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

Reserved on : 13th July, 2012
% *Date of Decision : 23rd July, 2012*

\+ **ITA No.254/2006**

M/s Lavish Apartment (P.) Ltd. .... Appellant
Through: Mr. Kaanan Kapur, Adv.

VERSUS

Asst. Commissioner of Income Tax .....Respondent
Through: Mr. Sanjeev Sabharwal, Sr.Standing Counsel
with Mr. Puneet Gupta, Jr. Standing Counsel

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

1. Whether Reporters of local papers may be allowed to see the judgment?
2. To be referred to the Reporters or not?
3. Whether the judgment should be reported in the Digest?

R.V. EASWAR, J.:

The following substantial question of law is framed:-

> "Whether the Income Tax Appellate Tribunal was right in law in holding that the assessee was not entitled to set off the brought forward business loss against the rental income, car and computer hire charges and the commission income received in the previous year relevant to the assessment year 1995-96, on a proper interpretation of Section 72(1) of the Income Tax Act, 1961?

2. The assessee is a private limited company carrying on the business of sale and purchase of properties and also earning rental and other income. In the return filed for the assessment year 1995-96, for the previous year ended on 31st March, 1995, it filed a return of income on 30th November, 1995. In the return, the assessee set off the business loss brought forward from the assessment year 1994-95 against its income by way of rent, car and computer hire charges and commission income and declared a net

loss of Rs.14,20.460/-. The assessing officer was of the view that the rental income of Rs.6,49,235/- received while letting out the properties is chargeable to tax under the head "income from house property" and that the hire charges and commission income of Rs. 6,92,220/- was chargeable to tax under the head "income from other sources" and, therefore, the brought forward business loss was not permitted to be set off against the income shown under the aforesaid two heads of income under Section 72(1) of the Act. He was of the view that the Section permitted adjustment of brought forward business loss only against profits assessed under the head "business". In this view of the matter, he called upon the assessee to explain the claim for set off.

3. The assessee argued that it was carrying on the business of leasing, selling and renting of real estate properties, that renting of the properties was also one of the main objects of the company according to the Memorandum of Association, that the hire charges and commission income was also business income and that, therefore, the brought forward business losses could be properly set off against these items of income. It was submitted that though the rental income is chargeable to tax under the head "income from house property" and the hire charges and commission income were assessed under the head "income from other sources", that was only because of the provisions of the Income Tax Act but they in fact represented income from the business carried on by the assessee judged by commercial principles and there was no bar under Section 72(1) of the Income Tax Act, (hereinafter referred to as the 'Act') to the brought forward losses being set off against the aforesaid items of income.

4. These contentions did not find favour with the Assessing Officer. He noted that the assessee was deriving rental income only from two properties, namely, HS-28, Kailash Colony and HS-32, Kailash Colony, both of New Delhi. HS-32, Kailash Colony was constructed in 1989-90 and thereafter let out to Union Bank of India and HS-28 was acquired in 1984 along with the tenancy in favour of one Ram Swaroop Anand and further construction on the said property was completed in April, 1994 and was subsequently let out to Smt.Vimla Devi Jhunjhunwala. According to him the

assessee-company was not in the business of renting out properties, and that it was only in the business of sale and purchase of properties which had not been carried on during the year and on this ground the rental income could not be considered as the business income of the assessee, so as to be utilized to set off the brought forward business loss. He also noted that house-owning, however profitable, cannot be a business or trade for the purpose of the Income Tax Act and even on this reasoning rental income could not be adjusted against the brought forward business loss. The Assessing Officer also noted that the assessee had not claimed any depreciation on the buildings which were let out.

5. As regards the service charges received from M/s Tulika Advertising and Marketing Pvt. Ltd., the Assessing Officer observed that the assessee could not substantiate why they should be assessed as rental income. He held that the service charges were neither assessable as "income from house property" nor assessable under the head "business", and was properly assessable only under the residual head, namely, "income from other sources". In this view, the Assessing Officer rejected the assessee's plea that brought forward business loss could be adjusted against the service charges received from M/s Tulika Advertising and Marketing Pvt. Ltd.

6. With regard to the car and computer hire charges and the commission received from M/s Tulika, all of which aggregated to Rs. 5,78,220/-, the assessee submitted that it had procured business to the tune of Rs.24,46,200/- from Delhi Police, Zee TV, Doordarshan and COSMO to M/s Tulika Advertising and Marketing Pvt. Ltd. and in support of the claim a copy of the letter dated 30th March, 1995 was filed and it was contended that the commission of Rs.2,44,620/- received from M/s Tulika represented business income available for set off of the brought forward business loss. This claim was rejected by the Assessing Officer who held that the commission income can be classified and assessed only under the residual head and not as the business income of the assessee. He noted that the assessee itself has shown the commission income under the head "other income" in its profit and loss accounts.

7. As regards the car and computer hire charges aggregating to Rs.3,30,600/- the Assessing Officer noted that these were also shown in the profit and loss account as "other income". According to him, these receipts do not constitute business income of the assessee and that it had not entered into any lease agreement for the purposes of hiring out the cars and the computer. He noted that till the earlier year the computer and the car were used by the company and it was only in the previous year relevant to the assessment year 1995-96 that the assessee "finding its cars and computers idle, decided to give them on hire to others and to earn some income from such activity of hiring out of the assets". In his opinion this fact established that the assessee was not engaged in the business of hiring out computers or cars but had only hired out the assets to augment its income. Such income cannot be considered as business income, but has to be considered only as "income from other sources". The Assessing Officer also added that on the cars and the computers the assessee did not claim any depreciation.

8. For the aforesaid reasons, the Assessing Officer refused to accept the assessee's claim for set-off of the brought forward business loss from the assessment year 1994-95 against the income for the assessment year 1995-96 by way of rent, car and computer hire charges and the commission income.

9. The assessee carried the matter in appeal to the CIT (Appeals). He found that the properties let out by the assessee were shown in the balance sheet as stock-in-trade and thus constituted trading assets. According to him the rental income arising from these trading assets was available for being adjusted against the brought forward business loss. As regard the rent of ₹1,14,000/- received from M/s Tulika Advertising and Marketing Pvt. Ltd., it was held by the CIT (Appeals) that the office space let out included a telephone connection, electricity and office furnishing. It was held that complete details of the letting out were furnished to the Assessing Officer. The office space was at No.23, Community Centre, East of Kailash, New Delhi which has been sub-let out to M/s Tulika for which rent was received by the assessee. The CIT

(Appeals) held that the income received from M/s Tulika, described as service charges by the assessee, also had to be treated as rental income and since letting out of the properties was the assessee's business, the service charges were also available for being set off against the brought forward business loses.

10. Turning to the income by way of car and computer hire charges and commission income, it was held by the CIT (Appeals) that the activities of letting out the vehicles and computers and earning commission income amounted to business carried on by the assessee, even on the footing that income derived by letting out idle business assets, though temporary, can amount to business. It would appear that before the CIT (Appeals) the assessee had contended that the objects clause of Memorandum of Association permitted it to carry on such business and in any case the minutes book reflected that the company had been carrying on the business of commission agency and hire charges. This contention was accepted by the CIT (Appeals). According to him carrying on a business activity was not confined to activities by way of trade, commerce or manufacture, but also took into account the rendering of services to others, which may be of a variegated character, which would also amount to business.

11. The CIT(Appeals) on a consideration of the aforesaid facts and submissions and on the basis of the authorities cited before him took the view that though the rental income was classified as "income from house property" under Section 22 of the Income Tax Act, that was only for the purpose of assessment under the Act and that it did not preclude the assessee from contending that the activity of letting out which was one of the objects of the company under the Memorandum of Association, amounted to a business activity applying commercial principles and, therefore, the brought forward business loss can be adjusted or set off against the rental income which was nothing but the business income of the assessee. As regards the car and computer hire charges and the commission income, the CIT (Appeals) was of the view that the hire charges arose out of a temporary letting of the business assets and thus

amounted to business income. As regards the commission income, he held that it was a business activity and, therefore, the business loss brought forward can be set off against such income. The CIT (Appeals) thus decided the appeal in favour of the assessee and held that the brought forward business loss can be set off against the rental income, car and computer hire charges and the commission income under Section 72(1) of the Act.

12. The Revenue carried the matter in appeal to the Tribunal. The Tribunal took the view, for reasons stated in its order, that the business loss brought forward from the earlier year cannot be set off against the rental income and income from car and computer hire charges, commission income, etc. It is against the decision of the Tribunal that the assessee has filed the present appeal.

13. We are unable to sustain the decision of the Tribunal. The relevant section in the Act which deals with the set off of brought forward losses is Section 72. Under sub-section (i), the brought forward business loss shall be set off against the profits and gains, if any, of any business carried on by the assessee and assessable for that assessment year. It may be necessary to reproduce the relevant part of the Section in order to expose the fallacy in the reasoning of the Tribunal: -

> "***Carry forward and set off of business losses.***
> *72. (1) Where for any assessment year, the net result of the computation under the head "Profits and gains of business or profession" is a loss to the assessee, not being a loss sustained in a speculation business, and such loss cannot be or is not wholly set off against income under any head of income in accordance with the provisions of section 71, so much of the loss as has not been so set off or, where he has no income under any other head, the whole loss shall, subject to the other provisions of this Chapter, be carried forward to the following assessment year, and –*
>
> *(i) it shall be set be off against the profits and gains, if any, of any business or profession carried on by him and assessable for that assessment year;*"

14. This Section is substantially the same as Section 24 of the Indian Income Tax Act, 1922 (hereinafter referred to as the 'old Act'). Section 24 of the old Act came up for consideration before the Supreme Court in *CIT, Andhra Pradesh v. Cocanada Radhaswami Bank Ltd.*, (1965) 57 ITR 306. It was observed by Subba Rao, J. (as he then was) as under: -

> "*A comparative study of sub-sections (1) and (2) of section 24 yields the same result. While in sub-section (1) the expression "head" is used, in sub-section (2) the said expression is conspicuously omitted. This designed distinction brings out the intention of the legislature. The Act provides for the setting off of loss against profits in four ways. To illustrate, take the head "profits and gains of business, profession or vocation". An assessee may have two businesses. In ascertaining the income in each of the two business, he is entitled to deduct the losses incurred in respect of each of the said businesses. So calculated, if he has loss in one business and profit in the other both falling under the same head, he can set off the loss in one against the profit in the other in arriving at the income under that head. Even so, he may still sustain loss under the same head. He can then set off the loss under the head "business" against profits under another head, say "income from investments", even if investments are not part of the trading assets of the business. Notwithstanding this process he may still incur loss in his business. Section 24(2) says that in that event he can carry forward the loss to the subsequent year or years and set off the said loss against the profit in the business. Be it noted that clause (2) of section 24, in contradistinction to clause (1) thereof, is concerned only with the business and not with its heads under section 6 of the Act. Section 24, therefore, is enacted to give further relief to an assessee carrying on a business and incurring loss in the business though the income there from falls under different heads under section 6 of the Act.*"

15. A similar position emerges on a reading of Section 72 (1) of the present Act. The opening part of the sub-section refers to the net result of the computation under the head "profits and gains of business or profession". Thus the computation of the loss should have been made under the particular head of income. However, when it comes to the set off of the loss computed under the head "profits and gains of business" against the profits and gains of the business of assessee in the subsequent

year, the condition that the computation of the profits and gains of the business carried on by the assessee in the subsequent year should be under the head "profits and gains of business or profession" is conspicuously absent. This will be clear from clause (i) of the sub-section which does not refer to the head of income but merely makes reference to "the profits and gains, if any, of any business or profession carried on by him". In view of the similarity in the language of Section 24 (1) & (2) of the old Act and Section 72 (1) of the Act, the ruling of the Supreme Court cited above and the observations which we have extracted earlier apply with equal force to the interpretation of provisions of Section 72 (1) of the Act.

16. It is not necessary to multiply authorities on the point and the position which emerges is that in the subsequent year in which the assessee claims set off of the brought forward business loss, there is no condition that the business income against which the brought forward loss is claimed to be sought for should have been computed under the head "profits and gains of business". The income against which the brought forward loss is claimed to be set-off should represent business income judged by the application of commercial principles, and not on an application of the provisions of the Act.

17. The matter does not end there. It calls for an inquiry as to whether the rental income and the income by way of hire charges and commission earned by the assessee, though assessed under the head "income from house property" and "income from other sources" can be treated as the business income of the assessee as to be eligible for adjustment against the brought forward loss. Here again there has to be distinction between the slotting of the income of an assessee under different heads of income in accordance with the Act and the business income or profits and gains of business as understood in accordance with commercial principles. The position was explained first by the Supreme Court in *United Commercial Bank Ltd. v. CIT*, (1957) 32 ITR 688. This judgment was referred to in a latter judgment of the Supreme Court in *CIT v. Chugan Das*, (1965) 55 ITR 17 where it was observed as under: -

> "*The heads described in section 6 and further elaborated for the purpose of computation of income in sections 7 to 10 and 12, 12A, 12AA and 12B are intended merely to indicate the classes of income : the heads do not exhaustively delimit sources from which income arises. This is made clear in the judgment of this court in the United Commercial Bank Ltd.'s case, that business income is broken up under different heads only for the purpose of computation of the total income : by that break up the income does not cease to be the income of the business, the different heads of income being only the classification prescribed by the Indian Income-tax Act for computation of income.*"

18. The aforesaid observations of the Supreme Court in the case of *Chugan Das & Co. (supra)* were approvingly cited in *Cocanada (supra)*. Elucidating the position further Subba Rao, J. (as he then was) observed as under: -

> "*The scheme of the Act is that the income tax is one tax. Section 6 only classifies the taxable income under different heads for the purpose of computation of the net income of the assessee. Though for the purpose of computation of the income, the interest on securities is separately classified, income by way of interest from securities does not cease to be part of the income from business if the securities are part of the trading assets. Where a particular income is part of the income from a business falls to be tested not on the basis of the provisions of Section 6 but on commercial principles……..if the income from the securities was the income from its business, the loss could, in terms of that section, be set off against that income*".

19. There is thus high authority for the proposition canvassed before us on behalf of the assessee quite forcefully and we think his contention has to be conceded. We also find justification for his criticism that the Tribunal overlooked the legal position and decided the appeal merely on the basis that the rental income has to be statutorily assessed under the head "income from house property" and the hire charges and commission income have to be assessed compulsorily as "income from other sources". The Tribunal would be right if the controversy before them was merely as to under which head these items of income should be assessed, having regard to the provisions of the Act. The controversy before the Tribunal, however, was not limited to this question. One had to apply the provisions of Section 72 (1) to ascertain whether, notwithstanding the pigeon-holing of the receipts into the specific heads of income as

provided under the Act, by applying commercial principles these receipts could be considered as the business income of the assessee company on a commercial perspective. The Tribunal had, with respect, missed this aspect in its order.

20. The main objects of the assessee company are, according to its memorandum of association the carrying of business of leasing, selling and renting of real estate properties, and others. The assessee has stated so before the Assessing Officer himself who has not disputed this position. Even before the CIT (Appeals) it would appear that this point was put forth and that authority has not impeached the same. The company itself was formed for the purpose of dealing in real estate and also in renting and leasing them out. That there were only two properties from which rental income was derived, one from the year 1989-90 and another from April, 1994 cannot detract from the position that the company was carrying on the business activity of letting out properties. The finding of the CIT (Appeals) is that the properties were shown in the balance sheet as stock-in trade and thus they are part of the trading assets. Even this finding is not under challenge. So far as the hire charges for car and computers are concerned, the CIT (Appeals) has affirmed that these activities are supported by the decision taken by the company, reflected in its minutes book, to embark upon these activities. It has also been stated by him that if the idle assets belonging to the company, namely, car and computer are temporarily let out on hire that will amount to a business venture and fall to be considered as a prudent utilization of idle assets amounting to business. So far as the commission income is concerned, the assessee had right through contended that it was earned by procuring business to M/s. Tulika. The business was procured by the assessee from Delhi Police, Zee TV, Doordarshan and Cosmo and the total business procured was to the tune of 24,46,200/- on which the assessee earned commission at the rate of 10% namely ₹2,44,620/-. All these facts go to show that the activities of hiring out the car and the computer and in earning commission by procuring business for others were dictated by business and commercial considerations and it would therefore be a reasonable inference to hold

that these activities wore the badges of trade. It is true that the Assessing Officer could not have brought the rental income to tax under any head other than "income from house property"; nor did he bring the hire charges and the commission income to tax under any head other than "income from other sources" but as we have already noticed on the basis of the judgments of the Supreme Court, the question whether the activities carried on by the assessee amounted to a business has to be decided not on the basis of the head of income under which the result of those activities is assessed for the purposes of the Income Tax Act, but on the basis of commercial principles. We have no doubt that on the findings recorded by the lower authorities, it would follow that the rental income, hire charges from car and computer and the commission income all represent the profits and gains of business carried on by the assessee in the assessment year 1995-96. It follows that the brought forward business loss can be set off against these items of income.

21. It was said on behalf of the Revenue that in the judgment in *East India Housing and Land Development Trust Ltd. v. CIT*, (1961) 42 ITR 49 it has been held that the income realised from the tenants of the shops and stalls built by a company, incorporated with the object of buying landed properties and promoting and developing markets in Calcutta, was not liable to be taxed under the head "profits and gains of business" because there was a specific provision in the Act to assess such income under the head "income from house property". It was on this basis contended that the Tribunal cannot be faulted for holding that the rental income earned by the assessee in the present case was taxable only under the head "income from property" and the income by way of hire charges and commission were assessable under the head "income from other sources". This contention misses the point. There can be no quarrel with the contention if we are concerned only with the heads of income under which these receipts were assessable under the Act. But, as noted earlier, when it comes to the application of Section 72 (1), the heads of income lose their relevance and we have to only apply commercial principles to find out whether the activities

embarked upon by the assessee amount to business activities. This aspect of the matter has been specifically recognized in *Cocanada* (supra) where the judgment of the Supreme Court in the case of *East India Housing and Land Development Trust Ltd.* (supra) was relied upon on behalf of the Revenue to raise a contention identical to the one raised before us. The judgment was held not applicable in the interpretation of Section 24 of the old Act, whose provisions are substantially similar to Section 72 (1) of the present Act. After noticing the contention, the Court held that the decision in *East India Housing and Land Development Trust Ltd.* (supra) *"does not lay down that the income from the shops is not the income in the business"*. If the Supreme court in Cocanada (supra) had accepted the contention of the Revenue based on *East India House and Land Development Trust Ltd.* (supra), then *Cocanada* (supra) could not have been decided in the way it was.

22. With particular reference to the activity of renting out properties, by a company incorporated for that purpose, it will be apposite to refer to the observations of Hidaytullah, J. (as he then was) as to the test to be applied in *Karanpura Development Co. Ltd. v. CIT*, (1962) 44 ITR 362: -

> "*Ownership of property and leasing it out may be done as a part of business, or it may be done as land owner. Whether it is the one or the other must necessarily depend upon the object with which the act is done. It is not that no company can own property and enjoy it as property, whether by itself or by giving the use of it to another on rent. Where this happens, the appropriate head to apply is "income from property" (section 9), even though the company may be doing extensive business otherwise. But a company formed with the specific object of acquiring properties not with the view to leasing them as property but to selling them or turning them to account even by way of leasing them out as an integral part of its business, cannot be said to treat them as landowner but as trader. The cases which have been cited in this case both for and against the assessee company must be applied with this distinction properly borne in mind. In deciding whether a company dealt with its properties as owner, one must see not to the form which it gave to the transaction but to the substance of the matter.*"

23. The facts of the present case, judged in the light of the above observations lend support to the contention of the assessee that by letting out the properties held as stock-in-trade, it was carrying on a business activity. With regard to the hiring of car and computers we have already noted that the CIT (Appeals) has found that they were hired out as they remained idle and assessee thought it prudent to exploit them by letting out temporarily to others. The commission income received by the assessee from Tulika is for obtaining or procuring business for the latter which undoubtedly is a business activity though it may be a single instance only.

24. We may refer to only two more judgments as they are judgments of this Court. The first is of a Division Bench in the case of *CIT v. R. Dalmia,* (1974) 96 ITR 463. There the brought forward business loss was sought to be set off against the dividend income earned by the assessee in the subsequent year. It was held by the High Court that since the dividend income was derived from the shares held as stock-in-trade, the brought forward losses could be set off against the same notwithstanding that the Act required that the dividend income should be assessed under the head *"income from other sources"*. It is interesting to note that before the Court the Revenue abandoned its contention that the brought forward loss cannot be set off against the dividend income, realising that the shares were held as stock-in-trade. The only contention advanced by the Revenue in that case was that there were no sufficient facts to justify the conclusion of the Tribunal that the shares were held as stock-in-trade. The proposition that the brought forward loss could be set off against the dividend income of the subsequent year if the dividend was derived from the shares held as stock-in-trade itself was not questioned as it was sought to be questioned before us on behalf of the Revenue. It is expected of the Revenue to take consistent positions on matters involving legal principles, particularly before different High Courts since the Income Tax Act is an all India statute and the department of income tax being one for the entire country it cannot possibly adopt different or inconsistent legal positions before the Courts or the Tribunals.

25. The other decision of this Court is in *Snam Progetti S.P.A. v. Addl. CIT*, (1981) 132 ITR 70. In this case following the judgment of the Supreme Court in *Cocanada* (supra) and *Chugan Das & Co.* (supra) it was held by the Division Bench of this Court that the brought forward business loss can be set off against the interest earned by the assessee from bank deposit in the subsequent year, if such interest can be attributed to a business activity of the assessee, notwithstanding that such interest is assessable under the head *"income from other sources"* under the Act.

26. For the aforesaid reasons we answer the substantial question of law in the negative, in favour of the assessee and against the Revenue. The appeal is, therefore, allowed. There shall be no order as to costs.

(R.V. EASWAR)
JUDGE

(S. RAVINDRA BHAT)
JUDGE

JULY 23, 2012
Bisht/hs