

**आयकर अपीलीय अधिकरण, कटक न्यायपीठ, कटक**

IN THE INCOME TAX APPELLATE TRIBUNAL CUTTACK BENCH CUTTACK  
BEFORE SHRI N.S.SAINI, AM & SHRI PAVAN KUMAR GADALE, JM

आयकर अपील सं./ITA Nos.429/CTK/2016,  
68/CTK/2017 & 107/CTK/2018

(निर्धारण वर्ष / A.Ys :2011-2012, 2013-2014 & 2014-2015)

MJSJ Coal Limited, At/PO:Balanda, Talcher, Dist-Angul, Odisha-759116	Vs.	ITO, Ward-2, Dhenkanal / ITO, Ward-1(3), Bhubaneswar
स्थायी लेखा सं./जीआइआर सं./PAN/GIR No. : <b>AAGCM 1095 E</b>		
(अपीलार्थी /Appellant)	..	(प्रत्यर्थी / Respondent)

निर्धारित की ओर से /Assessee by : Shri K.K.Bal, AR

राजस्व की ओर से /Revenue by : Shri Subhendu Dutta, CITDR

सुनवाई की तारीख / Date of Hearing : **28/08/2018**

घोषणा की तारीख/Date of Pronouncement **31/08/2018**

**आदेश / ORDER**

**Per Shri Pavan Kumar Gadale, JM:**

These are the appeals filed by the assessee against the separate orders of CIT(A)-1&3, Bhubaneswar, dated 28.04.2016, 04.11.2016 & 04.12.2017 passed in I.T.Appeal Nos.0120/2014-15, 0472/15-16 and 0254/16-17, for the assessment years 2011-2012, 2013-2014 & 2014-2015.

2. Since issues the above appeals are common, therefore, they are heard together and disposed off by this consolidated order. For the sake of convenience we shall take up assessee's appeal i.e. ITA No.429/CTK/2016 for assessment year 2011-2012 and the grounds and facts mentioned therein, wherein the assessee has raised the following grounds of appeal :-

*GROUND OF APPEAL*

- We are not agreeing with the computation of tax on interest earned by company made by assessing officer.
- During the assessment, the cases we submitted to justify our claim (as mentioned in statement of facts) has not been paid any emphasis for deciding the case by the A.O and CIT (Appeal-3), Bhubaneswar. On the other hand the A.O and CIT (Appeal-3) finally imposed his decision based on the facts of Alkali Tuticorin Chem. And fertilizers Ltd. in which it has earned interest on the funds, were borrowed funds only

Whereas in our case the money which was deposited, is the amount contributed by the shareholders towards Equity Share Capital for the purpose strictly capital in nature, for mining project and it is clarified that "Interest on short term deposits of capital receipts [share capital money (equity)] is capital receipt only and not taxable." The main objective of our Company owned by Govt. of India is Coal production which boosts to Indian economy, Social lifestyle of citizen of India & help in every sector / society which basic core raw material is coal. The company is not even commenced its coal production till date.

As per Supreme Court & HC: Above type of capital receipts (similar to our case) is not taxable and this is "inextricably linked" to the setting up of the business. Such income is to be treated as capital receipt is required to be capitalized to be set off against pre-operative expenses. (case laws attached for reference) (CIT Vs. Bokaro Steel Ltd. (1999) 236 ITR 315 Supreme Court, Pr. CIT Vs. FACOR POWER LTD ITA 1011/2015, Jdg.07-01-2016, HC Delhi and etc)

- Hence, the amount which is deposited in our banks shall not be seen as borrowed funds as in the case of Tuticorin Alkali Chemicals and Fertilizers Ltd v. CIT (1997) 227 ITR 172 (SC) (as this is a revenue nature income and taxable as per SC). In Alkali CFL, the objective of borrowed fund is to earn interest income but not in our case. In that case it is to state that the said company has borrowed funds and utilized as short term deposits to earn interests, and in our case is Capital fund, so this case is not similar to our case, because the nature of Capital fund and borrowed fund is different. So taxation is also different

In our present case, This should be decided on the basis of nature of principle (equity, not through borrowings) and "inextricably linked" to the setting up of the business including objective and it is similar to case "Pr. CIT Vs. FACOR POWER LTD ITA 1011/2015, Jdg.07-01-2016, HC Delhi", " CIT Vs. Bokaro Steel Ltd. (1999) 236 ITR 315 Supreme Court" and etc.

The following cases are enlisted to justify our claim for Refund as under. –

- 1- CIT Vs. Bokaro Steel Ltd. (1999) 236 ITR 315 SC

- 2- Pr. CIT Vs FACOR POWER LTD ITA 1011/2015, Jdg.07-01-2016, HC Delhi
- 3- ITO Vs Facor Power Ltd(TTAT Delhi VTTA No.4300/DEL/2012,Date of Decision: 10.06.2015.
- 4- CIT Vs. Jaypee DSC Ventures Ltd. ITA 357/2010 HC Delhi
- 5- CIT Vs Saraswati kunj Co. op Housing Building Society( 2006 287 ITR 22) HC Delhi
- 6- CIT Vs Arihant Thread Ltd.(2011)-49 DTR(T&H 251)
- 7- CIT Vs NTPC Sail Power Co. Ltd. ITS 1238/2011 HC Delhi
- 8- CIT v. Govinda Choudhury and Sons (1993) 203 ITR 881 (SC)
- 9- CIT v. Madhya Bharat Energy Corporation Ltd. (2011)337ITR 389 (Del)
- 10- Indian Oil Panipat Power Consortium Ltd. v. ITO (2009) 315 ITR 255 (Del) 1 I-Mazagaon Dock Ltd v. CIT/Excess Profits Tax (1958) 34 ITR 368 (SC),
- 12- Narain Swadeshi Weaving Mills v. Commissioner of Excess Profits Tax (1954) 26 ITR 765 (SC)
- 13- S.G. Mercantile Corporation P. Ltd v. CIT (1972) 83 ITR 700 (SC).

- *The imposed demand is prejudicial and offers unnecessary hardship on us, since our affairs is still lying on the verge of development only, we do not have commenced yet.*

- *We have the valid reason for taking that interest earned (Rs 91,56,600.00 and TDS of Rs 12,72,540.00,Tax Demand of Rs 22,33,130.00) is for capitalization in our books and further utilization into acquisition of Capital assets or any other similar purposes, by the way of interest or in any other manner on funds which are otherwise "inextricably linked" to the setting up of the business, such income is to be treated as capital receipt is required to be capitalized to be set off against pre-operative expenses. As in our case the operations is still lying in the developmental phase and therefore our plea shall be accepted and necessary refund shall be processed in the said case (i.e. A.Y.2011-12).*

- *We are genuine in the eye of law and followed valid procedure for computation of tax for refund as per laws.*

- *In preview of the case reference mentioned by AO & CIT (Appeal-3) regarding Tuticorin Alkali Chemicals and Fertilizers Ltd v. CIT (1997) 227 ITR 172 (SC). The said company has borrowed funds and utilized to in short term deposits to earn interests with the bank which is difficult to follow the reasoning of earning income on such capital receipts. Whereas in our case the money which was deposited, is the amount contributed by the shareholders towards Equity Share Capital for the purpose strictly capital in nature for mining project which is main objective of the company owned by Govt, of India Hence, the amount which is deposited in our banks shall*

*not be seen as borrowed funds as in the case of Alkali Tuticorin Chem. And fertilizers ltd.*

- *Since the project for which MJSJ Coal Ltd. was established was not even commenced till date, the amounts which are deposited in the bank and finally generated interest cannot be named as Surplus funds. And such amount is only Equity Capital, shall be utilized for the mining developments and capital expenditures only in future after obtaining clearance from the Central Govt, and State Govt, as well.*
- *Therefore we believe our plea has been, misconstrued the ratio of judgments of the court cases we submitted earlier ( i.e. A.Y.2011-12) mentioned above. The ratio of the Supreme Court judgment in Bokaro Steel Ltd. (1999) 236 ITR to our mind is that if income earned by the way of interest or in any other manner on funds which are otherwise "inextricably linked" to the setting up of the business, such income is to be treated as capital receipt is required to be capitalized to be set off against pre-operative expenses. As in our case the operations is still lying in the developmental phase and therefore our plea shall be accepted and necessary refund shall be processed in the said case (i.e. A.Y.2011-12).( The latest case is attached for your reference " CIT Vs FACOR POWER LTD ITA 1011/2015, Jdg.07-01-2016, HC Delhi")*
- *Therefore the tax refund claimed Rs 35,05,670.00 (as TDS of Rs 12,72,540.00 and Tax demand paid of Rs 22,33,130.00) on interests earned is of capital nature . This is "inextricably linked" to the setting up of the business (please refer the case of Bokaro Steel Ltd. (1999) 236 ITR and the latest decision of "Pr. CIT Vs FACOR POWER LTD ITA 1011/2015, Jdg.07-01-2016, HC Delhi") and shall be refunded to us , because such income is to be treated as capital receipt is required to be capitalized and to be set off against pre-operative expenses. As in our case the operations is still lying in the developmental phase and therefore our plea shall be accepted and necessary refund shall be processed in the said case (i.e. A.Y.2011-12).*

*Hope above ground of appeal is valid for taking the matter in appeal."*

3. Brief facts of the case are that the assessee is a joint venture and subsidiary of Mahanadi Coal Field Ltd. incorporated in the year 2008-09 to carry on the business of coal mining. The partners in the venture are Mahanadi Coal Field having 60% share holding, M/s JSW Ltd. having 11% share holding, M/s JSW Energy Ltd. having 11% share holding, M/s

Shyam Mettalics and Energy Ltd. having 9% share holding and M/s Jindal Stainless Ltd. having 9% share holding. Since the process of land acquisition for extraction of coal and geological survey was under process, the assessee company was yet to commence its commercial production in the said financial year, whereas the assessee company has filed return of income electronically on 24.09.2011 declaring total income at Rs.Nill for the assessment year 2011-2012. Subsequently, the case was selected for scrutiny under CASS and notices u/s.143(2) & 142(1) of the Act were issued to the assessee. In compliance, Id. AR of the assessee appeared before the AO from time to time and produced the books of accounts and other relevant documents. Subsequently AO completed the assessment assessing total income at Rs.94,32,204/- and passed order u/s.143(3) of the Act, dated 18.03.2014 making addition u/s.56 of the Act, on account of interest on bank deposits and expenses of contractual payments, audit fees and hire charges.

4. Aggrieved by the order of AO, the assessee preferred an appeal before the CIT(A). In the appellate proceedings Id. AR reiterated the submissions made before the AO and the CIT(A) after considering the findings of the AO and submission of the assessee partly allowed the appeal of the assessee.

5. Aggrieved by the order of CIT(A) in confirming the addition made under the head income from other sources, the assessee has filed an appeal before the Tribunal.

6. Ld. AR of the assessee before us submitted that the amount deposited in the bank in the form of fixed deposits is contributed by the shareholders towards Equity Share Capital for the purpose of mining project and also interest on short term deposits, is a capital receipt. Ld. AR emphasized that since the project of assessee company is yet to commence its operations, therefore, the assessee company has deposited the amounts in the bank for short term deposits and the interest on fixed deposits cannot be considered as income from other sources. The equity Capital, shall be utilized for the mining developments and incurring of capital expenditures after obtaining clearance from the Central Government and State Government and other agencies. The Id. AR mentioned that the mining operations are in the developmental phase and supported the submissions with judicial decisions and prayed for allowing the appeal of the assessee.

7. Contra, Id.DR relied on the order of lower authorities.

8. We have heard rival submissions and perused the material on record. The sole matrix of the disputed issue is with respect of assessing the interest on bank deposits under income from other sources. In the present case we find the AO in the assessment proceedings observed that the company was formed to set up a mining project and the process of setting up is got delayed and utilization of share capital in bank deposits cannot be considered as inextricably link with the process of setting of its plant and machinery. In appellate proceedings, the CIT(A) confirmed the addition on the ground that the primary objective of holding

the share capital as investment is for purpose of deriving interest income in absence of commencement of business, where the contentions of Id. AR is that when the AO in the assessment proceedings has accepted the fact that the assessee company has not started its commencement of business and temporarily kept the funds in bank as fixed deposits out of the share capital amount which was kept for a specific purpose of utilization for establishment/commencement of the business and therefore, interest earned temporarily on fixed deposits is capital receipt and shall be capitalized in the work in progress and the said interest amount cannot be taxable under income from other sources. The contention of Id.AR is that the reliance placed by the lower authorities of Hon'ble Supreme Court in the case of Tuticorin Alkali Chemicals [1997] 227 ITR 172 (SC) is not applicable to the present facts of the case. In the present case the assessee company has not commenced its business and the interest from bank deposits is duly capitalized under the head work-in-progress as per guidelines and are directly linked/nexus with the activities of setting up the plant and machinery. Therefore, the receipts are inextricably linked with the setting up of the capital structure of the assessee company. We find the Hon'ble Supreme Court in the case of CIT Vs. M/s Shree Rama Multi Tech Ltd., 403 ITR 426 (SC), has held as under :-

*“8. The Respondent company had come out with initial public issue during the year under consideration and the amount of share application money received was deposited with the banks on which interest of Rs. 1,71,30,202/- was earned which was shown in the return of income originally filed as income from other sources which was also referred to in Col. 13(d) of the Tax Audit report filed under*

*Section 44AB of the IT Act. Even though initially the income from the interest was shown as income from other sources in the return of income, however, the Respondent had raised an additional ground before the Tribunal to allow the set off of such interest against the public issue expenses. The issue was examined by the Tribunal and was set aside for fresh adjudication by the Assessing Officer. During the course of fresh proceedings, an opportunity was given to the Respondent to file the details of interest on share application money. The Respondent stated that the details of interest income on share application money was already furnished at Annexure No. 7 of their letter dated 11.03.2003 at the time of original assessment. The verification of the said Annexure reveals that the Respondent had earned the interest income on FDRs placed with the bank, however, the period for which such FDRs were placed and the specific period of the interest earned was not found to have been mentioned. Under the circumstances, it was not possible to identify as to what portion of interest earned on FDRs was relating to the period prior to the allotment of shares or after the allotment of shares. Keeping in view the specific guidelines of the Tribunal in this regard and in the absence of specific working of interest for pre-allotment and post-allotment, the claim of the Respondent was not allowed and added to the total income under the head income from the other sources as was declared in the original return of income filed by the Respondent.*

**9.** *Coming back to the facts of the case, we may reiterate that the Respondent was statutorily required to keep share application money in the separate account till the allotment of shares was completed. Interest earned on such separately kept amount was to be adjusted towards expenditure for raising share capital. We are, therefore, of the opinion that interest earned was inextricably linked with requirement of company to raise share capital and was thus adjustable towards the expenditures involved for the share issue. Though learned counsel for the Appellant contended that part of the share application money would normally have to be returned to unsuccessful applicants, and therefore, the entire share application money would not ultimately be appropriated by the Company, insofar as present case is concerned, we do not see how this factor would make any significant difference. Interest earned from share application money statutorily required to be kept in separate account was being adjusted towards the cost of raising share capital. In that view of the matter, we are of the opinion that the High Court was right in allowing such deduction.*

**10.** *In light of the above developments in the case, the question of law has been decided by this Court in case in Bokaro Steel Ltd. (supra), wherein the company was set up to produce steel. When the construction of plant was yet not completed, company earned interest on advances to contractor, rent from quarters let out to employees of the contractor as well as other income such as hire charges on plant and machinery let out to contractor, royalty on stones removed from its land. It was in this background that this Court held that the amounts were directly connected to and*

*incidental to construction of plant by the company, amounts were capital receipts and not income from any independent source.*

**11.** *Further, the rationale of judgment of Bokaro Steel Ltd. (supra) was followed in CIT v. Karnal Co-operative Sugar Mills Ltd. [2001] 118 Taxman 489/[2000] 243 ITR 2 (SC). In this case, the company had deposited certain amount with the bank to open letter of credit for purchase of machinery for setting up plant. On the money so deposited, it earned interest. In that background, this Court observed that this is not a case where any surplus shares capital money which was lying idle had been deposited in the bank for the purpose of earning interest. The deposit of money is directly linked with the purchase of plant and machinery.*

**12.** *The common rationale that is followed in all these judgment is that if there is any surplus money which is lying idle and it has been deposited in the bank for the purpose of earning interest then it is liable to be taxed as income from other sources but if the income accrued is merely incidental and not the prime purpose of doing the act in question which resulted into accrual of some additional income then the income is not liable to be assessed and is eligible to be claimed as deduction. Putting the above rationale in terms of the present case, if the share application money that is received is deposited in the bank in light of the statutory mandatory requirement then the accrued interest is not liable to be taxed and is eligible for deduction against the public issue expenses. The issue of share relates to capital structure of the company and hence expenses incurred in connection with the issue of shares are to be capitalized because the purpose of such deposit is not to make some additional income but to comply with the statutory requirement, and interest accrued on such deposit is merely incidental. In the present case, the Respondent was statutorily required to keep the share application money in the bank till the allotment of shares was complete. In that sense, we are of the view that the High Court was right in holding that the interest accrued to such deposit of money in the bank is liable to be set-off against the public issue expenses that the company has incurred as the interest earned was inextricably linked with requirement of the company to raise share capital and was thus adjustable towards the expenditure involved for the share issue.*

**13.** *In view of the forgoing discussion, we are of the view that the High Court was right in upholding the decision of the Tribunal dated 21.10.2011 that the interest income earned out of the share application money is liable to be set off against the public issue expenses. The judgment passed by the Division Bench of the High Court in remanding the matter to the Tribunal on other issues requires no interference.*

**14.** *The appeals are accordingly dismissed. The parties to bear their own cost."*

9. Similarly the Hon'ble Delhi High Court in the case of Indian Oil Panipat Power Consortium Limited, New Delhi Vs. ITO, 315 ITR 255 (Delhi), has held as under :-

**3.** *We have heard the learned counsel for the parties at length. Following substantial question of law arises for our consideration :*

*"Whether the Tribunal misdirected itself in law in holding that interest which accrued on funds deployed with the bank could be taxed as income from other sources and not as capital receipt liable to be set off against pre-operative expenses ?"*

*We are called upon to really decide as to whether given the facts obtaining in the assessee's case it would be covered by the line of cases which follow the ratio of the decision of the Supreme Court in Tuticorin Alkali Chemicals (supra) or those which follow the ratio of the Supreme Court in the case of CITv. Bokaro Steel Ltd. [1999] 236 ITR 315. At the outset we must note that the Supreme Court in the case of Bokaro Steel Ltd.'s case (supra) has noticed the judgment of the Supreme Court in Tuticorin Alkali Chemicals & Fertilizers Ltd. case (supra). Therefore, in these circumstances it would be incumbent to note the following brief facts as recorded by the authorities below :*

**3.1** *The assessee-company was incorporated on 6-10-1999 in pursuance of a joint venture entered into between Indian Oil Corporation and Marubeni Corporation of Japan. The joint venture was conceived to set-up a power project at Panipat in the State of Haryana. It was expected that the project would be set-up by the end of the financial year 2000-01. In order to effectuate the purpose for which joint venture was conceived, share capital was contributed by Indian Oil Corporation and Marubeni Corporation of Japan which included Rs. 20 crores by way of additional share capital.*

**3.2** *To be noted that the assessee had taken a stand before the Assessing Officer that these funds were required primarily for purchase of land and development of infrastructure. However, due to legal entanglements with respect to title of land, which the Haryana Government was to acquire for the assessee, in the interregnum, the funds acquired by way of share capital were put in a fixed deposit with the Tokyo Mitsubishi Bank by the assessee.*

**3.3** *The assessee earned interest in the sum of Rs. 1,65,75,906 in assessment year 2001-02 and Rs. 1,54,62,098 in the assessment year 2002-03. As mentioned hereinabove the Assessing Officer applied the ratio of the judgment of the Supreme Court in Tuticorin Alkali Chemicals & Fertilizers Ltd.'s case (supra) and the judgment of the Supreme Court in the case of CIT v. Autokast Ltd. [2001] 248 ITR 110 and held that the interest which accrued to the assessee was assessable under the head "income from other*

sources" and could not be set-off against pre-operative expenses as claimed by the assessee.

**3.4** Aggrieved by the order the assessee preferred an appeal to the CIT(A). The CIT(A) examined the facts in detail. It is pertinent to note that the CIT(A) in paragraph 4 of his Order dated 6-2-2003 categorically found that the funds were placed in fixed deposit so that liquidity was ensured and money would remain available when required for purchase of land and infrastructure development and hence the interest earned was 'inextricably linked' with the setting up of the power plant. Based on this line of reasoning, the CIT(A) applied the judgment of the Supreme Court in Bokaro Steel Ltd.'s case (supra) and allowed the claim of the assessee by directing the Assessing Officer to delete the addition and consider the same for capitalization towards pre-operative expenses.

**3.5** The Tribunal in an appeal preferred by the Revenue, by virtue of the impugned judgment, has reversed the decision of the CIT(A).

**4.** It is important to note that the Tribunal without holding that the finding of fact of the CIT(A), that the interest earned was 'inextricably linked' with the setting up of the power plant reversed the decision of the CIT(A) by making a bald observation that the "deposit of share capital has no or very remote connection with setting up of plant and machinery". The Tribunal further observed that it was an independent income earned in a similar fashion as was the case in Tuticorin Alkali Chemicals & Fertilizers Ltd.'s case (supra).

**5.** In our opinion the Tribunal has misconstrued the ratio of the judgment of the Supreme Court in the case of Tuticorin Alkali Chemicals & Fertilizers Ltd.'s case (supra) and that of Bokaro Steel Ltd. (supra). The test which permeates through the judgment of the Supreme Court in Tuticorin Alkali Chemicals & Fertilizers Ltd.'s case (supra) is that if funds have been borrowed for setting up of a plant and if the funds are 'surplus' and then by virtue of that circumstance they are invested in fixed deposits the income earned in the form of interest will be taxable under the head 'income from other sources'. On the other hand the ratio of the Supreme Court judgment in Bokaro Steel Ltd.'s case (supra) to our mind is that if income is earned, whether by way of interest or in any other manner on funds which are otherwise 'inextricably linked' to the setting up of the plant, such income is required to be capitalized to be set off against pre-operative expenses.

**5.1** The test, therefore, to our mind is whether the activity which is taken up for setting up of the business and the funds which are garnered are inextricably connected to the setting up of the plant. The clue is perhaps available in section 3 of the Act which states that for newly set-up business the previous year shall be the period beginning with the date of setting up of the business. Therefore, as per the provision of section 4 of the Act which is the charging section income which arises to an assessee from the date of setting up of the business but prior to commencement is chargeable to tax

depending on whether it is of a revenue nature or capital receipt. The income of a newly set-up business, post the date of its setting up can be taxed if it is of a revenue nature under any of the heads provided under section 14 in Chapter IV of the Act. For an income to be classified as income under the head "profit and gains of business or profession" it would have to be an activity which is in some manner or form connected with business. The word "business" is of wide import which would also include all such activities which coalesce into setting up of the business. See *Mazagaon Dock Ltd. v. CIT & EPT* [1958] 34 ITR 368 (SC), and *Narain Swdeshi Weaving Mills v. CEPT* [1954] 26 ITR 765 (SC). Once it is held that the assessee's income is an income connected with business, which would be so in the present case, in view of the finding of fact by the CIT(A) that the monies which were inducted into the joint venture company by the joint venture partners were primarily infused to purchase land and to develop infrastructure - then it cannot be held that the income derived by parking the funds temporarily with Tokyo Mitsubishi Bank, will result in the character of the funds being changed, inasmuch as, the interest earned from the bank would have a hue different than that of business and be brought to tax under the head 'income from other sources'. It is well-settled that an income received by the assessee can be taxed under the head "income from other sources" only if it does not fall under any other head of income as provided in section 14 of the Act. The head "income from other sources" is a residuary head of income. See *S.G. Mercantile Corpn. (P.) Ltd. v. CIT* [1972] 83 ITR 700 (SC) and *CIT v. Govinda Choudhury & Sons* [1993] 203 ITR 881 (SC).

**5.2** It is clear upon a perusal of the facts as found by the authorities below that the funds in the form of share capital were infused for a specific purpose of acquiring land and the development of infrastructure. Therefore, the interest earned on funds primarily brought for infusion in the business could not have been classified as income from other sources. Since the income was earned in a period prior to commencement of business it was in the nature of capital receipt and hence was required to be set off against pre-operative expenses. In the case of *Tuticorin Alkali Chemicals & Fertilisers Ltd. (supra)* it was found by the authorities that the funds available with the assessee in that case were 'surplus' and, therefore, the Supreme Court held that the interest earned on surplus funds would have to be treated as 'income from other sources'. On the other hand in *Bokaro Steel Ltd.'s case (supra)* where the assessee had earned interest on advance paid to contractors during pre-commencement period was found to be 'inextricably linked' to the setting up of the plant of the assessee and hence was held to be a capital receipt which was permitted to be set off against pre-operative expenses.

**6.** There is another perspective from which the present issue can be examined. Under section 208 of the Companies Act, 1956 a company can pay interest on share capital which is issued for a specific purpose to defray expenses for construction of any work

and which cannot be made profitable for a long period subject to certain restrictions contained in sub-sections (2) to (7) of section 208. This section was specifically noted by the Supreme Court in *Challapalli Sugars Ltd. v. CIT* [1975] 98 ITR 167. The Supreme Court went on to observe as follows:

*"We have already referred to section 208 of the Companies Act which makes provision for payment of interest on share capital in certain contingencies. Clause (b) of sub-section (1) of that section provides that in case interest is paid on share capital issued for the purpose of raising money to defray the expenses of constructing any work or building or the provision of any plant in contingencies mentioned in that section, the sum so paid by way of interest may be charged to capital as part of the cost of construction of the work or building or the provision of the plant. The above provision thus gives statutory recognition to the principle of capitalizing the interest in case the interest is paid on money raised to defray expenses of the construction of any work or building or the provision of any plant in contingencies mentioned in that section even though such money constitutes share capital. The same principle, in our opinion, should hold good if interest is paid on money not raised by way of share capital but taken on loan for the purpose of defraying the expenses of the construction of any work or building or the provision any plant. The reason indeed would be stronger in case such interest is paid on money taken on loan for meeting the above expenses." (p. 175)*

**6.1** *In our view the situation in the instant case is quite similar except here instead of paying interest on funds brought in for specific purpose interest is earned on funds brought in by way of share capital for a specific purpose. Could it be said that in the former situation interest could have been capitalized and in the later situation it cannot be capitalized. To test the principle we could extend the example, that is, would our answer be any different had assessee passed on the interest to the respective shareholders. If not, then in our view the only conclusion possible is that interest earned in the present circumstances ought to be capitalized.*

**7.** *In view of the discussion above, in our opinion the Tribunal misdirected itself in applying the decision of the Supreme Court in *Tuticorin Alkali Chemicals & Fertilizers Ltd.'s case* (supra) in the facts of the present case. In our opinion on account of the finding of fact returned by the CIT(A) that the funds infused in the assessee by the joint venture partner were inextricably linked with the setting up of the plant, the interest earned by the assessee could not be treated as income from other sources. In the result we answer the question as framed in favour of the assessee and against the revenue. These appeals are allowed and the impugned judgment is set aside.*

10. We also find similar issue was dealt by the coordinate bench of the Tribunal in the case of POSCO-India Pvt. Ltd. Vs. DCIT, ITA Nos.186,462&461/CTK/2011, dated 14.02.2013, where the Tribunal has observed that, the head "income from other sources" is a residuary head of income. In the present case, on perusal of the facts and application of judicial decisions, there share capital were infused in the company for a specific purpose of acquiring land and the development of infrastructure and therefore, the interest earned on funds primarily brought for infusion in the business could not have been classified as 'income from other sources'. Since the income was earned in a period prior to commencement of business, it in the nature of capital receipt and, hence, set off against pre-operative expenses. The observations of the Tribunal at para 5 read as under :-

*"5. We have heard the rival parties and perused the material available on record. On our careful consideration of the facts and circumstances of case as brought on record by the authorities below, we are inclined to find the contention of the learned Counsel of the assessee appropriate to the extent that it was never a change of stance on the facts remaining the same beginning from Assessment Year 2006-07. It was a misconstruction of the facts for the purpose of finding applicability of the provisions of law enunciated by the Hon'ble Apex Court in the case of Tuticorin Alkali Chemicals & Fertilizers Ltd v. CIT (supra). The law enunciated in the case of Tuticorin Alkali Chemicals & Fertilizers Ltd v. CIT(supra) cannot alone be considered as favoring Revenue insofar as it also talks about capitalization of the interest and the circumstances, which circumstances have been dealt with by the Hon'ble Delhi High Court in the case of India Oil Panipat Power Consortium Ltd v. ITO (supra) and further more in the case of NTPC Sail Power Company Pvt. Ltd., v. CIT decided on 17.07.2012 in ITA No.1238/2011 (copy placed on record) which has also been relied on by the learned Counsel of the assessee. The learned Counsel of the assessee has submitted the financial statements duly audited under the provisions of the I.T.Act as well as under the Companies Act which have been verified by the Assessing Officer requiring no reference to be made to the Transfer Pricing Officer under the provisions of Section 92CA. In other words, no business*

*income has been generated by the assessee. The expenditure claimed therefore was only for the purpose of setting up the project envisaged and there is no method for balancing interest, if any, passed on to the share holders on account of dividend or business income by the assessee. The test, therefore, to our mind is whether the activity which is taken up for setting up of the business and the funds which are garnered are inextricably connected to the setting up of the plant. The clue is perhaps available in section 3 of the Act which states that for newly set up business the previous year shall be the period beginning with the date of setting up of the business. Therefore, as per the provision of Section 4 of the Act which is the charging section income which arises to an assessee from the date of setting of the business but prior to commencement is chargeable to tax depending on whether it is of a revenue nature or capital receipt. The income of a newly set up business, post the date of its setting up can be taxed if it is of a revenue nature under any of the heads provided under section 14 in Chapter IV of the Act. For an income to be classified as income under the head "Profits and gains of business or profession" it would have to be an activity which is in some manner or form connected with business. The word "business" is of wide import which would also include all such activities which coalesce into setting up of the business. Once it is held that the assessee's income is an income connected with business, which would be so in the present case, in view of the finding of fact by the Commissioner of Income-tax (Appeals) that the monies which were inducted into the joint venture by the Koreans were primarily infused to purchase land and to develop infrastructure then it cannot be held that the income derived by parking the funds temporarily with Bank, will result in the character of the funds being changed, inasmuch as, the interest earned from the bank would have a hue different than that of business and be brought to tax under the head "Income from other sources". It is well-settled that an income received by the assessee can be taxed under the head "Income from other sources" only if it does not fall under any other head of income as provided in section 14 of the Act. The head "Income from other sources" is a residuary head of income. In the instant case, it was clear upon a perusal of the facts as found by the authorities below that the funds in the form of share capital were infused for a specific purpose of acquiring land and the development of infrastructure. Therefore, the interest earned on funds primarily brought for infusion in the business could not have been classified as 'income from other sources' Since the income was earned in a period prior to commencement of business, it was in the nature of capital receipt and, hence, was required to be set off against pre-operating expenses. We are inclined to find a meaning to the insertion of the proviso to Section 36(l)(iii) that interest paid, in respect of capital borrowed for acquisition of an asset for extension of existing business or profession was being allowed as deduction u/s.36(l)(iii) of the Act as revenue expenditure was amended w.e.f. 1.4.2004 when the amount of interest paid in respect of capital borrowed for acquisition of an asset for extension of existing business or profession whether*

capitalized in the books of account or not for any period beginning from the date on which the capital was borrowed for acquisition of the asset till the date on which such asset was first put to use, shall not be allowed as deduction, holds true for the income insofar as once having identified that the income from interest is from the Banks where the share capital was parked was to not earn interest to be balanced interest on capital borrowed when the assessee's own funds were being utilised for the purpose of incurring the project cost which took undue delay due to Government and other interference. In the case of Tuticorin Alkali Chemicals & Fertilizers Ltd v. CIT (supra), Hon'ble Apex Court has held - "if the company, even before it commences business, invests the surplus funds in its hands for purchase of land or house property and later sells it at profit, the gain made by the company will be assessable under the head 'Capital gains'. Similarly, if a company purchases a rented house and gets rent, such rent will be assessable to tax under section 22 as income from house property. Likewise, a company may have income from other sources.....The company may also, as in that case, keep the surplus funds in short-term deposits in order to earn interest. Such interest will be chargeable under section 56 of the Income-tax Act". Subsequently Hon'ble Apex Court in the case of CIT v. Bokaro Steel Ltd (supra) held - "However, while interest earned by investing borrowed capital in short-term deposits is an independent source of income not connected with the construction activities or business activities of the assessee, the same cannot be said in the present case where the utilisation of various assets of the company and the payments received for such utilisation are directly linked with the activity of setting up the steel plant of the assessee. These receipts are inextricably linked with the setting up of the capital structure of the assessee company. They must, therefore, be viewed as capital receipts going to reduce the cost of construction. " Merits for consideration as brought on record for the AYs in appeal before us are as under :

Particulars.	As on 31.3.2006	As on 31.3.2007	As on 31.3.2008
1. Share Capital	22500.00	22500.00	22500.00
2. Land (CW1P)	307.00	664.74	1440.85
3. In Bank Deposit.	19190.00	1289.00	-
4. Interest from Bank	637.44	1,04.17	432.67
5. Pre-operative Expenses.	629.76	3736.28	5280.69

The returns filed by the assessee for the AYs 2006-07 and 2007-08 clearly indicate that the assessee at no point of time was having income from other sources irrespective of the accounting of the income having been capitalized when the claim of expenditure of 10% was purely on estimation when apparently it was not the business of the assessee to earn income but parking of its funds when the interest income sought to be considered exempt for computing expenditure under the provisions of Section 14A for the purpose of I.T.Act. The learned Counsel of the assessee, therefore,

*has clarified that the assessee cannot be subjected to taxation in the impugned Assessment Year on the interest income capitalized and at the same time allow amortization thereof in the hope that project will see the light of the day in the years to come when the I.T.Department will allow less deduction than otherwise claimed will be multiplication of assessments for no fault of the assessee appellant. We are therefore inclined to hold that the learned Counsel of the assessee has submitted a bulk Paper Book which inter alia correlates to earning of interest on the amounts deposited in the Banks to be utilised for the purpose of business of the assessee as per the project envisaged and as per the project approved by the Government of Orissa but taken time due to reason beyond the assessee's control insofar as sanction and authorization have taken its toll when the fact finding is whether capitalization by reducing the preoperative expenses could be isolated for the purpose of taxation as income from other sources following the case laws annunciated by Hon'ble Supreme Court in the case of Tuticorin Alkali Chemicals & Fertilizers Ltd v. CIT (supra) when again Hon'ble Apex Court have clarified the stand in the case of CIT v. Bokaro Steel Ltd (supra) was whether the business of the assessee was to claim the expenditure incurred for earning of such interest having been adjusted against the other expenses incurred rather leans in favour of the assessee to the extent that the interest was inextricably linked to the expenditures incurred which project cost did not require further approval but was taking time which time earned interest to the assessee when recoding expenditure have been claimed from the interest earned for consideration of 10% thereof was not to be disturbed at all. In this view of the matter, we are of the considered view that for the Assessing Year 2008-09 the interest cannot be taxed as income from other sources in the hands of the assessee and therefore, the subsequent disallowance of expenses claimed at 10% to earn that income has been infused in the total project cost cannot be disallowed insofar as the whole of the income has been capitalized was rightly considered for revision by the assessee before the Assessing Officer filing NIL return. The appeal for the Assessment Year 2008-09, therefore, is allowed on the basis of facts and figures brought on record by the Assessing Officer as well as the learned CIT(A) and as mentioned above. However in view of the principles laid out above, we are inclined to restore the issue to the file of the Assessing Officer for the Assessment Year s 2006-07 and 2007-08 to consider the case of the assessee de novo on establishing the fact that the interest has been earned on the parking of share capital and not any surplus generated as was considered by the Hon'ble Apex Court insofar as the earning of interest has been capitalized by reducing the project cost to be amortized has to be considered as a nullity after verification. Needless to say, an opportunity of being heard to the assessee be granted to establish the fact as have been narrated before us in the light of Assessment Year 2008-09 when it is not a change of stance as contested by the learned DR but on the same set of facts the interest portion cannot be isolated for the purpose of taxation.”*

11. Recently, this bench of the Tribunal in the case of POSCO-India Private Limited, in ITA Nos.403&344/CTK/2017, vide order dated 27.07.2018, wherein the CIT(A) has dealt on the disputed issue and observed that interest on FDs cannot be taxed in the hands of the assessee u/s.56 of the Act and the Tribunal confirmed the findings of the CIT(A).

12. We find that the funds of the assessee company kept in the short term fixed deposits out of the share capital amount and not any surplus arising out of the running business, the interest earned on funds primarily brought for infusion in the business activity cannot be termed as income from other sources, whereas the interest income on bank deposits earned by the assessee company to commencement of its business is in the nature of capital receipt and accordingly be set off against pre-operative expenses. We considering the judicial precedence and the facts and circumstances of the present case, are of the substantive opinion that if the assessee company receives any amount which is inextricably linked with the process of setting up its plant and machinery, such receipts will go to reduce the cost of its assets. Hence such receipts are capital in nature and cannot be taxed as income under income from other sources. The assessee company was formed to set up a mining project and the process of setting up was got delayed and deposits of share capital amount received from the share applicants with the bank in the form of fixed deposits for short term, is to be considered as inextricably linked with the process of setting of its plant and machinery. Accordingly, we hold

that the interest earned by the assessee should not be treated as income from other sources and we allow the grounds of appeal of the assessee. Therefore, the appeal of the assessee for assessment year 2011-2012 is allowed.

13. Now, we shall take up the appeals of the assessee in ITA No.68/CTK/2017 & ITA No.107/TK/2018. Similar grounds have been raised by the assessee in its appeals for the assessment years 2013-2014 & 2014-2015, wherein the sole grievance of the assessee is that the CIT(A) erred in treating the interest income to be taxed under income from other sources. We have already decided the issue in favour of the assessee while considering the appeal of the assessee in ITA No.429/CTK/2018 for the assessment year 2011-2012, wherein we have held that interest income earned by the assessee could not be treated as income from other sources. Therefore, our observations in the aforesaid appeal for the assessment year 2011-2012, shall apply *mutatis mutandis* to the appeals of the assessee for assessment years 2013-2014 & 2014-2015 in ITA No.68/CTK/2017 and ITA No.107/CTK/2018, respectively.

14. Thus, all the three appeals of the assessee are allowed.

Order pronounced in the open court on this 31/08/ 2018.

**Sd/-**  
**(N.S.SAINI)**

लेखा सदस्य / ACCOUNTANT MEMBER

**Sd/-**  
**(PAVAN KUMAR GADALE)**

न्यायिक सदस्य / JUDICIAL MEMBER

कटक Cuttack; दिनांक Dated 31/08/2018

प्र.कु.मि/PKM, Senior Private Secretary

**आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :**

1. अपीलार्थी / The Appellant-
2. प्रत्यर्थी / The Respondent-
3. आयकर आयुक्त(अपील) / The CIT(A),
4. आयकर आयुक्त / CIT
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, कटक / DR, ITAT, Cuttack
6. गार्ड फाईल / Guard file.

सत्यापित प्रति //True Copy//

आदेशानुसार/ BY ORDER,

**(Senior Private Secretary)**

आयकर अपीलीय अधिकरण, कटक /  
ITAT, Cuttack