

IN THE INCOME TAX APPELLATE TRIBUNAL  
BANGALORE BENCHES “ A ” BENCH: BANGALORE  
**BEFORE SHRI A.K. GARODIA, ACCOUNTANT MEMBER  
AND  
SHRI PAVAN KUMAR GADALE, JUDICIAL MEMBER**

ITA No.1348/Bang/2019  
(Assessment Year: 2014-15)

Asst. Commissioner of Income Tax,  
Circle 4(1)(1), Bangalore-560095

....Appellant

Vs.

M/s. Kappec Ltd.,  
No.17, General K S Thimmaiah Road,  
Richmond Road, Bangalore.

.....Respondent.

Assessee By:	None.
Revenue By:	Shri A. Ramesh Kumar, JCIT(D.R)

Date of Hearing :	02.03.2020
Date of Pronouncement :	06.03.2020

**ORDER**

**PER SHRI PAVAN KUMAR GADALE, JM :**

The revenue has filed an appeal against the order of Commissioner of Income Tax (Appeals)-12, Bangalore passed under Section 143(3) and 250 of the Income Tax Act, 1961 ('the Act').

2. The revenue has raised the following grounds of appeal:

1. The Order of the Ld.CIT (A) is opposed to the law and facts of the case.
  2. Whether on the facts and circumstances of the case, the Ld. CIT(A) ought to have appreciated that the interest received on the grants received from Government of Karnataka is an income in the hands of the company.
  3. Whether on the facts and circumstances of the case, the Ld. CIT(A) was justified in giving relief to the assessee on the basis of decision of Hon'ble High Court of Karnataka in assessee's own case which has not been accepted by the Department and further appeal is pending as SLP before Hon'ble Supreme Court.
  4. For these and other grounds that may be urged at the time of hearing, it is prayed that the order of the CIT (A) in so far as it relates to the above grounds may be reversed and that of the Assessing Officer may be restored.
  5. The appellant craves leave to add, alter, amend and/or delete any of the grounds that may be urged.
3. The Brief facts of the case are that, the assessee company is engaged in trading of agricultural products and filed the Return of Income for the Assessment Year 2014-15 on 17.09.2014 with total income of Rs.5,79,23,958/-.Subsequently the case was selected for scrutiny and notice under Section 143(2) and 142(1) of the Act were issued. In compliance, the learned Authorized Representative appeared from time to time and filed the details. The assessee company is a public sector company established by the Government of Karnataka to trade on

agricultural products and through approved channelized agents of seeds, onions etc. The Assessing Officer based on the details filed by the assessee, found that the assessee has a Bank Balance as per Balance Sheet of Rs.34.71 Crores including deposits with Banks of Rs.33.11 Crores. The Assessing Officer issued show cause notice to treat the interest on Fixed Deposits (FDs) as income from other sources. Further, the Assessing Officer observed that the interest component cannot be treated as grant-in-aid and dealt at Para 4 to 4.3 of the order and taxed the entire interest earned by the assessee on FDs are out of the grant-in-aid as income from other sources and assessed the total income of Rs.9,03,66,445/- and passed the order under Section 143(3) of the Act dt.28.12.2016. Aggrieved by the order, the assessee has filed an appeal with the CIT(Appeals), whereas the CIT(Appeals) considering the grounds of appeal, findings of Assessing Officer and submissions of the assessee on the disputed issue observed that the interest on FDs cannot be treated as 'income from other sources' relying on the judicial decisions and allowed the assessee appeal. Aggrieved by the order of CIT(Appeals), the revenue has filed an appeal before the Tribunal.

4. At the time of hearing, the learned Departmental Representative submitted that the CIT(Appeals) has erred in deleting the disallowance of interest made by the Assessing Officer as the decision of Hon'ble High Court of Karnataka in the case of CIT & Anr. Vs. Karnataka Urban Infrastructure & Finance

Corporation(Karnataka)(284 ITR 582) relied on by the CIT(Appeals) was challenged by the revenue and the Revenue has filed SLP before the Hon'ble Supreme Court. Contra, the LdAr supported the orders of CIT(Appeals).

5. We heard the rival contentions and perused the material on record. The sole disputed issue argued by the Id.DR that the CIT(Appeals) has granted relief without appreciating the fact that the interest on fixed deposits with bank are out of the grant-in-aid received from the Govt. of Karnataka and is taxable in the hands of the assessee. Further the decision relied by the CIT(Appeals) of Hon'ble High Court of Karnataka is challenged before the Hon'ble Supreme Court in SLP by the Revenue. We found that the revenue has relied only on the SLP filed before the Hon'ble Supreme Court and the the observations of the CIT(Appeals) at page 3 Para 9 to 15 of the order is read as under :

9. On examination of the judgement and it cannot be denied that the Hon'ble High Court has held that the interests obtained in this case is not taxable. In this case Karnataka Urban Infrastructure & Finance Corporation is a company created and owned by the Government of Karnataka. The Hon'ble high court has clearly propounded in its judgement that **"..It is not the case of the Revenue that the assessee was carrying on any business or activities of its own while implementing the scheme in question.."**

10. In the case of Commissioner of Income Tax vs Karnataka Urban Infrastructure Development Finance Corporation, the Hon'ble High Court of Karnataka held that:

Section 4 of the Income-tax Act, 1961 – Assessee which is a State Government-owned company, was appointed as a nodal agency for implementation of Mega-city Scheme worked out by Planning Commission. Both Central and State Governments provided requisite finances for implementation of said project. Assessee parked money so received in various bank deposits during unutilized

period. Interest earned during year on those deposits was directly transferred to Mega-city Scheme account. Assessing Officer treated interest so earned and received by assessee to be an income of assessee and brought interest amounts to tax. The Hon'ble High Court of Karnataka held that interest accrued on bank deposits could not be treated as income of assessee as interest was earned out of money given by Government of India for purpose of implementation of Mega-city Scheme and interest earned was also utilised for implementation of Mega-city Scheme.

The Judgement in the case is extracted below:

*"1. The Revenue has preferred this appeal against the order passed by the Tribunal, Bangalore Bench in ITA No. 868/Bang/2000 dt. 3rd Nov., 2004 setting aside the orders passed by the assessing authority as well as the first appellate authority holding **that the income earned by the respondent to the tune of Rs. 4,66,75,814 cannot be treated as income liable to tax under the provisions of the IT Act (for short hereinafter referred to as 'the Act')** as the respondent is acting as a nodal agency for implementing certain Central and State Government projects.*

*2. Few facts leading to this appeal, are as under:*

The respondent M/s Karnataka Urban Infrastructure Development and Financial Corporation (for short hereinafter referred to as 'the assessee') is a fully Karnataka State Government owned company. The assessee was appointed as a nodal agency for the implementation of the mega-city scheme worked out by the Planning Commission of Ministry of Urban and Employment for development of urban infrastructure to Bangalore city. The Central Government has provided the money to the assessee for implementing the said scheme. The money so received from the Government of India was parked by the assessee in various bank deposits during the unutilised period. **The interest earned during the year on these deposits were transferred to the mega-city scheme account directly with an appropriate disclosure in the notes to the accounts.** The assessee has been involved in other projects of development of infrastructure apart from the activity as a nodal agency

for the implementation of the mega-city scheme undertaken by the Government of India. The interest earned and received by the assessee out of the amount which it had received from the Central and State Governments and deposited in various banks, was treated as an income of the assessee and the AO brought the aforesaid amounts to tax. The assessee preferred an appeal and the said appeal came to be dismissed affirming the order of the AO. Aggrieved by the same, the assessee preferred second appeal to the Tribunal. The Tribunal looked into the guidelines which provided the background of the scheme. The Tribunal also looked into the terms of the scheme. Therefore, the Tribunal proceeded to hold that the assessee is nothing but trustee of funds entrusted to carry out the objects of the Government while implementing the scheme. The assessee infact acted as an agent of the Governments of both the Central and the State for implementing the scheme of the Government, This being the factual position, the lower authorities committed serious error in treating the interest as income of the assessee and bringing the same to tax. Therefore, the Tribunal set aside the orders of the AO and the first appellate authority and the claim of the assessee was allowed. As noticed by us earlier, aggrieved by the said order the Revenue has preferred this appeal.

3. Sri M.V. Seshachala, learned Counsel for the Revenue submitted that all incomes, which are not exempted under Section 10 of the Act, are liable to tax under Section 4 of the Act and, therefore, the order of the Tribunal requires to be set aside.

4. The material on record shows that the very purpose of constitution of the assessee was to act as a nodal agency for implementation of mega-city scheme worked out by the Planning Commission. Both the Central and the State Governments are expected to provide requisite finances for implementation of the said project. The funds from the Central and State Governments will flow directly to the specialised institutions/nodal agencies as grant and the nodal agency will constitute a revolving fund with the help of Central and State shares out of which finance could be provided to various agencies such as water, sewerage boards, municipal corporations, etc. **The objective is to create and maintain a fund for the development of infrastructural assets on a continuing basis** and, therefore, the assessee is a nodal agency formed/created by the Government of Karnataka as

*per the guidelines; there is no profit motive as the entire fund entrusted and the interest accrued therefrom on deposits in bank though in the name of the assessee has to be applied only for the purpose of welfare of the nation/States as provided in the guidelines; the whole Of the fund belongs to the State Exchequer and the assessee has to channelize them to the objects of centrally sponsored scheme of infrastructural development for mega-city of Bangalore. Funds of one wing of the Government is distributed to the other wing of the Government for public purpose as per the guidelines issued. The monies so received, till it is utilised, is parked in a bank. The finding recorded by the Tribunal clearly shows that the entire money in question is received for implementation of the scheme which is for a public purpose and the said scheme is implemented as per the guidelines of the Central Government and, therefore, the assessee is only acting as a nodal agency of Central Government for implementation of these projects. It is **not the case of the Revenue that the assessee was carrying on any business or activities of its own while implementing the scheme in question. The unutilised money, during which the***

*project could not be fully implemented, is deposited in a bank to earn interest. That interest earned is also again utilised for the implementation of the mega-city scheme which is also permitted under the scheme. Therefore, in computing the total income of the assessee for any previous year the interest accrued on bank deposits cannot be treated as an income of the assessee as the interest is earned out of the money given by the Government of India for the purpose of implementation of mega-city scheme.*

*5. Therefore, we do not find any error in the conclusion reached by the Tribunal that there was no income earned by way of interest by the assessee and setting aside the order of AO which is affirmed by the first appellate authority. The finding given by the Tribunal is purely a question of fact. We do not find any substantial question of law involved in this appeal and therefore, this appeal is liable to be dismissed at the stage of admission itself."*

11. This clearly brings out that the Hon'ble Court of Karnataka has pronounced that the ~~interest~~ interest earned on unutilized money from the allotted funds is again utilized for the purpose for which the grants were initially obtained. Hence, the interest incurred cannot be treated as income of the assessee while computing the total income.
12. Further, in **the judgement of Karnataka Municipal Data Society v .Income-tax Officer, Ward-9(2), Bangalore by the Hon'ble High Court of Karnataka**, the court has held that Government money was released to assessee-society for utilizing it in government schemes and interest was accrued on grant money. In such case neither grant amount nor interest thereon could be held as income of assessee as Assessee-society held fund only as a custodian and full command for utilization remained with Government.
13. Similar judgement is pronounced in the Hon'ble High Court of Karnataka in the appellant's own case for AY 2008-09 in **Commissioner of Income-tax, Bangalore v. Karnataka State Agricultural Produce Processing & Export Corporation Ltd.**

14. In this case, Section 4 of the Income-tax Act, 1961 - Income - Chargeable as (Interest) - Assessee was a Government owned company, engaged in trading in agricultural produce - In order to facilitate infrastructure facilities, for increasing export of horticultural produce, a sum of Rs. 10 crores was granted to assessee by State Government. Before utilisation of said grant, it was temporarily kept in fixed deposits and interest was earned. It was found that assessee had acted as a nodal agency for implementation of said scheme and there was no profit motive as entire fund entrusted and interest accrued from deposits had to be utilised only for purposes of scheme originally granted. Further, whole of fund belonged to State exchequer and assessee had to channelize them to achieve objects of centrally sponsored scheme of infrastructural development as specified in Government order. In this case the Hon'ble High Court of Karnataka pronounced that **interest earned on depositing these grants was not an income in hands of assessee.**

15. In the case present before me, the appellant M/s. KAPPEC LIMITED receives grants from Karnataka Government and utilizes it for various purposes. Out of the grants received, the appellant has deposited the un-utilized funds in FDs in bank and obtained interest on the same. The interest so obtained is further utilized for the purpose for which the grants were obtained. Hence, as per the decisions pronounced by Hon'ble High Court of Karnataka as stated above in various cases including

appellant's own case, the interest does not form a part of the appellant's income and should not be taxed. In view of the above, the addition of Rs. 3,60,91,132/- i.e. interest received on FDs out of Government of Karnataka fund is deleted. Hence the addition made by the AO in this matter is deleted.

16. The order of the AO is modified accordingly.

17. Ground No. 4 is general in nature and needs no separate adjudication.

18. Ground 5 is regarding interest u/s 234B. The interest u/s 234B is consequential.

19. Therefore, the appeal of the assessee is allowed.

6. The Id. DR could not controvert the observations of the CIT(Appeals) with any new evidence or cogent material. Accordingly, we are not inclined to interfere with the order of CIT(Appeals) and confirm the same and dismiss the grounds of appeal of revenue.

7. In the result, the revenue's appeal is dismissed.

Pronounced in the open court on the date mentioned on the caption page.

Sd/-

**(A.K. GARODIA)**  
**ACCOUNTANT MEMBER**

Sd/-

**(PAVAN KUMAR GADALE)**  
**JUDICIAL MEMBER**

Dated: 06.03.2020.

\*Reddy GP

Copy to

1. The appellant
2. The Respondent
3. CIT (A)
4. Pr. CIT
5. DR, ITAT, Bangalore.
6. Guard File

By order

Assistant Registrar  
Income-tax Appellate Tribunal  
Bangalore