

REPORTABLE

* **IN THE HIGH COURT OF DELHI : NEW DELHI**

+ **ITA No. 643/2008**

% Judgment reserved on : 19.11.2008
Judgment delivered on : 27.11.2008

**COMMISSIONER OF INCOME TAX
DELHI-XI, NEW DELHI**

..... Appellant

versus

M/S COSMOS INTERNATIONAL

..... Respondent

Advocates who appeared in this case:

For the Revenue : Ms Prem Lata Bansal
For the Respondent : None

CORAM :

**Hon'ble Mr. Justice Badar Durrez Ahmed
Hon'ble Mr. Justice Rajiv Shakdher**

1. Whether the Reporters of local papers may be allowed to see the judgment ?
2. To be referred to Reporters or not ?
3. Whether the judgment should be reported in the Digest ?

Rajiv Shakdher, J.

1. This is an appeal under Section 260A of the Income Tax Act, 1961 (hereinafter referred to as the 'Act') against judgment dated 07.09.2007 passed by the Income Tax Appellate Tribunal (hereinafter referred to as the

‘Tribunal’) in ITA No. 3967/Del/2006 pertaining to the assessment year 2003-04.

2. The Revenue is aggrieved by the impugned judgment, in so far as, the Tribunal held that interest income on fixed deposits earned by the assessee be treated as ‘business income’, as against, ‘income from other sources’. The consequent effect of which would be that the assessee would be required to deduct 90% of such interest from the ‘profits of the business’ under Section 80HHC of the Act.

3. At this stage, it may be noted that we had issued notice in the appeal by our order dated 02.07.2008. As per the service report, the respondent has been served. Despite, service of notice, the respondent has chosen not to put in an appearance before this Court. This has left us with no alternative but to proceed to decide the present appeal in the absence of the respondent and/or its authorised representative.

4. The learned counsel for the revenue, Ms Prem Lata Bansal has contended before us, that the impugned judgment of the Tribunal deserves to be set aside in view of the fact that it is contrary to the judgment of this Court passed in the case of *Commissioner of Income Tax v Shri Ram Honda Power Equip: (2007) 298 ITR 475*. We have examined the orders passed by the authorities below and upon perusal of the same, we have come to the

conclusion that the submission of the learned counsel for the Revenue has to be accepted. Before we delve into the reasons for coming to such a conclusion the following brief facts, which are necessary for disposal of the present appeal, require to be noted:-

5. On 31.10.2003 the assessee had filed his return of income for the assessment year 2003-04 declaring a total income of Rs 35,16,882. On 6.5.2004 the return of the assessee was processed under Section 143(1) (a) of the Act. However, as it transpires, that the assessee's return was picked up for scrutiny and accordingly, a notice under Section 143(2) of the Act dated 12.10.2004 was issued, and duly served, on the assessee. During the course of scrutiny it was revealed, inter alia, that the assessee had received interest on fixed deposit amounting to Rs 1,51,869/- which, the assessee had, shown as 'business income'.

6. The Assessing Officer by an order dated 09.1.2006 came to the conclusion that the interest income earned on the fixed deposit had to be treated as 'income from other sources' and accordingly, deduction under Section 80HHC of the Act, on the interest income, was disallowed.

7. Aggrieved by the same, the assessee filed an appeal before the Commissioner of Income Tax (Appeals) [hereinafter referred to as the

‘CIT(A)’. The CIT (A) in the operative part of its order dated 07.09.2006 held as follows:

“.....Therefore, in view of the facts and the legal position the assessee is not entitled to get deduction u/s 80-HHC on account of interest income generated out of fixed deposits in the bank. However only 90% of such interest is to be deducted from the profits of the business in view of the specific provision contained in section 80HHC.....”

8. Aggrieved by the decision, the Revenue preferred an appeal before the Tribunal, on the ground that, the interest income earned on the fixed deposit by the assessee had been treated by the CIT(A) as ‘business income’, as against, ‘income from other sources’ as held by the Assessing Officer with a direction to the Assessing Officer to reduce 90% of such profits from ‘profits of business’.

9. The Tribunal in Paragraph 13 of the impugned judgment, after noting the reasoning of the CIT(A), concluded as follows:

“.....After considering rival submissions, we find that since direct nexus has been found with the assessment of interest income the same was rightly treated as business income. The reliance by Id. Departmental Representative on the decision of Delhi High Court in Sriram Honda 289 ITR 475 is not applicable to the present set of facts. In the same case the High Court has not put a total embargo on treating the interest income as business income. It is held that if the circumstances so warranted the interest income can be treated as income from business. Since there is direct nexus between borrowal of fund and placing in the deposit, the action of Id. Commission of Income-tax (Appeals) needs no interference.”

10. Having noted the facts obtaining in the instant case and the orders of the authorities below, we find that the judgment of this Court in *Sriram Honda Power Equip* (*supra*) is not only applicable on all fours but also that its ratio has been misconstrued by the Tribunal. This is evident upon reading Paragraphs 35 and 36 at Pages 496-497 of the said judgment. The observations of the Division Bench, in so far as, they are relevant for purposes of disposal of this appeal are extracted below:

“.....We are, therefore, of the view that where surplus **funds are parked with the bank and interest is earned thereon it can only be categorized as income from other sources.** This receipt merits separate treatment under section 56 of the Act which is outside the ring of the profit and gains from business and profession. It goes entirely out of the reckoning for the purpose of section 80 HHC. To give effect to this position, the Assessing Officer while computing profits of the export business will have to remove from the debit side of the profit and loss account the corresponding interest expenditure that has been “laid out” to earn such income from other sources. Otherwise this will depress the profits by an amount which is out of the reckoning of section 80HHC, a consequence not intended to be brought about.

36. The other category is where the exporter is required to **mandatorily keep monies in fixed deposit in order to avail of credit facility for the export business.** The argument on behalf of the assessee is that but for such a stipulation by the bank there was no need for the exporter to keep the money in fixed deposit and therefore the income earned from such fixed deposits bears a direct nexus to the business activity itself. **Given the repeated affirmation by the Hon’ble Supreme Court of three judgments of the Kerala High Court on the same issue, we are inclined to follow the view expressed by the Kerala High Court on each of these occasions. We accordingly hold that interest earned on fixed deposits for the purpose of availing of credit facilities from the bank,**

does not have an immediate nexus with the export business and therefore has to necessarily be treated as income from other sources and not business income. Question (a) and issue (i) are answered accordingly.”

11.b In view of the above, we have no hesitation in coming to the conclusion that the impugned judgment of the Tribunal is erroneous on this aspect of the matter. Accordingly, the impugned judgment is set aside. The Assessing Officer is directed to allow deduction in accordance with our observation made hereinabove and the judgment of this Court in *Sriram Honda (supra)*.

RAJIV SHAKDHER, J.

BADAR DURREZ AHMED, J.

November 27 , 2008

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