



Development charges paid by lessee for acquiring an industrial plot on a long-term lease is not rent and hence withholding of tax is not required under the Income-tax Act

Background

Recently, the Jaipur Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Gupta Fabex Pvt. Ltd.¹ (the taxpayer) held that development charges paid by the taxpayer-lessee towards allotment of an industrial plot on a long-term lease for 99 years is not rent, and accordingly there is no requirement for withholding Tax Deducted at Source (TDS) under Section 194I of the Income-tax Act, 1961 (the Act)

Facts of the case

- The taxpayer is engaged in the manufacturing of readymade garments for various brands like Bombay Dyeing, Lifestyle, etc. The Rajasthan State Industrial Development and Investment Corporation Ltd. (RIICO) allotted a plot to the taxpayer for the establishment of an Industry at Ramchandra Pura Industrial Area, Sitapura Extension, Jaipur.
- As per the said allotment letter and the lease agreement, the land was allotted to the taxpayer on lease for 99 years and subsequently was required to pay the amount of INR6.05 crores (comprising of development charges of INR4.8 crores payable in installments, interest on development charges of INR1.1 crores, security money of INR4.8 lakhs and economic rent of INR11 thousand)
- The taxpayer paid 25 per cent of the development charges as per the terms and conditions of the allotment letter and opted for paying the balance 75 per cent amount in 19 equal quarterly installments along with interest. During the relevant years i.e. assessment year (AY) 2011-12 and AY 2012-13, the taxpayer paid INR1.6 crores to RIICO, the major component of which was development charges.
- The spot verification was carried out for the purpose of TDS verification by the Revenue. During the course of such verification, the taxpayer was asked to explain the applicability of section 194I to the payments made to RIICO as above. The taxpayer filed a detailed response.

¹ Gupta Fabtex Pvt. Ltd. v. DCIT (TDS) (ITA Nos. 647 & 648/JP/2013) – Taxsutra.com

- However, the Assessing Officer (AO) rejected the contentions of the taxpayer and held that 'lease rent' paid by the taxpayer falls within the definition of Section 194I of the Act and that the taxpayer is in default for not deducting TDS on the amount paid to the taxpayer. The Commissioner of Income Tax [CIT(A)] upheld the order of the AO.

Tribunal's ruling

- The purport of Section 194I of the Act is not to bring in its purview payments of any or every kind; rather only those payments which are in the nature of 'use' of land come within the ambit of section 194 I of the Act. The word 'use' is therefore of prime importance for transactions where the consideration paid for the property would be termed as 'rent'. The term 'use' has to be interpreted keeping in mind the relationship between the landlord and the tenant. The same cannot be extended to bring within its purview exploitation of any kind with reference to the property by changing its identity for its own benefit and thereafter selling it for profit. If that be so and the word 'use' is given an extended meaning, there would be no difference between a sale transaction and a transaction between the landlord and the tenant. This would render the intention of the legislature in importing the word 'use' in Section 194I of the Act otiose.
- The landlord-tenant relationship does not contemplate such a right being given to the tenant. However, there may be transactions of the lease that may be identical to the transactions between a landlord and tenant, which is why the definition of rent includes lease, sublease, etc.
- The amount paid by the taxpayer towards development charges has no connection with the market rent of the property leased to the taxpayer.
- Furthermore, the term of the lease deed is for a considerable period of 99 years which further supports the case of the taxpayer that the payment made was for the acquisition of rights in the land along with the right of possession,

right of possession, right of exploitation of property, its long-term enjoyment, to mortgage the property, to sell the property, and the likewise.

- Besides, the above lease document has used the 'development charges' and 'economic rent' to be payable by the taxpayer. As the document has used two different phrases to connote different obligations, therefore, development charges cannot be read as rent within the purview of Section 194I of the Act.
- Further, the lease document has provided the consequences towards non-payment of the development charges by the taxpayer, who if fails to pay the development charges, as mentioned in the agreement, the possession was liable to be taken over by RIICO. Therefore, development charges cannot be considered as rent.
- The terms of the lease deed leave no manner of doubt that the development charges along with interest were paid for the acquisition of rights in the leasehold property rather than the use of land. Therefore, the provisions of Section 194I of the Act are not applicable in the case of the taxpayer.
- The Tribunal also considered various judicial pronouncements² on the matter while providing its aforesaid ruling. It also observed that where there are conflicting views, the view favourable to the taxpayer should be adopted as per the mandate of the Supreme Court in the case of Vegetable products³.

Our comments

The applicability of TDS on development charges/lease premium has been a subject matter of litigation at various forums, and several judicial pronouncements have been rendered in this context. The above ruling of the Jaipur Tribunal is a welcome decision on the matter.

² Foxconn India Developer Pvt. Ltd. v. ITO [2012] 53 SOT 213 (Chen), CIT v. Panbari Tea company Ltd. [1965] 57 ITR 422 (SC), CIT v. Purnendu Mullick [1979] 116 ITR 591 (Cal), Bharat Steel Tubes Ltd. v. CIT [2001] 252 ITR 622 (Del), ITO v. Wadhwa & Associates Realtors Pvt. Ltd. [2014] 146 ITD 0694 (Mum), ITO (TDS) v. Navi Mumbai SEZ Pvt. Ltd. [2014] 147 ITD 261 (Mum)

³ CIT v. Vegetable Products Ltd. [1973] 88 ITR 192 (SC)

However, it is crucial to note that what has weighed in the Tribunal's decision is the factual aspect in the case that the lease development charges did not constitute payment for use of land but was paid for the acquisition of land under a long-term lease along with a bundle of related rights.

The issue of the applicability of TDS on lease premiums/development charges needs to be ascertained on the basis of factual aspects of the case, definition of 'rent' under Section 194I of the Act and more importantly, on the analysis of whether or not the said payment can be said to be for the 'acquisition' or for the 'use' of land.



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