



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

+ **Income Tax Appeal No. 338/2011**

% **Reserved on: 31st October, 2011**
Date of Decision: 8TH November, 2011

Commissioner of Income Tax-IVAppellant
 Through Mr. N.P. Sahni and Mr. Ruchesh Sinha,
 Advocates.

Versus

M/s Francis Wacziarg ...Respondent
 Through Mr. Salil Kapoor, Mr. Sanat Kapoor and
 Mr. Vikas Jain, Advocates.

CORAM:
HON'BLE MR. JUSTICE SANJIV KHANNA
HON'BLE MR. JUSTICE R.V. EASWAR

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

SANJIV KHANNA, J.

With the consent of the learned counsel for the parties, the present appeal under Section 260A of the Income Tax Act, 1961 (Act, for short) against the order of the Income Tax Appellate Tribunal (Tribunal, for short) dated 23rd April, 2010, relating to the assessment year 2003-04 in the case of Francis Wacziarg, was taken up for hearing and disposal.



2. As several separate subject matters/issues are raised, it would be appropriate to deal with them under separate headings.

A. Whether income earned by the respondent assessee from one property located at Pondicherry and two properties located at Ramgarh should be taxed under the head of 'Income from business and profession' or under the head 'income from house property' and whether deletion of disallowance of 80% of the expenses and depreciation amounting to Rs.53,18,761/- is correct?

3. The assessing officer had held that income of Rs.13,27,855/- and Rs.1,20,000/- (total Rs.14,47,855/-) received from Neemrana Hotels Private Limited (NHPL, for short) towards and on account of Pondicherry and Ramgarh properties were rental income. The assessing officer observed that these properties were being run as hotels by NHPL and possession of the properties was transferred to them, while ownership remained with the assessee. The reasoning given by the assessing officer is as under:-

"A perusal of the above depicts that the Ramgarh and Pondicherry properties were let out by the assessee to M/s Neemrana Hotels (P) Ltd but the arrangement was made in a manner so that the income of the same treated as "Income from business & Profession" in the hands of the assessee in order to claim the expenditure and the huge depreciation thereon. Since, the property has been let out by the assessee, possession has also been transferred, ownership remained with the assessee and business run by Neemrana Hotels Private Limited. All these facts clearly fit the case to treat the income of the assessee on letting out of the property at Ramgarh and Pondicherry to NHPL as "Income from House Property" On the basis of the above, it can be said that the property which has actually been used by the assessee for the hotel business was only the Metharan Property which qualifies



for the depreciation. Hence the depreciation on other properties and the expenses other than the operating expenses be disallowed since the main business of the assessee is the operation of the hotels, the consultancy fees/service charges has to be treated as 'Income From Other Sources' and all the expenses including depreciation but excluding operating expenses being related to other income is disallowed but keeping in view the natural justice and the fair play, 20% of all the following expenses other than depreciation is being allowed to the assessee by treating that the same might have incurred for the purpose of the business only. Thus, the disallowance of the following expenses are being made:

| | |
|--|--------------------|
| Staff Salaries & Other Expenses (80%) | 3,69,864/- |
| Travelling & Conveyance (80%) | 7,499/- |
| Postage, Telephone and Courier (80%) | 72,730/- |
| Rent Paid (80%) | 1,07,520/- |
| Rent received adjusted in rent paid (80%) | 3,36,000/- |
| Repair & Maintenance (80%) | 7,79,308/- |
| Depreciation (Other than Metharan Property) (as claimed by the assessee) | 36,45,840/- |
| | <u>53,18,761/-</u> |

4. The assessing officer disallowed expenses to the extent of 80% under the head staff salary and other expenses; travelling and conveyance; postage, telegraph and courier; rent received adjusted against the rent paid; repair and maintenance; and depreciation. The



assessing officer has further recorded that notice dated 8th March, ---- under Section 131 of the Act was issued for summoning the Principal Officer/Managing Director of NHPL, but they did not appear and it was stated that they were out of country and would be available in April, 2006, and as the case was getting time barred and was to be decided by 31st March, 2006, the assessment order was passed. It may be interesting to note that the assessing officer while disallowing 80% of the expenses amounting to Rs.53,18,761/- and adding Rs.14,47,855/- under the head 'income from house property', did not reduce the same amount of Rs.14,47,855/- from income declared by the assessee under the head 'business from business and profession'. An application filed by the assessee under Section 154 remained pending till the matter was taken up and heard in appeal by the Commissioner of Income Tax (Appeals) [CIT (Appeals), for short].

5. The respondent assessee filed detailed grounds of appeal and written submissions before the CIT (Appeals). The assessing officer was asked to furnish a remand report. The respondent assessee before the CIT (Appeals) pointed out that he was owner of the properties at Matherana, Pondicherry and one property at Ramgrah, while the fourth property at Ramgarh was taken on lease from the Uttrakhand Government. Further he had constructed 14 rooms at Pondicherry to



be run as a hotel and 7 rooms in the two properties at Ramgarh
run as hotels. All the rooms were fully furnished having all facilities including air conditioners, generators, crockery, EPABX machines, fax machines, refrigerator, telephone facilities, computers, televisions, bed sheets, blankets, bath towels, face towels, provisions for meals/beverages etc.

6. The respondent's stand was that NHPL had been permitted to operate and manage these hotels but NHPL was not a tenant in possession of the properties. No lease deed had been executed. The respondent was a Director in the NHPL and was having control over the working of the hotels. All purchases, correspondences, cheques or payments etc. from NHPL passed through him. The respondent had a revenue sharing agreement with NHPL and was entitled to 20% of the gross operating profit calculated in terms of the agreement in the case of Pondicherry property. Similarly, there was agreement in respect of the Ramgarh properties.

7. The CIT (Appeals) after considering the contentions of the parties had held as under:-

“Thus, considering the facts and circumstances of the case and the nature of activities carried out by the appellant and also on going through the judgments as stated by the appellant. It is seen that the appellant is receiving license fee from Nimrana Hotels (P) Ltd as revenue share for running of the property at Pondechery. It is also seen that the the appellant is involved in all the aspects of management and day to day running of the properties



being used as hotels etc. It is also seen that the licence fee received by the appellant for various years is not a fixed sum of money as in the case of income from house property but it has been varying from year to year as it is based on a revenue sharing arrangement, which arises according to the receipts. It is also seen that the appellant has been substantially increasing the capacity of the hotels, income from which is being shared by the appellant and Mis. Nimrana Hotels (P) Ltd as per their terms and conditions. There does not seem to be any conclusive fact which could point towards the income received by the appellant to be in the nature of rental income. The AO's contention that the assessee has so arranged his affairs in the manner that income of the same be treated as income from business or profession so that the claim of expenditure can be made and huge depreciation can be claimed. does not seem to fit in the facts and circumstances of the case. The quantum of depreciation claimed by the appellant does not change the nature of the head in which income has to be assessed. The AO's observation that the business is being run by Mis. Nimrana Hotels (P) Ltd. and not by the appellant does not also appear to be totally correct. It is not correct to say that the exclusive use and maintenance of these properties are with M/s Nimrana Hotels (P) Ltd.. The AO seems to have branded the license agreement between the appellant and M/s. Nimrana Hotels (P) Ltd as a –sham agreement without any cogent finding. except that the appellant is incurring huge expenses and claiming huge depreciation. Even otherwise the AO has made the addition without arriving at any definite conclusion as it has been observed by the AO In the assessment order that certain enquiries are pending on this issue and the assessment has to be completed by 31.3.2006 and therefore. "the stand taken by the assessee is not accepted subject to pending verification at later stage."

The above facts and circumstances reflect that there is no conclusive evidence to show that the appellant's income should fall under the head income from house property and not business income. In fact all the facts and circumstances point towards the income of the appellant being income from business and profession. Therefore, under the circumstances it is held that the income of Rs. 14,47,855/- cannot be treated as income from house property.

Further it has been pointed out that while adding the income of Rs. 14,47,855/- to the income from house



property. The AO has not reduced the same from business income shown by the appellant. It is stated that this has resulted in double taxation of the same income twice – once under the head income from profits and gains of business or profession and the second time as income from; house property.

The above contention of the appellant has been examined and it seems to be correct. This issue can be resolved by resort to the provisions of Sec. 154 of the Act. However, since the above income of Rs. 14,47,855/- has been held to be business income of the appellant in the preceding paragraphs the amended ground of appeal taken up by the appellant becomes irrelevant and is, therefore, ignored. This disposes of the ground No. 2(b)."

8. In view of the findings recorded above, the CIT (Appeals) went on to consider the second question of 80% disallowance in the expenditure by the assessing officer, under various heads mentioned above. It appears from the order of the assessing officer that 80% adhoc reduction on account of the expenses was made as income from the three properties had been treated and taxed as 'income from house properties'. However, there is no discussion in the assessment order on what basis what principle expenses to the extent of 80% were disallowed.

9. CIT (Appeals) deleted the aforesaid additions recording as under:-

"After carefully examining the submissions of the appellant and other details submitted during the appellate proceedings, it is seen that the expenses amounting to Rs.53,18,761/- [including depreciation of Rs.36,45,840/-] are expenses relating to the business income of the appellant, It is clear that the appellant is carrying on the business of running hotels on various properties as discussed in the preceding paragraphs, It is also a matter of record that the appellant is using the premises at A-58



for his business purposes and the expenses incurred therein are for the purposes of earning of business income only, The AO's stand that these expenses are not related to the business of the assessee cannot be upheld. The AO has disallowed 80% of these expenses by observing that the main business of the assessee being operation of hotels, consultancy fee/service charges has to be treated as income from other sources. After having said that the AO should have disallowed the entire claim of expenses made by the appellant, However, the AO disallowed only 80% and allowed the balance 20% by observing that "keeping in view the natural justice and the fair play, 20% of all the expenses other than depreciation is being allowed to the assessee by treating that the same might have incurred for the purposes of the business only. This clearly shows that the AO is herself not entirely sure about the stand taken by her. It appears that the disallowance has been made without any cogent reason, Further no basis has been brought out in the assessment order as to why the proportion of 80%:20% has been applied. Since it is clear that the various properties are being used for the purpose of the appellants hotel business, the disallowance of these expenses @ 80% does not appear to be justified. These expenses are related to the claiming(sic) of the appellant's business income. These expenses are related to the earning of the appellants business income Hence the disallowance made by the AO deserves to be deleted."

10. In the appeal preferred by the Revenue before the tribunal, the following grounds were raised :-

- “1. On the facts and circumstances of the case and in law, the CIT(a) has erred in deleting the addition of Rs.3,69,864/- on account of staff ties and other expenses which are not related to business.
2. On the facts and circumstances of the case and in law, the CIT(A) has erred in deleting the addition of Rs.7,499/- on account of traveling and conveyance expenses, which are not related to business.
3. On the facts and circumstances of the case and in law, the Ld. CIT(A) has erred in deleting the addition of Rs.72,730/- on account of postage, telephone & courier expenses, which are not related to business.
4. On the facts and circumstances of the case and in



law, the CIT(A) has erred in deleting the addition of Rs.1,07,520/- on account, of rent paid.

5. On the facts and circumstances of the case and in law, the CIT(A) has erred in deleting the addition of Rs.3,36,000/- (sic) on account of rent received adjusted in rent paid.

6. On the facts and circumstances of the case and in law, the CIT(A) has erred in deleting the addition of Rs.7,79,308/- on account of repairs & maintenance.

7. On the facts and circumstances of the case and in law, the CIT(A) has erred in deleting the addition of Rs.36,45,840/- on account of depreciation.

8. On the facts and circumstances of the case and in law, the CIT(A) has erred in deleting the addition of Rs.1,34,400/- on account of discrepancy in rent note.

9. On the facts and circumstances of the case and in law, the CIT(A) has erred in deleting the addition of Rs.1,89,201/- on account of business development expenses incurred on producing opera.

10. On the facts and circumstances of the case and in law, the CIT(A) has erred in deleting the addition of Rs.115,14,506/- on account of deemed dividend u/s 2(22)(e) of the Act.”

11. It is noticeable from the aforesaid grounds that the Revenue did not specifically challenge the finding of the CIT (Appeals) that income from the three properties was taxable under the head ‘income from business or profession’ and not under the head ‘income from house property’. In these circumstances, we fail to understand, how the Revenue can now in the present appeal on substantial question of law challenge the order of the tribunal on the ground that income from the three properties is chargeable under the head ‘income from house



property' and not under the head of 'income from business or profession'.

12. Even otherwise, we find that CIT (Appeals) has given detailed factual finding why income earned by the assessee from the three properties is taxable under the head 'income from business or profession' and not under the head 'income from house property'. The reasoning given by the assessing officer is cryptic and she has not considered the relevant aspects. On the basis of findings recorded by her, it is not possible to hold that the finding of fact recorded by the CIT (Appeals)/tribunal are unfounded or unreasonable. In any case, the said findings are not perverse and are based on documents and material placed on record. The reasoning is cogent and well explained. Therefore, we do not find that any question of law arises on the first aspect and we are not inclined to frame any substantial question of law whether the income earned by the respondent assessee is taxable under the head 'income from house property'.

13. Once it is held that the income from the three properties is taxable under the head 'income from business or profession' depreciation has to be allowed under the provisions of Section 32 of the Act. Similarly, disallowance of 80% from the expenses deleted by the CIT(Appeals)/tribunal has been explained and supported by cogent



reasoning. The CIT (Appeals) has rightly pointed out that there was no confusion in the mind of the assessing officer when she had passed the above order, disallowing 80% of the expenses. It may be noted that the assessee had filed the revised income declaring income of Rs. 19,35,067/- which included income from consultancy services provided to third parties. Besides the assessee was running his office from A-58 Nizamuddin (East), New Delhi 110013 and had engaged staff of about 20 persons who are paid salary, ESI, PF and other perks. The assessee was also running a hotel at Matheran. In view of the foresaid, we do not find any reason to interfere with the order of the tribunal in respect of the said disallowances. No substantial question of law arises and the appeal on the said subject matter is dismissed.

B. Whether the tribunal is right in upholding the order of the CIT (Appeals) deleting addition of Rs.1,34,400/- on account of discrepancy in the rent note?

14. Premises No. A-58, Nizamuddin (East), New Delhi 110 013, does not belong to the assessee and was taken on rent from Dugal Brothers. The assessee had produced a rent note dated 5th April, 2001, before the assessing officer, but addition of Rs.1,34,400/- was made on the ground that the rent note was signed by one of the owners and not by both owners who were equally receiving the rent and as per the books of accounts, the total rent paid was Rs.1,32,000/- but as per the profit and



loss accounts/return, Rs.1,34,400/- was shown as rent paid.

reasoning given by the assessing officer to make the said addition reads

as under:-

**“5. Service Charges from M/s Neemrana Motels (P) Ltd.
Rs.4,20,000/-”**

In this regard, vide questionnaire dated 30.01.2006, the assessee was show caused as under:

“As per your explanation, the service charges from M/s Neemrana Hotels Private Limited amounting to Rs.4,20,000/- has been credited to the Rent Paid account which is paid to Dugal Brothers, being joint owner of the property at A-58, Nizamuddin, Delhi. In support, you have also submitted the copy of the Rent Note dated 05.04.2001. First of all, the said Rent Note is signed by only one owner out of the two owners who are receiving the income equally on the said property and secondly as per the ledger account of Rent paid, the net expense is Rs.1,32,000/- but as per the Profit & Loss Account, it is Rs.1,34,400/-. Please explain the same.”

In response to this, the assessee vide reply dated 03.02.2006, acknowledged the discrepancies in the Rent Note which clearly gives rise to a perfect case for application of section 69C, hence the amount of expenditure to the tune of Rs.1,34,400/- is disallowed. Penalty proceedings u/s 271(1)(c) is initiated on this point for furnishing of wrong particulars.

(Disallowance Rs.1,34,400/-)”

15. The aforesaid reasoning is laconic and has to be rejected as perverse. The CIT (Appeals) examined the said aspect and has rightly recorded that the addition cannot be sustained. The rent was deposited in the bank account of Dugal Brothers and even tax at source was deducted. The respondent was not the owner of the property. The assessing officer did not hold that Dugal Brothers were not owners. Once



payment of rent was not disputed and admitted, signature on rent becomes inconsequential. Oral tenancy is legal and recognized. The respondent had paid security service charges per quarter to the Security Agency appointed by the Welfare Association of Nizamuddin (East). Thus, the respondent assessee had paid Rs.2,400/- in addition to rent of Rs.1,32,000/-. The aforesaid order of the CIT (Appeals) was affirmed by the tribunal. We fail to understand why and on what ground Revenue has filed appeal on this ground. Accordingly, the appeal of the Revenue is dismissed on the above issue.

C. Addition of deemed dividend under Section 2(22)(e) amounting to Rs.115,14,503/- (sic.).

16. It was admitted during the course of hearing of the appeal that the total amount is not Rs.115,14,503/- but Rs.15,14,503/-. The break-up of the said amount is as under:-

| | | |
|-------|-----------------------------------|----------------|
| (i) | NHPL | Rs.11,97,918/- |
| (ii) | M/s Fawn Trade & Travels (P) Ltd. | Rs. 1,88,129/- |
| (iii) | M/s Delhi Warehousing (P) Ltd. | Rs. 1,28,459/- |

17. The reasoning given by the assessing officer was that the aforesaid amounts were shown as credit balance in the books of the assessee and were outstanding and, therefore, were in the nature of advances.



18. CIT (Appeals) deleted the said additions recording as under:-

(a) The credit balance payable by NHPL was on account of licence fee which had to be paid in installments and the said credit balance had been recorded, but as per the terms of the licence deed, the licence fee was payable after the close of the year. The amount was the share of the respondent from gross profit earned by NHPL.

(b) Amount payable to Fawn Trade & Travels (P) Ltd. was on account of outstanding bills for various purchases and no loan or advance was given to the assessee. In fact the assessee had given loan to Fawn Trade & Travel (P) Ltd. and outstanding balance as on 31/3/2003 was Rs.61,42,095/-.

(c) The outstanding balance payable by Delhi Warehousing Pvt. Limited, was towards "cheques in hand" which were subsequently cleared.

19. CIT (Appeals) deleted the said additions recording as under:-

"After carefully examining the details, facts and submissions and the assessment order as discussed above, it is seen that the amounts treated. As deemed dividend by the AO are neither advances nor loans given to the assessee by these companies. The copies of A/cs and confirmations filed by the appellant before the AO have not been discussed by her in the body of the assessment order. Nor the explanations of the appellant have been discussed or found to be incorrect by the AO. In view of the confirmations and copies of accounts filed by the appellant showing that the amounts appearing in the account were in fact receipts due to the appellant, in his normal course of business dealings with these companies, it is held that the receipts of the appellant from these



companies cannot be treated as loans and advances, Hence the AO was not correct in treating these receipts as deemed dividend u/s. 2(22)(e).”

20. The tribunal has rightly dismissed the appeal of the Revenue. In fact there is hardly any justification and reason for the assessing officer to make these huge additions. Appeal on this ground is dismissed.

D. Disallowance of Rs.1,89,201/- on account of business development expenses incurred on production of Opera.

21. After hearing the learned counsel for the parties, the following substantial question of law is framed:-

- Whether the tribunal was right in allowing the appeal of the assessee and deleting addition of Rs.1,89,201/- on account of business development expenses for production of Opera?

22. The assessing officer had disallowed the said expense on the ground that the assessee's daughter had participated in an opera but this did not justify and cannot be regarded as a business expense. The total cost of the Opera of Rs.80 lakhs was borne by Delhi Symphony Society and the respondent assessee was not in the business of Opera production etc. There was no need for the assessee to incur the said expenditure. Referring to the explanation of the assessee, it was held that the same should be disallowed as capital in nature. This was after recording statement of Gautam Kaul, Secretary of the Delhi Symphony Society in which he had stated that the Opera was a dream project of the assessee and it was in process since the year 1999. The CIT



(Appeals) had dismissed the appeal of the assessee on this ground.....

However, it appears that both the Revenue and the assessee had filed appeals before tribunal. It appears that both the sides were confused on this aspect as to the actual effect of the order of the CIT (Appeals). On a reading of the order of the CIT (Appeals), it is clear that the said expense was disallowed. The CIT (Appeals) had recorded as under:-

“These submissions of the appellant are very general-in nature and the AO has given a finding in the assessment order that it was organized with a view to promote the career of the appellant’s daughter who is a soprano. Under these circumstances the allowing of this expenditure as revenue expenditure does not seem justified. Further the AO has observed that the Balance Sheet of Delhi Symphony Society was not tiled by the appellant for necessary verification. In addition the AO has correctly pointed out that the business of the assessee does not envisage the staging of Opera productions etc. Keeping in view the above facts and circumstances, it is held that this expenditure of Rs. 1,89,201/- has been rightly disallowed by the AO and is accordingly upheld. However, it is held that the 80% disallowance made by the AO separately in this regard will be deleted as the same expenditure cannot be disallowed twice.”

23. Tribunal in this regard has held as under:-

“7. We have heard both sides. The CIT(A) has discussed this issue in para 10 of his order. All these expenses were incurred on producing “The Fakir of Banaras” which was a show organized by Delhi Symphony Society. The reasoning given by the assessing officer to make disallowance are strange. Merely because the assessee’s daughter participated in the show, does not warrant disallowance, as it is very common for the family members of the assessee to assist the family business of the assessee. Moreover, the assessing officer wanted the production of the balance-sheet of Delhi Symphony Society, on which the assessee had no control. The assessee had only incurred some expenses like printing of invitations etc. which is totally insignificant comparing to



the total expenditure incurred for conducting the show. All these expenses are incurred for the purpose of business as rightly pointed out by the CIT(A). We agree with him and decline to interfere.”

24. The order of the tribunal is not clear and in fact contrary to the findings of the CIT (Appeals) as it has been held that they were in agreement with CIT (Appeals) and it is further stated that “we are not inclined to interfere”. This aspect requires fresh consideration and decision by the Tribunal. Accordingly, the aforesaid question is partly answered in favour of the Revenue and against the assessee and an order of remit is passed. Parties will appear before the Additional Registrar on 30th November, 2011, when a date of hearing shall be given.

25. The appeal is accordingly disposed of. There will be no order as to costs.

(SANJIV KHANNA)
JUDGE

(R.V. EASWAR)
JUDGE

November 8th, 2011

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