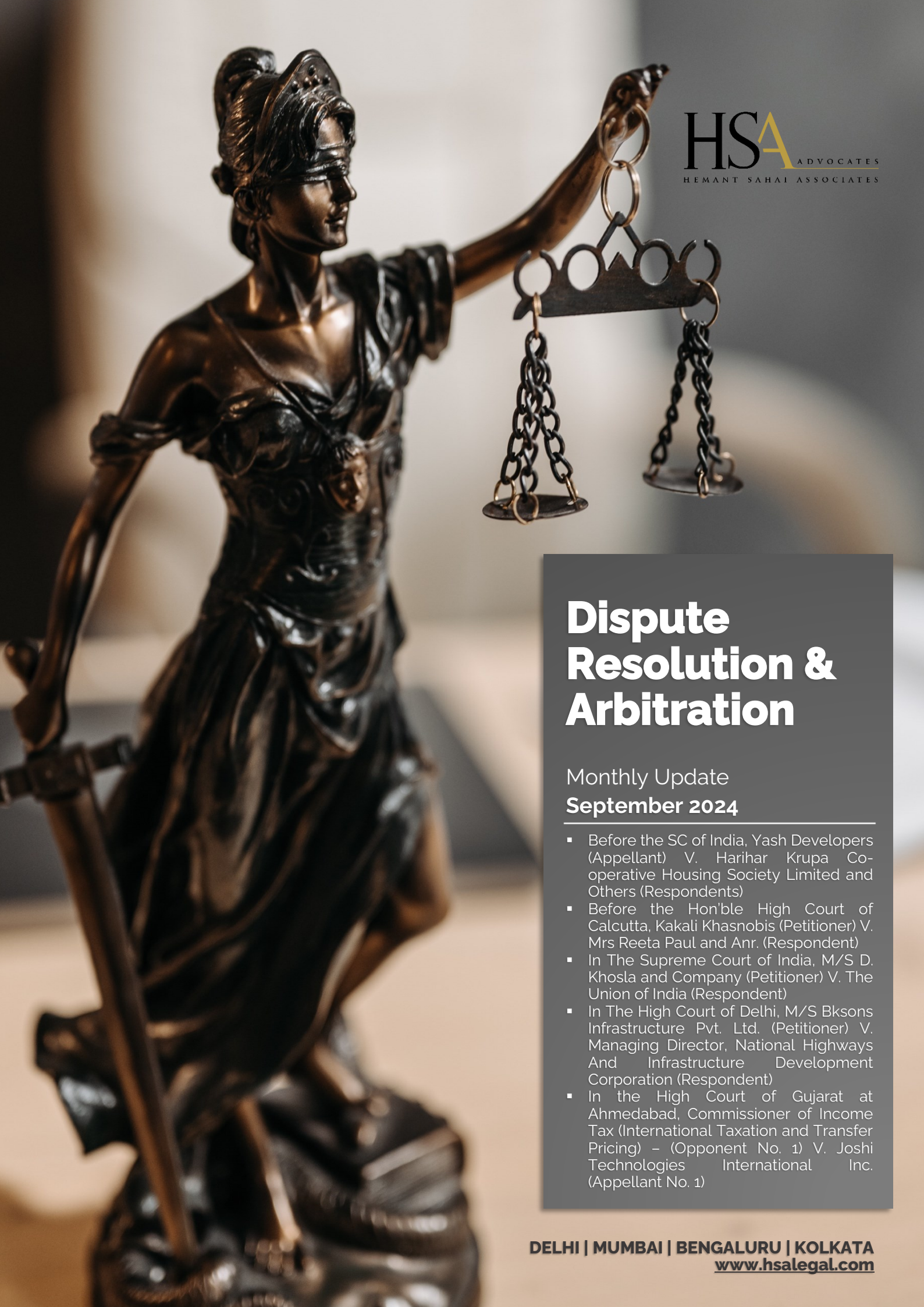

HSA ADVOCATES
HEMANT SAHAI ASSOCIATES

Dispute Resolution & Arbitration

Monthly Update
September 2024

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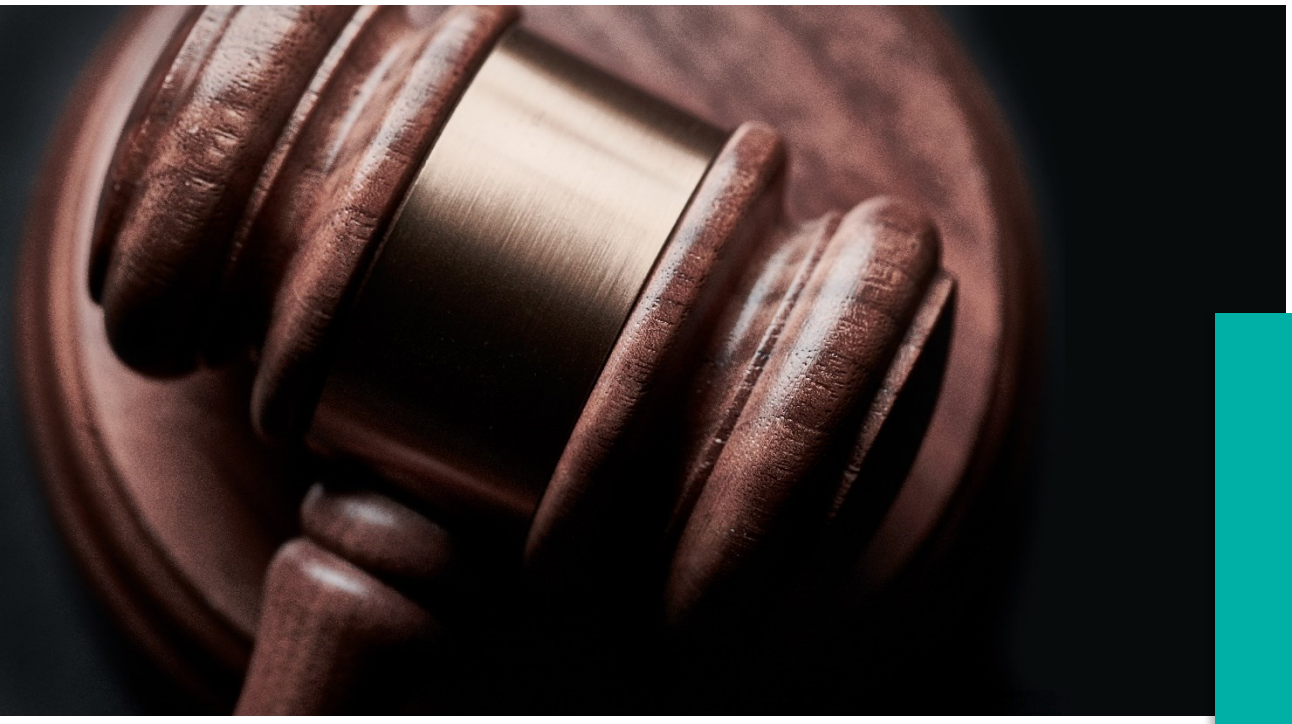
DISPUTE RESOLUTION AND ARBITRATION UPDATE



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Before the SC of India, Yash Developers (Appellant) V. Harihar Krupa Co-operative Housing Society Limited and Others (Respondents)

Civil Appeal No. 8127 of 2024

Background facts

- The case above referred to involves a dispute between a competing real estate developer under the guise of rehabilitating slum dwellers, as governed by the Maharashtra Slum Areas (Improvement, Clearance, and Redevelopment) Act, 1971. Yash Developers ("**Appellant**") is a real estate developer appointed by a cooperative housing society of slum dwellers and Harihar Krupa Co-operative Housing Society Limited ("**Respondent No. 1**") is a cooperative housing society consisting of slum dwellers in Borivali, Mumbai.
- In 2003, the Appellant was appointed as the developer by the cooperative housing society to redevelop the land where the slum dwellers had their hutments. This land was declared a "slum area" under the Maharashtra Slum Areas (Improvement, Clearance, and Redevelopment) Act, 1971 ("**The Act**").
- The development project was significantly delayed, stretching over two decades i.e., 18 years without completion. This prolonged delay led to dissatisfaction among the slum dwellers and raised questions about the Appellant's ability to fulfill the obligations under the redevelopment agreement.
- Due to the extensive delay, the Apex Grievance Redressal Committee ("**AGRC**") terminated the development agreement in favor of the Appellant on 04.08.2021. The AGRC exercised its power under Section 13 of the Maharashtra Slum Areas (Improvement, Clearance, and Redevelopment) Act, which allows the competent authority to redevelop the land at its own cost if the original developer fails to commence or complete the project within the stipulated time.
- The Appellant challenged the AGRC's termination order before the Hon'ble HC of Bombay. The Hon'ble HC of Bombay, however, upheld the AGRC's decision, noting that the Appellant had failed to meet the basic requirement of commencing construction within a reasonable time. The Hon'ble HC of Bombay also emphasized that the right to shelter of the slum dwellers, which is part of their right to livelihood under Article 21 of the Constitution, should not be nullified by such undue delays.

- The Hon'ble HC of Bombay further held that the developer's removal for failing to commence construction within a reasonable time is not fatal to the statutory intent behind a Slum Rehabilitation Scheme. This means that the purpose of the scheme is not defeated by removing a developer who fails to act within a reasonable time.
- The slum dwellers' right to shelter under Article 21 of the Constitution cannot be nullified by the developer's unconscionable delay in commencing construction. The HC also emphasized the limited scope of judicial review under Article 226 of the Constitution against the decision of the statutory authority-AGRC.
- The Appellant aggrieved by the order of the HC and the AGRC filed the present Civil Appeal before the Supreme Court.

Issue(s) at hand

- Whether the removal of a developer for non-fulfilment of the basic requirement to commence construction of a slum rehabilitation building for a long period of 18 years is fatal to the object and intention of a statutory intent behind a Slum Rehabilitation Scheme.
- Whether the right to shelter, which is part of the slum dwellers' right to livelihood guaranteed under Article 21 of the Constitution, can be continued to be nullified by such actions of unconscionable delay on the part of the developer, in not commencing construction of the slum project even by an inch more particularly when the nature of such work awarded to a developer for him is purely a commercial venture, for profit.

Arguments of the Parties

- **Arguments by the Appellant**
- **Delay between 2003 and 2011 -** The Appellant argued that the delay during this period was inevitable and caused by prolonged litigation between the Appellant and Omkareshwar Co-operative Housing Society, as well as Siddhivinayak Developers. The Appellant had no role in this delay, and was beyond its control.
- The Appellant claimed that it had the required 70% consent from slum dwellers and was legally entitled to develop the property. The issue was settled only on 07.06.2011, after which the Letter of Intent ("**LOI**") could be issued.
- **Delay between 2011 and 2014- Further**, the Appellant stated that the delay was due to the time required to obtain necessary permissions, approvals, and Environmental Clearances ("**EC**"). The Appellant applied for ECs in 2011 and received it in 2014, which was necessary before commencing construction.
- **Delay between 2014 and 2019 -** The Appellant contended that the delay during this period was due to the non-cooperation of certain slum dwellers, which led to the stalling of the project. The Appellant had to initiate eviction proceedings, which were not decided until 2021.
- **Delay between 2015-2017) -** The Appellant argued that the delay from 2015 to 2017 was justified due to the draft development plan ("**DP**") published by the Municipal Corporation, which proposed a road passing through the property. This plan was eventually deleted, but the delay was unavoidable during that period.
- The Appellant was of the view that the financial capacity to complete the project, as evidenced by agreements with third parties for financial assistance. The agreements were made to secure the necessary funds to continue the project.
- The Appellant stated that many complaints filed against it by the Managing Committee members of the Respondent No. 1, were withdrawn, and thus proceedings should have been dropped. Although the managing committee of Respondent No. 1 had initially terminated the development agreement, this termination was revoked on 28.02.2021. The revocation of termination was because the agreement was terminated by Mr. Rai, who did not have the requisite authorisation.
- The Respondent No. 1 did not object to the withdrawal of the termination of the development agreement of the Appellant, and in fact, wanted the appellant to continue as the developer. Further submitted that Mr. Rai was acting without the authorisation of the other members, and hence, he also could not have filed an appeal before the AGRC on behalf of Respondent No. 1 against the order of the CEO of the Slum Rehabilitation Authority ("**SRA**").

Arguments by the Respondents-

- **Delay between 2003 and 2011-** The Respondents argued that the Appellant was responsible for the delay between 2003 and 2011, as it failed to take timely action to obtain the LOI. The HC upheld the view that the Appellant was not diligent in procuring the LOI, and the litigation with Omkareshwar did not prevent the Appellant from starting the project.

- **Delay between 2011 and 2014-** The Respondents contended that the delay was attributable to the Appellant, as the EC was not required for the commencement of certain parts of the project, like the rehabilitation building. The Appellant's inaction was unjustified.
- **Delay between 2014-2019-** The Respondents argued that the delay from 2014 to 2019 was due to the Appellant's failure to take active steps to resolve the eviction proceedings.
- **Delay between 2015-2017-** The Respondents contended that the DP could justify a delay of only 2 months and not the extended period claimed by the Appellant.
- The Respondents argued that the Appellant did not have the financial capacity to complete the project and relied on financial agreements with third parties, which indicated its inability to execute the scheme.
- The Respondents argued that even if some complaints were withdrawn, the complaint filed by Mr. Rai and others still survived, and the appeal before the AGRC was maintainable. They also contended that the SRA had the power to proceed against the Appellant suo moto, and the withdrawal of complaints did not preclude the AGRC from deciding the appeal.

Findings of the Court

- The SC stated that the findings of the AGRC and the HC were correct on law and fact. Further, the SC noted that there was a delay in executing the project by the time the termination order was issued. The Appellant tried to justify this delay by breaking it down into different periods (2003-2011, 2011-2014, and 2014-2019).
- The SC rejected the Appellant's approach of examining each period of delay independently. It held that the overall delay could not be justified by looking at individual periods in isolation. The SC emphasized that the inquiry should be whether it would be unjust to exclude these delays when considering the termination order.
- The SC noted that the HC of Bombay was correct in stating that, the developer's reliance on third-party financing for the slum rehabilitation project was counterproductive and risky. If any of these financers had withdrawn their support, the project would have faced severe financial instability, potentially leading to its collapse. The developer's financial stability is crucial for the successful implementation of slum schemes. In this case, the developer's actions in seeking finance without informing the society or authorities raised concerns about their commitment to the project.
- In respect of the specific periods of delay the SC stated as follows-

  2003-2011: 8-year delay due to disputes with a competing builder was unjustified.

  2011-2014: Developer should have anticipated and prepared for environmental clearance delays.

  2014-2019: Delays due to non-cooperation of slum dwellers and DP road issues were not valid excuses.
- The SC emphasized that the Slum Rehabilitation Scheme is not merely a real estate project but involves a public purpose connected to the right to life of citizens living in poor conditions. The delays in the project were particularly unjustifiable given this context.
- While rejecting the Appellant's justifications for the delay, the Court also expressed dissatisfaction with the SRA and its CEO for failing to ensure that the project was completed on time. The SCheld the SRA accountable for its inaction and negligence.
- The SC agreed with the High Court's findings that the Appellant's financial instability was detrimental to the project. The Appellant's repeated reliance on third-party agreements for financial resources was seen as a risk that could lead to the collapse of the project. The Court found that the Appellant lacked the necessary financial stability to successfully implement the slum scheme.
- The SC ruled that the Slum Rehabilitation Authority (SRA) has a duty to ensure timely project completion under Section 13(2) of the Act, regardless of applications made. Dismissing the Appeal, the SC reflected on the Act's performance, citing challenges like inefficiencies, manipulation, and inadequate provisions. With 1,612 pending cases, including 135 over 10 years old, the SC recommended that the Chief Justice of the Bombay High Court initiate a suo motu review of the Act's implementation to identify issues and advise reforms.

HSA
Viewpoint

The SC reaffirms the findings of the AGRC and HC and emphasized the importance of timely implementation and accountability in slum rehabilitation projects. SC orders timely completion of slum rehabilitation projects, holding developers accountable for diligence and financial responsibility. It emphasizes SRA's monitoring role, warns of severe consequences for delays, and recommends reviewing the Maharashtra Slum Areas Act, 1971 to improve efficiency and address shortcomings.

Further, in response to the escalating trend of developer defaults, a Public Interest Litigation (PIL No. 109 of 2019) was filed before the Hon'ble Bombay High Court, seeking redress for the non-payment of transit rent to eligible slum dwellers by developers. The PIL drew attention to the significant outstanding dues owed to slum dwellers, highlighting the need for intervention. The Hon'ble Court, acknowledging the gravity of the situation and the concomitant hardships faced by slum dwellers, issued an Order on 19.07.2023, directing the Slum Rehabilitation Authority (SRA) to adopt proactive measures to verify and ensure the payment of transit rent to slum dwellers, thereby mitigating the potential for multiple individual litigations and addressing the issue through a comprehensive and systemic approach. In lieu of the above, the Slum Rehabilitation Authority ("SRA") has taken proactive measures in order to ascertain whether transit rent is being paid to the slum dwellers wherein the SRA issued a Circular ("SRA Circular") on 01.08.2023 with directions that the developer shall deposit advance rent of two years and a post-dated cheque for the remaining period of completion at the stage of Annexure III and the Letter of Intent in favour of the Developer shall be issued only pursuant to depositing the advance rent. No new proposals of defaulting developer/firms and its partners/directors to be accepted unless all dues are cleared in respect of payment of transit rent. The defaulting developer/firm and its partners/directors shall not be entitled to be appointed as developers irrespective of the consent of society, in the existing SRA proposals wherein the previous developers are terminated. The developers of the Slum Rehabilitation Scheme who have failed to handover the PAP/PTC tenements to the SRA shall not be entitled to submit any new proposal in order to protect the interests of slum dwellers.

Before the Hon'ble High Court of Calcutta.
Kakali Khasnobis (Petitioner) V. Mrs Reeta Paul and Anr. (Respondent)

Arbitration Petition – Commercial No. 701 of 2024

Background facts

- The present matter pertains to a challenge to an application under Section 11 of the Arbitration and Conciliation Act, 1996 ("**Act**"). Owing to certain disputes between Kakali Khasnobis ("**Petitioner**") and Reeta Paul and Anr. ("**Respondents**"), the Petitioner filed an application under section 11 of the Act, seeking the appointment of an arbitrator to resolve the disputes between the parties. Challenging the aforesaid application, the Respondents presented the following two-fold arguments:
- First, they argued that the aforesaid application was time-barred. It was the claim of the Respondents that the Petitioner had previously filed an application under Section 9 of the Act in July 2021, which came to be dismissed in July 2024, owing to the failure of the parties to take effective steps to appoint an arbitrator. Accordingly, the Respondents argues that the instant Section 11 application, filed after the dismissal of the Section 9 application would be time-barred.
- Secondly, the Respondents also claimed that the Petitioner had not complied with the pre-requisite of giving a notice to the Respondents for appointment on an Arbitrator under Section 21 of the Act. In support of the above, the Respondents placed on record past decisions of the Hon'ble Delhi High Court, Hon'ble Mumbai High Court and the Hon'ble Calcutta High Court ("**Hon'ble Court**").
- The Petitioner on the other hand contended that the application under Section 11 was well within the limitation period, as the same had been filed before the expiry of 3 years from the filing of the application under Section 9 of the act. Additionally, the Petitioner argued that it would also be entitled to the Covid-9 relaxations on limitation periods, as granted by the Hon'ble Supreme Court of India.
- Hence the present challenge was heard and decided by the Hon'ble Court.

Issue(s) at hand?

- The following issues were put before the Hon'ble Court:
  - Whether the application under Section 11 was barred by limitation?
  - Whether non-compliance with Section 21 rendered the application under Section 11 invalid?

Decision of the Court

- The Hon'ble Court, on the first issue of limitation, held that the application under Section 9 of the Act filed in July 2021, marked the start of the cause of action and the subsequent application under Section 11 of the Act, filed in July 2024, was within the three-year limitation period prescribed by Article 137 of the Limitation Act, 1963. Additionally, the Hon'ble Court acknowledged that the Hon'ble Supreme Court's Covid-19 relaxations extended the limitation period, confirming that the instant application under Section 11 was well within the period of limitation.
- On the second issue regarding non-compliance with pre-requisite of giving a notice under Section 21 of the Act, the Hon'ble Court clarified the distinction between Sections 11(5) and 21 of the Arbitration Act. The Hon'ble Court observed that Section 11(5) of the Act requires a request for the appointment of an arbitrator, while Section 21 of the Act governs the commencement of arbitral proceedings. The Hon'ble Court opined that the absence of a notice under Section 21 of the Act does not invalidate an application under Section 11(5) of the Act, which deals only with the appointment process.
- The Hon'ble Court noted that the Petitioner had sufficiently complied with Section 11(5) of the Act by invoking the arbitration clause vide a letter dated July 2021, a copy of which was served to the Respondents, who not only acknowledged the same, but also did not raise any objections to the notice itself. The only objection raised by the Respondents was limited to the unilateral appointment of an arbitrator, which was later addressed by the Petitioner through the present application under Section 11 of the Act.
- In view of the above, the Hon'ble Court held that both objections raised by the Respondents, challenging the present application under Section 11 of the Act, were without merit. Accordingly, the Hon'ble Court allowed the application and appointed a sole arbitrator to resolve the disputes between the parties.

HSA
Viewpoint

In our opinion, the present decision of the Hon'ble Calcutta High Court clarifies that an application under Section 11(5) of the Arbitration and Conciliation Act does not require a prior request for arbitration under Section 21 and the same would be governed by the limitation period prescribed under Article 137 of the Limitation Act, 1963. This decision also emphasizes the distinct roles of Sections 11 and 21 in the arbitration process and rightly upholds the Petitioner's application as timely, considering the Covid-19 limitation relaxations.

In The Supreme Court of India.
M/S D. Khosla and Company (Petitioner) V. The Union of India (Respondent)

Special Leave Petition (Civil) No.812 Of 2014

Background facts

- M/s D. Khosla and Company ("Petitioner") entered into a contractual agreement with the Union of India ("Respondent") during the 1984-85 period. A dispute arose between the parties under the contract, as a result, the matter was referred to arbitration under the Indian Arbitration Act, 1940 ("Act").
- On September 17, 1997, the Arbitrator passed an award in favour of the Petitioner, which was made a rule of the court under Section 14 read with Section 17 of the Act. The award included a specific provision for the payment of interest, divided into two distinct periods:
  - **Pre-Award Period**: Simple interest at the rate of 12% per annum was awarded on the principal amount from the date of completion of the work until the date of the award.
  - **Post-Award Period**: Simple interest at the rate of 15% per annum was awarded from the date of the award until the realisation of the decretal amount.
- The Respondent paid the principal amount along with the interest calculated at the rates specified for both the pre-award and post-award periods.
- However, the Petitioner was dissatisfied with the interest paid by the Respondent, and argued that the 15% interest awarded for the post-award period should be calculated not only on the principal amount but also on the interest accrued during the pre-award period (i.e., 12% interest) and hence moved an Execution Petition for realization of certain amount.
- The Principal Senior Civil Judge, Khambhalia, in Execution Petition No.9 of 2006, rejected the Petitioner's claim, holding that the Arbitrator had awarded simple interest of 12% and 15% on the principal amount only. The Gujarat High Court upheld this decision on September 6, 2013, affirming that the Petitioner was entitled only to simple interest at 15% on the principal sum awarded, without including the accrued pre-award interest.
- Aggrieved by these ruling of the High Court, the Petitioner approached the Supreme Court via the present Special Leave Petition.

Issue at hand?

- Whether the 15% interest awarded for the post-award period should be calculated on the principal sum alone or on the principal sum plus the accrued 12% interest for the pre-award period?

Decision of the Court

- At the outset, the Hon'ble Supreme Court held that as per Section 29 of the Act, the court can award interest at the rate it deems reasonable on the principal sum awarded in the decree. In view of the same the Supreme Court held that as per the Section 29 interest can only be awarded on the principal sum awarded.
- The Hon'ble Supreme Court also held that since the award passed by the Ld. Arbitrator under the Act was in nature of a decree and hence it would attract provisions of the Code of Civil Procedure, 1908 ("CPC").
- In view of the same the Hon'ble Supreme Court examined Section 34 of the CPC and Section 3(3) Interest Act, 1978 and held that courts are not entitled to award interest upon interest unless specifically provided either under any statute or under the terms and conditions of the contract.
- The Hon'ble Supreme Court also referred to the judgment in the cases of ***Oil and Natural Gas Commission v. M.C. Clelland Engineers S.A.***[1] and ***State of Haryana and Others v. S.L. Arora and Company***[2], wherein it was held that interest is not permissible on interest awarded unless it is clearly stipulated or specified in the contract or provided under a statute.
- In view of the above legal position the Hon'ble Supreme Court concluded that the Arbitrator's award only contemplated simple interest on the principal sum awarded and nowhere specifically contemplated for awarding 15% interest on the principal amount as well as the accrued 12% interest for the pre-award period.
- Hence the Hon'ble Supreme Court dismissed the Special Leave Petition.

HSA
Viewpoint

The decision clarifies that an arbitrator can only award interest on the principal sum and interest on interest cannot be awarded under the Act, unless specifically specified under any statute or the contract. The significance of this judgment is that it removes all ambiguities and makes it clear that an arbitral award only attracts simple interest on the principal sum awarded under the Act. This case underscores the importance of clear and explicit terms in the arbitral contract for the purpose of applying compound interest on the principal sum awarded.

In The High Court of Delhi.

M/S Bksons Infrastructure Pvt. Ltd. (Petitioner) V. Managing Director, National Highways And Infrastructure Development Corporation (Respondent)

Arbitration Petition 498 of 2024

Background facts

- M/s BKSONS Infrastructure Pvt. Ltd. ("Petitioner") entered into an Engineering, Procurement and Construction ("EPC") Contract with National Highways and Infrastructure Development Corporation represented through its Managing Director ("Respondent") on June 1st 2020.
- The primary objective of the EPC Contract was to upgrade a two-lane section of National Highway 117 into a four-lane section. Article 26 of the EPC Contract outlined the dispute resolution process to be adopted for resolving disputes between the Petitioner and the Respondent.
- As dispute arose between both the parties, the Petitioner formally wrote to the Respondent on January 2 2023, calling upon them to appoint a Conciliator for looking into the matter and resolving the dispute. In furtherance to the said letter, the Petitioner once again addressed a letter dated June 8th 2023 reiterating their request for appointment of a Conciliator.
- Subsequently, the Petitioner addressed a letter dated July 25, 2023, whereby they proposed the name of three Conciliators and requested the Respondent to select one Concilator among the three names suggested for resolving the dispute through Conciliation.
- Since, the Respondent did not act on the request of the Petitioner they approached the Chairman of the Respondent by way of a letter dated November 18th 2023. The Petitioner vide the said letter dated November 18th 2023 prayed that a mutual meeting between the Petitioner and the Respondent be conducted as per Article 26.2 of the EPC Contract for resolving the disputes.
- In view of the same a meeting took place on December 27th 2023 between the Petitioner and the Respondent. Subsequently, the Petitioner vide a letter dated January 11th 2024 was informed that their claims have been rejected.
- The Petitioner thereafter proceeded to issue a notice upon the Respondent under Section 21 of the Arbitration and Conciliation Act, 1996 ("Act"). The Respondent replied to the said notice on February 5th 2024 directing the Petitioner to approach the Conciliation Committee of Independent Experts constituted by them in terms of Article 26.2 of the EPC Contract.
- Instead of approaching the Conciliation Committee of Independent Experts the Petitioner filed the present Petition.

Issue(s) at hand?

- Whether the Petitioner can approach the Hon'ble Court under Section 11(6) of the Act when the mandatory pre-arbitral protocol contained in the EPC Contract was not duly followed?

Decision of the Court

- At the outset, the Hon'ble Court meticulously examined the dispute resolution clause outlined in Article 26.2 of the EPC Contract and stated that the EPC Contract contained a 3-Stage procedure for resolving any dispute. As per Stage 1, the contractor is to seek a decision on its claim by an independent Contractor. If the decision is adverse to the contractor then as per Stage 2, the contractor shall approach the Chairman of the Respondent for arranging a joint meeting between the parties to resolve the dispute. If the said meeting fails then as per Stage 3, the contractor has to approach the Conciliation Committee of Independent Experts and only thereafter can the parties invoke arbitration for settling the dispute.
- The Hon'ble Court further held that the court's jurisdiction under Section 11(6) of the Act is triggered immediately when one party fails to adhere to the agreed-upon procedure stipulated for the appointment of an Arbitrator. Hence the court acquires jurisdiction immediately upon a party's default in following the pre-arbitral or arbitral procedures outlined in the contract.
- The Hon'ble Court held that the Respondent failed to appoint an independent Conciliator despite receiving three reminders from the Petitioner and hence failed to adhere to the pre-arbitral procedure provided in the EPC Contract.
- The Hon'ble Court stated that the Petitioner's subsequent act of approaching the Chairman of Respondent for resolving the dispute does not negate the Respondent's default in appointing the Conciliator. The Hon'ble Court further held that failure of the Respondent to appoint a Conciliator as required under the EPC Contract constituted a default under Section 11(6) a of the Act.
- Hence the Hon'ble Court held that the Petitioner was entitled to invoke arbitration since the Respondent failed to adhere to the pre-arbitral procedure.

HSA
Viewpoint

This decision clarifies that the court acquires jurisdiction under Section 11 (6) of the Act immediately on the default of pre-arbitral procedure. This ruling reinforces the principle that while pre-arbitral procedures are valuable for saving time and costs, they should not unduly constrain the parties' ability to resolve disputes through arbitration. In our view, this judgment takes a pro-arbitration approach as it holds that non-compliance with pre-arbitration steps does not result in disallowing a party to undergo arbitration if the other party is at fault for non-compliance with the pre-arbitral steps. In other words, this judgement makes it clear that no party can claim benefit of pre-arbitral procedure if the party itself has failed in complying the same.

- In view of the same the Hon'ble Court thereby appointed Senior Advocate Mr. A.K. Behera as the Arbitrator to arbitrate on the disputes between the parties.

In the High Court of Gujarat at Ahmedabad.

Commissioner of Income Tax (International Taxation and Transfer Pricing) (Opponent No.1) V. Joshi Technologies International Inc. (Appellant No. 1)

R/TAX APPEAL No. 347 of 2024

Background facts

- Joshi Technologies International Inc. (**Appellant/Assessee**), involved in the exploration of petroleum oil in the Dholka and Wavel Oil fields used to transport petroleum to the Oil and Natural Gas Corporation Central Storage for further processing for which the Appellant installed oil wells.
- When the Appellant/ Assessee submitted its Income Tax Returns for the Assessment Year 2007-08, the Assessing Officer (**AO**) allowed the depreciation at the rate of 10% by treating the oil wells as 'building' as per Entry 1 of Appendix -I of the Income Tax Rules, 1962 (**Rules)**. According to the Appellants the oil wells should have been considered as 'plant and machinery' as per Entry 8 of Appendix-1 of the Rules and accordingly the depreciation on oil wells should have been at the rate of 60%.
- Aggrieved by the decision of AO, the Appellant/ Assessee filed an appeal before the Dispute Resolution Panel (**DRP**). The DRP allowed depreciation at the rate of 15% to the Appellant/ Assessee on oil wells and affirmed the decision of the AO considering the oil wells to be "building" as per the Rules. Aggrieved by the Order of the DRP, the Appellant/ Assessee filed an Appeal before Income Tax Appellate Tribunal (**ITAT)**. The ITAT ruled in favour of the Appellant and considered the oil wells to be "plant and machinery".
- Aggrieved by the order of the ITAT, the Opponent preferred an Appeal before the High Court of Gujarat. The Commissioner of Income Tax (International Taxation And Transfer Pricing) (**Opponent**) contended that the ITAT had made a mistake in classifying oil wells as "Plant & Machinery" for the purpose of calculating additional depreciation. It was argued that the Section 32 (1) (ii a) of the Income Tax Act, 1961 (**Act**) did not intend for such a classification and cited previous instances in which various interpretations were applied.
- Appellant contended that the classification of oil wells as "Plant & Machinery" was sound and consistent with prior rulings, such as the renowned ***Niko Resources Ltd. v. Assistant Commissioner of Income Tax***[1]. The Appellant emphasised that oil wells meet the criteria of a "Plant" because of their durability and their essential function in the extraction of mineral oil.

Issues at hand?

- Whether the Income Tax Appellate Tribunal (ITAT) erred in classifying the oil well as 'plant and machinery' for the purpose of availing depreciation benefits?

Decision of the Court

- The Court held that term 'Plant' is widely recognised as encompassing durable and indispensable assets that are crucial for corporate operations. The Court restated that for an asset to be considered as 'Plant', it must serve as a tool used in the business operations.
- The Court referred to its prior views in the ***Niko Resources Case*** which established that mineral oil wells are classified as 'Plant' according to Section 32 of the Act. The Court was of the view that oil wells must be considered as 'Plant & Machinery' and must be permitted to have further depreciation applicable to them.
- The High Court held that ITAT correctly applied the interpretation of 'Plant and Machinery' to grant the Appellant additional depreciation, and the High Court correctly concurred with the ITAT's decision. Hence, the revenue appeal was dismissed.

HSA
Viewpoint

The classification of oil wells as "Plant & Machinery" for the purpose of obtaining depreciation benefits under Section 32 of the Act is in accordance with the broader definition of "Plant". Oil wells, by their very nature, satisfy this criterion, as the term "Plant" refers to enduring assets that are essential tools used in the core business operations. The established judicial understanding that prioritises the functional and operational significance of an asset in determining its classification was overlooked by the ITAT.

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