



Income from the sub-licensing of property is taxable as house property income and not business income

Background

Recently, the Supreme Court in the case of Raj Dadarkar and Associates¹ (the taxpayer) held that the income from the sub-licensing of property is taxable as 'house property' income and not business income. Merely because there is an entry in the object clause of the business showing a particular object, would not be the determinative factor to arrive at a conclusion that the income is to be treated as business income.

Facts of the case

- The Maharashtra Housing and Developing Authority (MHADA) had constructed buildings known as Shyam Sunder Cooperative Society, Ram Darshan Cooperative Society and Sindhu Cooperative Society in Mumbai
- However, there was a reservation for Municipal retail market on the plot on which MHADA had constructed. Therefore, MHADA handed over the ground floor [stilt portion] of the above said buildings admeasuring around 17,925 sq. ft. (Market portion) to Market Department of Municipal Corporation Greater Bombay (MCGB).
- In 1993, the Markets Department of the MCGB auctioned the property on a monthly license [stallage charges] basis to run the municipal market.
- The taxpayer participated in the auction and was the successful bidder. Accordingly, MCGB handed over possession of the market portion to the taxpayer.
- The premises allotted to the taxpayer was a bare structure, on stilts, that is, a pillar/column, sans even four walls. In terms of the auction, it was the taxpayer who had to make the entire premises fit to be used a market, including the construction of walls, construction of entire common amenities such as toilet blocks, etc.
- Accordingly, after taking possession of the premises, the taxpayer spent a substantial amount on additions/alternations of the entire premises, including demolishing the existing platform and, thereafter, reconstructing the same according to the new plan sanctioned by the MCGB.
- The taxpayer constructed 95 shops and 30 stalls of different carpet areas on the premises under the market name 'Saibaba Shopping Centre'. The taxpayer also obtained, in terms of the conditions of the auction, the necessary registration certificate for running a business under the Shop and Establishment Act and other licenses/permissions from MCGB and other Government and semi-Government bodies for carrying on trading activities on the said premises.
- The taxpayer was responsible for day-to-day maintenance, cleanliness and upkeep of the market premises. The appellant also had to incur/pay water charges, electricity charges, taxes and repair charges.

¹ Raj Dadarkar and Associates v. ACIT (Civil Appeal No. 6455-6460 OF 2017) (SC) – Taxsutra.com

- The taxpayer collected the following types of receipts from the sub-licensees:
 - Compensation from sub-licensees [same rate of stallage charges and on the same terms and condition as given to the taxpayer by the MCGB]
 - Leave and license fees
 - Service Charges for providing various services, including security charges, utilities, etc.
- The taxpayer filed the returns of income and right from the year 1999 till 2004, it had been offering the income from the aforesaid shops and stalls sub-licensed by it as business income.
- However, the case of the taxpayer for the Financial Year 1999-2000 was reopened by the AO by issuing notice under Section 148 of the Act and in response to the same the taxpayer filed its return. Thereafter, notice under Section 143(2) of the Act was issued and served by the AO. Reassessment order was framed and AO computed the income from the shops, and the stalls under head 'Income from House Property'.
- The Commissioner of Income-tax (Appeals) [CIT(A)] allowed the appeal of the appellant and reversed the action of the respondent. However, the Income-tax Appellate Tribunal (the Tribunal) reversed the order of the CIT (Appeals) and confirmed the action of the AO.
- Aggrieved by the Tribunal's order, the taxpayer filed an appeal before the High Court. The High Court dismissed the appeal filed by the taxpayer.

Supreme Court's decision

- Wherever there is an income from leasing out of premises and collecting rent, normally such an income is to be treated as income from house property, in case provisions of Section 22 of the Act are satisfied with primary ingredient that the taxpayer is the owner of the said building or lands appurtenant thereto.
- Section 22 of the Act makes 'annual value' of such a property as income chargeable to tax under this head. How annual value is to be determined is provided in Section 23 of the Act. 'Owner of the house property' is defined in Section 27 of the Act which includes certain situations where a person not actually the owner shall be treated as the deemed owner of a building or part thereof.

- In the present case, the appellant is held to be 'deemed owner' of the property in question by virtue of Section 27 of the Act.
- Merely because there is an entry in the object clause of the business showing a particular object, would not be the determinative factor to arrive at a conclusion that the income is to be treated as income from business. Such a question would depend upon the circumstances of each case.
- The Tribunal being the last forum insofar as factual determination is concerned, the findings have attained finality. The Tribunal held that the service charges received were inseparable from the basic charges of rent. Also, it was undisputed that the taxpayer did not undertake any systematic or organized activity of providing services to the occupiers, which can constitute receipt as business income for the taxpayer.
- It was for the taxpayer to produce sufficient material on record to show that its entire income or substantial income was from letting out of the property which was the principal business activity of the taxpayer. The taxpayer did not argue on this aspect and did not make any efforts to show as to how the findings of the Tribunal were perverse.
- Reliance placed by the taxpayer on the judgments of this Court in *Chennai Properties & Investments Ltd.*² and *Rayala Corporation (P) Ltd.*³ would be of no avail.

Our comments

The Supreme Court in the instant case has dealt with the issue of characterisation of income from the sub-licensing of property. The Supreme Court held that the object clause of the business showing a particular object, would not be the determinative factor to arrive at a conclusion that the income is from business. On the basis of facts of the case, the Supreme Court held that income earned by the taxpayer is not taxable as business income but it would be taxable as income from house property.

This decision will help taxpayers to determine the characteristic of income received from property.

² Chennai Properties and Investments Limited v. CIT (2015) 14 SCC 793

³ Rayala Corporation Private Limited v. ACIT (2016) 15 SCC 201

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