from India Tax & Regulatory Services

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

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In brief

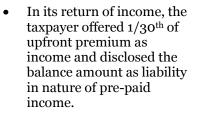
The Bangalore Bench of Income-tax Appellate Tribunal (Tribunal) held that the upfront premium received by the taxpayer for leasing out port land to companies for 30 years on build-operate-transfer (BOT) basis was taxable on receipt basis. The taxpayer's claim to spread the premium income over the period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

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



- 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 taxpaver 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



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 revceived.

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 nonrefundable, 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. Limited² 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:

Tax & Regulatory Services – Financial Services

Gautam Mehra, *Mumbai* +91-22 6689 1154 gautam.mehra@in.pwc.com

Nitin Karve, *Mumbai* +91-22 6689 1477 <u>nitin.karve@in.pwc.com</u>

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

Our Offices

Ahmedabad

President Plaza 1st Floor Plot No 36 Opp Muktidham Derasar Thaltej Cross Road, SG Highway Ahmedabad, Gujarat 380054 +91-79 3091 7000

Hyderabad

Plot no. 77/A, 8-2-624/A/1, 4th Floor, Road No. 10, Banjara Hills, Hyderabad – 500034, Andhra Pradesh Phone +91-40 44246000

Gurgaon

Building No. 10, Tower - C 17th & 18th Floor, DLF Cyber City, Gurgaon Haryana -122002 +91-124 330 6000

Bangalore

6th Floor Millenia Tower 'D' 1 & 2, Murphy Road, Ulsoor, Bangalore 560 008 Phone +91-80 4079 7000

Kolkata

56 & 57, Block DN. Ground Floor, A- Wing Sector - V, Salt Lake Kolkata - 700 091, West Bengal +91-033 2357 9101/ 4400 1111

Pune

7th Floor, Tower A - Wing 1, Business Bay, Airport Road, Yerwada, Pune – 411 006+91-20 4100 4444

Chennai

8th Floor Prestige Palladium Bayan 129-140 Greams Road Chennai 600 006 +91 44 4228 5000

Mumbai

PwC House Plot No. 18A, Guru Nanak Road(Station Road), Bandra (West), Mumbai - 400 050 +91-22 6689 1000

For more information

Contact us at <u>pwctrs.knowledgemanagement@in.pwc.com</u>

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