

**IN THE INCOME TAX APPELLATE TRIBUNAL, DELHI 'H' BENCH,
NEW DELHI**

**BEFORE SHRI N.K. BILLAIYA, ACCOUNTANT MEMBER, AND
SHRI KUL BHARAT, JUDICIAL MEMBER**

ITA No. 7833/DEL/2019 [A.Y 2009-10]

M/s Vatika Hotels Pvt Ltd
621-A, Devika Tower
6, Nehru Place, New Delhi

Vs. The A.C.I.T
Central Circle - 8
New Delhi

PAN: AABCI 2522 B

(Applicant)

(Respondent)

Assessee By : Shri C.S. Aggarwal, Sr. Adv
Shri Ravi Pratap Mall, Adv

Department By : Shri Sanjai Kumar Yadav, Addl. CIT-DR

Date of Hearing : 07.11.2022
Date of Pronouncement : 11.11.2022

ORDER

PER N.K. BILLAIYA, ACCOUNTANT MEMBER:-

This appeal by the assessee is preferred against the order of the
ld. CIT(A) - 23, New Delhi dated 29.07.2019 pertaining to A.Y. 2009-10.

2. The grievances of the assessee read as under:

"1. That the learned CIT(A) has erred both on facts and in law in confirming an addition of Rs.23,31,717/- out of an addition of Rs. 46,92,827/- made by the learned AO.

2. That the learned CIT(A) has failed to appreciate that the interest accrued of Rs.23,31,717/- on FDR's bears the same character as that of interest earned aggregating to Rs.22,90,821/- on FDR's which has been held as capital receipt to be deducted from the cost of project.

2.1 That the learned CIT(A) has failed to appreciate that the assessee who had undertaken the construction of Hotel is in the stage of construction and had not become operational and that the interest had been earned on deposits made out of its own capital earn marked for the project.

2.3 That the learned CIT(A) has failed to appreciate that the assessee had incurred a liability by way of payment of interest in respect of the amounts raised by it and as such, without prejudice to the contention that the sums received could not be treated as income ought to have held that the amount of interest paid of Rs.1 1,13,77,224/- deserved to have been held as allowable u/s 57(ii) of the Income Tax Act.

2.4 That the learned CIT(A) has failed to appreciate that the facts of the case of the assessee are pari-materia with the facts of the case of CIT vs. Bokaro Steel Ltd. reported in 236 ITR 315

2.5 That the learned CIT(A) has failed to appreciate that there is an inextricable link between the deposit made in the bank and the margin money, provided by it against which credit facilities had been allowed by the Bank to the assessee. The finding that there is no such inextricable link is completely misconceived and is factually incorrect.

2.6 That the learned CIT(A) has further failed to appreciate that an amount of Rs. 46,446/- was earned on account of interest on auto sweep fixed deposits which establishes and beyond doubt that the amounts were inextricably linked with the cost of project and could not have been held as not inextricably linked.

3.....That the learned CIT(A) has further erred in sustaining a disallowance of Rs. 8,97,700/- being 1/5th of Rs. 44,88,500/- as preliminary expenses. In sustaining the aforesaid disallowance, the learned CIT (A) has failed to appreciate that the aforesaid sum had been allowed by the learned CIT(A) himself for the preceding two assessment years and was allowable expenditure.

3.1 That the learned CIT(A) has failed to appreciate that the expenditure incurred of Rs.44,88,500/- represented expenditure incurred for registration of amendment of the Memorandum of Association and not for the purpose of issue of shares.

It is therefore prayed that the addition sustained by the learned CIT(A) of Rs. 23,31,717/- be deleted and in the alternative it be held that the expenditure incurred by way of interest is to be allowed as deduction. It is further prayed that the disallowance sustained of Rs. 8,97,700/- be also deleted.

3. The representatives of both the sides were heard at length, the case records carefully perused and relevant documentary evidences brought on record in the form of Paper Book in light of Rule 18(6) of ITAT Rules duly considered.

4. Briefly stated, the facts of the case are that during the year under consideration, the assessee company is engaged in the business of running and managing of hotels, resorts, motels, restaurants, café tavern, beer house, pub, refreshment room, etc.

5. To carry on the aforementioned business, the assessee had purchased land, and all the expenses pertaining to the construction of the hotel building had been reflected in the balance sheet as 'Project and pre-operative Expenses' and the cost of construction has been capitalised as 'Capital Work in Progress' in the balance sheet. The return for the year was filed on 18.02.2010 declaring loss of Rs.50, 25, 543/-.

6. Return was selected for scrutiny assessment and, accordingly, statutory notices were issued and served upon the assessee.

7. During the course of scrutiny assessment proceedings and on examining the financial statement of accounts, the Assessing Officer was of the opinion that the assessee is yet to set up its business, as is evident from the Profit and Loss Account, wherein no revenue has been shown for any of the years and on examination of the balance sheet, it was found that a sum of Rs.74.80 crores is shown as Capital Work in Progress and a further sum of Rs.42.32 crores is shown as 'Project and Pre-operative Expenses' pending capitalization.

8. On perusal of the details furnished by the assessee with regard to project and pre-operative expenses pending capitalization, the Assessing Officer found that the assessee has adjusted/set off an amount of Rs. 46,92,827/- from the said expenses.

9. The assessee was asked to explain the same and to show cause as to why the said interest income should not be brought to tax and assessed to tax as 'Income from Other Sources'

10. It was explained that the sum of Rs. 7,62,46,669/- is reflected as on 31.03.2009 against deposit amount as against Rs. 3,13,00,000/- in the immediately preceding year and it was explained that this deposit account has been made for margin money against letter of credits and bank guarantees. It was further explained that in order to construct hotel building it had imported various items from abroad for which different letter of credits were got executed and certain bank guarantees were also taken by the assessee for the purpose of construction activity and in order to secure the bank for issue of letter of credit and for bank guarantees, the assessee had to deposit an amount stated under the head "Cash and Bank Balance" as deposit account. Therefore, the interest earned on such deposit is directly linked to the business of the assessee and in fact, to the project and pre-operative expenses of the assessee.

11. Reply/explanation of the assessee did not find any favour with the Assessing Officer who was of the firm belief that the 'interest income' is to be assessed as 'business income' or as 'income from other sources' and referring to the decision of the Hon'ble Supreme Court in the case of Tuticorn Alkalies 227 ITR 192 addition of Rs. 46,92,827/- was made by the Assessing Officer.

12. Addition was challenged before the ld. CIT(A). Contentions were reiterated.

13. After examining the facts and the submissions, the ld. CIT(A) was convinced that the interest earned aggregating to Rs. 22,90,821/- on FDRs was capital receipt to be deducted from cost of project. However, addition of Rs. 23,31,717/- was confirmed.

14. Before us, the learned counsel for the assessee vehemently stated that on identical set of facts and on identical explanation, the CITA grossly erred in partly accepting the interest on FDR as capital receipt. It is the say of the ld. counsel that the FDRs have been purchased by the assessee to provide letter of credits and bank guarantees to various suppliers from abroad and since the interest accrued on the said FDRs was part of the construction project, the same was reduced from the cost of project which has been partly accepted by the CIT(A) but for no valid reason part has been disallowed.

15. Per contra, the ld. DR strongly supported the findings of the Assessing Officer.

16. We have given thoughtful consideration to the orders of the authorities below. It is an undisputed fact that all the FDRs were purchased by the assessee for letter of credits and bank guarantees given to various suppliers of goods from abroad. The details have been furnished before the lower authorities, which have been examined and no adverse inference has been drawn in so far as details for issue of letters of credit/bank guarantee in favour of the supplier is concerned. It is also not in dispute that the assessee has reduced interest accrued on FDRs from the Project and Pre-operative Expenses' reflected in the balance sheet. Entire transaction has been duly explained by way of Notes to the respective Schedule to the Balance Sheet by the assessee and the auditors.

17. Hon'ble High Court of Delhi in the case of Indian Oil Panipat Power Consortium Ltd 315 ITR 255 has held as under:

"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 precommencement 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.

6.1 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. The appeals are allowed and the impugned judgment is set aside.”

18. The decision of the Hon'ble Supreme Court relied upon by the Assessing Officer has been duly considered by the Hon'ble High Court of Delhi.

19. In light of the afore-stated judgement, we are of the considered view that the assessee has filed complete details of FDs and has also provided details of LC/BG against which FD was taken and it can be safely concluded that the interest earned on FD is inextricably linked to the setting up the hotel as such and, therefore, the findings of the Id. CIT(A) in treating interest of Rs. 23,31,717/- as income from other sources is not only erroneous but against the facts of the case in hand as explained hereinabove.

20. Considering the facts of the case in totality, we direct the Assessing Officer to consider the interest of Rs. 23,31,717/- as part of capital receipt to be deducted from the cost of project.

21. Ground Nos. 1 and 2 with all sub ground are allowed.

22. The next issue relates to the disallowance of Rs. 8,97,700/- being 1/5 of preliminary expenses.

23. Briefly stated, the underlying facts in this issue are that an expenditure of Rs. 44,88,500/- was incurred by the assessee in Assessment Year 2007-08 towards payment of ROC fees. The said was claimed as revenue expenditure under the head "Rates and Taxes". However, during the course of assessment proceedings, the assessee prayed that the said expenses may be allowed as per provisions of section 35D of the Act. The said prayer was not accepted by the Assessing Officer who disallowed the said claim of expenditure.

24. Order of the assessing officer was challenged before the Id. CIT(A) who, vide order dated 09.12.2011, allowed the claim of the assessee and directed the Assessing Officer to allow 1/5th of the expenses under section 35D of the Act.

25. Similar was the claim in Assessment Year 2008-09.

26. The Id. CIT(A) observed that while deciding the appeal for Assessment Year 2007-08, his predecessor did not discuss any reasoning for deciding the matter in favour of the assessee. The Id. CIT(A) was also not convinced with the claim that in rest of 4 assessment years, deduction is automatic and should have been allowed to the assessee in the normal course of assessment proceedings. Referring to the decision of the Hon'ble Delhi High Court in the case of Hindustan Insecticides Ld 116 taxman 406, the CIT(A) rejected the plea of the assessee.

27. Before us, the Id. counsel for the assessee vehemently stated that since the 1/5th of the expenses have been allowed u/s 35D of the Act, for Assessment Year 2007-08, similar claim in subsequent assessment years cannot be denied to the assessee. Strong reliance

was placed on the decision of the Hon'ble Bombay High Court in the case of Paul Brothers 216 ITR 548, Sourashtra Cement and of Chemicals Industries Ltd 123 ITR 669 Gujarat High Court and Sassoon Chemicals and Drugs Ltd 388 ITR 1 [Supreme Court].

28. Per contra the learned DR strongly supported the findings of the ld. CITA.

29. We have carefully perused the orders of the authorities below. It is true that the said claim was made during the assessment proceedings for Assessment Year 2007-08 wherein the Assessing Officer denied the claim of expenses but the CIT(A) allowed 1/5th of the expenses u/s 35D of the Act. It is equally true that once the claim has been allowed in the initial assessment year, the said claim cannot be denied in the subsequent assessment years on identical set of facts.

30. We find that the expenditure of Rs.44,88,500/- was incurred by the assessee towards fees paid to the Registrar of Companies and the said expenditure was incurred in Assessment Year 2007-08 and since it has been considered as preliminary expenses in the said assessment year and since 1/5th of the same has been allowed u/s 35D of the Act,

balance has to be allowed in the subsequent four assessment years following the ratio of the Hon'ble Supreme Court in the case of Sassoon Chemicals and Drugs Ltd [supra]. We accordingly direct the assessing officer to allow the said claim. Ground No. 3 with sub grounds is allowed.

31. In the result, the appeal of the assessee in ITA No. 7833/DEL/2019 is allowed.

The order is pronounced in the open court on 11.11.2022.

Sd/-

**[KUL BHARAT]
JUDICIAL MEMBER**

Sd/-

**[N.K. BILLAIYA]
ACCOUNTANT MEMBER**

Dated: 11th November, 2022.

VL/

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR

Asst. Registrar,
ITAT, New Delhi

Date of dictation	
Date on which the typed draft is placed before the dictating Member	
Date on which the typed draft is placed before the Other Member	
Date on which the approved draft comes to the Sr.PS/PS	
Date on which the fair order is placed before the Dictating Member for pronouncement	
Date on which the fair order comes back to the Sr.PS/PS	
Date on which the final order is uploaded on the website of ITAT	
Date on which the file goes to the Bench Clerk	
Date on which the file goes to the Head Clerk	
The date on which the file goes to the Assistant Registrar for signature on the order	
Date of dispatch of the Order	