

IN THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD BENCH "A", HYDERABAD

BEFORE SHRI A. MOHAN ALANKAMONY, ACCOUNTANT MEMBER
AND
SHRI S.S. GODARA, JUDICIAL MEMBER

	ITA No.33/Hyd/2019		
	Assessment Year: 2014-15		
Income Tax Officer, Ward-2(1), Hyderabad.	Vs.	KSK Wind Energy Halagali Benchi Private Limited, Hyderabad. PAN: AAECK 1965 F	
(Appellant)		(Respondent)	
	Assessee by:	Sri S. Rama Rao	
	Revenue by:	Sri Sunil Gowtham, Sr. AR	

	ITA No.34/Hyd/2019		
	Assessment Year: 2014-15		
Income Tax Officer, Ward-2(1), Hyderabad.	Vs.	KSK Wind Power Sankonahatti Athni Private Limited, Hyderabad. PAN: AAECK 1900 C	
(Appellant)		(Respondent)	
	Assessee by:	Sri S. Rama Rao	
	Revenue by:	Sri Sunil Gowtham, Sr. AR	

	ITA No.35/Hyd/2019		
	Assessment Year: 2014-15		
Income Tax Officer, Ward-2(1), Hyderabad.	Vs.	KSK Wind Power Aminabhavi Chikodi Private Limited, Hyderabad. PAN: AAECK 1888 R	
(Appellant)		(Respondent)	

Assessee by:	Sri S. Rama Rao	
Revenue by:	Sri Sunil Gowtham, Sr. AR	

	ITA No. 36/Hyd/2019		
	Assessment Year:2014-15		
Income Tax Officer, Ward-2(1), Hyderabad.	Vs.	KSK Wind Energy Mothalli Haveri Private Limited, Hyderabad. PAN: AAECK 1987 D	
(Appellant)		(Respondent)	
Assessee by:	Sri S. Rama Rao		
Revenue by:	Sri Sunil Gowtham, Sr. AR		
Date of hearing:	24/11/2021		
Date of pronouncement:	25/01/2022		

ORDER

PER A. MOHAN ALANKAMONY, AM.:

All the captioned appeals are filed by the Revenue against the orders of the Ld. CIT (A)-2, Hyderabad in appeal No.0693, 0692, 0697 and 0691/2016-17/CIT(A)-2, CIT(A), Hyderabad—2/10417, 10416, 10402 & 10415/2016-17, dated 16/11/2018 passed u/s. 143(3) r.w.s 250(6) of the Act for the AY 2014-15.

2. The Revenue has raised one effective ground in all the four appeals relating to different assessees for the AY 2014-15 and the ground is abridged herein below for adjudication.

“The Ld. CIT (A) has erred in treating the interest income earned by the assessee as “capital receipt” instead of treating it as “income from other source” u/s. 56 of the Act, and reduced the same from “capital work in progress”

3. The brief facts of the case with respect to all the four assessees are that during the relevant assessment year all the four assessee’s companies had not commenced their business activities however, they earned interest income on the fixed deposit kept with banks. The claim of the assessee was that since the idle funds were meant for capital expenditure the interest earned out of those idle funds during the gestation period should be treated as capital receipt and the same has to be reduced from capital work-in-progress. Accordingly, the interest income earned out of the idle funds reserved for capital expenditure need not be treated as revenue receipt during the relevant assessment year. However, the Ld. AO relying on the various decisions of higher Judiciary held in the case of all the assessees that the interest income earned on idle funds has to be treated as revenue receipts by observing as under:

“8. To sum up, it is worthwhile to mention here that the judgment of Apex Court in *CIT v Bokaro Steel Ltd 236 ITR 315* has been rendered in a context where advances were given to the contractors to enable them to purchase plant and machinery which were to be used in the project and interest was received on those advances. Some buildings belonging to the assessee were let out to the contractors for rent so that the labourers employed by the contractors can be housed there. Income earned under these heads was found by the Court to be Inextricably linked to the project under

construction. For the same reason, the interest earned on monies with banks for obtaining bank guarantees and letters of credit, is treated as capital receipt and allowed to be set off against preoperative expenses.

- 8.1 On the other hand, interest earned on fixed deposits made out of surplus funds lying idle pending allocation and utilization cannot be treated as capital receipts as the Interest Income emanated from an Independent source of income and the taxability of which was already decided by the Hon'ble Supreme Court in the case of *Mis Tuticorin Alkalies*. The settled position of law was reiterated by the Hon'ble Supreme Court in the case of *Mis Bokaro Steels*, which was discussed in this order in Para Nos. 5.1. & 5.2. The expression "Inextricably linked" needs to be examined in the context of purpose for which the deposit is made. These deposits are not made out of any compulsion/obligation nor related to construction activity. These deposits are made only for the effective utilization of funds and have nothing to do with the activity of construction.
9. The ratio of decisions rendered by the Hon'ble Supreme Court in the cases of *Tuticorin Alkali Chemicals and Fertilizers Ltd. v. CIT* (1997) 227 ITR 172, and *CIT v Bokaro Steel Ltd.* [1999] 236 ITR 315. have been extensively relied upon by various High Courts while deciding the issue -In number of other cases which are squarely covered in the instant case. A few of such recent judgments rendered by other High courts-are as under:
- i) Madhya Pradesh High Court in the case of *Bharat Oman Refineries Ltd v CIT* [2013] 35 taxmann.com 187.
- ii) Delhi High court in the case of *CIT v. Indian Vaccines Corporation Ltd* (2014) 363 ITR 295.
10. Without prejudice to the above stand, it is seen that the entire interest income's earned out of deposits made out of 'Share Holders Funds' and nothing out of 'borrowed funds'. Therefore, deduction if any, on account of interest expenditure can be allowed only out of interest income earned on borrowed funds and not on interest income earned on share holders funds kept as fixed deposits with Banks. Interest earned on short term deposits of share capital cannot be set off against interest paid on capital borrowed for setting up Industry (*CIT vs V.P. Gopinathan* (SC) 248 ITR 449)
11. The assessee had not offered any explanation as to why interest earned on ICDs and capitalized should not be taxed. The assessee has not explained the same. Under any circumstances, and in any form or substance, the same is taxable u/s 55 of IT Act, as 'Income from other sources'.

12. *In the light of foregoing discussion and in view of settled position of law as decided by Hon'ble Supreme Court in the cases of M/s. Tuticorin alkali Chemicals and Fertilizers Ltd vs. CIT (1997) 227 ITR 0172 and CIT vs. Bokaro Steel Ltd (1999) 236 ITR 315, the interest income of Rs.....earned by the assessee on surplus / idle funds pending project allocation is not allowed to be capitalized.”*

4. On appeal, the ld. CIT(A) decided the issue in favour of the assessee by relying on the order of the Tribunal dated 30/11/2017 in ITA No. 1098, 1099, 1100 to 1105/Hyd/2017 in the assessee's own case.

5. At the outset, we find that the identical issue was decided in favour of the Revenue by the Hyderabad Bench of the Tribunal in ITA No. 1534/Hyd/2016 in the case of M/s. Thermal Powertech Corporation India Limited for the AY 2012-13 vide Order dated 26/04/2017. The questions framed and answered by the Tribunal in that decision on the identical issue are as follows:

(a) Whether the interest earned is capital receipt?

(b) Whether the interest income can be set off to interest paid?

(c) Whether the interest income was taxable as income from business?

(d) Whether the nature / character of interest can be different from the related interest expense?

(e) Whether business loss carried forwarded can be set off to the interest income?

6. The relevant portion of the order of the Tribunal cited supra is reproduced herein below for reference:

16. We have considered the rival submissions and also perused the material available on record. Admittedly the assessee is in the process of setting up of power project. For the purpose of setting up of the project the assessee has availed funds from banks. Admittedly, the assessee invested a part of the borrowed funds from banks, which was not immediately required in short term deposits with an intention to earn interest ostensibly to reduce the interest liability. The question arises for consideration is whether the interest income of Rs. 22,35,48,281/- received by the assessee on temporary deposit of funds in with banks is assessable as income of the assessee or it would go to reduce the cost of borrowings? In other words, whether the interest amount of Rs. 22,35,48,281/- received by the assessee would be set off against the interest payment of Rs. 127,84,98,794/- on the borrowed funds. As rightly submitted by the learned CIT DR, the Apex Court in the case of Tuticorin Alkali Chemicals & Fertilizers Ltd. (supra) had examined an identical situation. The question which was referred to the Supreme Court is as follows:

"Whether, on the facts and in the circumstances of the case, interest derived by the assessee from borrowed funds which were invested in short term deposits with banks would be chargeable to tax under the head 'Income from other sources' or would go to reduce the interest payable by the assessee on the term loan secured by the assessee from financial institutions which would be capitalised after commencement of commercial production?"

17. In the case before the Apex Court, the assessee for the purpose of setting up of a factory has taken term loans from various banks and financial institutions. A part of the borrowed fund which was not immediately required by the assessee was kept invested in short term deposits with banks. The assessee claimed before the Assessing Officer that the interest of Rs.2,92,440 received on the term deposit with banks would go to reduce the pre-production expenses such as interest and financial charges which would ultimately be capitalised. Accordingly the assessee claimed that the interest of Rs.2,92,440 was not exigible to tax. However, the ITO rejected the claim of the assessee. The CIT(A) as well as the Tribunal confirmed the order of the Assessing Officer. However, the Tribunal found that there were conflicting judgments of the Madras High Court in CIT vs. Seshasayee Paper and Boards Ltd. (1985) 156 ITR 542 and A.P. High Court in CIT vs. Nagarjuna Steels Ltd. (1988) 171 ITR 63. Accordingly a reference was made to the Apex Court. The Apex Court after examining the facts of the case and the judgment of the Madras High Court in Seshasayee Paper and Boards Ltd. (supra) and Andhra Pradesh High Court in Nagarjuna Steels Ltd. (supra) confirmed the judgment of the Madras High Court. The Apex Court has specifically observed as follows at pages 180 and 181 of the Report:

"It is true that the company will have to pay interest on the money borrowed by it. But that cannot be a ground for exemption of interest earned by the company by utilizing the borrowed funds as its income. It was rightly pointed out in the case of Kedar Narain Singh v. CIT [1938] 6 ITR 157 (All) that "anything which can properly be described as income

is taxable under the Act unless expressly exempted ". The interest earned by the assessee is clearly its income and unless it can be shown that any provision like section 10 has exempted it from tax, it will be taxable. The fact that the source of income was borrowed money does not detract from the revenue character of the receipt. The question of adjustment of interest payable by the company against the interest earned by it will depend upon the provisions of the Act. The expenditure would have been deductible as incurred for the purpose of business if the assessee's business had commenced. But that is not the case here. The assessee may be entitled to capitalise the interest payable by it. But what the assessee cannot claim is adjustment of this expenditure against interest assessable under section 56. Section 57 of the Act sets out in its clauses (i) to (iii) the expenditures which are allowable as deduction from income assessable under section 56. It is not the case of the assessee that the interest payable by it on term loans is allowable as deduction under section 57 of the Act. If that be so, under which other provision of law can the assessee claim deduction or set-off of his income from other sources against interest payable on the borrowed funds? There are specific provisions in the Income-tax Act for setting off loss from one source against income from another source under the same head of income (section 70), as well as setting off loss from one head against income from another (section 71). In the facts of this case the company cannot claim any relief under either of these two sections, since its business had not started and there could not be any computation of business income or loss incurred by the assessee in the relevant accounting year. In such a situation, the expenditure incurred by the assessee for the purpose of setting up its business cannot be allowed as deduction, nor can it be adjusted against any other income under any other head. Similarly, any income from a non-business source cannot be set off against the liability to pay interest on funds borrowed for the purpose of purchase of plant and machinery even before commencement of the business of the assessee."

18. No doubt, the Apex Court found that it is not the case of the assessee that the interest payable by it on term loan is allowable as deduction u/s. 57 of the Act. The Apex Court after referring to the judgment of the Orissa High Court in *CIT vs. Electrochem Orissa Ltd.* (1995) 211 ITR 552 and the judgment of the Madras High Court in *Seshasayee Paper and Boards Ltd.* (supra) disapproved the reading of the judgment of the Madras High Court in *Seshasayee Paper and Boards Ltd.* (supra) by the Orissa High Court. In fact, the Apex Court has observed as follows:

"Our attention was drawn to two other decisions where the view of the Andhra Pradesh High Court was followed. In the case of CIT v. Electrochem Orissa Ltd. [1995] 211 ITR 552, the Orissa High Court preferred the view expressed by the High Court of Andhra Pradesh to the view expressed by the Madras High Court in Seshasayee Paper and Boards Ltd.'s case [1985] 156 ITR 542 on the ground that the Madras case was based on a finding of fact that there was no direct connection between the interest paid and the interest received. In our view, it will not be right to read the judgment in Seshasayee Paper and Boards Ltd.'s case [1985] 156 ITR 542 (Mad) in that way. The court's finding in Seshasayee Paper and Boards Ltd.'s case [1985] 156 ITR 542 (Mad) was that the interest earned by the assessee from the bank deposits had to

be assessed under the head " Other sources ". Consequently, the interest paid on the borrowings for the purpose of purchase of plant and machinery could not be allowed or adjusted against this income under section 57(iii) nor were such adjustments permissible under section 70 or 71 of the Act because the business of the assessee had not commenced. The Madras High Court (see [1985] 156 ITR 542) categorically held: " In this case, admittedly, the borrowing has not been made exclusively and solely for the purpose of earning interest in which case alone it should be taken as an income which should be deducted from the interest receipts." An assessee-company may have raised its capital by issue of shares or debentures or by borrowing. But when that capital or a portion of it was utilised for whatever reason, even for a short period, to earn interest, that interest must be treated as revenue receipt and will have to be taxed accordingly. Any set off or deduction of any expenditure can only be made in accordance with the provisions of the Act."

In view of the observation of the Apex Court, it is obvious that the Apex Court is conscious of the provision of section 57(iii) and it was held that when the assessee borrowed the funds for business, the interest earned on short term deposit of such funds cannot be allowed as deduction.

19. We have carefully gone through the judgment of the Madras High Court in Seshasayee Paper and Boards Ltd. (supra). The assessee company invested its paid-up share capital and loans obtained from banks and received interest income. The interest income received by the assessee was adjusted towards the interest payable on its loan. Accordingly the interest received by the assessee was not offered as income for taxation. The claim of the assessee that the interest income received by the assessee would go to reduce the interest payment on borrowed funds was rejected by the Income-tax authorities. However, the Tribunal allowed the claim of the assessee. On a reference to the Madras High Court, after referring to the judgment of the Apex Court in CIT vs. Rajendra Prasad Moody (1978) 115 ITR 519 and various other judgments of the High Courts, found that the borrowing has not been exclusively and solely for the purpose of earning interest in which case alone it should be taken as income which should be deducted from the interest receipt. This judgment of the Madras High Court in Seshasayee Paper and Boards Ltd. (supra) was specifically taken note of by the Apex Court and it was observed that interest paid on borrowings for the purpose of purchase of plant and machinery could not be allowed or adjusted against the income u/s. 57(iii) of the Act. The Apex Court finally concluded that the view expressed by the Madras High Court in Seshasayee Paper and Boards Ltd. is correct and the views expressed in other cases are erroneous. From the above it is obvious that even though the Apex Court found that the assessee in the case of Tuticorin Alkali Chemicals & Fertilizers Ltd. (supra) has not specifically made any claim u/s. 57 of the Act for setting off of the interest received on the FD with interest payment on borrowed fund, the Apex Court after referring to the judgment in the case of Seshasayee Paper and Boards Ltd. (supra) of the Madras High Court found that the claim of the assessee cannot be allowed even u/s. 57(iii) of the Act. In our opinion, the judgment of the Apex Court in the case of Tuticorin Alkali Chemicals & Fertilizers Ltd. (supra) on identical set of facts has answered a similar question against the assessee. Therefore, the interest received by the assessee on temporary deposit of funds which are not required immediately has to be assessed as

'Income from other sources' and it cannot be set off against the interest payable by the assessee on borrowed funds.

20. Admittedly deposit of funds in the bank is not the business of the assessee. The assessee borrowed the funds for the purpose of establishing the Power project. So long as the assessee uses the funds in the process of setting up of the project, we can say that the assessee has utilised the funds for the purpose of business. In this case the assessee has deposited the funds in FD for a temporary period, since the same was not required immediately. As observed by the Madras High Court in the case of Seshasayee Paper and Boards Ltd. (supra) which was approved and confirmed by the Apex Court in Tuticorin Alkali Chemicals & Fertilizers Ltd. (supra) the interest earned by the assessee by investing the borrowed fund which was not required immediately in fixed deposit has nothing to do with the actual borrowing. The payment of interest has no connection with the receipt of interest. Admittedly the borrowing has not been made for the purpose of earning interest income in which case alone the interest received by the assessee can be deducted from the interest payable. In view of the judgment of the Madras High Court in the case of Seshasayee Paper and Boards Ltd. (supra) and the judgment of the Apex Court in the case of Tuticorin Alkali Chemicals & Fertilizers Ltd. (supra), we are unable to uphold the contention of the assessee. The distinction sought to be made by categorising the funds as committed funds and surplus funds, in our view, cannot be accepted as in both the events the nature of fund is the they are not required immediately for the project.

21. In this regard, it is interesting to note that in all the mentioned decisions by assessee, reliance has been placed on the decision of the Hon'ble Supreme Court in the case of CIT Vs. Bokara Steels (supra). Further, in all such cases, various judicial authorities have tried to differentiate the decision of Hon'ble Supreme Court in the case of Tuticorin Alkali Chemicals & Fertilizers (supra) with the decision of Hon'ble Supreme Court in the case of Bokara Steels (supra). However, in reality, the proposition of law laid down by Hon'ble Supreme Court in the case of Tuticorin Alkali Chemicals and Fertilizers has not been overruled or distinguished by Hon'ble Supreme Court in its own decision in the case of Bokaro Steels (supra). On the other hand, in the case of Bokaro Steels Ltd.(supra) the Hon'ble Supreme Court has once again reiterated and supported its decision in the case of Tuticorin Alkali Chemicals & Fertilizers(supra) with regard to the issue of treatment of interest earned on short term deposits made out of borrowed funds during the period prior to the commencement of the business of the assessee. in the case of Bokaro Steels (supra), that company received certain income from the contractor who was assigned the job of constructing the factory. During the course of construction activities carried on by the contractor, the contractor had availed certain facilities and services from the company and paid certain consideration to the company. The nature of the services and consideration/ income received by the company from the contractor are noted as below :-

- i. Let out of its dwelling units to the contractor which were used for the purpose of housing the workers/labourers and staff for construction work;*
- ii. Hire charges received by the company from the contractor in connection with hiring of the plant and machinery owned by the company to the contractor which were used by the contractor in the construction work*

- iii. *Interest received by the company from the contractor on account of advances made to the contractor which were used for the purpose of construction work of the factory by the contractor; and*
 iv. *Royalty received by the company from the contractor in connection with permitting the contractor to excavate / mine the stones from the land owned by ; the company which were used in the construction activity of the company. In this connection, the Hon'ble Supreme Court held that the income received by the company ie. from the contractor under various sources mentioned above is inextricably linked with the setting up of the factory building / capital structure of the company and, therefore, such income has to be treated as capital receipt going to reduce the cost of construction of the assessee company.*

22. *However, in the same case of Bokaro steels, there was an issue with regard to treatment of interest income received by the company on short term deposits made with banks out of the amounts borrowed by it for the construction work which were not immediately required. On this issue, the AO treated the interest received as income of the assessee from "other sources" and brought to tax accordingly. However, as observed by the Hon'ble Supreme Court, the assessee had accepted the same and not filed any appeal against such finding and decision of lower authorities before Supreme Court. In view of this, Hon'ble Supreme Court made a mention in its judgement at Para No.4 stating that "we were not called upon to examine this issue" and further made a reference that in any" case, this question now concluded by the decision of Hon'ble Supreme Court in the case of Tuticorin Alkali Chemicals and Fertilizers (supra). The relevant portion of the decision at Para No.4 is as under::*

"During these assessment years, the respondent-assessee had invested the amounts borrowed by it or the construction work which were not immediately required, in short-term deposits and earned interest. It has been held in these proceedings that the receipt of interest amounts to income of the assessee from other sources. The assessee has not filed any appeal (rom this finding which is given against it. In any case, this question is now concluded by a decision of this court in Tuticorin Alkali Chemicals & Fertilizers Ltd. v. CIT (1997) 227 ITR 172 (sq. Hence, we are not called upon to examine that issue." (Emphasis supplied).

This issue of difference between the treatment of income received from contractor and the interest income received from the banks on account of short term deposits is once again highlighted by Hon'ble Supreme court in the case of Bokaro Steels (supra) at Para No.7. The relevant portion of the same is reproduced below:

"The appellant, however, relied upon the decision of this court in Tuticorin Alkali Chemicals & Fertilizers Ltd. case (supra). That case dealt with the question whether the investment of borrowed funds prior to commencement of business, resulting in earning of interest by the assessee, would amount to the assessee earning any income. This court held that if a person borrows money for business purposes, but utilises that money to earn interest, however, temporarily, the interest so generated will be his income. This income can be utilised by the assessee whichever way he likes. Merely because he utilised it to repay the interest on the loan taken will not make the interest income as a capital

receipt. The department relied upon the observations made in that judgment (at page 179) to the effect that if the company, even before it commences business, invests 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 rented house and gets rent, such rent will be assessable to tax under section 22 as income from house property. Likewise, the 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 Act. This court also emphasized the fact that the company was not bound to utilise the interest so earned to adjust it against the interest paid on borrowed capital. The company was free to use this income in any manner it liked. 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 resent 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. In the case of Challapalli Sugars Ltd. vs. CIT (1975) 98 ITR 167 (SC), this court examined the question whether interest paid before the commencement of production by a company on amounts borrowed for the acquisition and installation of plant and machinery would form a part of the actual cost of the asset to the assessee within the meaning of that expression in section 10(5) of the Indian Income Tax Act, 1922 and whether the assessee will be entitled to depreciation allowances and development rebate with reference to such interest also. The court held that the accepted accountancy rule for determining cost of fixed assets is to include all expenditure necessary to bring such assets into existence and to put them in working condition. In case money is borrowed by a newly started company which is in the process of constructing and erecting its plant, the interest incurred before the commencement of production on such borrowed money can be capitalised and added to the cost of the fixed assets created as a result of such expenditure. By the same reasoning if the assessee receives any amounts which are inextricably linked with the process of setting up its plant and machinery, such receipts will go to reduce the cost of its assets. These are receipts of a capital nature and cannot be taxed as income." (Emphasis supplied)

23. Under the facts and circumstances, it cannot be construed that the interest earned on account of parking the un utilized borrowed funds is inextricably linked with the setting up of the capital structure of the assessee company, inasmuch as such interest income is not received from the contractor to whom the assessee has assigned the construction work of its power project. In view of this, the ratio laid down by Hon'ble Supreme Court in the case of Bokaro Steels(supra) is not applicable to the facts of the assessee's case. As such, in view of the similar set of facts and circumstances involved in the case of the assessee as well as in the case of Tuticorin Alkali Chemicals & Fertilizers (supra), the proposition of law laid down by the Hon'ble Supreme court in that case is squarely applicable without any deviation.

24. Further, a clear-cut differentiation between treatment of interest income from short term deposits made out of borrowed funds and other categories of income received during the period prior to the commencement of business, more so, income received from the contractor undertaking the work of set up of the business of the assessee, has once again been made out by the Hon'ble Supreme Court in its later decision in the case of *Bongaigaon Refinery and Petrochemicals Ltd. Vs. CIT (2001) 251 ITR 329 (SC)*. In this judgment, the Hon'ble Supreme Court has reiterated the law that excluding interest derived by the assessee during the period prior to the commencement of business, other items of income such as hire charges for it equipment and recoveries from contractors on account of water and electricity charges shall be adjusted against the project cost or the business of oil refinery and petro chemicals. As such, in regard to interest income earned prior to commencement of the business, it is once again reiterated by the Hon'ble Supreme Court as income under "other sources" by reiterating the law laid down in the case of *Tuticorin Alkali Chemicals & Fertilizers (supra)*. The relevant portion of - the said decision of Hon'ble Supreme Court is reproduced below:

*"The High Court has already held that the interest income derived by the assessee during its formative period was taxable income. What remains for consideration is the income which the assessee derived from house property, its guest house, charges for equipment and recoveries from the contractors on account of water and electricity supply. These items are covered by the decision in *Bokaro Steel Ltd.s case (supra)*. To the extent that it relates to these items, i.e., items excluding interest, the question must be answered in the affirmative and in favour of the assessee. The order under challenge will stand modified to that extent".*

25. Also, it is pertinent to note that in the case of *Totgars Cooperative Sale Society Ltd. Vs. ITO (2010) 322 ITR 283*, the Hon'ble Supreme Court has once again held that interest earned on investment of surplus funds on hand not immediately required in short term deposits and securities would not fall under business income but income from other sources.

26. We have also carefully gone through the judgment of the Delhi High Court in *Indian Oil Panipat Power Consortium Ltd. (supra)*. The Hon'ble Delhi High Court distinguished the judgment of Apex Court in *Tuticorin Alkali Chemicals & Fertilizers Ltd. (supra)* on the ground that the funds in the form of share capital were infused for a specific purpose of acquiring land and 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'. After referring to the judgment of Apex Court in *Tuticorin Alkali Chemicals & Fertilizers Ltd. (supra)*, the Hon'ble Delhi High Court found that the interest on surplus funds would have to be treated as 'Income from other sources'. We find that the Madras High Court on another occasion, in *South India Shipping Corporation (supra)*, considered an identical situation and after referring to the Apex Court judgment in the case of *Tuticorin Alkali Chemicals & Fertilizers Ltd. (supra)* observed s follows at page 31 of the Report:

*"Coming now to the questions that have been referred to us at the instance of the Revenue, these questions are required to be answered in favour of the Revenue and against the assessee, in view of the decision of the Supreme Court in the case of *Tuticorin Alkali Chemicals an**

Fertilizers Ltd. (1997) 227 ITR 172, wherein the apex court, inter alia, held that in view of section 57(iii) of the Incometax Act, interest paid on overdraft obtained for the purpose of business could not be deducted from the interest earned on monies kept in fixed deposits as such income derived by way of interest on fixed deposits was to be taxed under the head 'Income from other sources. We, however, make it clear that though the assessee may not be entitled to have interest paid by it on overdraft to the bank, deducted from the interest received by it on the short-term fixed deposits, the assessee is entitled to deduction of the same from its business income."

27. In view of this judgment of the Madras High Court and the judgment of the Apex Court in the case of Tuticorin Alkali Chemicals & Fertilizers Ltd. (supra), and other judgments of Hon'ble Supreme court, in our opinion, the judgment of the Delhi High Court in the case of Indian Oil Panipat Power Consortium Ltd. (supra) and other case relied on by Ld. Counsel in his arguments may not be applicable to the facts of this case. In view of the above discussion, we do not find any infirmity in the order of the lower authority. Accordingly, the same is confirmed.

28. Now the issue whether the assessee business has been set up or commenced. This issue was also decided by the Hon'ble Supreme court in the case of Tuticorin Alkali Chemicals and Fertilisers Ltd (supra). In the facts and circumstances of that case the Hon'ble Supreme Court held that the company cannot claim set off of income under the head "other sources" against the pre-operative / pre-production expenses to be capitalized in future under the head "profits and gains of business or profession" inasmuch as in the year under consideration, the business of the assessee had not started and there could not be any computation of business income' or loss incurred by the assessee in the relevant accounting year. It is further held by the Hon'ble Supreme Court that the expenditure incurred by the assessee for the purpose of setting up its business cannot be allowed as deduction, nor can it be adjusted against any other income under any other head. Similarly, any income from a non-business source cannot be set-off against liability to pay interest on funds borrowed for the purpose of establishing the business including purchase of plant and machinery even before commencement of the business of the assessee.

29. While deciding the core issue of taxability of interest earned on short term deposits made out of borrowed funds during the period prior to the commencement of the business, the Hon'ble Supreme Court has also laid down proposition of law that no income under the head "profits and gains of the business or profession" could be computed during the accounting year prior to commencement of the business of the assessee. Further, the Hon'ble Supreme Court gave a finding of fact that the assessee had not commenced / started its business and accordingly ruled that there could not be any computation of business income or loss of the assessee in the relevant accounting year. The relevant portion at Para No. 17 of the order is as under:

"There are specific provisions in the Income-tax Act for setting off loss from one source against income from another source under the same head of income (section 70), as well as setting off loss from one head against income from another (section 71). In the facts of this case the company cannot claim any relief under either of these two sections, since its business had not started and there could not be any computation of

business income or loss incurred by the assessee in the relevant accounting year. In such a situation, the expenditure incurred by the assessee for the purpose of setting up its business cannot be allowed as deduction, nor can it be adjusted against any other income under any other head. Similarly, any income from a non-business source cannot be set off against the liability to pay interest on funds borrowed for the purpose of purchase of plant and machinery even before commencement of the business of the assessee." (Emphasis supplied)

The Hon'ble Supreme Court reiterated the same fact of noncommencement of business and its decision that until and unless the company commences its business, there cannot be any question of assessment of income of the assessee under "profits and gains of business or profession". However, the Hon'ble Supreme Court laid down the law that any income earned which would fall under the other heads of income such as "capital gains", "house property", "income from other sources" etc. are subject to tax under respective heads even before the assessee commences its business activities. The relevant portion of the same at Para No. 12 of the order:

"The basic proposition that has to be borne in mind in this case is that it is possible for a company to have six different sources of income, each one of which will be chargeable to income-tax. Profits and gains of business or profession is only one of the heads under which the company's income is liable to be assessed to tax. If a company has not commenced business there cannot be any question of assessment of its profit and gains of business. That does not mean that until and unless the company commences its business, its income from any other source will not be taxed. 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. It may buy shares and get dividends. Such dividends will be taxable under section 56 of the Act. The company may also, as in this case, keep the surplus funds in short-term deposits in order to earn interest. Such interest will be chargeable under section 56 of the Act." (Emphasis supplied)

After having held that no business income could be computed prior to the commencement of the business, the Hon'ble Supreme Court has adjudicated the matter with regard to assessment of interest income under the head "other sources" and non-adjustment of interest paid on borrowed capital against such income. The relevant portion of the decision at Para No. 18 & 19 is as under::

"It has been argued that the source from which the company has earned interest is borrowed capital. The company has to pay interest to its creditors on the same borrowed capital. Having regard to the identity of the fund on which interest is earned and interest is payable, the company should be allowed to set off its income against interest payable by it on the same fund. We are of the view that no adjustment can be allowed except in accordance with the provisions of the Income-tax Act. However desirable it may be from the point of view of equity, this adjustment cannot be made unless the law specifically permits such

adjustment. Next, it has been argued that according to well established accountancy practice the interest earned by the company even before the commencement of business from investing borrowed capital will have to be set off against interest payable by the company on that borrowed capital. The argument based on accountancy practice has little merit, if such practice cannot be justified by any provision of the statute or is contrary to it." (Emphasis supplied)

30. Further, the distinction between set up and commencement was also explained by Ld. CIT Dr in his arguments. We agree with the same. The following case law relied also support the Revenue stand. i. CIT Vs. Omer Khayyam Wineries (P) Ltd. (1979) 120 ITR 859 (AP High Court) ii. K. Sampath Kumar Vs. CIT (1986) 158 ITR 25 (Madras High Court) iii. CIT Vs. Industrial Solvents and chemicals Pvt. Ltd. (1979) 119 ITR 608 (Bombay HC) iv. CIT Vs. Sponge Iron India Ltd. (1993) 201 ITR 770 (AP High Court) v. CWT Vs. Ramaraju Surgical Cotton Mills Ltd. (1967) 63 ITR 478 (SC) vi Travencor – Cochin Chemicals Pvt Ltd. Vs CWT 65 ITR 651 (SC) vii. CIT Vs Electron India 241 ITR 166 (MAS)

31. Respectfully following the principles laid down as discussed above, we are of the opinion that the preoperative expenditure was to be capitalized to the assets and Assessee was eligible for depreciation on the value of assets. Therefore in the given facts of the case, we hold that Assessee has only setup the business but has not commenced the business, therefore, the claim of revenue expenditure is not allowable as the provisions of Sec. 28 of the IT Act does not apply.

32. Since the principles laid down by the Hon'ble Supreme Court in the case of Tuticorin Alkali Chemicals and Fertilisers Ltd (Supra) a three judge bench decision is followed other cases relied on by assessee do not apply to the facts of the case. We reiterate that the decision of coordinate Bench of Hyderabad in the case of Kakinada SEZ Pvt Ltd (ITA No. 1215/Hyd/2010) has to be followed as the same relied on the principles laid down by the judgment of the Hon'ble Supreme Court in Tuticorin Alkali Chemicals & Fertilizers Ltd., Vs CIT (supra).

33. As seen from the above, the Hon'ble Supreme Court has clearly laid down the law that- i. Before the commencement of the business of the assessee, income earned in the form of interest on deposits made with banks out of the funds borrowed from banks and financial institutions which was not immediately required for the purpose of setting up of the business should be assessed to tax under the head "other sources". ii. Similarly, no expenditure can be claimed under the head "Profits and Gains of business or profession" during the period prior to the commencement of the business; and iii. Any expenditure incurred including the interest on funds borrowed for the purpose of setting up of the business/purchase of plant and machinery etc., cannot be set-off against the interest income under the head "other sources".

34. The Hon'ble jurisdictional High Court in the case of CIT Vs. Rasi Cement Ltd., [232 ITR 554] has answered similar questions involved in favour of the Revenue. The question before the Hon'ble High Court was whether the interest earned on surplus funds deposited in the banks during the installation of the company, the status of the company before commencement of the business. The Hon'ble High Court has held that such interest has to be separately treated as income from other sources and cannot be taken as part of the capital structure

following the decision of the Hon'ble Supreme Court in the case of Tuticorin Alkali Chemicals and Fertilizers Ltd., Vs. CIT [227 ITR 172] (SC). It was categorically held that interest earned on surplus funds deposited in banks during installation of company, prior to commencement of business, has to be brought to tax as 'income from other sources' u/s. 57. Respectfully following the jurisdictional High Court decision also, the contentions of assessee that this amount has to be adjusted towards capital account cannot be accepted.

35. In view of the above, we hold that there is no merit in assessee contentions on all the grounds raised and accordingly they are rejected. The orders of AO and CIT(A) are accordingly confirmed”

7. Further, the Hyderabad bench of the Tribunal in its recent decision in the case of Hinduja National Power Corporation Limited vs. ITO in ITA Nos. 1263 & 1264/Hyd/2018 vide order dated 18/02/2021 has held as follows:

“5. At the outset, we do not find any merit in the orders of the Ld. Revenue Authorities in this regard. In the case of the assessee the decisions relied by the Ld. Revenue Authorities have no application. The facts in the case of the assessee are that it has borrowed funds from the bank for the purpose of its business. Since the entire funds could not be utilised during the relevant AYs the same were placed in bank deposit in order to cut down the interest expenditure incurred towards the borrowed funds. Provisions of section 57(iii) of the Act clearly lays down that while computing the income chargeable under the head 'income from other source', any expenditure other than capital expenditure expended wholly and exclusively for the purpose of earning such income shall be allowable as deduction. Therefore, when the unutilised borrowed interest-bearing funds are parked in the bank as fixed deposit the corresponding interest expenditure incurred shall be allowable as deduction by virtue of section 57(iii) of the Act. Hence, We hereby direct the Ld. AO to verify whether the assessee has parked the unutilised borrowed funds in the bank account as fixed deposit and if so, grant deduction in accordance with section 57(iii) of the Act. Accordingly, the concise Ground of the appeal in ITA No. 1263/H/2018 for the AY 2012-13 and the concise Ground No.2 of the appeal in ITA No. 1264/H/2018 for the AY 2013-14 are disposed off.”

8. Following the above decision of the Hyderabad benches of the Tribunal and the earlier decision of the Tribunal cited supra, we hereby set aside the order of the Ld. CIT (A) and confirm the order of the Ld.

AO. However, we also make it clear that if the assessee is incurring any interest expenditure/expenditure relating to the idle funds kept aside which is to be utilised for capital expenditure, proportionately such interest expenditure/expenditure has to be treated as deduction from the interest income earned during the relevant assessment year in accordance with section 57(iii) of the Act as we have held in the case ITA No's. 1263 & 1264/Hyd/2018 vide Order dated 18/02/2021. It is ordered accordingly.

9. In the result, all the four appeals of the Revenue are allowed.

Pronounced in the open Court on the 25th January, 2022.

Sd/-
(S.S. GODARA)
JUDICIAL MEMBER

Sd/-
(A. MOHAN ALANKAMONY)
ACCOUNTANT MEMBER

Hyderabad, Dated: 25th January, 2022.

OKK

Copy to:-

- 1) **Appellant:** (i) Income Tax Officer, Ward-2(1), R.No.506, 5th Floor Signature Towers, Opposite Botanical Garden, Kondapur-500 084.
- 2) **Respondent:** (i) M/s. KSK Wind Energy Halagali Benchi Private Limited, 8-2-293/82/A/431/A, Road No.22, Jubilee Hills, Hyderabad.
(ii) KSK Wind Power Sankonahatti Athni Private Ltd., 8-2-293/82/A/431/A, Road No.22, Jubilee Hills, Hyderabad.
(iii) KSK Wind Power Aminabhavi Chikodi Private Limited, 8-2-293/82/A/431/A, Road No.22, Jubilee Hills, Hyderabad.
(iv) M/s. KSK Wind Energy Mothalli Haveri Private Limited, 8-2-293/82/A/431/A, Road No.22, Jubilee Hills, Hyderabad.
- 3) (i) The CIT (A)-2, Hyderabad.

- 4) (i) The Pr. CIT-2, Hyderabad.
- 5) The DR, ITAT, Hyderabad
- 6) Guard File