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IN THE HIGH COURT OF DELHI AT NEW DELHI

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ITA No.792 of 2011

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RESERVED ON: JUNE 02, 2011
PRONOUNCED On: JULY 11, 2011

PSB INDUSTRIES INDIA PVT. LTD.

. . . APPELLANT

through : Mr. C.S. Aggarwal, Sr.
Advocate with Mr. Prakash
Kumar, Advocate.

VERSUS

COMMISSIONER OF INCOME TAX

. . . RESPONDENT

through: Mr. Deepak Chopra,
Advocate.

CORAM :-

HON'BLE MR. JUSTICE A.K. SIKRI
HON'BLE MR. JUSTICE M.L. MEHTA

1. Whether Reporters of Local newspapers may be allowed to see the Judgment?
2. To be referred to the Reporter or not?
3. Whether the Judgment should be reported in the Digest?

A.K. SIKRI, J.

1. This appeal was admitted on the following substantial questions of law:

“(1) Whether the Income Tax Appellate Tribunal was justified in law in holding that the assessee was liable for penalty of ₹17,82,078/- under Section 27(1)(c) of the Income Tax Act, 1961?

(2) Whether the Income Tax Appellate Tribunal was justified in law in confirming imposition of penalty under Section 27(1)(c) of the Income Tax Act, 1961 despite the fact that addition has been made on the

basis annual value estimated by the registered valuer?”

2. As is clear from the aforesaid questions, the assessee has been fastened with the penalty under Section 271(1)(c) of the Income Tax Act (hereinafter referred to as ‘the Act’) by the Assessing Officer, which has been upheld by the CIT(A) as well as the Income Tax Appellate Tribunal (‘the Tribunal’ for brevity). This penalty was imposed under the following circumstances:

The assessee entered into a Memorandum of Intent dated 24.03.2001 with the Bank of Punjab Limited to let out its property bearing Khasra No.258 & 261, Khevat No.430/250 and Khatauni No.520 situated at Manesar Raod, Gurgaon. Thereafter, the prescribed Form No.37-I was filed on 16.04.2001 before the appropriate authority constituted under the provisions of Chapter XX-C of the Act under Section 269UC of the Act seeking no objection by the appropriate authority. Thereafter, the appropriate authority issued a certificate dated 30.07.2001 under Section 269UL(3) of the Act giving no objection. Thereafter, the appellant by a Lease Agreement dated 06.08.2001 had leased out its aforesaid property to the Bank of Punjab Limited at rental ₹1,00,000 per annum. As per the aforesaid Lease Agreement, the property admeasuring 11,499 sq. yds (10,682.83 sq. mts.) situated at Manesar Road,

Gurgaon together with five existing buildings or structure standing thereon was let out on rent to Bank of Punjab Limited. The assessee had leased out the said premises having aggregate constructed area of 1,23,490 sq. ft. for a term of 25 years commencing from 24.03.2001. The assessee had received a sum of ₹67,00,00,000/- as interest free deposit from the lessee i.e. Bank of Punjab Limited.

3. For the Assessment Year 2006-07, the assessee filed a return of income, declaring loss of ₹3,87,912/- along with computation of income and annual audited accounts. In the return of income, the assessee had shown rental income of ₹1,00,000/- per annum based on the aforesaid Agreement dated 06.08.2001 entered into with Punjab National Bank i.e. the lessee. The said return of income filed by the assessee company was accepted in an intimation under Section 143(1) of the Act. Thereafter, the case was selected for scrutiny in issuance of notice under Section 143(2) of the Act.
4. During the course of assessment proceedings, the Assessing Officer (AO) asked the assessee to furnish valuation report of annual rental value of the premises let out to Bank of Punjab Limited. The assessee furnished valuation report dated 26.11.2008 from a Government registered Valuer, according to

which the annual rental value was determined at ₹75,63,360/- as on 01.04.2005. The AO by an order of assessment under Section 143(3) of the Act assessed the income of the assessee at ₹52,94,352. The AO adopted the annual value of the aforesaid premises at ₹75,63,360/- as determined by the registered valuer in the report dated 26.11.2008. After deducting ₹22,69,008/- under Section 24(a) of the Act, the AO made net addition of ₹52,94,352/-. The AO also initiated penalty proceedings under Section 271(1)(c) of the Act. Show cause notice was issued under Section 271(1)(c) read with Section 274 of the Act to the assessee to show cause as to why an order imposing penalty under Section 271(1)(c) of the Act be not passed. The assessee filed a reply before the AO. During the penalty proceedings under Section 271(1)(c) of the Act, the assessee submitted before the AO that since the assessment was made on the notional income i.e. the fair market value of the property determined by the registered valuer and the same was admitted during the course of the assessment proceedings, the penalty proceedings should be dropped. The AO imposed penalty of ₹17,82,078/- under Section 271(1)(c) of the Act by an order on account of tax allegedly sought to be evaded.

5. The CIT(A) confirmed the levy of penalty under Section 271(1)(c) of the Act.
6. The Tribunal vide order dated 04.02.2011 dismissed the appeal of the assessee and upheld the action of the CIT(A) in confirming the penalty of ₹17,82,078/- imposed by the AO under Section 271(1)(c) of the Act.
7. It is clear from the aforesaid narration of facts that the main reason for the AO to imposed the penalty upon the assessee was that the annual rental value of ₹1 lac disclosed by the assessee in the income tax return, on the basis of Lease Agreement dated 06.08.2001 was clearly wrong and having regard to the fact that the assessee had also received a sum of ₹67 Crores as interest free deposit from the lessee, annual rental value would be much higher, which was ultimately determined at ₹75,63,360/- as on 01.04.2005 on the basis of valuation report of the Government registered Valuer submitted by the assessee imposed. In this wake, according to the Revenue, the assessee had concealed material particular and furnished inaccurate particular of income.
8. Challenging this line of action of the Department, which is upheld by the Tribunal, the contention of the assessee is that

the Tribunal has failed to appreciate that in the return of income the assessee had shown rental income of ₹1 lac per annum based on the aforesaid Lease Agreement entered into with Punjab National Bank i.e. the lessee. During the course of assessment proceedings, the AO asked the appellant to justify the said rental income of ₹1 lac per annum by furnishing a valuation report from the registered Valuer in respect of such property. The assessee accordingly obtained the valuation report dated 26.11.2008 from Government Registered Valuer and duly submitted the same before the AO wherein the Registered Valuer had determined the annual rental value at ₹76,63,360/- under Section 23 of the Act. The assessee in order to avoid prolonged litigation and buy peace, voluntarily accepted the said valuation of ₹76,63,360/- as annual rental value of its property. It is further evident in the instant case that apart from the disclosing such rental income in its computation of income the assessee had also produced copy of the rent/lease agreement (entered between the assessee and the Bank of Punjab Limited, which was duly signed by both the parties and was duly registered) before the AO which further substantiates the assessee's contention that there was no intention of the assessee to conceal any particulars of income. Furthermore, the assessee had duly shown the security deposit of ₹67 Crores received by the lessee i.e. Bank of Punjab Limited in the

audited annual accounts under the head “Current Liabilities” and has also given necessary disclosures under the notes to accounts. The aforesaid facts, goes to prove the *bona fide* act of the assessee, as such on the facts of the instant case, non-penalty under Section 271(1)(c) of the Act was exigible.

9. Thus, the basic contention of Mr. C.S. Aggarwal, learned Senior Counsel appearing for the assessee was that it was not a case of concealment of income or furnishing wrong particulars. Annual rental value shown on the basis of Lease Agreement which recorded the rent at which premises were let out. It was clearly a *bona fide* move. On the other hand, annual rental value adopted by the AO was notionally arrived at. In support of his submission, the learned counsel referred to and relied upon the following judgments of the Supreme and this Court and submits that in a case like this, no penalty was sustained:

- (1) ***Commissioner of Income Tax Vs. Zoom Communications Pvt. Ltd. [327 ITR 510].***
- (2) ***Commissioner of Income Tax Vs. Reliance Petro Products Pvt. Ltd. [322 ITR 158].***
- (3) ***Commissioner of Income Tax Vs. M.K. Subba [333 ITR 38].***

(4) ***Commissioner of Income Tax Vs. Suresh Chandra Mittal [251 ITR 9].***

(5) ***K.P. Madhusudhanan Vs. Commissioner of Income Tax [251 ITR 99].***

10. Mr. Deepak Chopra, learned counsel for the Revenue, countered the aforesaid submission. He relied upon the reasoning given by the authorities below in imposing/sustaining the penalty. He also referred to the provisions of Section 23 of the Act on the basis of which he submitted that the annual rent in the Lease Agreement was suppressed. It was the duty of the assessee to state the rent which this property could reasonably fetch which was the duty cast upon him having regard to the provisions of Section 23 of the Act.

11. Thus in every case, it is seen, on the facts of the case, as to whether the assessee had furnished wrong/false particulars of income or had concealed the income. That is the principle of law laid down by the various judgments cited by both the sides about which there is no quarrel. The question is whether the conditions stipulated in Section 23(1) are satisfied in the instant case. To examine the same, we reproduce the provisions of Section 23 of the Act:

“Section 23. Annual Value how determined.

(1) For the purposes of section 22, the annual value of any property shall be deemed to be -

(a) The sum for which the property might reasonably be expected to let from year to year; or

(b) Where the property is let and the annual rent received or receivable by the owner in respect thereof is in excess of the sum referred to in clause (a), the amount so received or receivable :

Provided that where the property is in the occupation of a tenant, the taxes levied by any local authority in respect of the property shall, to the extent such taxes are borne by the owner, be deducted (irrespective of the previous year in which the liability to pay such taxes was incurred by the owner according to the method of accounting regularly employed by him) in determining the annual value of the property of that previous year in which such taxes are actually paid by him :

Provided further that the annual value as determined under this sub-section shall, - (a) In the case of a building comprising one or more residential units, the erection of which is begun after the 1st day of April, 1961, and completed before the 1st day of April, 1970, for a period of three years from the date of completion of the building, be reduced by a sum equal to the aggregate of -

(i) In respect of any residential unit, whose annual value as so determined does not exceed six hundred rupees, the amount of such annual value;

(ii) In respect of any residential unit whose annual value as so determined exceeds six hundred rupees, an amount of six hundred rupees;

(b) In the case of a building comprising one or more residential units, the erection of which is begun after the 1st day of April, 1961, and completed after the 31st day of March, 1970, but before the 1st day of April, 1978, for a period of five years from the date of completion of the building, be reduced by a sum equal to aggregate of -

(i) In respect of any residential unit whose annual value as so determined does not exceed one thousand two hundred rupees, the amount of such annual value;

(ii) In respect of any residential unit whose annual value as so determined exceeds one thousand two hundred rupees, an amount of one thousand two hundred rupees;

(c) In the case of a building comprising one or more residential units, the erection of which is completed after

the 31st day of March, 1978 but before the 1st day of April, 1982, for a period of five years from the date of completion of the building, be reduced by a sum equal to the aggregate of -

(i) In respect of any residential unit whose annual value as so determined does not exceed two thousand four hundred rupees, the amount of such annual value;

(ii) In respect of any residential unit whose annual value as so determined exceeds two thousand four hundred rupees, an amount of two thousand four hundred rupees;

(d) In the case of a building comprising one or more residential units, the erection of which is completed after the 31st day of March, 1982 but before the 1st day of April, 1992, for a period of five years from the date of completion of the building, be reduced by a sum equal to the aggregate of - (i) In respect of any residential unit whose annual value as so determined does not exceed three thousand six hundred rupees, the amount of such annual value;

(ii) In respect of any residential unit whose annual value as so determined exceeds three thousand six hundred rupees, an amount of three thousand six hundred rupees."

12. Section 22 of the Act makes "income from house property" as chargeable to income tax. After excluding such portions of such property as he may occupy for the purposes of any business or profession carried on by him the profits of which are chargeable to income-tax. It is the annual value of the property which becomes chargeable to income tax under this head. Section 23, already extracted above, stipulates the manner in which such an annual value is to be determined. It is clear from Clause (a) of sub-Section (1) of Section 23 of the Act that in case the annual rent received is less than the sum for which the property might reasonably be expected to let

from year to year, it is the said sum and not the annual rent which would be the annual value chargeable to tax. Only in case where the property is let and the annual rent received or receivable by the owner in respect thereof is in excess of the sum referred to in clause (a), the amount so received or receivable shall be taxed. Thus, it is the higher of the two which is chargeable to tax. Along with this specific provisions under Section 23, there is no defence of the assessee that disclosing the annual rent as the annual letting value for the purposes of tax was *bona fide*. In the instant case, the assessee had entered into an agreement to lease out the property to Punjab National Bank Ltd. on a sum of ₹1 lac per annum. The total area of constructed building leased out by the assessee is given in second schedule to the Lease Agreement, which is 1,23,490 sq. ft. The approved valuer has valued the annual letting value of total constructed area of 1,23,490 sq. ft. at ₹75,63,360/-

13. Interestingly, when the AO found that the sum of ₹67 Crores was taken as interest free security and in these circumstances, the property would reasonably expect adjustment of rent than mentioned in the Lease Agreement and the assessee was called upon to give the valuation. The assessee himself filed the annual letting value by the approved valuer of total

constructed area of 1,23,490 sq. ft. at ₹75,63,360/-. This was done at the instance of the AO when the assessee was exposed and confronted with the aforesaid facts. Had the assessee kept in mind the provisions of Section 23 of the Act, which it was supposed to, the assessee would have found that the sum for which the property might reasonably be expected from year to year is adjustment than the sum disclosed in the Lease Agreement. In this behalf, the Tribunal has observed, and rightly so, is as under:

“The word “reasonably” appearing in Clause (a) is very important. What the landlord might reasonably expect to get from a hypothetical tenant, if the building were let from year to year, affords the statutory yardstick for determining the annual value. The actual rent payable by a tenant to the landlord would, in normal circumstances, afford reliable evidence of what the landlord might reasonably expect to get from a hypothetical tenant, unless the rent is inflated or depressed by reason of extraneous consideration such as relationship, expectation of some other benefit etc. There would be ordinarily be in a free market close approximation between actual rent received by the landlord and the rent which he might reasonably expect to get from a hypothetical tenant. In the case before us, the assessee had received interest free deposits of ₹67 Crores because which the rent received was low. The annual rent of ₹1 lac of the property having area of 1,23,490 sq. ft. let out to a bank cannot be treated as reasonable to which property could be let out from year to year. In the case of **Babulal Raj Garhia [4 ITR 148]**, the Calcutta High Court held that a Lease Deed is not a conclusive evidence of *bona fide* annual value of the property. Therefore, the contention of the assessee that rent received by the assessee is evidenced by Lease Deed is not a conclusive evidence of *bona fide* annual value of the property. Further, the deeming provisions of Section 23(1) are mandatory in nature and, therefore, the assessee was required to admit the annual value of the property for which, it might reasonably be let out from year to year rather than adopting the figure of ₹1 lac per annum which is grossly depressed because of security deposit of ₹67 Crores

equivalent 6700 years of annual rent received by the assessee.

Further, the assessee had received ₹67 Crores as security deposit which has been given by the assessee to its sister concerns without any interest. The assessee had let out 1,23,490 sq. ft. of the area to Punjab National Bank for a sum of ₹1 lac, which gives annual rent per sq. ft. at ₹0.80/-. It is unbelievable that the annual letting value of any property in city like Gurgaon will be at the rate of ₹0.80 per sq. ft. The assessee was aware of its annual letting value because of which he had taken interest free advance of ₹67 Crores which has been diverted free of interest to sister concerns. Had this money been put in fixed deposit @ 8%, the assessee would have received interest of ₹5,36,00,000/- per annum. If the assessee had offered any income from security deposits or invested in its own business, it would have been argued for the purpose of penalty under Section 271(1)(c) of the Act that the assessee was under *bona fide* belief to admit income as per Lease Agreement, though the income of the house property was to be assessed as per provisions of Clause (a) of Section 23(1) of the Act. The assessee preferred to divert the security deposits of ₹67 Crores to group concerns free of interest. The assessee's valuer has valued annual letting value of the property at ₹75,63,360/- which has been accepted by the assessee and the same has not been agitated before the appellate authorities. Therefore, the annual letting value of the property at ₹75,63,360/- has attained finality. The difference in market rent as determined by approved valuer (₹61.25/sq.ft./annum) and rent received (₹0.80/sq.ft./annum) is too large to believe that the assessee was under *bona fide* belief that market rent was ₹0.80 per square feet. From these facts, it is evident that the assessee had planned its affairs in such a way that minimum tax would be payable."

14. In a case like this, we are of the view that explanation of the assessee was not *bona fide*. Explanation 1 to Section 271(1)(c) of the Act would be fully applicable and the AO was justified in imposing the penalty which was upheld upto the Tribunal level.

15. We, thus, answer the aforesaid questions against the assessee and in favour of the Revenue, as a consequence, this appeal is dismissed.

(A.K. SIKRI)
JUDGE

(M.L. MEHTA)
JUDGE

JULY 11, 2011
pmc