

**INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH "B": NEW DELHI**

**BEFORE SHRI H.S. SIDHU, JUDICIAL MEMBER
AND
SHRI O.P. KANT, ACCOUNTANT MEMBER**

ITA No. 1156/Del/2002
Asstt. Year. 1994-95

The Instalment Supply Ltd. 46, Janpath, New Delhi – 110 001.	Vs.	DCIT, Circle 16(1), New Delhi.
(Appellant)		(Respondent)

Assessee by:	Shri Barun Kumar, CA
Department by :	Ms. Ashima Neb, Sr. DR
Date of Hearing	29/11/2018
Date of pronouncement	19/12/2018

ORDER

PER O.P. KANT, A.M.

This appeal has been remitted back by the Hon'ble Delhi High Court vide decision dated 17/04/2012 for examining the controversy whether the agreement entered between the assessee and "HCL Hewlett Packard Limited" for leasing of computer spare parts and claim of depreciation thereon, was a finance agreement or operating lease agreement, in the light of judicial decisions discussed by the Hon'ble High Court.

2. For ready reference, the finding of the Hon'ble High Court is reproduced as under:

"11. We have elucidated and reproduced the relevant reasoning given by the Tribunal. The real issue and question involved in the present case is, whether or not the agreement in question was a finance agreement or an operating lease. The aforesaid question cannot be decided by merely looking at the title of the agreement itself or the nomenclature given to the said agreement. The terms and conditions mentioned in the agreement may be relevant but we have to also take into account the surrounding circumstances as well as the type and nature of the asset. It is this aspect which has been ignored and not given due credence.

12. The two types of transactions i.e.1 finance agreement and operational lease are different. Explaining this difference in Asea Brown Boveri Limited versus Industrial Finance Corporation of India and Others, (2004) 12 SCC 570 it has been observed:

"13. What is a lease finance? According to Dictionary of Accounting & Finance by R. Brockington (Pitman Publishing, Universal Book Traders, 1996 at p. 136):

"A finance lease is one where the lessee uses the asset for substantially the whole of its useful life and the lease payments are calculated to cover the full cost together with interest charges. It is thus a disguised way of purchasing the asset with the help of a loan. SSAP 23 required that assets held under a finance lease be treated on the balance sheet in the same way, as if they have been purchased and a loan had been taken out to enable this."

(emphasis supplied)

14. *In Lease Financing & Hire Purchase by Dr. J.C. Verma (4th Edn., -1999 at p. 33), financial lease has been so defined:*

"Financial lease is a long-term lease on fixed assets, it may not be cancelled by either party. It is a source of long-term funds and serves as an alternative of long-term debt financing. In financial lease, the leasing company buys the equipment and leases it out to the use of a person known as the lessee. ,It is a full payout lease involving obligatory payment by the lessee to the lessor that exceeds the purchase price of the leased property and finance cost.

Financial lease has been defined by International Accounting Standards Committee as 'a lease that transfers substantially all the risks and rewards incident to ownership of an asset. Title may or may not eventually be transferred'. Lessor is only a financier and is not interested in the assets. This is the reason that financial lease is known as full payout lease where contract is irrevocable for the primary lease period and the rentals payable during which period are supposed to be adequate to recover the total investment in the asset made by the lessor."

(emphasis supplied)

'15. *According to Lease Financing & Hire Purchase by Vinod Kothari (2nd Edn., 1986 at pp. 6 & 7), a finance*

lease, also called a capital lease, is nothing but a loan in disguise: It is only an exchange of money and does not result in creation of economic services other than that of intermediation. The learned author has quoted T.M. Clark, one of the most authentic writers on the subject who defines lease and operating lease in the undergoing words:

"A financial lease is a contract involving payment over an obligatory period of specified sums sufficient in total to amortise the capital outlay of the lessor and give some profit.

An operating lease is any other type of lease - that is to say, where the asset is not wholly amortised during the non-cancellable period, if any, of the lease and where the lessor does not rely for his profit on the rentals in the non-cancellable period."

16. The features of the financial lease, according to the learned author are as under:

"1. The asset is use-specific and is selected for the lessee specifically. Usually, the lessee is allowed to select it himself.

2. The risks and rewards incident to ownership are passed on to the lessee. The lessor only remains the legal owner of the asset.

3. Therefore, the lessee bears the risk of obsolescence.

4. *The lessor is interested in his rentals and not in the asset. He must get his principal back along with interest. Therefore, the lease is non-cancellable by either party.*

5. *The lease period usually coincides with the economic life of the asset and may be broken into primary and secondary period.*

6. *The lessor enters into the transaction only as a financier. He does not bear the costs of repairs, maintenance or operation.*

7. *The lessor is typically a financial institution and cannot render specialised service in connection with the asset.*

8. *The lease is usually full payout, that is, the single lease repays the cost of the asset together with the interest."*

17. *In our opinion, financial lease is a transaction current in the commercial world, the primary purpose whereof is the financing of the purchase by the financier. The purchase of assets or equipments or machinery is by the borrower. For all practical purposes, the borrower becomes the owner of the property inasmuch as it is the borrower who chooses the property to be purchased, takes delivery, enjoys the use and occupation of the property, bears the wear and tear, maintains and operates the machinery/equipment, undertakes indemnity and*

agrees to bear the risk of loss or damage, if any. He is the one who gets the property insured. He remains liable for payment of taxes and other charges and indemnity. He cannot recover from the lessor, any of the abovementioned expenses. The period of lease extends over and covers the entire life of the property for which it may remain useful divided either into one term or divided into two terms with clause for renewal. In either case, the lease is non-cancellable."

13. The aforesaid distinction has been again highlighted by the Supreme Court in Association of Leasing and Financial Service Companies versus Union of India, (2011) 2 SCC 352 with reference to service tax imposed under Section 65(12) and 65(105)(zn) by Finance Act, 2001, which underwent some changes by Finance Act, 2004 and 2007. Referring to the difference between the two agreements/transactions, the Supreme Court has held:

"34. In this connection, a; and by way of illustration we need to give an illustration which brings out the distinction between a "finance lease" and "operating lease". A finance lease transfers all the risks and rewards incidental to ownership, even though the title mayor may not be eventually transferred to the lessee. In the case of "finance lease" the lessee could use the asset for its entire economic life and thereby acquires risks and rewards incidental to the ownership of such assets. In substance, finance lease is a financial loan from the lessor to the lessee. On the other hand an operating lease is a lease other than the finance lease.

Accounting of a "finance lease" is under AS 19, which as stated above, is mandatory for NBFCs. It is a completely different regime.

35. According to Chitty on, Contract, a hire purchase agreement is a vehicle of instalment credit. It is an agreement under which an owner lets chattels out on hire and further agrees that the hirer may either return the goods and terminate the hiring or elect to purchase the goods when the payments for hire have reached a sum equal to the amount of the purchase price stated in the agreement or upon payment of a stated sum. The essence of the transaction is bailment of goods by the owner to the hirer and the agreement by which the hirer has the option to return the goods at some time or the other (see Paras 36.242 and 36.243). Further, in the bailment termed "hire" the bailee receives both possession of the chattel and the right to use it in return for remuneration to be paid to the bailor (see Para 32.045). Further, under the head "equipment leasing", it is explained that it is a form of long-term financing. In a finance lease, it is the lessee who selects the equipment to be supplied by the dealer or the manufacturer, but the lessor (finance company) provides the funds, acquires the title to the equipment and allows the lessee to use it for its expected life. During the period of the lease the risk and rewards of ownership are' transferred to the lessee who bears the risks of loss, destruction and depreciation or malfunctioning. The bailment which underlies finance

leasing is only a device to provide the finance company with a security interest (its reversionary right). If the lease is terminated prematurely, the lessor is entitled to recoup its capital investment (less the realisable value of the equipment at the time) and its expected finance charges (less an allowance to reflect the return of the capital) (Para 32.057): In the case of hire-purchase agreement the periodical payments made by the hirer are made up of:

(a) consideration for hire, and

(b) payment on account of purchase.

36. To sum up, NBFCs essentially are loan companies. They basically conduct their business as loan companies. They could be in addition thereto in the business of equipment leasing, hire purchase finance and investment. Because NBFCs are basically loan companies, they are required to show the assets leased as "receivables" in their balance sheets. That, the activities of hire-purchase finance/equipment leasing undertaken by NBFCs come under the category of "para banking". That, in substance a finance lease, unlike an operating lease, is a financial loan (assistance/facility) by the lessor to the lessee. That, in the bailment termed "hire" the bailee receives both possession of the chattel and the right to use it in return for remuneration. On the other hand, equipment leasing is long-term financing which helps the borrower to raise funds without outright payment in

the first instance. Here the "interest" element cannot be compared to consideration for lease/hire which is in the nature of remuneration (consideration) for hire."

14. *The aforesaid distinction was elucidated earlier also in a litigation in which tile assessee was involved (see In re Instalment Supply (P) Limited versus Union of India and Others, AIR 1962 SC 63 and Instalment Supply Limited versus STO, (1974) 4 SCC 739).*

15. *In Sundaram Finance Limited versus State of Kerala, AIR 1966 SC 1178 it was observed as under*

"24. The true effect of a transaction may be determined from the terms of the agreement considered in the light of, the surrounding circumstances, In each case, the Court has, unless prohibited by statute, power to go behind the documents and to determine the nature of the transaction, whatever may be the form of the documents. An owner of goods who purports absolutely to convey or acknowledges to have conveyed goods and subsequently purports to hire them under a hire-purchase agreement is not estopped from proving that the real bargain was a loan on the security of the goods. If there is a bona fide and completed sale of goods, evidenced by documents, anterior to and independent of a subsequent and distinct hiring to the vendor, the transaction may not be regarded as a loan transaction, even though the reason for which it was entered into was to raise money. If the real transaction is a loan of money secured by a right of seizure of the goods, the property ostensibly passes under the documents embodying the transaction, but subject to the terms of the hiring

agreement, which become part of the buyer's title, and confer a licence to seize. When a person desiring to purchase goods and not having sufficient money on hand borrows the amount needed from a third person and pays it over to' the vendor, the transaction between the customer and the lender will unquestionably be a loan transaction. The real character of the transaction would not be altered if the lender himself is the owner of the goods and the owner accepts the promise of the purchaser to pay the price or the balance remaining due against delivery of goods. But a hire-purchase agreement is a more complex transaction. The owner under the , hire-purchase agreement enters into a transaction of hiring out goods on the terms and conditions set out in the agreement, and the option to purchase exercisable by the customer or, payment of all the instalments of hire arises when tile instalments are paid and not before. In such a hire-purchase agreement there is no agreement to buy goods; the hirer being under no legal obligation to buy has an option either to return the goods or to become its owner by payment in full of the stipulated hire and the price for exercising the option. This class of hire-purchase agreements must be' distinguished from transactions in which the customer is the owner of the goods and with a view to finance his purchase he enters into an arrangement which is in the form of a hire-purchase agreement with the financier, but in substance evidences a loan transaction, subject to a hiring agreement under which the lender is given the license to seize the goods.

25. *A few illustrative cases decided by the Courts in England, which do not import complications arising from the Bills of Sale Act 1878, and the Hire Purchase Act, 1938, may be briefly noticed. In Re Watson Ex parte Official Receiver in Bankruptcy it was held that in adjudging the true nature of a transaction purporting to be a sale of personal chattels, followed by a hiring and purchase agreements, whereby the vendor agreed to hire the chattels from the purchaser and to pay quarterly sums for such hire until a certain amount was paid, when the chattels were to become again the property of the vendor, and power was given to the purchaser to take possession of the chattels on default of payment, the form of the transaction cannot be given undue importance. The Court held that no sale or hiring of the chattel was intended, the object in truth being to create a security for a loan of money to the supposed vendor from the supposed purchaser. The transaction was therefore one of loan. Lord Esher, M.R., observed at p. 37:*

" when the transaction is in truth merely a loan transaction, and the lender is to be repaid his loan and to have a security upon the goods, it will be unavailing to cloak the reality of the transaction by a sham purchase and hiring. It will be a question of fact in each case whether there is a real purchase and sale complete before the hiring agreement. If there be such a purchase and sale in fact and afterwards the goods are hired, the case is not within the Bills of Sale Act.

The document itself must be looked at as part of the evidence; but it is only part, and the Court must look at the other facts, and ascertain the actual truth of the case."

16. *Majority further elucidated and explained the legal position*

as under:

"28. In the light of these principles the true nature of the transactions of the appellants may now be stated. The appellants are carrying on the business of financiers: they are not dealing in motor-vehicles. The motor-vehicle purchased by the customer is registered in the name of the customer and remains at all material times so registered in his name. In the letter taken from the customer under which the latter agrees to keep the vehicle insured, it is expressly recited that the vehicle has been given as security for the loan advanced by the; appellants. As a security for repayment of the loan, the customer executes a promissory-note for the amount paid by the appellants to the dealer of the vehicle. The so-called "sale letter" is a formal document which is not made effective by registering the vehicle in the name of the appellants and even the insurance of the vehicle has to be effected as if the customer is the owner. Their right to seize the vehicle is merely a licence to ensure compliance with the terms of the hire-purchase agreement. The customer remains qua the world at large the owner and remains in possession, and on condition of performing the covenants has a right to continue to remain in possession. The right of the appellants may be extinguished by payment of the amount due to them under the terms of the hire-purchase agreement even before the dates fixed for payment. The agreement undoubtedly contains several onerous covenants, but they are all intended to secure to the appellants recovery of the amount advanced. We are accordingly of the view that the intention of the appellants in

obtaining the hire-purchase and the allied agreements was to secure the return of loans advanced to their customers, and no real sale of the vehicle was intended by the customer to the appellants. The transactions were merely financing transactions."

"17. In view of the aforesaid position we feel that the matter has not been examined and considered by the tribunal from the right perspective, the real issue and controversy has not been examined. The tribunal has not considered the legal position to reach its conclusion.

18. In these circumstances, we answer this substantial question of law mentioned above in negative, I.e., in favour of the Revenue and against the assessee. An order of remand is passed directing the tribunal to examine the controversy a fresh in the light of what has been stated above and without being influenced by the earlier order. The appeal is disposed of. In the facts of the case, there will be no order as to costs."

3. Before us, the Ld. Counsel filed two paper books containing pages 1 to 23 and pages 1 to 38 respectively and submitted that the assessee is engaged primarily in leasing activity for so many years and the present lease in question is also one of the operating lease. He referred to page 9 of paper book –II and submitted that the assessee purchased computer spare parts worth Rs. 40,00,000/- vide sale bill/invoice number CC/A 9304118 Dated 26.02.94 from “HCL Hewlett Packard Limited” and subsequently leased those parts to the same company for a lease period of 6 years or 72 months. According to him, the assessee received total lease rental income of Rs. 53,04,000/- for 6 years and which was offered for taxation. He

submitted that depreciation has been claimed on those assets in accordance with law. He referred to various clauses of the agreement placed on paper book pages 7-17 of PB-I to claim that it was a pure operating lease. The Ld. Counsel referred to clause (e) of miscellaneous clause of the agreement, available on page 12 of PB-I and submitted that ownership of the assets (equipment) was vested with the lessor of the equipment. The Ld. Counsel also referred to the CBDT Circular No. 2 dated 09/02/2001 to support the contention that the CBDT itself has acknowledged the existence of finance lease agreements. The Ld. Counsel referred to schedule 13 of the balance sheet and submitted that the assessee has shown lease charges income of Rs. 8,93,36,519/- during the year into consideration, which goes to prove that the assessee was engaged in business of leasing equipments. Alternatively, he submitted that in case the transaction is treated as finance transaction, then lease rental income should be adjusted against principal amount of loan.

4. The Ld. DR on the other hand, referred to the direction of the Hon'ble High Court in the matter and submitted that the agreement and other circumstantial evidences establish that the transaction in the case of the assessee was of a pure finance transaction and it was given the form of a lease transaction to avail benefit of the depreciation only. She referred to page 8 of the assessee's paper book-II, and submitted that the assessee itself bifurcated the total lease rental amount of Rs. 53,04,000/- into amount of principal of Rs. 40,00,000/- and interest amount of Rs. 13,04,000/-. She submitted that the lease period in the case of the parts claimed to be leased was of 6 years, which is totally useful life of the parts leased. According to her, all the risk and rewards of the ownership of the assets in question were with "HCL Hewlett Packard Ltd." and the lessor could be at most

treated as legal owner of the assets. She drawn our attention to warranty clause of the agreement, available on page 8 of assessee's paper book-I and submitted that the lessee has made the selection of the equipment even prior to the purchase of those equipments by the lessor. She also submitted that the in this case the lessor was not responsible for any repairs, service or defects in the equipment. According to her, in case of operating lease, the lessor is responsible for any defects in the equipments. She also submitted that as per the agreement, the equipment were to be delivered directly at the location of the lessee and in the event of the damage to the equipment in transit, the lessee was made solely responsible for all loss and damages. She submitted that in the above referred agreement even installation of equipments was made the responsibility of the lessee . She further submitted that the Special Bench of Mumbai Tribunal in the case of IndusIND bank limited in ITA No. 6566/Mum/2002 and ITA No. 606/mum/2003 for assessment year 1998-99 and 99-2000 respectively has laid down various test for examining finance lease following the decision of the Hon'ble Supreme Court in the case of Asea Brown Boveri Ltd (supra) and Association of Leasing and Financial Services companies (supra).

5. We have heard the rival submissions and perused the relevant material on record including agreement entered into between the parties in the light of the direction of the Hon'ble High Court. We find that the Hon'ble High Court has directed for examining whether the transaction is a finance transaction or operating lease transaction taking into consideration the findings of the Hon'ble Supreme Court in the cases of Asea Brown Boveri Limited (supra), Association of Leasing and Financing Service Companies (supra), Instalment Supply Private Limited(supra) , Sundaram Finance Ltd. (supra).

6. In view of the above, whether the transaction in the instant case is finance lease or operating lease transaction, we proceed to examine the lease agreement entered into on 23/02/1994 between the assessee and M/s HCL Hewlett Packard Ltd, a copy of which is available on page 7-17 of the assessee's paper book-I, and determine whether it satisfies the various condition of finance lease agreement in above decisions of the Hon'ble Supreme Court dismissed by the Hon'ble High Court as under:

(i) The asset is use specific and selected for the lessee specifically. Usually the lessee is allowed to it itself:

6.1 We find that the Ld. CIT(A) recorded the fact that items included spare parts of the computers, printers, networking and items like keyboard, RAM, logic cards, adapter cards, power supply etc, The terms of warranty under the agreement has mentioned that lessee has made selection of the equipment upon its own judgement even prior to the purchase thereof by the lessor.

(ii) Lease agreement is non-cancellable and is fixed obligation on lease:

6.20 We note that in the instant agreement, the clause on period of lease it is mentioned as under:

"The lessee shall take the Equipment for its use on lease for the terms specified in the Lease Summary Schedule hereunder written. The Lessee shall have the option to renew the lease of the Equipment for further periods as may be decided upon by the Lessee with the specific consent of the Lessor subject, however, to the proviso that such further extension of the lease period shall not have any one renewal exceed 5 years at a

time. Such periods for which the lease is renewed are hereinafter referred to as Secondary Lease Period(s). The Lessee shall pay to the Lessor lease rentals at the rate of applicable to the Secondary lease Period(s) specified in the Lease Summary Schedule herein written, the other terms and conditions for the renewed lease remaining the same as contained in this Agreement for the Secondary Lease Period(s) also.”

6.21. The lease summary schedule available on page 17 of the paper book-I, it is evident that lease rental was fixed for at least 60 months period. Further, we also note that in the miscellaneous clause of agreement available on page 12 of the paperbook, the lessee agreed that the lease agreement is non-cancellable. In the agreement, the clauses “ event of failure” and “remedy” available on page 13 and 14 of the paperbook, the lessor has only been given authority to terminate the agreement if the lessee fails to honour payment of lease rental or fail to perform other covenant of the agreement and in case of a failure on the part of the lessee and termination of the agreement, the lessor has been given the right to recover full value of the invoice price of the equipment or enter into the premises of the lessee and take immediate possession and remove the asset. The clause on page 16 of the paperbook also provide as under:

“The Agreements and Contracts executed between parties hereto pursuant to this Agreement cannot be cancelled or terminated except as expressly provided herein. The Lessee hereby agrees that Lessee’s obligations to pay all lease rentals and any other amounts owing hereunder shall be absolute and unconditional. This Agreement cannot be amended except in writing and shall be binding upon. And

to the benefit of the parties hereto, their permitted successors and assigns.”

6.22. All these terms and condition indicate that lease agreement is non-cancellable by the lessee and there’s a fixed obligation on the lessee for payment of lease rental for the entire period of the lease or value equivalent to the asset, notwithstanding that lease may be cancelled.

(iii) Lease period is fixed to sufficiently recover the cost of the asset plus interest:

6.30. The Ld. Counsel has provided the copy of submissions filed before the Assessing Officer, which is available on page 8 of the paper book-II and according to which the lease rentals for period of 6 years was worked out on the basis of the principal loan amount and interest thereon. For ready reference, said working is reproduced as under:

“Lease Rentals @ Rs. 88,400 p.m.

FINANCE GROSS

<i>AMOUNT</i>	<i>RECEIVABLE</i>	<i>PRINCIPAL</i>	<i>INTEREST</i>
<u>4000,000</u>	<u>5,304,000</u>	<u>4,000,000</u>	<u>1,304,000</u>

LEASE

<i>FIN.YEAR</i>	<i>ASST.YEAR</i>	<i>RENTALS</i>	<i>PRINCIPAL</i>	<i>INTEREST</i>
<i>1993-94</i>	<i>1994-95</i>	<i>88,400</i>	<i>66,667</i>	<i>21,733</i>
<i>1994-95</i>	<i>1995-96</i>	<i>1,060,800</i>	<i>800,000</i>	<i>260,800</i>
<i>1995-96</i>	<i>1996-97</i>	<i>1,060,800</i>	<i>800,000</i>	<i>260,800</i>
<i>1996-97</i>	<i>1997-98</i>	<i>1,060,800</i>	<i>800,000</i>	<i>260,800</i>
<i>1997-98</i>	<i>1998-99</i>	<i>1,060,800</i>	<i>800,000</i>	<i>260,800</i>
<i>1998-99</i>	<i>1999-2000</i>	<i>972,400</i>	<i>733,333</i>	<i>239,067</i>

<i>5,304,000</i>	<i>4,000,000</i>	<i>1,304,000</i>
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6.31. It is evident from the above that period of lease is equal to or very close to the economic life of the asset and the assessee recovered principal amount along with interest within the lease period of 6 years.

(iv) liability of repairs and insurance of the lessee:

6.40. The warranty clause available on page 8 of the paperbook reads as under:

“The Lessee has made the selection of the Equipment based upon its own judgment prior to the purchase thereof by the Lessor and expressly declares that it has not relied upon any statements or representations made by the Lessor. The Lessor makes no express or implied warranties including those of merchantability or fitness for particular use of the Equipment and hereby disclaimed the same. Save as otherwise provided in this Agreement, the Lessor shall not be responsible for any repairs, service or defects in the Equipment or the operation thereof.”

6.41. Further responsibility has been given to lessee to take care of the asset in transit as under:

“The Equipment hereunder leased, will be delivered by the manufacturers/suppliers to the location specified by the Lessee. The Lessor shall not be responsible for any damage incurred to the Equipment prior to or during delivery. Prior to the despatch of the Equipment, the Lessee shall ensure that transit insurance on the Equipment being despatched is provided by the supplier naming the Lessor as Loss Payee. Alternatively, the Lessee shall at its own cost obtain such

insurance naming the Lessor as Loss Payee. In the event of damage to the Equipment in transit, the Lessee shall be solely responsible for all loss and damage and rectification of such damages and shall effect payment of lease rentals on the damaged Equipment notwithstanding the costs and delays attendant to the repairs of the above. In that event, the Lessor agrees to refund any insurance claim received by the Lessor forthwith to the Lessee.”

6.42. Further the clause on “repairs loss and damage” available on page 10 of the paperbook also the responsibility has been fastened on the lessee as under:

“During the term of the lease and any renewal thereof, the Lessor shall not be called upon to keep the Equipment in good repair, condition and working order and the Lessee at its own cost and expense will keep the Equipment in good repair, condition and working order. All parts, mechanisms and devices or any replacements made by the Lessee to the Equipment shall immediately be deemed part of the Equipment for all purposes thereof and shall become the property of the Lessor, without any payment for such parts, mechanisms and devices from the Lessor.

In the event, any item of Equipment is lost, stolen or destroyed or damaged beyond repair for any reason, the Lessee shall promptly pay to the Lessor the amount of lease rentals then remaining unpaid, including any renewal options contained herein or entered into pursuant to this Agreement, whereupon Lessor will transfer to the Lessee without recourse or warranty all of the Lessor’s right, title and interest if any, in such item.

The Lessor shall, in such event, refund to the Lessee any insurance claims subsequently received by the Lessor.”

6.43. Similarly, the lessee has been made responsible for payment of insurance premium as under:

“The Lessee shall for the benefit of and on behalf of the Lessor obtain and maintain for the entire term of this Agreement at its own expense insurance against normal risks and such other risks of loss as are customarily insured against on the type of Equipment leased hereunder and by the business in which the Lessee is engaged in for such amount, provided however, that the amount of insurance against loss or damage to the Equipment shall not be less than the original cost of the Equipment. Alternatively the Lessor may insure the Equipment as aforesaid and the Lessee shall reimburse the insurance premium and other costs and expenses to the Lessor.

Each Insurance Policy will be in the joint names of the Lessor and the Lessee and note the names of the Lessor and its designated banker as Loss Payees. The Lessee shall furnish to the Lessor a Certificate of Insurance or other satisfactory evidence that such insurance coverage is in effect. All insurance premium should be borne and paid by the Lessee during the term of this Agreement. It is further agreed between the parties hereto that in the event of the Lessee not furnishing evidence of Insurance cover within a period of 30 days from the date of installation of the Equipment, the Lessor may in its absolute discretion arrange such insurance cover as may be needed. In such an event, it is agreed between the parties hereto that the cost of such insurance taken by the Lessor or

the amount of premium paid by the Lessor shall be forthwith reimbursed by the Lessee.”

6.44. Thus, it is evident that in case of loss of the asset, the insurance claim would be received by the lessor and the lessor has been guaranteed to receive the amount equivalent to the principal amount of loan.

(v) **Lessee to pay sales tax**

6.5 Under the clause “sales tax”, on page 11 of the paperbook, the lessee has undertaken to pay the lessor all sums paid or payable and demanded as the sales tax on the transaction or any part thereof.

(vi) **Risk and reward**

6.60 Risk and reward incidental to the ownership have been passed on to the lessee and the lessor only remains the legal owner of the asset:

6.61. Under the clause of manufacturers warranty, the lessee has been made to entitled to the benefit of the warranties. Similarly in case of any liability during transportation/possession operation and use of the equipment has been fastened on the lessee. The relevant indemnity clause is reproduced as under:

“The Lessee agrees to comply with all laws and regulations relating to the transportation, possession, operation and use of the Equipment and assumes all liabilities including injuries to or deaths of persons arising from or pertaining to the transportation, possession, operation or use of the Equipment. The Lessee does hereby agree to indemnify and keep indemnified and hold safe and harmless the Lessor

against all such liabilities and against loss of the Equipment by seizure by any person other than the Lessor for any reason whatsoever or resulting from any legal process instituted by any person other than the Lessor, provided that such indemnity shall not apply to such loss as has arisen or arises due to any act, lapse, fault, or other causes on the part of the Lessor. The indemnities contained in this paragraph shall survive the termination of this Agreement, in so far as they pertain to events/occurrences that transpired during the period of the lease and any renewals thereof. Any fees, taxes or other charges legally payable by the Lessee in relation to the possession and use of the Equipment and which is paid by the Lessor, in the event of the Lessee's failure to pay shall at the Lessor's option become immediately due from the Lessee to the Lessor. All breakages will be to the account of the Lessee."

7. The Ld. CIT(A) also noted that the assessee has not submitted any details on how the spare parts of computers (i.e. the assets in question) have been returned back to the assessee after expiry of the so-called lease periods.

8. Though the Ld. Counsel of the assessee referred to the CBDT circular (supra) and various decision of the Hon'ble Courts other than the decision discussed by the Hon'ble High Court while remanding the matter. We have not discussed those decisions and CBDT circular cited by the Ld. Counsel, as we have to decide the issue in dispute in the light of the direction of the Hon'ble High Court.

9. We have also from facts of case mentioned by the Hon'ble High Court in para 5 of the order dated 17.4.2012 that the assessee in its declaration under Voluntary Disclosure of Income Scheme 1997 (VDIS 1997) withdrew the claim of depreciation on the assets purchased from and leased back to Western Pacques (India) Limited and offered the depreciation for taxation. The assessee also withdrew claim of depreciation on the assets purchased from Agritech Hatchem and leased to Alpha Engineers. These transactions were treated as finance translation by the assessee itself.

10. In view of the above discussion, we can summarise in the instant case that the lease agreement is non-cancellable as far as lessee is concerned, the asset has been leased for a period 6 years, which is equal to economic life of the assets (spare parts), the lessee has been made solely responsible for bearing repair and maintenance cost, insurance premium and also sales tax etc, the assets have been selected by the lessee, the parts leased are not machinery, which could function independently. Thus, the assessee satisfy the criterion of Finance lease held in the decisions cited by the Hon'ble High Court.

11. The Hon'ble High Court has in para 16 has given example of the motor vehicles purchased by the customer through financing companies as an example of financing transactions. Similar to the insurance of motor vehicles by the customer , in the instant case also the lessee was made responsible for insuring the assets and assets remained with the lessee for the economic life of the asset. The lessee was engaged in manufacturing of the computer hardware and the leased spare parts, were in the nature of the raw material to be consumed in the manufacturing process of the lessee. Thus buying of the very same product from the lessee and again giving back to the

lessee of those products on lease, does not support the contention of the operating lease by the assessee.

12. Accordingly, we hold the transaction of purchasing the computer parts from HCL Hewlett Packard Limited for Rs. 40.00 lacs and leasing the same back as financial transaction and consequently the depreciation claimed on the assets is liable to disallowed.

13. In the result, the appeal of the assessee is dismissed.

This decision was pronounced in the Open Court on 19th December, 2018.

sd/-
(H.S. SIDHU)
JUDICIAL MEMBER

sd/-
(O.P. KANT)
ACCOUNTANT MEMBER

Dated: 19/12/2018

Veena

Copy forwarded to

1. Applicant
2. Respondent
3. CIT
4. CIT (A)
5. DR:ITAT

ASSISTANT REGISTRAR
ITAT, New Delhi