

**IN THE INCOME TAX APPELLATE TRIBUNAL  
DELHI BENCH 'B', NEW DELHI**

**Before Dr. B. R. R. Kumar, Accountant Member  
Sh. Yogesh Kumar US, Judicial Member**

**ITA No. 2443/Del/2019 : Asstt. Year : 2015-16**

|                                                                        |    |                                                |
|------------------------------------------------------------------------|----|------------------------------------------------|
| Claridge Hotels Pvt. Ltd.,<br>12, Aurangzeb Road,<br>New Delhi-1100011 | Vs | DCIT,<br>Central Circle-3,<br>New Delhi-110055 |
| <b>(APPELLANT)</b>                                                     |    | <b>(RESPONDENT)</b>                            |
| <b>PAN No. AAACC0022B</b>                                              |    |                                                |

**Assessee by : Sh. Gaurav Jain, Adv. &  
Sh. Sanket Gupta, CA  
Revenue by : Sh. Mahesh Shah, CIT DR**

**Date of Hearing: 25.05.2022**

**Date of Pronouncement: 27.06.2022**

**ORDER**

**Per Dr. B. R. R. Kumar, Accountant Member:**

The present appeal has been filed by the assessee against the order of the Id. CIT(A)-23, New Delhi, dated 26.02.2019.

2. In ITA No. 2443/Del/2019, following grounds have been raised by the assessee:

*"1. That on the facts and circumstances of the case and in law, the order dated 26.02.2019 passed by the Learned Commissioner of Income tax Appeals ("Ld. CIT(A)") is erroneous and bad in law.*

*2. The Ld. CIT (A) has erred on facts and in law in confirming the total income at Rs. 3,39,51,476/- as against the returned loss of Rs. 3,84,00,967 by confirming the disallowance-of Rs. 44,49,491 made by the Learned Assessing Officer ("Ld. AO") despite the fact that the Assessee has provided all documents and evidences to support his claim.*

3. *The Ld. CIT(A) has erred on facts and in law by confirming the action of the Ld. AO in making disallowance of Rs. 828,000 on account of lease equalization charges despite that fact that the Assessee has followed Accounting Standard -19 issued by ICAI and has submitted all documents in support of the claim.*

3.1 *Without prejudice to the above, the Ld. CIT(A) has erred on facts and in law in appreciating that the Assessee can be charged only on real income which can be calculated after applying the prescribed method.*

4. *The Ld. CIT(A) has erred on facts and in law by confirming the action of the Ld. AO in making disallowance of Rs. 36,21,491 on account of logo development expenses by treating them as capital in nature and disregarding the fact that the expenses are revenue in nature and incurred wholly and exclusively for the purpose of business.*

4.1 *Without prejudice to the above, the Ld. CIT(A) has erred on facts and in law in confirming the disallowance despite the fact that the contract was terminated mid way and the new logo was not delivered and no intangible asset alleged by the Ld. AO came into existence and the Assessee has submitted all documents in support of the claim.*

4.2 *The Ld. CIT(A) has erred on facts and in law by confirming the action of the Ld. AO without appreciating the fact that the expenses incurred are in nature of normal advertisement expenses and hence revenue in nature.*

4.3 *The Ld. CIT(A) has erred on facts and in law by confirming the action of the Ld. AO without appreciating the fact that the Ld. AO failed to issue show cause notice in respect of the addition.*

5. *That on the facts and circumstances of the case and in law, the Ld. CIT (A) has erred in law in summarily rejecting the additional evidence filed by*

*the Assessee under Rule 46A of the Income-tax rules, 1962 and has violated the principle laid down in Rule 46A.*

*6. The Ld. CIT(A) has erred on facts and in law by confirming the action of the Ld. AO in not granted adequate opportunity of being heard to the appellant and thereby violated the principles of audi alteram partem.*

*7. The Ld. CIT(A) has erred on facts and in law in relying upon various judicial decisions against the assessee which are unconnected and irrelevant and are distinguishable upon facts and in law.*

*8. That the grounds of appeal are independent and without prejudice to each other."*

### **Lease Equalization Charges:**

3. The entire part of the Assessment Order pertaining to this issue is as under:

*"2.1 On examination of books of accounts of the assessee and documents submitted during the course of scrutiny assessment proceedings, it was noticed that the assessee has made a 'Provision for rent of Rs. 8,28,000/-. The Assessee/AR was confronted about the same vide order sheet noting dt. 06.11.2017 and asked why such provision, which is not allowable for deduction under Income Tax Act, 1961 be not added back to the final computation of income. AR couldn't offer any satisfactory reply and submitted that they have created this provision and treated it in its books of accounts as Rent Equalization Reserve'. The submission of the assessee/AR is being perused and examined and not found in-sync with the provisions of the Income Tax Act. Accordingly, Rs. 8,28,000/- is being added back to the total income of the assessee."*

4. The Id. CIT(A) confirmed the addition invoking the provisions of Section 30 of the Income Tax Act, 1961 and held that no other deduction except as allowed u/s 30 be claimed. The Id. CIT(A) has also held that the judgment of the Hon'ble Apex Court was in terms of finance lease and not applicable to the facts of the instant case.

5. Aggrieved the assessee filed appeal before us.

6. Heard the arguments of both the parties and perused the material available on record.

7. The assessee entered into an agreement of granting lease hold right and determined the annual rent payable by the assessee to the lessee which is as under:

- a. For the period commencing from April 1<sup>st</sup> 2013 till March 31<sup>st</sup> 2016 shall be Rs.7,20,000/- (Rupees Seven Lakhs Twenty Thousand Only) per annum.
- b. For the period commencing from April 1<sup>st</sup> 2016 to March 31<sup>st</sup> 2021, shall be Rs.18,00,000/- (Rupees Eighteen Lakhs Only) per annum and
- c. For the period commencing from April 1<sup>st</sup> 2016 to March 31<sup>st</sup> 2023, shall be Rs.21,60,000/- (Rupees Twentry One Lakhs Sixty Thousand Only) per annum

8. The cumulative rent per year over the lease period of 10 years is Rs.154,80,000/- i.e. 15,48,000/- per year. For the period from 2013 to 2016, the assessee claims deduction of Rs.15,48,000/- which is more than Rs.7,20,000/- whereas the subsequent period, the assessee would be claiming deduction of

only Rs.15,48,000/- against the payment of Rs.18,00,000/- and Rs.21,60,000/-. Thus, the question before us is whether the assessee is allowed to claim uniform deduction over the period of 10 years on the entire rent payable cumulatively or only the rent which is paid on annual basis.

9. For this purpose, we have gone through the Accounting Standard 19, Provisions of Section 145, Provisions of Section 129 & Section 133 of Companies Act, 2013, notification issued by Central Government Companies (Accounting Standards) Rules, 2016, extracts of notification issued by Central Government, ruling of Hon'ble High Court of Andhra Pradesh & Telangana, ruling of Hon'ble Supreme Court of India.

## Accounting Standard (AS) 19

### Leases\*

*(This Accounting Standard includes paragraphs set in **bold italic** type and plain type, which have equal authority. Paragraphs in bold italic type indicate the main principles. This Accounting Standard should be read in the context of its objective and the General Instructions contained in part A of the Annexure to the Notification.)*

### Objective

The objective of this Standard is to prescribe, for lessees and lessors, the appropriate accounting policies and disclosures in relation to finance leases and operating leases.

### Scope

**1. This Standard should be applied in accounting for all leases other than:**

- (a) lease agreements to explore for or use natural resources, such as oil, gas, timber, metals and other mineral rights; and***
- (b) licensing agreements for items such as motion picture films, video recordings, plays, manuscripts, patents and copyrights; and***
- (c) lease agreements to use lands.***

2. This Standard applies to agreements that transfer the right to use assets even though substantial services by the lessor may be called for in connection with the operation or maintenance of such assets. On the other hand, this Standard does not apply to agreements that are contracts for services that do not transfer the right to use assets from one contracting party to the other.

\* In respect of assets leased prior to the effective date of the notification prescribing this Standard under Section 211 of the Companies Act, 1956, the applicability of this Standard would be determined on the basis of the Accounting Standard (AS) 19, issued by the ICAI in 2001.

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## Definitions

3. The following terms are used in this Standard with the meanings specified:

- 3.1 A lease is an agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time.
- 3.2 A finance lease is a lease that transfers substantially all the risks and rewards incident to ownership of an asset.
- 3.3 An operating lease is a lease other than a finance lease.
- 3.4 A non-cancellable lease is a lease that is cancellable only:
- (a) upon the occurrence of some remote contingency; or
  - (b) with the permission of the lessor; or
  - (c) if the lessee enters into a new lease for the same or an equivalent asset with the same lessor; or
  - (d) upon payment by the lessee of an additional amount such that, at inception, continuation of the lease is reasonably certain.
- 3.5 The inception of the lease is the earlier of the date of the lease agreement and the date of a commitment by the parties to the principal provisions of the lease.
- 3.6 The lease term is the non-cancellable period for which the lessee has agreed to take on lease the asset together with any further periods for which the lessee has the option to continue the lease of the asset, with or without further payment, which option at the inception of the lease it is reasonably certain that the lessee will exercise.
- 3.7 Minimum lease payments are the payments over the lease term that the lessee is, or can be required, to make excluding contingent rent, costs for services and taxes to be paid by and reimbursed to the lessor, together with:

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- (a) *in the case of the lessee, any residual value guaranteed by or on behalf of the lessee; or*
- (b) *in the case of the lessor, any residual value guaranteed to the lessor:*
  - (i) *by or on behalf of the lessee; or*
  - (ii) *by an independent third party financially capable of meeting this guarantee.*

*However, if the lessee has an option to purchase the asset at a price which is expected to be sufficiently lower than the fair value at the date the option becomes exercisable that, at the inception of the lease, is reasonably certain to be exercised, the minimum lease payments comprise minimum payments payable over the lease term and the payment required to exercise this purchase option.*

**3.8** *Fair value is the amount for which an asset could be exchanged or a liability settled between knowledgeable, willing parties in an arm's length transaction.*

**3.9** *Economic life is either:*

- (a) *the period over which an asset is expected to be economically usable by one or more users; or*
- (b) *the number of production or similar units expected to be obtained from the asset by one or more users.*

**3.10** *Useful life of a leased asset is either:*

- (a) *the period over which the leased asset is expected to be used by the lessee; or*
- (b) *the number of production or similar units expected to be obtained from the use of the asset by the lessee.*

**3.11** *Residual value of a leased asset is the estimated fair value of the asset at the end of the lease term.*

**3.12** *Guaranteed residual value is:*

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- (a) *in the case of the lessee, that part of the residual value which is guaranteed by the lessee or by a party on behalf of the lessee (the amount of the guarantee being the maximum amount that could, in any event, become payable); and*
  - (b) *in the case of the lessor, that part of the residual value which is guaranteed by or on behalf of the lessee, or by an independent third party who is financially capable of discharging the obligations under the guarantee.*
- 3.13 *Unguaranteed residual value* *of a leased asset is the amount by which the residual value of the asset exceeds its guaranteed residual value.*
- 3.14 *Gross investment in the lease* *is the aggregate of the minimum lease payments under a finance lease from the standpoint of the lessor and any unguaranteed residual value accruing to the lessor.*
- 3.15 *Unearned finance income* *is the difference between:*
  - (a) *the gross investment in the lease; and*
  - (b) *the present value of*
    - (i) *the minimum lease payments under a finance lease from the standpoint of the lessor; and*
    - (ii) *any unguaranteed residual value accruing to the lessor,**at the interest rate implicit in the lease.*
- 3.16 *Net investment in the lease* *is the gross investment in the lease less unearned finance income.*
- 3.17 *The interest rate implicit in the lease* *is the discount rate that, at the inception of the lease, causes the aggregate present value of*
  - (a) *the minimum lease payments under a finance lease from the standpoint of the lessor; and*
  - (b) *any unguaranteed residual value accruing to the lessor,*

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*to be equal to the fair value of the leased asset.*

**3.18** *The lessee's incremental borrowing rate of interest is the rate of interest the lessee would have to pay on a similar lease or, if that is not determinable, the rate that, at the inception of the lease, the lessee would incur to borrow over a similar term, and with a similar security, the funds necessary to purchase the asset.*

**3.19** *Contingent rent is that portion of the lease payments that is not fixed in amount but is based on a factor other than just the passage of time (e.g., percentage of sales, amount of usage, price indices, market rates of interest).*

4. The definition of a lease includes agreements for the hire of an asset which contain a provision giving the hirer an option to acquire title to the asset upon the fulfillment of agreed conditions. These agreements are commonly known as hire purchase agreements. Hire purchase agreements include agreements under which the property in the asset is to pass to the hirer on the payment of the last instalment and the hirer has a right to terminate the agreement at any time before the property so passes.

### **Classification of Leases**

5. The classification of leases adopted in this Standard is based on the extent to which risks and rewards incident to ownership of a leased asset lie with the lessor or the lessee. Risks include the possibilities of losses from idle capacity or technological obsolescence and of variations in return due to changing economic conditions. Rewards may be represented by the expectation of profitable operation over the economic life of the asset and of gain from appreciation in value or realisation of residual value.

6. A lease is classified as a finance lease if it transfers substantially all the risks and rewards incident to ownership. Title may or may not eventually be transferred. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incident to ownership.

7. Since the transaction between a lessor and a lessee is based on a lease agreement common to both parties, it is appropriate to use consistent definitions. The application of these definitions to the differing circumstances of the two parties may sometimes result in the same lease being classified differently by the lessor and the lessee.

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8. Whether a lease is a finance lease or an operating lease depends on the substance of the transaction rather than its form. Examples of situations which would normally lead to a lease being classified as a finance lease are:

- (a) the lease transfers ownership of the asset to the lessee by the end of the lease term;
- (b) the lessee has the option to purchase the asset at a price which is expected to be sufficiently lower than the fair value at the date the option becomes exercisable such that, at the inception of the lease, it is reasonably certain that the option will be exercised;
- (c) the lease term is for the major part of the economic life of the asset even if title is not transferred;
- (d) at the inception of the lease the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset; and
- (e) the leased asset is of a specialised nature such that only the lessee can use it without major modifications being made.

9. Indicators of situations which individually or in combination could also lead to a lease being classified as a finance lease are:

- (a) if the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee;
- (b) gains or losses from the fluctuation in the fair value of the residual fall to the lessee (for example in the form of a rent rebate equalling most of the sales proceeds at the end of the lease); and
- (c) the lessee can continue the lease for a secondary period at a rent which is substantially lower than market rent.

10. Lease classification is made at the inception of the lease. If at any time the lessee and the lessor agree to change the provisions of the lease, other than by renewing the lease, in a manner that would have resulted in a different classification of the lease under the criteria in paragraphs 5 to 9 had the changed terms been in effect at the inception of the lease, the revised agreement is considered as a new agreement over its revised term. Changes in estimates (for example, changes in estimates of the economic life or of the residual value of the leased asset) or changes in circumstances

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(for example, default by the lessee), however, do not give rise to a new classification of a lease for accounting purposes.

## Leases in the Financial Statements of Lessees

### Finance Leases

*11. At the inception of a finance lease, the lessee should recognise the lease as an asset and a liability. Such recognition should be at an amount equal to the fair value of the leased asset at the inception of the lease. However, if the fair value of the leased asset exceeds the present value of the minimum lease payments from the standpoint of the lessee, the amount recorded as an asset and a liability should be the present value of the minimum lease payments from the standpoint of the lessee. In calculating the present value of the minimum lease payments the discount rate is the interest rate implicit in the lease, if this is practicable to determine; if not, the lessee's incremental borrowing rate should be used.*

#### Example

- (a) An enterprise (the lessee) acquires a machinery on lease from a leasing company (the lessor) on January 1, 20X0. The lease term covers the entire economic life of the machinery, i.e., 3 years. The fair value of the machinery on January 1, 20X0 is Rs.2,35,500. The lease agreement requires the lessee to pay an amount of Rs.1,00,000 per year beginning December 31, 20X0. The lessee has guaranteed a residual value of Rs.17,000 on December 31, 20X2 to the lessor. The lessor, however, estimates that the machinery would have a salvage value of only Rs.3,500 on December 31, 20X2.

The interest rate implicit in the lease is 16 per cent (approx.). This is calculated using the following formula:

$$\text{Fair value} = \frac{\text{ALR}}{(1+r)^1} + \frac{\text{ALR}}{(1+r)^2} + \dots + \frac{\text{ALR}}{(1+r)^n} + \frac{\text{RV}}{(1+r)^n}$$

where ALR is annual lease rental,  
RV is residual value (both guaranteed and unguaranteed),

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| <p>n is the lease term,<br/>r is interest rate implicit in the lease.<br/>The present value of minimum lease payments from the stand point of the lessee is Rs.2,35,500.</p> <p>The lessee would record the machinery as an asset at Rs.2,35,500 with a corresponding liability representing the present value of lease payments over the lease term (including the guaranteed residual value).</p> <p>(b) In the above example, suppose the lessor estimates that the machinery would have a salvage value of Rs.17,000 on December 31, 20X2. The lessee, however, guarantees a residual value of Rs.5,000 only.</p> <p>The interest rate implicit in the lease in this case would remain unchanged at 16% (approx.). The present value of the minimum lease payments from the standpoint of the lessee, using this interest rate implicit in the lease, would be Rs.2,27,805. As this amount is lower than the fair value of the leased asset (Rs. 2,35,500), the lessee would recognise the asset and the liability arising from the lease at Rs.2,27,805.</p> <p>In case the interest rate implicit in the lease is not known to the lessee, the present value of the minimum lease payments from the standpoint of the lessee would be computed using the lessee's incremental borrowing rate.</p> |
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12. Transactions and other events are accounted for and presented in accordance with their substance and financial reality and not merely with their legal form. While the legal form of a lease agreement is that the lessee may acquire no legal title to the leased asset, in the case of finance leases the substance and financial reality are that the lessee acquires the economic benefits of the use of the leased asset for the major part of its economic life in return for entering into an obligation to pay for that right an amount approximating to the fair value of the asset and the related finance charge.

13. If such lease transactions are not reflected in the lessee's balance sheet, the economic resources and the level of obligations of an enterprise are understated thereby distorting financial ratios. It is therefore

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appropriate that a finance lease be recognised in the lessee's balance sheet both as an asset and as an obligation to pay future lease payments. At the inception of the lease, the asset and the liability for the future lease payments are recognised in the balance sheet at the same amounts.

14. It is not appropriate to present the liability for a leased asset as a deduction from the leased asset in the financial statements. The liability for a leased asset should be presented separately in the balance sheet as a current liability or a long-term liability as the case may be.

15. Initial direct costs are often incurred in connection with specific leasing activities, as in negotiating and securing leasing arrangements. The costs identified as directly attributable to activities performed by the lessee for a finance lease are included as part of the amount recognised as an asset under the lease.

**16. Lease payments should be apportioned between the finance charge and the reduction of the outstanding liability. The finance charge should be allocated to periods during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.**

| <b>Example</b>                                                                                                                                                                            |                             |                      |                                                 |                                    |  |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------|----------------------|-------------------------------------------------|------------------------------------|--|
| In the example (a) illustrating paragraph 11, the lease payments would be apportioned by the lessee between the finance charge and the reduction of the outstanding liability as follows: |                             |                      |                                                 |                                    |  |
| <i>Year</i>                                                                                                                                                                               | <i>Finance charge (Rs.)</i> | <i>Payment (Rs.)</i> | <i>Reduction in outstanding liability (Rs.)</i> | <i>Outstanding liability (Rs.)</i> |  |
| Year 1 (January 1)                                                                                                                                                                        |                             |                      |                                                 | 2,35,500                           |  |
| (December 31)                                                                                                                                                                             | 37,680                      | 1,00,000             | 62,320                                          | 1,73,180                           |  |
| Year 2 (December 31)                                                                                                                                                                      | 27,709                      | 1,00,000             | 72,291                                          | 1,00,889                           |  |
| Year 3 (December 31)                                                                                                                                                                      | 16,142                      | 1,00,000             | 83,858                                          | 17,031*                            |  |

17. In practice, in allocating the finance charge to periods during the lease term, some form of approximation may be used to simplify the calculation.

\* The difference between this figure and guaranteed residual value (Rs.17,000) is due to approximation in computing the interest rate implicit in the lease.

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**18. A finance lease gives rise to a depreciation expense for the asset as well as a finance expense for each accounting period. The depreciation policy for a leased asset should be consistent with that for depreciable assets which are owned, and the depreciation recognised should be calculated on the basis set out in Accounting Standard (AS) 6, Depreciation Accounting. If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset should be fully depreciated over the lease term or its useful life, whichever is shorter.**

19. The depreciable amount of a leased asset is allocated to each accounting period during the period of expected use on a systematic basis consistent with the depreciation policy the lessee adopts for depreciable assets that are owned. If there is reasonable certainty that the lessee will obtain ownership by the end of the lease term, the period of expected use is the useful life of the asset; otherwise the asset is depreciated over the lease term or its useful life, whichever is shorter.

20. The sum of the depreciation expense for the asset and the finance expense for the period is rarely the same as the lease payments payable for the period, and it is, therefore, inappropriate simply to recognise the lease payments payable as an expense in the statement of profit and loss. Accordingly, the asset and the related liability are unlikely to be equal in amount after the inception of the lease.

21. To determine whether a leased asset has become impaired, an enterprise applies the Accounting Standard dealing with impairment of assets<sup>1</sup>, that sets out the requirements as to how an enterprise should perform the review of the carrying amount of an asset, how it should determine the recoverable amount of an asset and when it should recognise, or reverse, an impairment loss.

**22. The lessee should, in addition to the requirements of AS 10, Accounting for Fixed Assets, AS 6, Depreciation Accounting, and the governing statute, make the following disclosures for finance leases:**

**(a) assets acquired under finance lease as segregated from the assets owned;**

<sup>1</sup> Accounting Standard (AS) 28, 'Impairment of Assets', specifies the requirements relating to impairment of assets.

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- (b) *for each class of assets, the net carrying amount at the balance sheet date;*
- (c) *a reconciliation between the total of minimum lease payments at the balance sheet date and their present value. In addition, an enterprise should disclose the total of minimum lease payments at the balance sheet date, and their present value, for each of the following periods:*
  - (i) *not later than one year;*
  - (ii) *later than one year and not later than five years;*
  - (iii) *later than five years;*
- (d) *contingent rents recognised as expense in the statement of profit and loss for the period;*
- (e) *the total of future minimum sublease payments expected to be received under non-cancellable subleases at the balance sheet date; and*
- (f) *a general description of the lessee's significant leasing arrangements including, but not limited to, the following:*
  - (i) *the basis on which contingent rent payments are determined;*
  - (ii) *the existence and terms of renewal or purchase options and escalation clauses; and*
  - (iii) *restrictions imposed by lease arrangements, such as those concerning dividends, additional debt, and further leasing.*

*Provided that a Small and Medium Sized Company, as defined in the Notification, may not comply with sub-paragraphs (c), (e) and (f).*

### **Operating Leases**

**23. Lease payments under an operating lease should be recognised**

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*as an expense in the statement of profit and loss on a straight line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.*

24. For operating leases, lease payments (excluding costs for services such as insurance and maintenance) are recognised as an expense in the statement of profit and loss on a straight line basis unless another systematic basis is more representative of the time pattern of the user's benefit, even if the payments are not on that basis.

25. *The lessee should make the following disclosures for operating leases:*

- (a) *the total of future minimum lease payments under non-cancellable operating leases for each of the following periods:*
  - (i) *not later than one year;*
  - (ii) *later than one year and not later than five years;*
  - (iii) *later than five years;*
- (b) *the total of future minimum sublease payments expected to be received under non-cancellable subleases at the balance sheet date;*
- (c) *lease payments recognised in the statement of profit and loss for the period, with separate amounts for minimum lease payments and contingent rents;*
- (d) *sub-lease payments received (or receivable) recognised in the statement of profit and loss for the period;*
- (e) *a general description of the lessee's significant leasing arrangements including, but not limited to, the following:*
  - (i) *the basis on which contingent rent payments are determined;*
  - (ii) *the existence and terms of renewal or purchase options and escalation clauses; and*
  - (iii) *restrictions imposed by lease arrangements, such as those concerning dividends, additional debt, and further leasing.*

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*Provided that a Small and Medium Sized Company, as defined in the Notification, may not comply with sub-paragraphs (a), (b) and (e).*

## **Leases in the Financial Statements of Lessors**

### **Finance Leases**

**26.** *The lessor should recognise assets given under a finance lease in its balance sheet as a receivable at an amount equal to the net investment in the lease.*

27. Under a finance lease substantially all the risks and rewards incident to legal ownership are transferred by the lessor, and thus the lease payment receivable is treated by the lessor as repayment of principal, i.e., net investment in the lease, and finance income to reimburse and reward the lessor for its investment and services.

**28.** *The recognition of finance income should be based on a pattern reflecting a constant periodic rate of return on the net investment of the lessor outstanding in respect of the finance lease.*

29. A lessor aims to allocate finance income over the lease term on a systematic and rational basis. This income allocation is based on a pattern reflecting a constant periodic return on the net investment of the lessor outstanding in respect of the finance lease. Lease payments relating to the accounting period, excluding costs for services, are reduced from both the principal and the unearned finance income.

30. Estimated unguaranteed residual values used in computing the lessor's gross investment in a lease are reviewed regularly. If there has been a reduction in the estimated unguaranteed residual value, the income allocation over the remaining lease term is revised and any reduction in respect of amounts already accrued is recognised immediately. An upward adjustment of the estimated residual value is not made.

31. Initial direct costs, such as commissions and legal fees, are often incurred by lessors in negotiating and arranging a lease. For finance leases, these initial direct costs are incurred to produce finance income and are either recognised immediately in the statement of profit and loss or allocated against the finance income over the lease term.

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**32. The manufacturer or dealer lessor should recognise the transaction of sale in the statement of profit and loss for the period, in accordance with the policy followed by the enterprise for outright sales. If artificially low rates of interest are quoted, profit on sale should be restricted to that which would apply if a commercial rate of interest were charged. Initial direct costs should be recognised as an expense in the statement of profit and loss at the inception of the lease.**

33. Manufacturers or dealers may offer to customers the choice of either buying or leasing an asset. A finance lease of an asset by a manufacturer or dealer lessor gives rise to two types of income:

- (a) the profit or loss equivalent to the profit or loss resulting from an outright sale of the asset being leased, at normal selling prices, reflecting any applicable volume or trade discounts; and
- (b) the finance income over the lease term.

34. The sales revenue recorded at the commencement of a finance lease term by a manufacturer or dealer lessor is the fair value of the asset. However, if the present value of the minimum lease payments accruing to the lessor computed at a commercial rate of interest is lower than the fair value, the amount recorded as sales revenue is the present value so computed. The cost of sale recognised at the commencement of the lease term is the cost, or carrying amount if different, of the leased asset less the present value of the unguaranteed residual value. The difference between the sales revenue and the cost of sale is the selling profit, which is recognised in accordance with the policy followed by the enterprise for sales.

35. Manufacturer or dealer lessors sometimes quote artificially low rates of interest in order to attract customers. The use of such a rate would result in an excessive portion of the total income from the transaction being recognised at the time of sale. If artificially low rates of interest are quoted, selling profit would be restricted to that which would apply if a commercial rate of interest were charged.

36. Initial direct costs are recognised as an expense at the commencement of the lease term because they are mainly related to earning the manufacturer's or dealer's selling profit.

**37. The lessor should make the following disclosures for finance leases:**

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- (a) *a reconciliation between the total gross investment in the lease at the balance sheet date, and the present value of minimum lease payments receivable at the balance sheet date. In addition, an enterprise should disclose the total gross investment in the lease and the present value of minimum lease payments receivable at the balance sheet date, for each of the following periods:*
- (i) *not later than one year;*
  - (ii) *later than one year and not later than five years;*
  - (iii) *later than five years;*
- (b) *unearned finance income;*
- (c) *the unguaranteed residual values accruing to the benefit of the lessor;*
- (d) *the accumulated provision for uncollectible minimum lease payments receivable;*
- (e) *contingent rents recognised in the statement of profit and loss for the period;*
- (f) *a general description of the significant leasing arrangements of the lessor; and*
- (g) *accounting policy adopted in respect of initial direct costs.*

*Provided that a Small and Medium Sized Company, as defined in the Notification, may not comply with sub-paragraphs (a) and (f).*

38. As an indicator of growth it is often useful to also disclose the gross investment less unearned income in new business added during the accounting period, after deducting the relevant amounts for cancelled leases.

### **Operating Leases**

39. *The lessor should present an asset given under operating lease in its balance sheet under fixed assets.*

40. *Lease income from operating leases should be recognised in the statement of profit and loss on a straight line basis over the lease term,*

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***unless another systematic basis is more representative of the time pattern in which benefit derived from the use of the leased asset is diminished.***

41. Costs, including depreciation, incurred in earning the lease income are recognised as an expense. Lease income (excluding receipts for services provided such as insurance and maintenance) is recognised in the statement of profit and loss on a straight line basis over the lease term even if the receipts are not on such a basis, unless another systematic basis is more representative of the time pattern in which benefit derived from the use of the leased asset is diminished.

42. Initial direct costs incurred specifically to earn revenues from an operating lease are either deferred and allocated to income over the lease term in proportion to the recognition of rent income, or are recognised as an expense in the statement of profit and loss in the period in which they are incurred.

***43. The depreciation of leased assets should be on a basis consistent with the normal depreciation policy of the lessor for similar assets, and the depreciation charge should be calculated on the basis set out in AS 6, Depreciation Accounting.***

44. To determine whether a leased asset has become impaired, an enterprise applies the Accounting Standard dealing with impairment of assets<sup>2</sup> that sets out the requirements for how an enterprise should perform the review of the carrying amount of an asset, how it should determine the recoverable amount of an asset and when it should recognise, or reverse, an impairment loss.

45. A manufacturer or dealer lessor does not recognise any selling profit on entering into an operating lease because it is not the equivalent of a sale.

***46. The lessor should, in addition to the requirements of AS 6, Depreciation Accounting and AS 10, Accounting for Fixed Assets, and the governing statute, make the following disclosures for operating leases:***

***(a) for each class of assets, the gross carrying amount, the***

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<sup>2</sup> Accounting Standard (AS) 28, 'Impairment of Assets', specifies the requirements relating to impairment of assets.

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*accumulated depreciation and accumulated impairment losses at the balance sheet date; and*

- (i) the depreciation recognised in the statement of profit and loss for the period;*
- (ii) impairment losses recognised in the statement of profit and loss for the period;*
- (iii) impairment losses reversed in the statement of profit and loss for the period;*
- (b) the future minimum lease payments under non-cancellable operating leases in the aggregate and for each of the following periods:*
  - (i) not later than one year;*
  - (ii) later than one year and not later than five years;*
  - (iii) later than five years;*
- (c) total contingent rents recognised as income in the statement of profit and loss for the period;*
- (d) a general description of the lessor's significant leasing arrangements; and*
- (e) accounting policy adopted in respect of initial direct costs.*

*Provided that a Small and Medium Sized Company, as defined in the Notification, may not comply with sub-paragraphs (b) and (d).*

### **Sale and Leaseback Transactions**

47. A sale and leaseback transaction involves the sale of an asset by the vendor and the leasing of the same asset back to the vendor. The lease payments and the sale price are usually interdependent as they are negotiated as a package. The accounting treatment of a sale and leaseback transaction depends upon the type of lease involved.

48. *If a sale and leaseback transaction results in a finance lease, any excess or deficiency of sales proceeds over the carrying amount should not be immediately recognised as income or loss in the financial*

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*statements of a seller-lessee. Instead, it should be deferred and amortised over the lease term in proportion to the depreciation of the leased asset.*

49. If the leaseback is a finance lease, it is not appropriate to regard an excess of sales proceeds over the carrying amount as income. Such excess is deferred and amortised over the lease term in proportion to the depreciation of the leased asset. Similarly, it is not appropriate to regard a deficiency as loss. Such deficiency is deferred and amortised over the lease term.

*50. If a sale and leaseback transaction results in an operating lease, and it is clear that the transaction is established at fair value, any profit or loss should be recognised immediately. If the sale price is below fair value, any profit or loss should be recognised immediately except that, if the loss is compensated by future lease payments at below market price, it should be deferred and amortised in proportion to the lease payments over the period for which the asset is expected to be used. If the sale price is above fair value, the excess over fair value should be deferred and amortised over the period for which the asset is expected to be used.*

51. If the leaseback is an operating lease, and the lease payments and the sale price are established at fair value, there has in effect been a normal sale transaction and any profit or loss is recognised immediately.

*52. For operating leases, if the fair value at the time of a sale and leaseback transaction is less than the carrying amount of the asset, a loss equal to the amount of the difference between the carrying amount and fair value should be recognised immediately.*

53. For finance leases, no such adjustment is necessary unless there has been an impairment in value, in which case the carrying amount is reduced to recoverable amount in accordance with the Accounting Standard dealing with impairment of assets.

54. Disclosure requirements for lessees and lessors apply equally to sale and leaseback transactions. The required description of the significant leasing arrangements leads to disclosure of unique or unusual provisions of the agreement or terms of the sale and leaseback transactions.

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55. Sale and leaseback transactions may meet the separate disclosure criteria set out in paragraph 12 of Accounting Standard (AS) 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies.

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**Illustration****Sale and Leaseback Transactions that Result in Operating Leases**

*The illustration does not form part of the accounting standard. Its purpose is to illustrate the application of the accounting standard.*

A sale and leaseback transaction that results in an operating lease may give rise to profit or a loss, the determination and treatment of which depends on the leased asset's carrying amount, fair value and selling price. The following table shows the requirements of the accounting standard in various circumstances.

| Sale price established at fair value (paragraph 50) | Carrying amount equal to fair value | Carrying amount less than fair value | Carrying amount above fair value |
|-----------------------------------------------------|-------------------------------------|--------------------------------------|----------------------------------|
| Profit                                              | No profit                           | Recognise profit immediately         | Not applicable                   |
| Loss                                                | No loss                             | Not applicable                       | Recognise loss immediately       |

| Sale price below fair value (paragraph 50)                          |                            |                              |                    |
|---------------------------------------------------------------------|----------------------------|------------------------------|--------------------|
| Profit                                                              | No profit                  | Recognise profit immediately | No profit (note 1) |
| Loss not compensated by future lease payments at below market price | Recognise loss immediately | Recognise loss immediately   | (note 1)           |
| Loss compensated by future lease payments at below market price     | Defer and amortise loss    | Defer and amortise loss      | (note 1)           |

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|                                                   |                           |                           |                                    |
|---------------------------------------------------|---------------------------|---------------------------|------------------------------------|
| <b>Sale price above fair value (paragraph 50)</b> |                           |                           |                                    |
| <b>Profit</b>                                     | Defer and amortise profit | Defer and amortise profit | Defer and amortise profit (note 2) |
| <b>Loss</b>                                       | No loss                   | No loss                   | (note 1)                           |

Note 1. These parts of the table represent circumstances that would have been dealt with under paragraph 52 of the Standard. Paragraph 52 requires the carrying amount of an asset to be written down to fair value where it is subject to a sale and leaseback.

Note 2. The profit would be the difference between fair value and sale price as the carrying amount would have been written down to fair value in accordance with paragraph 52.

10. Section 145(2) of the Income Tax Act, 1961 reads that the Central Government may notify in the Official Gazette from time to time income computation and disclosure standards to be followed by any class of assessee or in respect of any class of income.

11. Provisions of Section 129 of the Companies Act indicates that the financial statement shall give a true and fair view of the state of affairs of the company or companies, comply with the accounting standards notified under section 133 of the Companies Act and shall be in the form or forms as may be provided for different class or classes of companies in Schedule III:

Provided that the items contained in such financial statements shall be in accordance with the accounting standards:

Section 133 of the Companies Act indicate that the Central government may prescribe the standards of accounting or any addendum thereto, as recommended by the Institute of Chartered Accountants of India, constituted under section 3 of the Chartered Accountants Act, 1949 (38 of 1949), in consultation with and after examination of the recommendations made by the National Financial Reporting Authority.

12. Ministry of Corporate Affairs vide notification dated 07.12.2006 notified the Accounting Standards specified in the Rule 3 of Companies Act in consultation with National Advisory Committee on Accounting Standards as prescribed Accounting Standards 1 to 7 and 9 to 29 for the purpose of maintenance of account as per the Companies Act.

13. The lease equalization charge is bifurcation of lease rentals in order to arrive at real income. The assessee has claimed the deduction of lease equalization charges as per Accounting Standard 19 issued by the ICAI, a recognized body vested with the authority to recommend accounting standards for ultimate prescription by the Central Government in consultation with the National Advisory Committee of Accounting Standards for the presentation of true and fair view of financial statements. Para 23 of the Accounting Standard 19 specifies the treatment of operating lease payments in the statement of profit & loss account which is reproduced as under:

*"23. Lease payments under an operating lease should be recognized as an expense in the statement of profit and loss on a straight line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit."*

14. Therefore, the Accounting Standard expressly allows the claim of lease rent on straight line basis over the period of lease term.

15. Further, page no. 1 of lease deed shows the amount of average rent per year which is Rs. 15,48,000/-claimed by the assessee in its profit & loss account.

16. The deduction on the basis of average rent per year will not affect the tax revenue of the department because of the reason that when actual payment of lease rent is more than the average rent in subsequent years, then excess deduction

claimed in the earlier years would net off the difference and consequently at the end, there would be no difference in actual payment and amount of deduction claimed.

17. Besides, the deduction of lease equalization reserve has been allowed by the Hon'ble Supreme Court in its recent judgment in the case of CIT-VI Versus Virtual Soft Systems Ltd. in civil appeal Nos. 4358 to 4363/2018. Hon'ble Supreme Court allowed the claim of "lease equalization charges" relying on the Guidance Note issued by the ICAI "Accounting for leases". Hon'ble Court has held that the taxpayer can take recourse of Guidance note issued by the ICAI, particularly when there is no express bar in the Act. The ICAI publication i.e. Guidance Note reflects the best practices adopted by the accountants throughout the world.

18. Relevant paras of the Hon'ble Supreme Court judgment reproduced as under:

*"9. Section 211 of the Companies Act, 1956 as it stood before the amendment dealt with "the Form and contents of balance-sheet and profit and loss account". Sub clause (3C) of Section 211 was added vide 1999 amendment with retrospective effect The relevant portion of Section 211 of the Companies Act is reproduced herein as under:*

*"(3C) For the purposes of this section, the expression "accounting standards" means the standards of accounting recommended by the Institute of Chartered Accountants of India constituted under the Chartered Accountants Act, 1949 (38 of 1949), as may be prescribed by the Central Government*

*in consultation with the National Advisory Committee on Accounting Standards established under sub-section (1) of section 210A:*

*Provided that the standards of accounting specified by the Institute of Chartered Accountants of India shall be deemed to be the accounting standards until the accounting standards are prescribed by the Central Government under this sub-section."(Emphasis supplied by us)*

*10) The purpose behind the amendment in Section 211 of the Companies Act 1956 was to give dear sight that the accounting standards, as prescribed by the ICAI, shall prevail until the accounting standards are prescribed by the Central Government under this sub-section. The purpose behind the accounting standards was to arrive at a computation of real income after adjusting the permissible depreciation. It is not disputed that these accounting standards are made by the body of experts after extensive study and research.*

.....

*16) In the present case, the relevant Assessment Year is 1999-2000. The main contention of the Revenue is that the Respondent cannot be allowed to claim deduction regarding lease equalization charges since as such there is no express provision regarding such deduction in the IT Act. However, it is apt to note here that the Respondent can be charged only on real income which can be calculated only after applying the prescribed method. The IT Act is silent on such deduction. For such calculation, it is obvious that the Respondent has to take*

*course of Guidance Note prescribed by the ICAI if it is available. Only after applying such method which is prescribed in the Guidance Note, the Respondent can show fair and real income which is liable to tax under the IT Act Therefore, it is wrong to say that the Respondent claimed deduction by virtue of Guidance Note rather it only applied the method of bifurcation as prescribed by the expert team of ICAI. Further, a conjoint reading of Section 145 of the IT Act read with Section 211 (un-amended) of the Companies Act make it clear that the Respondent is entitled to do such bifurcation and in our view there is no illegality in such bifurcation as it is according to the principles of law. Moreover, the rule of interpretation says that when internal aid is not available then for the proper interpretation of the Statute, the court may take the help of external aid. If a term is not defined in a Statute then its meaning can be taken as is prevalent in ordinary or commercial parlance. Hence, we do not find any force in the contentions of the Revenue that the accounting standards prescribed by the Guidance Note cannot be used to bifurcate the lease rental to reach the real income for the purpose of tax under the IT Act.*

*17) To sum up, we are of the view that the Respondent is entitled for bifurcation of lease rental as per the accounting standards prescribed by the ICAI. Moreover, there is no express bar in the IT Act regarding the application of such accounting standards.*

*18) In view of above detailed discussion, we are not inclined to interfere in the impugned decision of the High Court. Accordingly, the appeal is hereby dismissed leaving parties to*

*bear their own cost In view of the above, other connected appeals are also disposed off accordingly."*

19. Further, Hon'ble Delhi High Court in their recent decision in case of CIT vs. MGF India Ltd. [2018] 91 taxmann.com 405 has also held that Lease equalization charges can be deducted while computing book profit.

20. In view of the above said judgments, provisions of Companies Act, Accounting Standard and Income Tax Act, we hereby direct that the assessee is eligible for the claim of lease equalization charges. In the result, the appeal of the assessee on this ground is allowed.

**Logo Development Expenses:**

21. The assessee had claimed logo development charges of Rs.36,21,491/- under the head advertisement & business promotion in its profit & loss account. During assessment proceedings, the assessee filed copy of invoice, 15CA, 15CB, payment voucher, ledger etc. to prove the genuineness of expenditure incurred.

22. The AO made the disallowance on the ground that payment to the advertising agency was to create a new brand and thus creating an intangible asset for the assessee company which will have enduring benefit whose benefit will be derived over several periods. Therefore, the AO rejected the claim of advertisement expenses claimed as revenue and treated the same as capital in nature.

23. In this regard, it was submitted that the assessee company is running hotel under name of "The Claridges". The assessee company had entered into contract with the advertisement company based in Denmark CO + Hogh A/S for the development of new logo for the assessee company to strengthen their brand and put more value into it. However, the contract could not be executed due to the failure of the advertisement company to accomplish the work of designing and creation of new logo as per the specifications and requirements of the assessee company. The contract was terminated in mid way since the advertisement company did not deliver the new logo to the assessee company and as a result thereof no further payment was made by the assessee company in this regard. There were several disagreements between the assessee company and the advertisement company over the design of new logo and its payment. Ultimately, the design of new logo could not be approved and the assessee company is still using the same logo which it has been using since inception.

24. The assessee company is presently and still using the same logo which was registered in 2004. Since, the contract with advertising agency could not be completed and terminated in mid way and consequently no new logo was ever made or delivered to the assessee company.

25. Since, no intangible asset in the form of new brand or logo as alleged by the AO came into existence, therefore the expenditure incurred cannot be treated as capital expenditure

but to be allowed to the assessee company as revenue expenditure u/s 37(1) or business loss u/s 28(i) of the Act.

26. Further, it is a settled law that if expenditure incurred is in respect of the same business which is already carried on by the assessee, even if it is for the expansion of the business, namely, to start a new unit which is same as earlier business and there is unity of control and a common fund, then such an expense is to be treated as business expenditure. In such a case, whether a new business/asset comes into existence or not would become a relevant factor. If there is no creation of a new asset, then the expenditure incurred would be of revenue nature.

27. On this proposition, the Hon'ble Jurisdictional High Court of Delhi held as under:

- a) In the case of Indo Rama Synthetics (I) Ltd. [2011] 333 ITR 18 (Delhi) has held that Assessee-company had engaged services of an international firm of consultancy for carrying out a detailed study on various aspects relating to its operations and to suggest measures for improving operational efficiency and profitability of its business - However, based on review of cost benefit analysis, said assignment was terminated shortly after mandate had been given - In respect of work already done by consultancy firm until date of termination of mandate, assessee paid certain sum to said firm and claimed deduction of said payment as revenue expenditure - Whether payment in question could be allowed as business expenditure - Held, yes

Relevant paras are reproduced herein under:

*"The approach of the Tribunal was not correct in law. Interestingly, the Tribunal had accepted the fact that even when there was no formal written agreement with the consultancy firm, the report was submitted by the said company for the task assigned. The report was produced before the Assessing Officer/Commissioner (Appeals). The Tribunal noted that as per the assessee, the perusal of the report clearly indicated that the engagement was for the purpose of improving the operational efficiencies of the assessee and to enhance the profitability of the existing business. In those circumstances, not much importance could be attached to the fact that there was no written agreement with the said consultants to ascertain the scope of the study when such scope of study could very well be discerned from the report submitted by the consultants.*

*The helplessness shown by the Tribunal, for want of written agreement, was, therefore, clearly inappropriate. Once it was accepted as a fact that the assignment given to the said consultants was for the purpose of improving operational efficiencies and was not to incur any enduring benefit in capita/ field, but to carry on the existing business more efficiently and profitably, the irresistible conclusion was that such expenditure was allowable as business expenditure."*

- b) In the case of CIT vs. Priya Village Roadshows Ltd. 332 ITR 594 (Delhi) has held that

*"A harmonious reading of Triveni Engg. Works Ltd. vs. CIT [1998] 232 ITR 639/100 Taxman 19 (Delhi) and CIT vs. Modi Industries 200 ITR 341/68 Taxman 114 (Delhi) would demonstrate that one has to keep in mind the essential purpose for which such an expenditure is incurred. If the expenditure is incurred for starting a new business which was not carried out by the assessee earlier, then such expenditure is held to be of capital nature. In that event, it would be irrelevant as to whether project really materialized or not. However, if the expenditure incurred is in respect of the same business which is already carried on by the assessee, even if it is for the expansion of the business, namely, to start a new unit which is same as earlier business and there is unity of control and a common fund, then such an expense is to be treated as business expenditure. In such a case, whether a new business/asset comes into existence or not would become a relevant factor. If there is no creation of a new asset, then the expenditure incurred would be of revenue nature. However, if the new asset comes into existence which is of enduring benefit then such expenditure would be of capital nature."*

In the instant case, expenditure was incurred in respect of same business, which was already carried on by the assessee. Two projects which were undertaken were for the expansion of the same business, namely, one for taking over another cinema for conversion into multiplex and operation and management thereof and other for

conversion of self- owned cinema into multiplex. Payments were made to the consultants for preparing feasibility reports in respect of both the projects. However, ultimately projects were not found to be financially and technically viable and were shelved. Thus, finding given, that no new asset came into existence, which was the basis adopted by the Assessing Officer for treating the expenditure as capital expenditure was wrong.

In the instant case, both the ingredients were satisfied, namely,—

(i) the feasibility study conducted by the assessee was for the same and existing business with a common administration and common fund, and

(ii) the study was abandoned, without creating any new asset

In such circumstances, the Tribunal was correct, in law, in holding that expenses on new project development were allowable as business expenditure under section 37.

c) In the case of CIT vs. ACL Wireless Ltd. [2014] 361 ITR 210 has held that expenditure incurred in ordinary course of business on upgradation, improvement, removal of glitches of existing or already developed software to improve its product is to be treated as revenue expenditure.

Relevant paras are reproduced herein under:

*"To keep pace with the requirements and ensure product sale ability, software development companies have to constantly incur expenditure to upgrade, improve and remove problem areas of the software. They have to employ professionals whose job is to continuously upgrade the software and provide newer features and updates on a regular basis. The shelf life of the software without constant improvement would be very small.*

*Expenditure which enables the profit making structure to work more efficiently leaving the source of profit making structure untouched, would be revenue in nature.*

*The aforesaid expenditure did not bring into existence a new asset but rectified and improved the product being sold. It was accepted that there had to be recurring expenditure which had to be incurred in the said business to ensure sale of the software. This expenditure was incurred for removal of obstructions, restrictions or disabilities on the sale and to ensure that there was demand of the said product. These were normal day-to-day expenses for running the business in Question and did not create enduring rights or advantage or benefit over a long period time. While determining and deciding a question whether the expenditure is capital or revenue in nature, the determination should be based upon consideration of facts and circumstances and by applying principles of commercial trading and business expediency. Enduring benefit test is not a universal test and can break down. The said principles had been rightly applied by the*

*Tribunal in the facts of the present case to hold that expenditure incurred was revenue in nature and not capital.”*

d) In the case of CIT vs. Euro India Ltd. [2014] 45 taxmann.com 173 (Delhi) has followed the decision of Indo Rama Synthetics (I) Ltd. (supra) and held that where expenditure is incurred on obtaining feasibility report for expansion of existing business where there is unity of control and common funds, then such expenditure would be treated as business expenditure.

e) Hon'ble Madras High Court in the case of Tamil Nadu Magnesite Ltd. vs. ACIT [2018] 95 taxmann.com 239 (Madras) has held that where assessee-company entered into an arrangement for implementation of a project which was later on ordered to be closed by Government, since said project was in same line of existing business of assessee and there was no creation of any new asset of enduring nature, entire exp. incurred on said project was to be allowed as revenue expenditure.

f) Hon'ble Bombay High Court in the case of CIT vs. Rajesh Khanna [2012] 28 taxmann.com 415 and in the case of CIT vs. Venus Records & Tapes (P.) Ltd. [2016] 66 taxmann.com 89 have held that entire expenditure incurred on production of film which is abandoned before it was completed is allowable revenue expenditure.

g) Hon'ble High Court of Andhra Pradesh in the case of CIT vs. Praga Tools Ltd. [1986] 157 ITR 282 (AP) has held that

*"the amounts which were expended by the assessee should be regarded as revenue expenditure. The facts would show that the so-called development expenditure incurred by the assessee was no more than expenditure which had been incurred by the assessee for the purpose of preparing and perfecting designs which were required with reference to the execution work of specific contracts of those years. The expenditure incurred in connection with the execution of those specific contracts could not therefore, be said to be an expenditure incurred for acquiring an asset of enduring nature. They were both in design and in purport the expenditure incurred only towards the execution of those contracts. It was therefore, held that the so-called development expenditure incurred was only revenue expenditure."*

*Similarly, the amounts paid to the consultancy firms also could not be regarded as expenditure incurred in acquiring any asset of enduring nature. The amount paid to the 'NPC' was for the benefit of increasing the manufacturing efficiency and formulating incentive schemes. In an age of speedy technological progress, no degree of permanency can be attached to these opinions given by the firms like the 'NPC' on how to increase the production. They are all susceptible to modifications and alterations. For that reason, it could not held that the fee paid to 'NPC' should be regarded as an expenditure incurred for acquiring a*

*capital asset. So was the case with the amounts paid to the ASC' and so was the case with the amounts paid to 'EMFC'. Therefore, the expenditure incurred was revenue in nature."*

28. In the instant case, the contract for new logo for existing business has been awarded, certain amounts were spent and the project has been shelved midway and abandoned. There was no creation of any asset and there is no existence of new business. The amounts have been spent in connection with the ongoing business operations. Hence, keeping in view the facts of the case and the judgments of the Hon'ble High Courts, we hereby allow the appeal of the assessee on this ground.

29. In the result, the appeal of the assessee is allowed.

Order Pronounced in the Open Court on 27/06/2022.

Sd/-

**(Yogesh Kumar US)**  
**Judicial Member**

**Dated: 27/06/2022**

\*Subodh Kumar, Sr. PS\*

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(Appeals)
5. DR: ITAT

Sd/-

**(Dr. B. R. R. Kumar)**  
**Accountant Member**

**ASSISTANT REGISTRAR**