

**HIGH COURT OF JUDICATURE FOR RAJASTHAN AT
JODHPUR**

D.B. Income Tax Appeal No. 54 / 2003

The Commissioner Of Income Tax

----Appellant

Versus

M/S Bhawal Synthetics (India) Udaipur

----Respondent

Connected With

D.B. Income Tax Appeal No. 46 / 2006

For Appellant(s) : Mr. KK Bissa

For Respondent(s) :



HON'BLE MR. JUSTICE GOVIND MATHUR

HON'BLE MR. JUSTICE VINIT KUMAR MATHUR

Judgment

Per Hon'ble Mr. Govind Mathur, J.

05/05/2017

By this judgment we are deciding two appeals being absolutely inter-related. It would be appropriate to first deal with D.B. Income Tax Appeal No.54/2003. This appeal under Section 260(A) of the Income Tax Act, 1961 is before us to question correctness of order dated 28.3.2003 passed by the Income Tax Appellate Tribunal, Jodhpur on the basis of the following substantial questions of law :-

"1. Whether in the facts and circumstances of the case, the interest earned on Fixed Deposit receipts used by

the assessee as borrowing margin money for funds for setting up the industry can be termed as inextricably linked with the process of setting up of industry so as to be considered as capital receipt and not revenue income ?

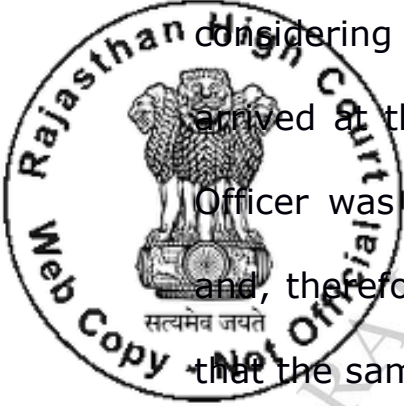


2. Whether in the facts and circumstances of the case the Tribunal was justified in law in holding that the enquiry conducted by the Assessing Officer before the assessment order was passed was proper and adequate enquiry so as not to render the assessment order erroneous and prejudicial to the interest of the revenue, as held by the CIT in his order u/s.263 of the I.T. Act ?”

In brief facts of the case are that the respondent-assessee filed return with no income, hence, that was selected under scrutiny and a notice as per provisions of Section 143(2) of the Income Tax Act, 1961 (hereinafter referred to as the 'Act of 1961') was issued. The Assessing Officer considering the explanation given by the assessee arrived at the conclusion that since no expenditure or depreciation claimed by the assessee, the addition sought to be made is set off and the returned income be treated as nil. The Commissioner of Income Tax on subsequent examination of record found the order passed by the Assessing Officer erroneous and prejudicial to the interest of revenue inasmuch as the interest earned on Fixed Deposit Receipts (FDRs)

amounting to Rs.9,31,572/- had not been brought to tax/wrongly set off and further that the Assessing Officer failed to make due and proper enquiry as required in the facts and circumstances of the case. A show-cause notice under Section 263 of the Act of 1961, thus, was issued. The Commissioner of Income Tax after considering all facts and circumstances and the law applicable, arrived at the conclusion that the order passed by the Assessing Officer was erroneous and prejudicial to the interest of revenue and, therefore, set aside the order of assessment with a direction that the same should be made afresh after making due and proper enquiry in accordance with the provisions of law laid down by Hon`ble the Supreme Court in 227 ITR 172(SC). A challenge was given to the order passed by the Commissioner of Income Tax invoking powers under Section 263 of the Act of 1961 by way of filing an appeal before the Income Tax Appellate Tribunal, Jodhpur Bench, Jodhpur. The Tribunal by its order dated 28.3.2003 accepted the appeal and set aside the order passed under Section 263 of the Act of 1961.

To challenge the order passed by the Income Tax Appellate Tribunal this appeal is before us with the contention that the interest earned by the assessee on Fixed Deposits is not business income but from other sources and, therefore, is liable to be taxed. It is also stated that the Assessing Officer passed order of assessment without proper and adequate enquiry and that was erroneous and prejudicial to the interest of revenue, as such, the



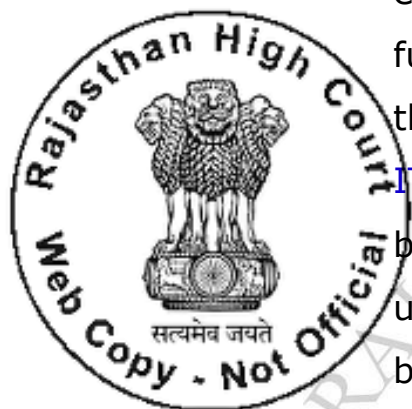
Income Tax Appellate Tribunal erred while setting aside the order under Section 263 of the Act of 1961.

Heard learned counsel for the appellant. None is present on behalf of the respondent-assessee.



As already stated, the Commissioner of Income Tax while invoking powers under Section 263 of the Act of 1961 held that the interest earned on FDRs was taxable as income and that could have not been set off by treating the same as margin money required for obtaining letter of credit or bank guarantee etc. The Income Tax Appellate Tribunal negatived the stand of the Commissioner of Income Tax by holding that the Fixed Deposit was pertaining to the amount that was to be adjusted in project cost and, therefore, the interest accrued thereon was rightly treated as business expenditure and was rightly set off by the Assessing Officer. Hon`ble Supreme Court while dealing with the issue of similar nature in *Tuticorin Alkali Chemicals & Fertilizers Limited Vs. Commissioner of Income Tax* reported in 227 ITR 172(SC) held that the interest earned on short-term investment of funds borrowed for setting up of factory during construction of factory before commencement of business has to be assessed as income from other sources and it cannot be said that interest income is not taxable on the ground that it would go to reduce interest on borrowed amount which would be capitalized. The Apex Court in the case aforesaid discussed the entire issue in

detail and that deserves to be quoted as follows :-



“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 utilising the borrowed funds as its income. It was rightly pointed out in the case of [Kedar Narain Singh vs. 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 anything 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 are allowable as deduction under [section 57](#)”.

In the case in hand, it is not in dispute that the assessee had income of interest through FDRs and while setting off that the Assessing Officer as well as the ITAT did not examine the aspect as to under which provision the assessee claimed deduction or set off of his income from other sources against interest payable on the borrowed fund. The reason given is that the amount pertaining to FDR was not surplus amount but part of amount that was kept to obtain letter of credit for purchase of machinery. While accepting the fact that the FDR was for obtaining letter of credit to purchase machinery but so far as interest earned thereon is concerned, that is nothing but income through other sources, as such, the Commissioner of Income Tax rightly treated the same as income taxable. So far as the second question is concerned as to whether the Commissioner of Income Tax was justified in invoking powers under Section 263 of the Act of 1961 by holding that the enquiry conducted by the Assessing Officer before the assessment order was neither proper nor adequate, we would like to state that the order passed by the Assessing Officer nowhere reflects about any enquiry said to be made. It simply refers the explanation given by the assessee and nothing beyond that.

In view of whatever stated above, we are inclined to accept this appeal. Accordingly, the appeal is allowed. The order passed by the Income Tax Appellate Tribunal dated 28.3.2003 is set aside.



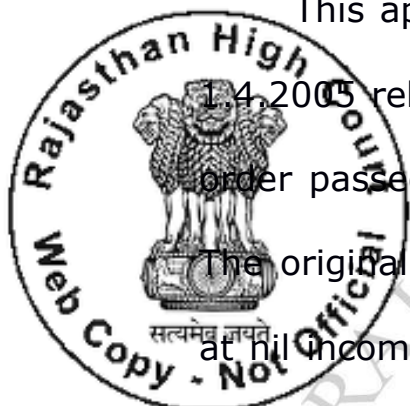
The order passed by the Commissioner of Income Tax invoking powers under Section 263 of the Act of 1961 stands restored.

D.B. Income Tax Appeal No.46/2006

This appeal is directed against the order of the Tribunal dtd. 1.4.2005 relating to assessment year 1996-97. It is sequel to the order passed by the Tribunal in ITA No.212/JU/01 on 28.3.2003. The original assessment for assessment year 1996-97 was made at nil income by the assessing officer accepting the contention of the assessee. However, in pursuance of order passed by the CIT in exercise of its power under Section 263, a fresh assessment for the year 1996-97 came into existence which is subject matter of this appeal and relates to including the interest earned on fixed deposit receipt as income of the assessee and not capital receipt resulting in reduction of cost of installation of the assessee's business.

Since the order passed by the CIT under Section 263 itself was set aside by the Tribunal vide its above referred order dtd.28.3.2003, order of assessment giving effect to the order passed under Section 263, the appeal of the assessee has been allowed as foundational order has ceased to exist.

A Coordinate Bench of this Court admitted this appeal without framing any substantial question of law. Having



considered all facts of the case, we are of the opinion that this appeal involves a substantial question of law in the terms that "Whether the Income Tax Appellate Tribunal was justified in setting aside the order of assessment which was made as a consequence to a revisional order under Section 263 of the Income Tax Act on the count that the order passed by the revisional authority was already set aside?" It is the position admitted that the order passed by the revisional authority under Section 263 of the Act of 1961 was set aside by the Income Tax Appellate Tribunal and, therefore, the consequential order of assessment was certainly not sustainable, as such, the Income Tax Appellate Tribunal under the order impugned did not commit any wrong in setting aside the same, however, the position has now been altered in view of the fact that the revisional order has already been restored, therefore, the order or assessment too deserves to be restored. Accordingly, this appeal is allowed. The order passed by the Income Tax Appellate Tribunal dated 01.4.2005 is set aside. The order passed by the Assessing Officer stands restored, hence, the ITAT is required to adjudicate the same on merits. The appeal ITA No.156/JU/2003 (A.Y. 1996-97), accordingly stands restored and is remanded to ITAT for adjudication on merits.

(VINIT KUMAR MATHUR)J.

(GOVIND MATHUR)J.

Sanjay