
(2007) 06 MAD CK 0161

In the Madras High Court

Case No : Tax Case (Appeals) No's. 609 and 610 of 2007

Commissioner of Income Tax

APPELLANT

Vs

VGR Foundations

RESPONDENT

Date of Decision : 14-06-2007

Acts Referred:

Income Tax Act, 1961 — Section 133A, 143(2), 148, 57

Citation : (2008) 298 ITR 132

Hon'ble Judges : P.P.S. Janarthana Raja, J;P.D. Dinakaran, J

Bench : Division Bench

Advocate : T. Ravi Kumar, for the Appellant;

Final Decision : Dismissed

Judgement

P.P.S. Janarthana Raja, J.—These appeals are filed by the Revenue against the order of the Income Tax Appellate Tribunal, "B" Bench, Chennai in I.T.A. Nos. 5/ Mds/2003 and 906/Mds/2003, dated July 15, 2004, raising the following common substantial question of law:

Whether, on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in holding that interest on moneys borrowed for the period prior to the commencement of business can be allowed as deduction from the interest u/s 57 of the Act while computing "Income from other sources" in respect of the interest received?

2. The facts leading to the above substantial question of law are as under:

3. The assessee is a partnership firm engaged in the real estate business. The relevant assessment years 1997-98 and 1998-99 and the corresponding accounting years ended on March 31, 1997, and March 31, 1998, respectively. A survey u/s 133A of the Income Tax Act ("1961 Act" in short) was conducted on January 27, 2000. Notices u/s 148 were issued on March 9, 2000. The assessee-firm filed "nil" returns of income and also filed letters stating that the returns filed vide acknowledgment No. 8869, dated February 14, 2000, for the

assessment year 1997-98 and acknowledgment No. 8871, dated February 14, 2000, for the assessment year 1998-99, have to be treated as the returns in response to the notices issued u/s 148 of the Act. Further, notices u/s 143(2) were issued on November 20, 2001. The Assessing Officer noticed that the statements filed along with the returns of income revealed that the assessee had incurred expenses prior to commencement of business and the assessee had also earned interest income from out of the fixed deposits with bank and the said income had been set off against the expenses. The Assessing Officer was of the view that the interest received on short-term deposits in bank during the pre-production stage is assessable as Income from other sources. Hence, the same was considered as Income from other sources, determining the total income at Rs. 1,59,350 and Rs. 1,16,400 for the assessment years 1997-98 and 1998-99, respectively. Aggrieved by the orders, the assessee filed appeals to the Commissioner of Income Tax (Appeals). The Commissioner of Income Tax (Appeals) dismissed the appeals and confirmed the orders of the Assessing Officer. Aggrieved, the assessee filed appeals to the Income Tax Appellate Tribunal ("Tribunal" in short). The Tribunal allowed the assessee's appeals and set aside the orders of the Commissioner of Income Tax (Appeals). Hence, the present tax cases by the Revenue.

4. Learned standing counsel appearing for the Revenue submitted that the assessee had set off interest earned, prior to the commencement of the business operation, against the expenses. The assessee is wrong in setting off the interest prior to the commencement of the business operation against the expenses. The interest income earned prior to the commencement of the business has to be assessed under the head "Income from other sources". Hence, the Assessing Officer is right in assessing the interest income under the head "Income from other sources".

5. Heard counsel. The Tribunal allowed the appeals by following its own earlier order and accepted the contention of the assessee. The Tribunal, in its order, held as follows:

5. Before me learned Counsel for the assessee also relied on the decision of the Supreme Court in the case of Commissioner of Income Tax, Karnataka Vs. M/s. Karnataka Power Corporation, wherein it was held that interest receipts/hire charges received during pre-production is on capital account. Learned Counsel for the assessee also relied on various decisions in support of his case, At the time of hearing he had also filed a copy of the order of this Tribunal in I.T.A. No. 1369/Mds/02, dated November 11, 2002, wherein on identical issue the Tribunal considering the various Supreme Court decisions observed and held as under:

4. The Supreme Court in Tuticorin Alkali Chemicals and Fertilizers Ltd., Madras Vs. Commissioner of Income Tax, Madras, was considering investment of borrowed funds prior to commencement of business and held that the interest earned was taxable. In Commissioner of Income Tax Bihar-II Patna Vs. Bokaro Steel Limited, Bokaro, it was a case of a Government company which during the

period of construction of the plant had advanced monies to contractors on which it was earning interest, received rent from quarters let out to employees, received hire charges on plant let out to contractors and received royalty on stones removed from the assessee's lands. The Supreme Court considered all these activities to be intricately connected with the construction activity and accordingly held that interest received, rent received, hire charges and royalty, etc., would be reduced from the cost of the assets and it would not be treated as income. Similar view was expressed by the Supreme Court in the case *Karnal Co-operative Sugar Mills Ltd.* [2000] 243 ITR 2. Identical view was also taken by the Supreme Court in the cases of *Bongaigaon Refinery and Petrochemicals Ltd.* [2001] 251 ITR 329 and *Karnataka Power Corporation* [2001] 247 ITR 268.

5. In our opinion, in view of the above clear cut ruling by the Supreme Court it is necessary to give a finding of fact in regard to monies that were kept in deposit from out of the share application monies. In the light of the Supreme Court decision in *Tuticorin Alkali Chemicals and Fertilizers Ltd.* [1997] 227 ITR 172, it is only in the event of interest earned from out of deposits made from borrowed funds that it would be in the nature of income. Share application monies do not fall into the category of borrowed funds and do not involve payment of interest. In effect share application monies, etc., are gathered for being used in setting up of an industry, unit, purchase of assets, and so on. Till such time the money is required for deferment of various items, obviously the money has to be kept in deposit with a bank. Keeping the money in current account would not yield any interest income. It can, therefore, be seen that it is during the course of construction that the monies are kept in deposits with the bank. In these circumstances in the light of the Supreme Court decisions in the cases of *Commissioner of Income Tax Bihar-II Patna Vs. Bokaro Steel Limited, Bokaro*, , *Commissioner of Income Tax Vs. Karnal Co-operative Sugar Mills Ltd.*, and *Commissioner of Income Tax, Karnataka Vs. M/s. Karnataka Power Corporation*, , the claim of the assessee is reasonable and deserves to be accepted. We accordingly uphold the claim of the assessee and delete the addition of interest made to the income. The legal plea was not insisted upon.

6. From a reading of the above, it is seen that the Tribunal has followed the principles enunciated in the Supreme Court judgments in the case of *Commissioner of Income Tax Bihar-II Patna Vs. Bokaro Steel Limited, Bokaro*, and in the case of *Commissioner of Income Tax, Karnataka Vs. M/s. Karnataka Power Corporation*, , and came to the correct conclusion. The Revenue is unable to give any further materials or evidence and also not able to furnish information as to whether they have filed any appeal against their earlier order or not.

7. Under the circumstances, we do not find any error or legal infirmity in the order of the Tribunal so as to warrant interference.

8. Hence, no substantial question of law arises for consideration of this Court and accordingly the tax cases are dismissed. Consequently, M.P. No. 1 of 2007 in T.C. (A) No. 610 of 2007 is closed. No costs.