Judges:** L.N. Reddy, J; Challa Kodanda Ram, J

**Bench:** Division Bench

**Judgement**

@JUDGMENTTAG-ORDER

L. Narasimha Reddy, J.
This reference is at the instance of the Revenue. The respondent is an assessee and she undertakes the activity of construction of buildings, giving them on lease and other allied activities.

2. Certain extent of land owned by the Young Men''s Christian Association at Secunderabad was taken on lease by the respondent. In terms of the agreement between the parties, construction was made and buildings were given on lease. The expenditure incurred for construction as well as the income derived from the buildings constituted the subject matter of assessment for various years under the Income Tax Act (for short ''the Act''). While for some years, the income derived from the buildings so constructed was treated as the one from business, for others the Assessing Authority treated it as the one from house property. Similarly, the claim of the respondent that the expenditure incurred for construction of the building must be treated as the revenue expenditure, was not accepted and it was treated as

capital expenditure.

3. The orders passed by the Assessing Authority were appealed against, and ultimately, the matter landed before the Income Tax Appellate Tribunal, Hyderabad Bench "B" (for short ''the Tribunal'') as I.T.A. Nos. 602 and 606 of 1993. The Tribunal agreed with the contention of the respondent herein and allowed the appeals.

4. The Department filed applications u/s 256 of the Income Tax Act, 1961 (for short ''the Act'') before the Tribunal with a request to refer certain questions covering the subject matter; to this Court. After hearing both the parties, the Tribunal passed an order, dated 17.07.1995, referring the following questions to this Court.

R.A. Nos. 545 to 549/Hyd/1994:

1. Whether, on the facts and circumstances of the case, the I.T.A.T. is correct in law in holding that the entire expenditure incurred by the assessee on the construction of the building on the leasehold land is a revenue expenditure?

2. Whether, on the facts and in the circumstances of the case, the I.T.A.T. is correct in law in holding that the provisions of Section 32(1A) of the Act will not apply to the present case?

R.A. Nos. 550 to 554/Hyd/1994:

1. Whether, on the facts and in the circumstances of the case, the I.T.A.T. is correct in law in holding that the rents received by the assessee from the building constructed on the leasehold land is assessable under the head ''business'' and not under the head ''property''?

2. Whether, on the facts and in the circumstances of the case, the I.T.A.T. is correct in law in holding that the assessee has never been the owner of the superstructure (building), which was constructed by the assessee on the leasehold land?

5. For the sake of convenience, we refer to the questions as "Question Nos. 1, 2, 3 and 4".

6. Sri S.R. Ashok, learned Senior Standing Counsel for the Income Tax Department, submits that the respondent herself incurred the expenditure for construction of the building and acquired the rights, akin to ownership vis-�-vis the premises and the expenditure incurred therefor deserves to be treated as ''capital expenditure''. He contends that the view taken by the Tribunal in its order of adjudication referable to Question No. 1 is correct and the reference to it is not necessary. As regards Question No. 2, learned Senior Standing Counsel submits that there is an inherent contradiction, inasmuch as the very basis for claiming the benefit u/s 32(1A) of the Act is on the premise that what is incurred as ''capital expenditure'' and the same does not go with Question No. 1. According to the learned Senior Counsel, the respondent is not entitled for the benefit u/s 32(1A) of the Act.

7. Coming to Question No. 3, learned Senior Standing Counsel submits that though the respondent may have taken the land on lease, she constructed the building with her own funds and leased the constructed premises, to the exclusion of the lessor and in that view of the matter, she deserves to be treated as the owner of the property at least, in the limited context of the relevant provisions of the Act. He submits that the income derived from the premises may be in the form of rents cannot be treated as the one from business.

8. Learned Senior Standing Counsel further submits that the ownership of the premises stood vested with the respondent at least for the period up to which the lease is subsisting. He seeks to derive support to his contention from the judgment of the Karnataka High Court in D.R. Puttanna Sons Pvt. Ltd. Vs. Commissioner of Income Tax, and the judgment of this Court in Commissioner of Income Tax Vs. Nandanam Constructions, .

9. Sri Y. Ratnakar, learned counsel for the respondent, on the other hand, submits that the subject matter of Question No. 1 is squarely covered by the judgment of the Hon''ble Supreme Court in Commissioner of Income Tax, Tamil Nadu II, Madras Vs. Madras Auto Service (P) Ltd., and the expenditure incurred for construction of the building deserves to be treated as the revenue expenditure and not capital expenditure. He fairly submits that if the contention of the respondent on Question No. 1 is accepted, Question No. 2 virtually becomes redundant and superfluous. Regarding Question No. 3, learned counsel submits that it is fairly settled in law that "once a lessee always a lessee" and unless a lease in respect of an immovable property between two persons is transformed into the one of ownership, in accordance with the procedure prescribed by law, the question of a lessee being treated as owner, does not arise. Learned counsel further submits that an attempt to treat a person as a lessee and a owner in respect of the same item of property would lead to several complications and that even the authorities of the Department have treated the income from the building constructed by the respondent as the one from business for the assessment year 1986-87. He further contends that when the respondent did not enjoy any right of ownership, the question of requiring her to prove that fact, does not arise.

10. While Question Nos. 1 and 2 touch one facet, Question Nos. 3 and 4 touch another. The first set is about the ''expenditure'' and the second set is about the ''income''.

11. In the first set, it becomes necessary to examine the manner in which the expenditure incurred by the respondent for construction of the building must be treated. While according to the Revenue, it must be treated as capital expenditure, the respondent wanted it to be treated as revenue expenditure.

12. It hardly needs any mention that the capital expenditure is the one which results in an enduring benefit. In other words, the expenditure so incurred must lead to the

coming into existence, of a property, which would last for quite a long time. It is axiomatic that the expenditure incurred in relation to an enduring property must be, by the one, who has rights of ownership vis-�-vis the property. It hardly needs any mention that the construction of a building needs investment of funds. What makes the difference is that if the expenditure is incurred by the owner, it needs to be treated as capital expenditure, whereas if the expenditure incurred by a person, who is not vested with the rights of ownership, it tends to become revenue expenditure.

13. In the instant case, the expenditure incurred by the respondent falls into the second category. The question is squarely covered by the judgment of the Hon''ble Supreme Court in CIT v. Madras Auto Service Pvt. Ltd. (supra) and following the same, we answer this question against the Revenue and in favour of the respondent.

14. Question No. 2 is nothing but an offshoot of Question No. 1. In a way, both of them do not coexist. Unless the expenditure incurred by the respondent for construction of the building is treated as capital expenditure, the question of her claiming the benefit u/s 32(1A) of the Act in relation thereto, does not arise. The Act does not maintain any distinction as to the purport of capital expenditure with reference to different provisions. Either it has to be treated as capital expenditure for all purposes covered by the Act or not at all. Viewed from that angle, Question No. 2 deserves to be answered in favour of the Revenue and against the respondent.

15. Question Nos. 3 and 4 touch a different aspect altogether, namely, ''income''. The respondent has admittedly derived income from the premises constructed by her on the land taken on lease. The whole controversy was as to whether the income must be treated as the one from house property or the one from business. The record discloses that the Income Tax Officer treated the income in the form of rents from the buildings constructed by her; as the one from business, for the assessment year 1986-87. It is only in the subsequent year, that an attempt was made to treat it as the one, from house property. Under both the heads, the income is taxable, except that the rates and other incidents differ.

16. In Nandanam Constructions''s case (supra), a Division Bench of this Court took the view that if an individual is to be treated as owner, it is not necessary that there must exist a sale deed in his favour. Their Lordships observed that if a person is in a position to enjoy the rights of ownership, the mere fact that the registration of sale deed did not take place, does not make any difference. Support was derived from the judgment of the Hon''ble Supreme Court in R.B. Jodha Mal Kuthiala Vs. The Commissioner of Income Tax, Punjab, Jammu and Kashmir, Himachal Pradesh and Patiala, and the judgment of this Court in Commissioner of Income Tax Vs. Trustees of H.E.H. The Nizam''s Miscellaneous Trust, . Their Lordships have also referred to the amendment caused to Section 27 of the Act, importing into it, the purport of

Section 53a of the Transfer of Property Act. That, however, was not a case in which a lessee was sought to be treated as owner of the property. The controversy was as to whether a person who paid the entire consideration and is in exclusive possession of the property can be treated as the owner of an item of immovable property, before the sale deed was executed.

17. The judgment of Karnataka High Court in D.R. Puttanna Sons''s case (supra) is on facts, which are to those of this case. The question in that case, as in the present one, was as to whether a lessee of a land for a particular period can be treated as the owner of the building constructed thereon, during the subsistence of the lease. The answer is in affirmative. Their Lordships have also sought to lay support on the judgment of the Hon''ble Supreme Court in S.G. Mercantile Corporation P. Ltd. Vs. Commissioner of Income Tax, Calcutta, . The discussion by the Karnataka High Court proceeded on the following premise:

"It is not in dispute that the assessee remained the owner of the building for the period of 30 years and upon expiry of that period, the land leased to the assessee with the building constructed thereon would revert to the lessor. The income by way of rent recovered from the tenant inducted by the assessee cannot, therefore, be considered as business income so long as the assessee remained the owner thereof."

18. The portion of the judgment of the Supreme Court in S.G. Mercantile corporation P. Ltd''s case (supra) that was relied upon by the Karnataka High Court reads:

"The liability to tax u/s 9 of the Income Tax Act, 1922, is of the owner of the buildings or land appurtenant thereto. In case, the assessee is the owner of the buildings or lands appurtenant thereto, he would be liable to pay tax u/s 9 even if the object of the assessee in purchasing the landed property was to promote and develop a market thereon. It would also make no difference if the assessee was a company which had been incorporated with the object of buying and developing landed properties and promoting and setting up markets thereon."

19. We find a bit difficult to fit the proposition enunciated by the Karnataka High Court into the observations made by the Supreme Court in S.G. Mercantile corporation P. Ltd''s case (supra).

20. The Transfer of Property Act maintains a clear distinction between the ownership, on the one hand, and the lease, on the other. The rights of the lessor and the lessee vis-�-vis the leased property are clearly delineated under Chapter V of that Act. We hardly find any circumstances or possibility where a lease can metamorphosize or transform into ownership, unless the parties to the transaction take the steps, those are required under law. The very statement that an individual remained as owner of the property for a period of 30 years during the lease was in force, does not accord with the basic tenets of those two concepts. Just as a lessee cannot be treated as owner, a person who acquires the rights of ownership would

cease to be a lessee. Both the concepts of law do not coexist.

21. A lessee, in a given case may be conferred with the right to sublease the property or to do certain activities, depending on the terms of agreement between the parties. Howsoever pervasive the control of a lessee, over the property may be, it would not have the effect of wiping away the ownership of the lessor over it. Conversely, the lessee under such a lease cannot become owner. The fact that the lease is for a fairly longer period, does not bring about any change in the character of rights. We, therefore, express our inability to fall in line with the judgment of the Karnataka High Court.

22. Even from the statement of the case by the Tribunal, while making the reference, it is evident that the respondent was treated as lessee, may be for a period of 30 years and for certain years, the income derived from the building by the respondent was treated as the one from business. The construction of the building on the land taken on lease was obviously for the purpose of business and not with an intention to own it. If the intention of the respondent was to own the property, the transaction would have been different altogether. Though the lease is one of the forms of transfer of property, it does not lead to conferment of rights of ownership. That would be possible only when a sale as defined u/s 54 of the Transfer of Property Act takes place. Therefore, we answer Question No. 3 against the Revenue and in favour of the respondent.

23. From a reading of Question No. 4, we find that there is serious defect in framing of it. A close perusal of Question No. 4 i.e. Question No. 2 in R.A Nos. 550 to 554 of 1994 reveals that there is some non-application of mind in the process. In case the Tribunal has taken the view that the assessee i.e. the respondent has never raised the superstructure on the leasehold land, it is just un-understandable as to how the income derived by her can be treated as the one from the house property. It is the specific case of the respondent that the income is from business. At any rate, the view expressed by the Tribunal is not germane for Question No. 3. We therefore treat Question No. 4 as superfluous and unnecessary.

24. The reference is answered accordingly.