

Upfront premium received for leasing out land on BOT basis taxable on receipt basis

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In brief

The Bangalore Bench of Income-tax Appellate Tribunal (Tribunal) held that the upfront premium received by the taxpayer for leasing out port land to companies for 30 years on build-operate-transfer (BOT) basis was taxable on receipt basis. The taxpayer's claim to spread the premium income over the period of the lease for tax purposes was denied.

In detail

Facts of the case

- The taxpayer¹ was a local authority providing port facilities at a port, which included docking of ships, loading/ unloading, warehousing, etc.
- The taxpayer formulated a BOT scheme under which it permitted three companies to develop certain facilities on the taxpayer's land, and use them for 30 years.
- Under the terms of the concession agreement, the taxpayer received an upfront lump-sum premium.
- Apart from upfront premium, the concessionaires were also required to pay the taxpayer regular facilities charges (licence fees/ royalty) for handling cargo in a designated port area.

- In its return of income, the taxpayer offered 1/30th of upfront premium as income and disclosed the balance amount as liability in nature of pre-paid income.
- The Tax Officer (TO) treated the entire amount received from the companies as the taxpayer's income in the year of receipt/ entering into the concession agreement.
- The Commissioner of Income-tax (Appeals) confirmed the additions made by the TO.

Issue before the tribunal

- Can the taxpayer claim the premium received upfront as taxable proportionately over the lease period?

Taxpayer's contentions

- The upfront premium paid as consideration by the concessionaire was a licence fee for the entire period of lease. It was towards the use of the

facility for a period of 30 years under the agreement. Only that part of the premium which related to the year under consideration could be described as the year's income.

- The taxpayer was subject to audit by the Controller & Auditor General (C&AG), who had indicated that upfront premium could not be entirely recognised as income for the year in which the agreement was signed. Thus, in accordance with the C&AG's advice, the taxpayer recognised 1/30th of the upfront premium as its income for the year in which the agreement was signed.
- The taxpayer claimed in its support the matching concept in accounting, and the accounting standard 19, issued by the ICAI.
- Thus, it claimed that the income on account of

¹ [TS-674-ITAT-2015 (Bangalore-Tribunal)]

upfront premium for the year under consideration could not be more than 1/30th of the entire fee.

Tax authorities' contentions

- The concession agreement stated that the upfront fee was payable on execution of the agreement.
- This amount could not be taken as income on proportionate basis, as the agreement did not specify the quantum to be apportioned over a period of 30 years.
- There was no provision in the Income-tax Act, 1961 that permitted spreading over of the income to future periods. The taxpayer had not shown the amount in question as advance, but had recognised the receipt as income.
- The income received during the year was without any corresponding obligation to be discharged by the taxpayer in future years. Hence, the entire income was assessable in the year in which upfront premium was received.

Tribunal's Ruling

- The transaction of leasing out the land for 30 years was completed by execution of the agreement. Thereafter

the taxpayer was not required to do or perform any act or obligation under the concession agreement.

- The taxpayer had received consideration for grant of license/ lease in lump-sum, apart from the annual license fee/ royalty, without any corresponding obligation to be discharged by the taxpayer.
- The upfront premium amount was admittedly non-refundable, even if the concession agreement was terminated prematurely.
- As per the Profit and Loss Account, the taxpayer itself had recognised the entire upfront premium received as income for the year under consideration. This showed that the entire receipt accrued during the year under consideration.
- Though the C&AG had raised some objections in his audit report to recognising the entire income as income of the year in which the upfront premium was received, and recommended that only a proportionate amount of upfront premium to be considered as income over 30 years, his remarks could not change the character or

incidence of accrual of the income. Thus, the taxpayer's claim was rejected, and the entire upfront premium received was treated as income of the current (first) year.

The takeaways

- The decision re-iterates the important principle of accrual while determining taxable income.
- The tests laid down by the Supreme Court in the case of *E. D. Sassoon & Co. Limited*² needs to be tested while determining accrual of income.
- The treatment in the books of accounts may not be conclusive for determining taxability of the income.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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² *E.D. Sassoon & Co. Limited v. CIT* [1954] 26 ITR 27 (SC)

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