

Vidarbha Irrigation Development Vs. Additional Commissioner of

Vidarbha Irrigation Development Vs. Additional Commissioner of

SooperKanoon Citation : sooperkanoon.com/72471

Court : Income Tax Appellate Tribunal ITAT Nagpur

Decided On : Feb-28-2003

Reported in : (2005)93ITD184(Nag.)

Judge : P Jagtap, N Vasudevan

Appellant : Vidarbha Irrigation Development

Respondent : Additional Commissioner of

Judgement :

1. This is an appeal by the Assessee against the order of CIT(A)-I, Nagpur, dated 11.12.2001 in Appeal No. 13/2001 -2002 and it relates to the A.Y. 1998-99.

2. The Assessee/Appellant is a statutory corporation which was set up under The Vidarbha Irrigation Development Corporation Ordinance, 1997 dated 12.3.1997 which was later replaced by the Vidarbha Irrigation Development Corporation Act, 1997 (Maharashtra Act No. XXVI of 1997) (hereinafter referred to as 'The VIDC Act') which came into force with effect from 12.3.1997. For A.Y.98-99 it filed its first return of income on 30.11.98 in the status of 'Domestic Company' showing a loss of Rs. 1,40,31,211/-. During the course of assessment proceedings the assessee however claimed its status to be that of a 'Local Authority' as against a 'Domestic Company' as originally stated in the Return of Income. The Assessee made such a claim since under Section 10(20) of the Income Tax Act, 1961 (hereinafter referred to as 'The Act') while computing the total income of a previous year of any person, any income of a local authority which is chargeable to tax

under the head income from house property, capital gains, income from other sources or from a trade or business carried on by it which accrues or arises from the supply of a commodity or service (not being water or electricity) within its own jurisdictional area or from the supply of water or electricity within or outside its own jurisdictional area, shall not be included.

3. The term 'Local Authority' has not been defined in the Act. The term Local Authority has however been defined under the General Clauses Act, 1897. Under Section 3(31) the term 'Local Authority' has been defined as follows: 'Local Authority' means a Municipal Committee, a District Board, a body of Port Commissioners, or other authority legally entitled to or entrusted by the Government with the control or management of a municipal or local fund.

The Act being a Central Act, the definition contained in Section 3(31) of the General Clauses Act, 1897 has to be considered in coming to a conclusion whether the Assessee can be said to be 'Local Authority' entitled to claim exemption under Section 10(20) of the Act. The definition of 'Local Authority' contained in Section 3(31) of the General Clauses Act, 1897 is in two parts. The first part refers to specific authorities like Municipal Committee, a District Board, a body of Port Commissioners. The second part is generic and covers any other authority legally entitled to or entrusted by Government with the control and management of a municipal or local fund. The second part therefore suggests that in order any other authority to be a local authority should be legally entitled to or entrusted by the Government with the control or management of a local fund and must also possess many, if not all, of the distinctive attributes and characteristics of a Municipal Committee, District Board or Body of Port Commissioners.

4. The case of the Assessee before the Assessing Officer was that the Honourable Supreme Court in the case of Union of India v. R.C. Jain AIR (1981) 951 S.C. has laid down the distinctive attributes and characteristics, all or many of which a Municipal Committee, District Board or Body of Port Commissioners shares with any other local authority and that the Assessee fulfills all the attributes and characteristics as laid down by the Honourable Supreme Court in the aforesaid judgment. The following were the attributes and characteristics which the

Honourable Supreme Court has laid down: First, the authorities must have separate legal existence as corporate bodies. They must not be mere governmental agencies but must be legally independent entities. Next, they must function in a defined area and must ordinarily, wholly or partly, directly or indirectly, be elected by the inhabitants of the area. Next, they must enjoy a certain degree of autonomy, with freedom to decide for themselves questions of policy affecting the area administered by them. The autonomy may not be complete and the degree of the dependence may vary considerably but, an appreciable measure of autonomy there must be. Next, they must be entrusted by statute with such governmental functions and duties as are usually entrusted to municipal bodies, such as those connected with providing amenities to the inhabitants of the locality, like health and education services, water and sewerage, town planning and development, roads, markets, transportation, social welfare services etc. etc. broadly we may say that they may be entrusted with the performance of civic duties and functions which would otherwise be governmental duties and functions. Finally, they must have the power to raise funds for the furtherance of their activities and the fulfilment of their projects by levying taxes, rates, charges, or fees. This may be in addition to moneys provided by government or obtained by borrowing or otherwise. What is essential is that control or management of the fund must vest in the authority.

In addition to the above the Honourable Supreme Court also adopted the another test laid down in the decision of supreme Court in *Municipal Corporation of Delhi v. Birla Cotton Mills* AIR 1968 SC 1232, wherein Hidayatullah, J., described some of the attributes of local bodies as subordinate, branches of governmental activity. They are democratic institutions managed by the representative of the people. They function for public purposes and take away a part of the government affairs in local areas. They are political subdivisions and agencies which exercise a part of State functions.

As they are intended to carry on local self-government the power of taxation is a necessary adjunct to their other powers. They functional under the supervision of the government. Supreme Court In *Valjibhai Muljibhai Soneji v. State of Bombay*, AIR 1963 SC 1890 wherein the question was whether the State Trading corporation was a local authority as defined by Section 3(31) of the General

Clauses Act, 1897. It was held that it was not, because it was not an authority legally entitled to or entrusted by the government with, control or management of a local fund. It was observed that though the corporation was furnished with funds by the government for commencing its business that would not make the funds of the corporation 'local funds'.

5. According to the Assessee it was established under the VIDC Act with the object of mobilizing resources to complete some ongoing irrigation projects in time bound manner, for promotion and operation of the said irrigation projects in Vidarba region, area development and schemes for generation of hydro-electric energy to harness the water of godavari and tapi rivers allocated to the State of Maharashtra under the Water Disputes Tribunal Award and other allied and incidental activities including flood control which was a sovereign function. It was a separate legal entity and its area of operation is clearly defined in the VIDC Act. The members of the Assessee Corporation also include elected representatives of the people besides official members and experts. It has autonomy and freedom to decide for itself question of policy affecting the area administered by it. It has power to collect taxes in the form of water charges and the control and management of the fund vests with the Assessee corporation.

6. The Assessing Officer however was of the view that the members of the Assessee are not elected directly or indirectly by the inhabitants of the area, they do not perform any functions and duties which are usually entrusted to municipal bodies such as providing civic amenities to the inhabitants of the locality like health, education, town planning, markets, transportation etc. and that the Assessee does not have powers for compulsory exaction of taxes. The Assessing Officer was of the view that the decision of the Supreme Court in the case of CIT v. U.P. Forest Corporation AIR 1998 SC 1125 would be applicable to the facts of the Assessee's case in which the supreme court applied the tests laid down in R.C. Jain's case (Supra) in coming to the conclusion that U.P. Forest Corporation was not a Local Authority under Section 10(20) of the Act, 1961. The Assessing Officer accordingly rejected the claim of the Assessee for adopting its status as a 'Local Authority'.

7. Thereafter the Assessing Officer made assessment of the income as per the Return of Income filed by the Assessee. The Assessing Officer noticed that the Assessee had claimed a sum of Rs. 1,40,31,211/- as loss and the Assessee also claimed carry forward of this loss. The Assessing Officer was of the view that under Section 42(2) of the VIDC Act, the net deficit, if any, in respect of any of the objects of the assessee shall be solely borne by the State Government. He was therefore of the view that the loss claimed was not Assessee's loss and therefore no carry forward of losses can be allowed.

8. Thereafter the Assessing Officer noticed that in June, 1997 the Assessee had issued bonds aggregating Rs. 100 Crores for augmenting the funds necessary for completing its projects. In connection with the said public issue expenditure to the extent of Rs 7,95,21,198/- was incurred. This sum was debited in the profit and loss account.

According to the Assessing Officer the expenditure was of a capital nature as laid down in the decision of the Honourable Supreme Court in the case of Madras Industrial Investment Corporation v. CIT 225 ITR 802 (SC) and such expenditure was to be written off proportionately over the period of redemption. In respect of A.Y.98-99 a sum of Rs. 1,19,28,180/- alone is allowable as deduction being proportionate write off for A.Y.98-99.

9. The Assessee had claimed deduction under Section 80-IA of the Act in the computation accompanying the' return. The claim was made on the ground that the Assessee was a industrial undertaking engaged in developing and operating infrastructure facility as defined under Section 80-IA(12)(ca). This claim was however withdraw by Assessee's letter dated 22.1.2001 in the course of assessment proceedings. The Assessing Officer however held that the Assessee is not entitled to deduction under Section 80-IA of the Act.

10. The Assessing Officer noticed that the Assessee in the Profit & Loss Account had claimed loss of Rs. 1,40,31,211/-. There was another debit of Rs. 21,84,05,35/- in the profit and loss account which was sought to be capitalized. The Assessing Officer called upon the Assessee to explain as to why the sum of Rs. 21,84,05,357/- is sought to be capitalized and why the loss shown in the Profit

& Loss A/C.alone is sought to be claimed as a loss of the previous year. The Assessee vide his reply dated 16.2.2001 has claimed that the Deficit shown in the Profit & Loss Account is being capitalized for the reason that till the end of the previous year none of the ongoing projects (irrigation, dams & canals etc.) were completed and ready for their intended use i.e., the qualifying asset was not ready for its intended use. Therefore all the borrowing cost incurred during the year including 1) Bond issue expenses; 2) Interest on bond paid to bond holders should essentially be capitalized, after deducting there from income received from temporary investment of those borrowed funds. This according to the Assessee was in keeping with the Accounting Standard AS-10 of the Institute of Chartered Accountants of India dealing with capitalization of Administrative and other general overhead expenses during the construction of projects.

11. According to the Assessing Officer this admission by the Assessee that its business has not commenced had very serious consequences. The first consequence being that no loss from business can be claimed and all expenditure whether of revenue or of capital nature should be capitalized. The Assessing Officer relied on the decision of the Honourable Supreme Court in the case of Challapalli Sugars Ltd. v. CIT 98 ITR 167 (SC) for the above proposition. The Assessing Officer therefore was of the view that the Profit & Loss Account of the Assessee can never be the basis to determine the income of the Assessee. The Assessing Officer thus in effect concluded that there could be no computation of income or loss from business, as the business had not yet commenced. The second consequence was that though the business of the Assessee had not commenced yet the Assessee was in receipt of income which can be classified under the other heads of income viz., Income from other sources and Income from House Property and these incomes will have to be determined under the respective heads of income. The further consequence was that the Assessee cannot seek to set off the income chargeable under the head income from other sources or income from house property against the interest paid on the bonds and Bond issue expenses. In coming to the above conclusion the Assessing Officer placed reliance on the following decisions: The Assessing Officer thereafter proceeded to determine the income of the Assessee by applying the principles laid down in the aforesaid decisions. He held that the following incomes received by

the Assessee are liable to be taxed under the head 'Income from other sources': Interest on FDR (Escrow A/C) Rs. 14,96,548 Interest on FDR (Collection A/C) Rs. 77,15,384 Interest on FDR (Operation A/C) Rs. 7,90,42,488 ----- 12. The Assessee had constructed residential quarters at its various project sites. These residential quarters were used to house the employees. The Assessee recovered a sum of Rs. 18,89,693/- as rent from the employees. This sum was construed by the Assessing Officer as Income from House Property chargeable to tax under the said head under Section 22 of the IT Act, 1961. He allowed a deduction of 1/5th of the rent received viz., Rs. 3,77,939/- towards repairs and collection charges and determined the net income chargeable under the head 'Income from House Property' at Rs. 15,11,754/-.

13. Thereafter what remained to be considered by the Assessing Officer was as to the various other incomes and expenditure set out in the profit and loss account: _____

Expenditure Rs. Rs. Sale of Water 1,12,09,306 Administrative Expns.

77,82,270 Interest recd from Contractors 20,03,410 Interest paid on bonds 22,75,94,879 Registr. Fees from Contractors 47,38,800 Bond Issue Expns.

7,95,21,198 Sale of Tender forms 26,29,797 Administrative Expns. Hire Charges of charged to works 24,62,58,111 Total 3,91,75,777 56,11,56,458 _____

The Assessing Officer allowed Rs. 52,19,80,681/- to be capitalized as pre commencement expenses. The total Income was thus determined as follows: Income from House property: Rs. 15,11,754 Income from other sources Rs. 8,82,54,420 ----- Total Income Rs. 8,97,66,170/- ----- 14. Aggrieved by the order of the Assessing Officer the Assessee preferred appeal before the CIT(A). Before the CIT(A) the following grounds were raised by the Assessee: i) That it was a Local Authority and that its income, if any, is exempt under Section 10(20) of the Act.

ii) That where funds are borrowed for the purpose of obtaining a qualifying asset, the amount of borrowing costs should be capitalized as cost of obtaining the qualifying asset. If the borrowed funds are utilized by making temporary

investments and in the process some income is earned, a interest received by the Assessee on temporary investment of borrowed funds will go to reduce the borrowing cost that has to be capitalized as cost of obtaining the qualifying asset. This according to the Assessee was in keeping with Paragraph 10 & 11 of the Accounting Standards (AS-16) issued by the Institute of Chartered Accountants of India.

iii) Alternatively, it was submitted by the Assessee that even if the interest income is treated as 'Income from other sources', then the amount of interest paid to the bondholders should be allowed as a deduction under Section 57 of the Act.

iv) If interest paid to the bondholders is set off against the interest income received, the result will be that there will be a loss under the head 'Income from other sources' as the interest received on temporary investment of borrowed funds far exceeds the interest paid to the bond holders. The Assessee pleaded that the loss so determined should be allowed to be carried forward to be set off against the profits of succeeding assessment years as per the provisions of the Act.

v) Alternatively, the assessee pleaded that the Interest income be treated as Income from Business and after setting off the interest paid to the bondholders (which is much more than the interest received by the Assessee), allow the net interest expenditure to be capitalized.

vi) Regarding the assessment of income received in the form of Rent from employees under the head 'Income from House Property', the Assessee contended that the houses were built at various sites/divisional offices of the Assessee corporation specifically to satisfy the needs of expediting the ongoing projects of the corporation and that they were not located in cities/town to fetch any 'rental income', in the real meaning of the term. The Assessee contended that it was income from exploitation of a business asset and therefore should be construed as income from business. The Assessee relied on the decision of the Honourable Supreme Court in the case of Universal Plast Ltd. v. CIT 237 ITR 454(SC). If construed as a Business income the assessee pleaded that the expenditure incurred in the form of interest paid to bondholders (which is much more than the income received from the property) to be allowed to be set off

against the said income and capitalize the net expenditure.

Apart from the above the Assessee raised some additional grounds before the CIT(A) and these additional grounds were as follows: i) That if the status of the Assessee is not held to be that of a "Local Authority", then hold that the Assessee is an Authority whose income is exempt from tax under Section 10(20A) of the Act.

ii) Alternatively hold that the Assessee is a State entitled to exemption of tax on its income under Article 289(1) of the Constitution of India.

iii) Alternatively hold that the Assessee is a Trust eligible for exemption under Section 11 of the Act.

15. The findings and conclusions of the CIT(A) on the various grounds raised by the Assessee in their appeal were as follows: 1. With regard to the claim of the Assessee that it is a 'Local Authority' entitled to exemption under Section 10(20) of the Act, the CIT(A) considered each one of the attributes which an authority must possess to come within the definition of 'Local Authority' as laid down in the decision of the Honouable Supreme Court in the case of Union of India v. R.C. Jain (Supra) and after elaborate discussion of the submissions of the Assessee and considering the various provisions of the VIDC Act, held as follows in paragraph 70 of her order: 1. The Appellant Corporation cannot be treated at par with a Municipal Committee, District Board or Body of Port Commissioner and it does not handle any governmental functions and duties as are usually entrusted to Municipal bodies.

2. It does not have a defined jurisdiction and in any case, the area of operation belonging to the corporation cannot be called a Local Area. 3. It does not have any power to levy any tax duty or cess. The water charges collected by it are nothing but on sale of water.

Thus, there is no compulsory exaction. It cannot levy betterment charges.

2. With regard to the claim of the Assessee that it is an Authority entitled to exemption under Section 10(20A) of the Act, the CIT(A) held that the Assessee is not involved in implementation of any housing programme or for the purpose of

planning, development or improvement of cities, towns and villages or for both but was formed for the purpose of completing some ongoing irrigation projects and Hydro-electric power projects, which cannot be said to be planning, development or improvement of any city, town or village though the activity of the corporation remotely and indirectly will have impact on the planning, development or improvement of city, town or village.

3. With regard to the claim of the Assessee that it is a State whose income is exempt under Article 289(1), the CIT(A) held that the Assessee was a body corporate having perpetual succession and a common seal capable of suing and being sued in its name with power to borrow and spend. On dissolution the properties, funds and dues realizable by the corporation and liabilities of the corporation vest in the State Government. In the light of the ratio laid down by the Honourable A.P. High Court in the case of APSRTC v. CIT 47 ITR 101 (AP) affirmed by the Honourable Supreme Court in 52 ITR 524 (SC) and the decision of the Honourable Bombay High Court in the case of Vidarbha Housing Board v. ITO 92 ITR 430 (Bom), the CIT(A) held that the Assessee cannot be a State whose income is exempt under Article 289(1) of the Constitution.

4. With regard to the claim of the Assessee that it is a trust whose income is exempt under Section 11 of the Act, the CIT(A) held that to claim exemption under Section 11 there must be a trust deed and an application made under Section 12A to the Commissioner of Income Tax and a registration under Section 12AA. The CIT(A) held that the Assessee not having raised this issue before the Assessing Officer it was not possible to give any findings in the appeal as held by the Honourable Supreme Court in the case of CIT v. U.P. Forest Corporation 230 ITR 945 (SC). She also held that the Assessee was a Company within the meaning of Section 2(17) of the Act and therefore cannot be held to be a Trust whose income is exempt under Section 11 of the Act.

5. With regard to the claim of the Assessee that Interest income and Income from House property has to be treated as business income and allowed to be capitalized, the CIT(A) held that the Assessee having not commenced business, no income under the head 'Profits & Gains of Business' can be earned by it. But

the company having earned income from other sources, viz., interest from investments and interest from house property, the same is required to be taxed under those respective heads. The CIT(A) in holding as above relied on the decision of Honourable Supreme Court in the following cases: 6. With regard to the claim of the Assessee that if interest income is held to be income from other sources, then the interest paid by the Assessee to the bondholders be considered as expenditure incurred in earning the interest and allow deduction under Section 57 of the Act, the CIT(A) held that what is contemplated under Section 57 is interest paid on borrowing for the purpose of earning the interest income. She held that the borrowing in the present case by the Assessee by issue of Bonds was for the purpose of completing ongoing projects handed over to it by the State Government. She therefore held that the Assessee cannot claim the interest paid to the bondholders as expenditure in connection with earning the interest income and disallowed the claim of the Assessee.

7. With regard to the claim of the Assessee for carry forward and set off of loss under the provisions of the Act, she held that under Section 42(2) of the VIDC Act, the net deficit, if any, in respect of any of the objects shall be solely borne by the State Government.

Therefore the Assessee cannot claim set off or carry forward of loss. We should mention in this connection that in the light of the findings by the Assessing Officer which findings was affirmed by the CIT(A) to the effect that the Assessee never commenced any business and its claim for business loss was rejected and the entire expenditure was allowed to be capitalized, there was no occasion to render any decision on this ground. The income determined under the head Income from other sources and Income from House Property was again a positive income and therefore there was no occasion for the CIT(A) to have rendered any decision on this aspect at all.

16. Aggrieved by the order of the CIT(A) the Assessee has preferred the present appeal. The original grounds of appeal were not specific, were argumentative in nature and therefore we directed the Learned Counsel for the Assessee to raise specific grounds of appeal. On our direction the Learned Counsel has filed specific

grounds of appeal. The Assessee has also requested that the following additional grounds of appeal be allowed to be raised and decided: The Appellant Corporation started its business on the inception and the Income & Expenditure Account and the Balance Sheet of the year under consideration should be read keeping in view this position.

The Net Deficit after deducting all the allowable business expenditure should be allowed to be recast and worked out and then the resulting losses should be allowed to be carried forward as per the provisions of the Income Tax Act, 1961.

The additional ground can be decided on the facts available on record and we are of the view that the Assessee should not be denied the opportunity of putting forth his objections on mere technicalities. We therefore deem it proper to permit him to raise the additional ground.

We shall deal with the various grounds of appeal and the additional ground at the appropriate place.

17. Before we deal with the various grounds of appeal of the Assessee, we deem it proper to narrate the circumstances under which the Assessee came to be established. The statement of objects and reasons for enacting the VIDC Act under which the Assessee was created describes the reason and the circumstances under which the Assessee came to be established. Some of the extracts from the same are as follows: The irrigation potential in the Vidarbha Region of Maharashtra State comprising 2 Revenue divisions, and 9 districts, is about 2 lac.ha.

Out of this about 7 Lac.ha.irrigation potential has been created by June, 1995. Thus an additional about 15 Lac.ha. potential is yet to be created through development of ongoing and future irrigation projects.

75% dependable yield in this region is about 981 Thousand Million cubic-foot (TMC) of water. However, the Maharashtra State can utilize 785.1 TMC of water because of the limitations imposed by the Inter State Water Dispute Tribunal Award. So far irrigation projects utilizing 177 TMC of water have been completed

and projects utilizing 186.19 TMC are under construction. Future projects establishing a use of 275.1 TMC of water are yet to be taken up. The balance cost of the ongoing projects, at 1994-95 price level, is RS. 4430 Crores and the cost of the future projects is about Rs. 9631 Crores. On an average Rs. 200 to 300 cr. Have been allocated annually for the irrigation projects in Vidarbha region. Since the cost of the ongoing projects is Rs. 4430 cr., it will require about 15 years to complete them. There is a irrigation backlog of about 2 lac.ha. in this region by June, 95 in terms of the Dandekar Samiti report. In order to remove this backlog, through a time bound programme, and to complete 10 selected ongoing projects, a fiscal provision of Rs. 3800 crores will be required in the next 5 years.

With the completion of these 10 projects, an irrigation potential of 5.89 Lac.ha. will be created, establishing a water use of 140 TMC. Therefore, the budgetary support will have to be supplemented through open market borrowings for the completion of these 10 projects in the above period. The experience of the Maharashtra Krishna Valley Development Corporation - a statutory corporation of the State, in raising funds by floating bonds-private/public issue, has been very much encouraging- Accordingly, Government of Maharashtra considers it expedient to set up a corporation called 'Vidarbha Irrigation Development Corporation' for the purpose of completion of 10 selected ongoing irrigation projects through a time bound programme. The Corporation would be a body corporate and functionary body consisting of official and non-official members including experts. The corporation would get initially funds from the State Government by way of grants, subventions, loans, advances etc. The Corporation is being empowered and entrusted with exhaustive powers and functions to complete 10 selected ongoing projects through a time bound programme. Power is also taken to the State Government to dissolve the corporation on achieving the objectives for which the corporation is established.

The Assessing Officer and Learned CIT(A) erred in arriving that the decision of Honourable Supreme Court in the matter of Union of India v. R.C. Jain in Delhi Development Authority case is not applicable to the Appellant Corporation and the Corporation is not 'Local Authority' within the meaning and scope as enumerated by the Supreme Court decision in the aforesaid order and therefore deprived the

Appellant of its legitimate claim of exemption under Section 10(20) of the IT Act.

Under Section 10(20) of the Act, while computing the total income of a previous year of any person, any income of a local authority which is chargeable to tax under the head income from house property, capital gains, income from other sources or from a trade or business carried on by it which accrues or arises from the supply of a commodity or service (not being water or electricity) within its own jurisdictional area or from the supply of water or electricity within or outside its own jurisdictional area, shall not be included. The term 'Local Authority' has not been defined in the Act. The term Local Authority has however been defined under the General Clauses Act, 1897. Under Section 3(31) the term 'Local Authority' has been defined as follows: 'Local Authority' means a Municipal Committee, a District Board, a body of Port Commissioners, or other authority legally entitled to or entrusted by the Government with the control or management of a municipal or local fund.

Income Tax Act, 1961 being a Central Act, the definition contained in Section 3(31) of the General Clauses Act, 1897 has to be considered in coming to a conclusion whether the Assessee can be said to be 'Local Authority' entitled to claim exemption under Section 10(20) of the Act.

The definition of 'Local Authority' contained in Section 3(31) of the General Clauses Act, 1897 is in two parts. The first part refers to specific authorities like Municipal Committee, a District Board, a body of Port Commissioners. The second part is generic and covers any other authority legally entitled to or entrusted by Government with the control and management of a municipal or local fund. The second part therefore suggests that in order any other authority to be a local authority should be legally entitled to or entrusted by the Government with the control or management of a local fund and must also possess many, if not all, of the distinctive attributes and characteristics of a Municipal Committee, District Board or Body of Port Commissioners. Union of India v. R.C.Jain AIR (1981) 951 S.C. has laid down the distinctive attributes and characteristics, all or many of which a Municipal Committee, District Board or Body of Port Commissioners shares with any other local authority. The question before the Honourable

Supreme Court in the said case was as to whether Delhi Development Authority was a Local Authority within the meaning of Payment of Bonus Act, 1965 and if it were a Local Authority the provisions Payment of Bonus Act did not apply to it. The term Local Authority was not defined in the Payment of Bonus Act, 1965. The Court therefore applied the definition of a Local Authority as contained in Section 3(31) of the General Clauses Act, 1897.

The following were the attributes and characteristics which the Honourable Supreme Court has laid down in deciding the question whether an authority is a local authority.

1. First, the authorities must have separate legal existence as corporate bodies. They must not be mere governmental agencies but must be legally independent entities.
2. Next, they must function in a defined area and must ordinarily, wholly or partly, directly or indirectly, be elected by the inhabitants of the area.
3. Next, they must enjoy a certain degree of autonomy, with freedom to decide for themselves questions of policy affecting the area administered by them. The autonomy may not be complete and the degree of the dependence may vary considerably but, an appreciable measure of autonomy there must be.
4. Next, they must be entrusted by statute with such governmental functions and duties as are usually entrusted to municipal bodies, such as those connected with providing amenities to the inhabitants of the locality, like health and education services, water and sewerage, town planning and development, roads, markets, transportation, social welfare services etc. etc. broadly we may say that they may be entrusted with the performance of civic duties and functions which would otherwise be governmental duties and functions.
5. Finally, they must have the power to raise funds for the furtherance of their activities and the fulfilment of their projects by levying taxes, rates, charges, or fees. This may be in addition to moneys provided by government or obtained by borrowing or otherwise. What is essential is that control or management of the

fund must vest in the authority.

20. The Learned Counsel for the Assessee referred to the various provisions of the VIDC Act and submitted that Appellant satisfies all the attributes as laid down by the Honourable Supreme Court in the case of Union of India v. R.C. Jain (supra). He referred to the various provisions of the Delhi Development Act, 1957 which was the subject matter in R.C. Jain's case (supra) and sought to compare the said provisions with that of the VIDC Act. We should in this context observe that the object sought to be achieved by the two enactments were not the same and though a comparison of the provisions of both the Acts would be necessary but what is material is that the tests laid down by the Honourable Supreme Court are broader principles and the Assessee should satisfy them so as to be called a Local Authority within the meaning of Section 3(31) of the General Clauses Act, 1897.

21. The Learned Standing Counsel for the Revenue on the other hand referred to the various provisions of the VIDC Act and submitted that the Appellant does not satisfy any of the attributes (except one attribute) as laid down by the Honourable Supreme Court in the case of Union of India v. R.C. Jain (Supra).

22. We shall now deal with each of the attributes laid down by the Honourable Supreme Court in the case of Union of India v. R.C. Jain (Supra) 23. With regard to the 1st attribute laid down by the Honourable Supreme Court viz., that the authority must have separate legal existence as corporate bodies and must not be mere government agencies, it is not in dispute that under Section 3(2) of the VIDC Act, the Assessee is a body corporate having perpetual succession and a common seal, with power to contract, acquire, hold and dispose of property, both movable and immovable and to do all things, necessary for the purpose of the VIDC Act, and it may sue be sued by its corporate name.

Therefore the Assessee satisfies the first attribute laid down by the Honourable Supreme Court.

24. The 2nd attribute laid down by the Honourable Supreme Court is that they must function in a defined area and must ordinarily, wholly or partly, directly or

indirectly be elected by the inhabitants of the area. This attribute is in two parts, the first part refers to the area of functioning of the Authority and lays down that such area should be a defined area. The second part deals with the constitution of the authority and lays down that its members must comprise partly, directly or indirectly be elected by the inhabitants of the area.

25. Regarding the area of functioning of the Assessee the VIDC Act lays down in Section 1 that it shall extend to the area of Godavari and Tapi Rivers Valley in Vidarbha Region of the State of Maharashtra, specified in the Schedule and such other area or areas as the State Government may, by notification in the official Gazette, specify. Section 2(a) defines 'Area of operation of the Corporation' as the area of the godavari and tapi rivers Valley specified in the Schedule and any other area or areas to which the provisions of the VIDC Act are extended by the State Government, by notification in the Official Gazette, under Sub-section (2) of Section 1.

26. According to the Learned Counsel for the Assessee the area of functioning of the Assessee is clearly defined. According to the Learned Standing Counsel the Area is not properly defined. He drew our attention to the Schedule to the VIDC Act wherein 10 irrigation projects spread over in 9 different districts of Vidarbha have been handed over by the State Government to the Assessee in respect of which the Act extends. He brought to our notice that the Schedule refers to Catchments area, submergence area and command area of the 10 irrigation projects within the geographical limits of the Districts specified against each of them. His submission in this regard is that the VIDC Act does not define as to what is a catchments area, submergence area and command area. His alternate submission is that even if what is a catchments area, submergence area and command area can be identified, the Assessee has not produced any material to show that these areas are identifiable.

27. We have considered the rival submission. We are of the view that from the Schedule to the VIDC Act it is not possible to say that the area is a defined area. What has been handed over to the corporation under the VIDC Act is 10 irrigation projects mentioned in the Schedule to the said Act. The Geographic limit is not the

geographic limits of the 9 Districts referred to in the Schedule. The geographic limit is in respect of Catchments area, submergence Area and Command Area of 10 irrigation projects within the geographic limits of the aforesaid 9 districts. In the absence of any definition or explanation as to what is catchments area, submergence Area and Command Area, it is not possible to identify the geographic area of operation of the Assessee from a mere perusal of the VIDC Act. Besides this we agree with the conclusion of the CIT(A) that the area administered by a local authority should be of such type and size which is clearly manageable by a municipal body and that the area administered by the Assessee extending to over 9 districts of Vidharba cannot be said to be a defined area. This view will be in consonance with the concept of local self government for which local authorities exist.

28. Regarding the second part of the Second attribute that the members of the authority must ordinarily, wholly, or partly directly or indirectly be elected by the inhabitants of the area, Section 4 (1) of the VIDC Act with regard to the members of the VIDC provides as follows: b) One non-official member to be nominated by the State Government - Vice Chairman.

d) Secretary (1) to Government, Irrigation Department- Ex-officio Managing Director.

e) Secretary (Command Area Development) to Government, Irrigation Department. - Ex-officio member; h) Secretary (Forest) to Government, Revenue and Forest Department - ex-officio member i) Secretary (Relief and rehabilitation) to Government, Revenue and Forests Department - ex-officio member.

j) Secretary to Government, Agriculture Department - ex-officio member k) Three non-official members representing reputed and recognized financial institutions, to be nominated by the State Government; l) Five members to be nominated by the State Government, from amongst the members of the Maharashtra State Legislative Assembly; m) Three members to be nominated by the State Government, from among the members of the Maharashtra State Legislative Council.

n) Two non official qualified members to be nominated by the State Government having graduation and special knowledge and practical experience, one each from the field of irrigation and finance respectively.

o) One officer not below the rank of Secretary to Government, from the cadre of engineering services of the irrigation department to be appointed by the State Govt. as Member-secretary of the corporation who shall be designated as the Executive Director of the Corporation.

According to the Learned Counsel for the Assessee there are at least 5 MLA's, 3 MLC's and One Minister of Irrigation who are members of the Assessee. There is thus popular representation in the matter of choosing members of the Assessee. The Learned Standing Counsel pointed out that there is no popular representation by the inhabitants of the Vidharba region where the Assessee functions. Referring to the Section 4(1) he submitted that the Minister, MLA's and MLC's could be elected representative from any area and not necessarily MLA's, Minister, MLC's from vidharbha region. This according to him will not be enough to fulfill the test of election by the inhabitants of the area where the Assessee functions. He also submitted that factually there was no member from the vidharbha region The Learned Counsel for the Assessee on the other hand referred to the fact that an MLA or Minister represents the whole of the State and therefore they can be said to represent the local inhabitants of the Vidharbha region also. He also referred to an amendment made to Section 4(1) of the VIDC Act, w.e.f.24.10.2000 whereby for the existing Section 4(1)(b) of the VIDC Act, the following Clause (b) was substituted: b) Two non official members from Vidarbha Region to be nominated by the State Government - ex-officio vice-chairman.

The amendment being clarificatory in nature should be deemed to apply retrospectively. This according to him is sufficient to hold that there are enough members who are elected by the inhabitants of Vidarbha.

29. We have considered the rival submissions. We find that the members are not either directly or indirectly chosen by the inhabitants of the vidharba region. Element of popular representation of the people of vidarbha is clearly missing. Even the amendment to the VIDC Act only refers to two non-official members and

such non official members need not necessarily be elected representatives of the Vidarbha region.

Besides this as a fact there was no members of the Assessee who were either MLA's, MLC's from the Vidarbha region. We are therefore inclined to conclude that the Second attribute laid down by the Honourable Supreme Court in R.C. Jain's case (Supra) is not fulfilled by the Assessee. While dealing with the second attribute as laid down in R.C.Jain's case by the Hon'ble Supreme Court, we have to keep in mind that the local bodies or subordinate branches of government activity, they are democratic institutions managed by the representative of the people. They function for public purposes and take away a part of the government affairs in local areas. They are intended to carry on local self government.

30. The 3rd attribute laid down by the Honourable Supreme Court in R.C. Jain's case (supra) is that the authority must enjoy a certain degree of autonomy, with freedom to decide for themselves questions of policy affecting the area administered by them. The autonomy may not be complete and the degree of the dependence may vary considerably but an appreciable measure of autonomy must be there. The Learned Counsel for the Assessee in this regard submitted that the following powers vested in the Assessee by the VIDC Act clearly show that the Assessee is an autonomous body. Under Section 18 the Assessee has freedom in the matter of promoting and operating, planning, investigating, designing, constructing and managing irrigation projects and their command area, to enter into contracts and do many activities as listed in the said section. Under Section 19 the Corporation has general powers to hold properties, movable and immovable and other powers as listed in Section 19. Under Section 12 it has power to appoint officers and servants.

Under Section 20 it has power to collect water charges. Under Section 22 it has power to restrict any person from constructing any dam, bandhara, weir etc within their area of operation. Under Section 24 it has power to exercise the powers under the Maharashtra Irrigation Act, 1976. Under Section 26 it has power to acquire lands. Under Section 30 all grants by State Govt. all other receipts, income will be the fund of the assessee and under Section 35 the assessee has power to

spend from and out of of the fund in any manner it likes. Under Section 33 it has powers to borrow upto Rs. 1000 Crores. All these powers according to the Learned Counsel for the Assessee would show that the Assessee functions with a great degree of autonomy. The fact that there are some provisions in the Act under which the State Government's approval is to be obtained will not make the authority non autonomous and those powers are merely supervisory and such powers vested in the State Government are usual in all enactments.

31. The Learned Standing Counsel on the other hand submitted that under the provisions of Section 2(c) of the VIDC Act and submitted that Area of operation as stated in the Schedule is 10 projects which were handed over to it by the State Government. Under Section 18 the functions of the corporation are restricted only to promote and operate the 10 projects which are mentioned in the Schedule to the VIDC Act. In other words it is a case where the Assessee has to merely execute the work entrusted to it by the State Government. In the process it enjoys some powers to execute the work entrusted to it. Executing projects alone does not give any sort of autonomy to the Corporation. He referred to the letter dated 8.10.2001 of the Assessee wherein the Assessee had stated that they had not executed any of the projects except the 10 projects transferred to it by the State Government. He pointed out that in the said letter it has been admitted by the Assessee that they have no powers to do any project without the approval of the State Government.

32. We have considered the rival submissions. We are of the view that the purpose for which the corporation was established as stated in the statement of objects and reasons as well as from the preamble of the Act is to mobilize resources for completion of 10 pending irrigation projects in a time bound manner. From a perusal of Section 2(a) & 2 (c) read with Section 18 it is clear that any irrigation project or hydro-electrical energy project within the area of operation of the corporation shall be decided only by the State Government. The Assessee cannot embark upon any new irrigation project or hydro-electrical energy project on it's own other than those mentioned in the Schedule to the Act. The General powers of the Corporation under Section 19 are restricted only to carrying out its functions under the Act which itself is subject to the area of operation determined

by the State Government. Under Section 2(e) 'Irrigation project' means the planning, construction, maintenance and management of major, medium and minor irrigation projects and shall include command area development, floor control and other allied activities. What is handed over to the corporation is only to mobilize resources and complete irrigation projects. The State Government therefore hands over an irrigation project to the Assessee. There is therefore no occasion for the Assessee to decide on any question of policy affecting any area administered by them. The State Government decides on the planning, construction, maintenance and management of irrigation projects and the Assessee merely executes those projects. Under Section 20 the Assessee has powers to levy water charges and such water charges shall be at least sufficient to meet the interest and loan repayment on the loans raised by the Corporation from the open market. Under Section 25 the State Government may issue to the Assessee such general or special directions as to policy or exercise of the powers or performance of the functions by the Corporation, excepting in respect of levying and recovery of water charges by the Assessee, as it may think necessary or expedient for carrying out the purposes of the VIDC Act and the Assessee shall be bound to follow and act upon such direction. Under Chapter V the Assessee does not have power to acquire land for the purpose of the VIDC Act only the State Government has the power. Even for disposal of the land vested in the Assessee under the Act, the Assessee will be bound by the rules made by the State Government in this behalf. Under Chapter VI the Assessee has financial autonomy in the sense that under Section 35 it has power to spend such sums as it thinks fit for the purposes authorized under the Act from and out of the fund of the corporation referred to in Section 30 or from the reserve and other funds referred to in Section 38. Under Section 33 it has power to borrow up to Rs. 1000 crores subject to such conditions as may be prescribed in this behalf. But there is rider to all these powers under Section 46 which provides that the Corporation shall in each financial year prepare and submit to the state government for approval an annual financial statement and the programme of work for succeeding financial year and the State Government may approve such financial statement and the programme of work of the corporation as submitted by the Corporation or with such variations as the State Government may think fit. Considering the various

provisions of the VIDC Act we are of the view that the degree of autonomy enjoyed by the Assessee is negligible and there is no occasion for it to make any decision on questions of policy affecting the area administered by it.

The 3rd attribute is therefore clearly missing in the case of the Assessee.

33. The 4th attribute laid down by the Honourable Supreme Court in R.C. Jain's case (Supra) is that the Authority must be entrusted by statute with such governmental functions and duties as are usually entrusted to municipal bodies, such as those connected with providing amenities to the inhabitants of the locality, like health and education services, water and sewerage, town planning and development, roads, markets, transportation, social welfare services etc. etc. broadly we may say that they may be entrusted with the performance of civic duties and functions which would otherwise be governmental duties and functions.

34. The Learned Counsel for the Assessee submitted that under Section 17 of the Act the employees of the State Government are deputed to the Corporation. The Irrigation Projects which were undertaken by the State Government have been transferred to the Assessee. Under Section 20 the Assessee has power to collect water charges. Under Section 24 the Assessee can exercise all the powers exercisable by the State Government under the Maharashtra Irrigation Act, 1976 & Bombay Canal Rules, 1934. Under Section 26 the Assessee has powers to acquire lands for the purposes of the VIDC Act. These provisions according to him are sufficient to hold that the Assessee is performing Governmental functions and duties. The objects of the Assessee corporation are also making available supply of water for domestic, industrial and agricultural sectors. The next part of the attribute viz., whether the government functions entrusted to the Assessee by the VIDC Act are such functions and duties as are usually entrusted to municipal bodies, such as those connected with providing amenities to the inhabitants of the locality, like health and education services, water and sewerage, town planning and development, road, markets, transportation, social welfare services etc. In this regard the submission of the learned counsel for the Assessee is that under Section 50 the Assessee has to rehabilitate persons affected by any of the Irrigation or hydro electric power projects in accordance with the provisions of the

Maharashtra Project Affected persons Rehabilitation Act, 1986 and the said Act the Assessee has resettle the persons affected in the same village and provide civic amenities to them, like health, education, services, water and sewerage town planning and development, roads, markets, transportation, social welfare services etc.

35. The Learned Standing Counsel referred to the provisions of Section 18 of the VIDC Act and submitted that a perusal of the various functions performed by the Assessee would show that these functions are not functions which are entrusted to municipal bodies like provisions of amenities to the local inhabitants. According to him irrigation is not a function which municipal bodies normally undertake and it is not a civic duty. Generally no municipality is given the job of ensuring proper irrigation facilities. His next submission on the provisions of Section 18 and the VIDC Act as a whole is that nowhere the Assessee is cast a duty to supply water. The various provisions only enable the Assessee to complete the irrigation projects entrusted to it. On the provisions of Section 20 which enable the Assessee to collect water charges for domestic, industrial and agricultural use, he submitted that the Act nowhere empowers supply of water directly to the inhabitants. Section 20 only enables the Assessee to supply to the State Government, Local Authority, Governmental agencies, cultivators and water user's association. According to him even on a reading of Section 20 it is clear that the Assessee does not supply water directly to the inhabitants and consequently there is no duty cast on the Assessee to supply water to inhabitants of the locality.

36. We have considered the rival submissions. We are of the view that providing Irrigation facility can be said to be a governmental function. But they are not governmental functions and duties which are usually entrusted to municipal bodies. According to the attribute laid down by the supreme Court, the functions and duties entrusted to an authority are further qualified by the words that the functions should be normally one entrusted to the municipal bodies and are restricted to the inhabitants of the locality and that they should be in relation to providing health and education services, water and sewerage, town planning and development, roads, markets, transportation, social welfare services etc. There is no duty cast on the Assessee to supply water to the inhabitants of the area within

which the Assessee operates.

Inhabitants of the area could consist of both agriculturist and non agriculturists. The provisions of the Act empower collection of water charges from the Agriculturists directly. When it comes to supply of water to non agriculturists the provisions only speak of the collecting water charge's from the state government, local authority, governmental bodies and water users association which by itself is an indication that the Assessee cannot supply water directly to all the inhabitants of the area. In other words supply of water to inhabitants of the area is only incidental or ancillary to the functions of the Assessee.

Moreover as rightly contended by the Learned Senior Standing Counsel the VIDC Act nowhere casts an obligation on the Assessee to supply water to any of the inhabitants of the area. Its function is restricted to construction of the irrigation projects and things incidental thereto and thereafter to maintain it. The true test of duty on the part of the Assessee to supply water to the inhabitants is to ask the question whether all the inhabitants have a right to demand water from the Assessee. The answer to the question will be that not all the inhabitants have a right to demand water except the Agriculturists.

37. The contention of the Learned Counsel of the Assessee that the Assessee has to rehabilitate persons affected by any of the irrigation projects and in the process they perform the function of health, education services, water and sewerage, town planning and development, roads, markets, transportation, social welfare services etc. is a far fetched argument. The person affected by the irrigation project of the Assessee cannot be said to be inhabitants of the area where the Assessee operates. They are only a part of the inhabitants. These provisions are merely provisions providing for compensation to the affected persons to ensure that he is put in the same position as he was before his displacement by reason of the irrigation project. We do not think that the Assessee is entrusted with any duties of provision of health, education services, town planning etc. We are of the view that the Assessee does not fulfill 4th attribute laid down by the Honourable Supreme Court in R.C. Jain's case (supra).

38. The 5th and last attribute laid down by the Honourable Supreme Court in R.C. Jain's case is that the authority must have the power to raise funds for the furtherance of their activities and the fulfillment of their projects by levying taxes, rates, charges, or fees. This may be in addition to moneys provided by government or obtained by borrowing or otherwise. What is essential is that control or management of the fund must vest in the authority.

39. The learned counsel for the Assessee submitted that this attribute viz., power of taxation it should be understood that the power referred to in this attribute has to be understood not in the strict sense of a tax but should be so construed as inclusive of a fee. The only requirement is that there should be compulsory exaction. In this regard he drew out attention to similar observations by the Honourable Supreme court in R.C. Jain's case. He submitted that under Section 20 of the Act the corporation is empowered to collect water charges and under Section 24 the Assessee has been given all the powers of a State Government under the Maharashtra Irrigation Act, 1976 and the Bombay Canal Rules, 1934 to collect water charges from users as well non users under certain circumstances. He next referred to the provisions of Section 46 of the Maharashtra Irrigation Act, 1976 and submitted that under Section 46(3) not only the holders or occupiers of lands within the irrigable command of a canal who wish to avail the facility of water supply during kharif or rabi sea from such canal are liable to pay water charges but also all occupiers of land within the irrigable command who do not wish to use the facility. The water charges from such persons are however collected at 50%. According to him this power is power of compulsory exaction.

40. The Learned Standing Counsel for the Revenue submitted that power to collect tax, rates, charges or fees would envisage that all inhabitants of the area have to pay the same irrespective of any benefit they get in return for the payment. Referring to the provisions of Section 20 he submitted that what is permitted to be collected by the Assessee is water charges from cultivators. Referring to the proviso to Section 20 he submitted that even this collection of water charges is subject to a minimum and the water charges so levied shall be enough to service the interest charges and repayment of the loan raised by the corporation from open market. The fact that under Section 46 of the Maharashtra Irrigation Act, 1976

the Assessee can collect water charges from the occupiers of the command area of a canal even if they do not use the irrigation facility provided by the Assessee at 50% of the charges paid by the persons who use the irrigation facility, by itself is not enough to conclude that there is compulsory exaction by the Assessee. He submitted that the occupiers of land in the command area whether they use the facility of irrigation or not are bound to get the facility of water due the fact that they would get the water facility due to the natural water stream as well as seepage of water owing to its closeness with the natural stream of water. This is the reason why they are asked to pay 50% of the water charges leviable. He next submitted that even as per the provisions of Section 59 of the Maharashtra Irrigation Act, 1976, the water charges supply rates are determined by the zilla parishad and not by the State Government and therefore it cannot be said that Assessee has any powers of compulsory exaction.

41. We have considered the rival submissions. In R.C. Jain's case the Honourable Supreme Court has observed as follows: In the first place when it is said that one of the attributes of a local authority is the power to raise funds by the method of taxation, taxation is to be understood not in any fine and narrow sense as to include only those compulsory exactions of money imposed for public purpose and requiring no consideration to sustain it, but in a broad generic sense as to also to include fees levied essentially for services rendered. It is now well recognized that there is no generic difference between a tax and a fee; both are compulsory exactions of money by public authority. In deciding the question whether an authority is a local authority, our concern is only to find out whether the public authority is authorized by statute to make a compulsory exaction of money and not with the further question whether the money so exacted is to be utilized for specific or general purposes. In the second place the Delhi Development Authority is constituted for the sole purpose of the planned development of Delhi and no other purpose and there is a merger, as it were, of specific and general purpose. The statutory situation is such that the distinction between tax and fee has withered away. In the third place we see no reason to hold that the charge contemplated by Section 37 is a fee and not a tax.

42. As can be seen from the above observation of the Honourable Supreme Court the same was in relation to the provisions of Section 37 of the Delhi Development Act, 1957 which was in relation to the levy by the Delhi Development Authority upon owners of properties betterment charges. These charges are generally exacted from the owners of properties in an area. The VIDC Act under Section 20 has the power to levy water charges: Section 20 reads as follows: The Corporation shall, from time to time, determine and levy water charges according to volume, for supply of water for irrigation, industrial and domestic purposes to the State Government, local authorities, Government agencies, cultivators and water users associations; (SIC) that the levy of water (SIC) charges so recovered shall be sufficient at least to cover the (SIC) charges and repayment of the loan raised by the corporation from the open market.

On a perusal of Section 20 of the VIDC Act three things are evident.

Firstly, the water charges are determined on the basis of interest charges and repayment of loan raised by the Assessee from the open market. Secondly, the water charges are recovered only from the consumers viz., the State Government, Local authorities, Government agencies, cultivators and water users associations. Thirdly, the water charges are payable in proportion to the consumption. The features are more like recovering cost for supply of an amenity. Therefore the Assessee cannot be said to have any powers of compulsory exaction of taxes. Under Section 24 of the VIDC Act, the Assessee can exercise all powers of the state government under the Maharashtra Irrigation Act, 1976. Even the tax on non users which the Assessee can claim to levy under Section 46 the Maharashtra Irrigation Act, 1976 can be levied only on occupiers of lands within the irrigable command of a canal. Even these occupiers if they have a well through which they irrigate the land, no water charges can be levied. As rightly contended by the Learned Standing Counsel, the occupiers of lands situate in a irrigable command of a canal will certainly benefit by the natural stream or seepage of water owing to nearness of the location of their land near the irrigation project. Under 59 of the Maharashtra Irrigation Act, 1976 water rates are determined by the appropriate authority, which is the zilla parishad under Section 59 of the said Act and not by the State Government. Thus the assessee will not have the power to determine

the supply rates even if the powers under the Maharashtra Irrigation Act, 1976 are sought to be exercised by the Assessee. We are therefore of the view that the Assessee does not fulfill the 5th attribute viz., compulsory exaction of taxes, fees, charges etc.

43. Apart from the above, the Learned Counsel for the Assessee submitted that the Assessee is vested with the control and management of a local fund under Section 30 of the VIDC Act. We have perused the relevant provisions of the VIDC Act. It is no doubt true that under Section 30 of the VIDC Act, the assessee shall have and maintain its own fund in which the moneys received by the assessee from the State Government, all fees, costs and charges received by the assessee under the Act, all moneys received by way of water charges, moneys received from disposal of land, buildings & other properties and (SIC) credited in this fund. Under (SIC) Corporation is empowered to borrow upto the limit not exceeding Rs. Thousand crores at a time. Under Section 35 of the VIDC Act, the corporation has authority to spend such amount as it thinks fit for the purposes authorised under VIDC Act, from and out of the fund of the Corporation. Under Section 39 the Corporation shall prepare the budget estimate and under Section 40 the budget estimates are required to be approved. Under Section 46, the Corporation is required to furnish for each financial year an annual statement and the programme of work of the Corporation for the succeeding financial year and these financial statements need to be approved by the State Government. The State Government has powers to make variation to the proposal submitted by the Corporation. It is clear from the analysis of the various provisions that whatever power has been vested with regard to the fund are subject to the prior approval of the State Government and thus, it cannot be said that the assessee has been vested with all powers of control and management of the local fund under the Act. Even if the provisions are construed having vested sufficient powers in the assessee in the matter of controlling it's own fund, the provisions of Section 46 of the Act are not merely supervisory in nature and all those powers are overriding powers vested in the State Government.

44. Now we shall discuss the various case laws relied upon by the learned Counsel for the assessee with regard to the 1st Ground of appeal. In R.C. Jain's

case (supra), the Hon'ble Supreme Court was dealing with the Delhi Development Authority (DDA) constituted under the Delhi Development Act, 1957. It is clear from the perusal of the decision in R.C. Jain's case that the DDA functions in a defined area and they had ascertained degree of autonomy in decision making relating to the policies and they were entrusted with the management of civic duties which are wholly performed by the Municipality. It was also found that they were under the control of local fund and had power of levy of taxes. We have already found in the present case that the assessee did not fulfil many of the attributes as laid down by the Hon'ble Supreme Court in R.C. Jain's case (supra). In coming to this conclusion, we have analyzed the provisions of the VIDC Act also. We find that the provisions of the VIDC Act and DDA Act, 1957 are not in pari materia the same. The provisions are made in a different context keeping in view the objectives sought to be achieved by the Delhi Development Authority. In the case of Kashi Vidyapeeth, AIR 1996 SC 2705, the Hon'ble Supreme Court no doubt held that the university established under the universities Act was to be considered as a local authority. The decision came to be rendered in the context of Land Acquisition Act. The question before the court was as to whether in the matter of acquiring land for the purpose of university, the fact that the fund for paying the compensation to the land owners came out of the state exchequer or not was to be decided. If the funds came from a local fund, the provisions of Chapter 7 of the Land Acquisition Act were not applicable. In that context, the Hon'ble Supreme Court held that since the funds of the University under the Universities Act were controlled by the state, it was held that the payment of compensation came from a local fund. We are of the view that in Kashi Vidyapeeth case, the narrow question came for consideration before the Hon'ble Supreme Court and the same cannot be applied in the context of the case of the assessee. In CIT v. U.P. Forest Corporation, AIR 1998 SC 1125, the Hon'ble Supreme Court considered the decision rendered in R.C. Jain's case and found that U.P. Forest Corporation did not satisfy many of the attributes that are necessary to be called a local authority under the Incometax Act. The decision in the U.P. Forest Corporation' case was rendered in the context of the provisions of U.P. Forest Corporation Act, 1975 and, therefore, we do not deem it necessary to discuss the facts of the said case.

The learned counsel for the assessee placed reliance on the decision of the Hon'ble Bombay High Court in the case of *Krishi Upaj Bazar Samiti v. G.P. Hardas*, 1985 MLR 377. We have perused the decision relied upon by the learned counsel for the assessee. From the perusal of the said decision, it is seen that under the APMC Act, while carrying out regulation of marketing of agricultural produce in a specified area, the state government declares by notification that marketing of agricultural produce specified in the notification shall be regulated under the APMC Act in the specified area. On issuance of such notification, the local authority notwithstanding anything contained in any other law for the time being in force are prohibited from establishing, authorizing, continuing or allowing to be established or continued in any place in the market for marketing of that agricultural produce. It is thus clear that in the case relied upon by the learned counsel for the assessee the authority created has substituted the functions of a local authority. Such feature is not in the present in the case of the assessee.

45. Apart from the above we find from a perusal of the various provisions of the Income tax Act, 1961, that a corporation established by the Central or State Act is assessable only in the status of a company as defined in Section 2(7) of the Incometax Act.

'Assessee' means a person by whom any tax or any other sum of money is payable under this Act, and includes:- (a) every person in respect of whom any proceedings under this Act has been taken for the assessment of his income or of the income of any other person in respect of which he is assessable or of the loss sustained by him or by such other person, or of the amount of refund due to him or to such other person; (b) every person who is deemed to be an assessee in default under any provision of this Act.

(c) Every person who is deemed to be an assessee in default under any provision of this Act" (ii) any body corporate incorporated by or under the laws of a country outside India, or (iii) any institution, association or body which is or was assessable or was assessed as a company for any assessment year under the Indian Income-tax Act, 1922 (11 of 1922), or which is or was assessable or was assessed under this Act as a company for any assessment year commencing on

or before the 1st day of April, 1970, or (iv) any institution, association or body, whether incorporated or not and whether Indian or non-Indian, which is declared by general or special order of the Board to be a company : Provided that such institution, association or body shall be deemed to be a company only for such assessment year or assessment years (whether commencing before the 1st day of April, 1971 or on or after that date) as may be specified in the declaration; "Indian company" means a company formed and registered under the Companies Act, 1956 (1 of 1956), and includes - (i) a company formed and registered under any law relating to companies formerly in force in any part of India (other than the State of Jammu and Kashmir [74 and the Union territories specified in Sub-clause (iii) of this clause) 74]; (ia) corporation established by or under a Central, State or Provincial Act; (ib) any institution, association or body which is declared by the Board to be a company under Clause (17); (ii) in the case of the State of Jammu and Kashmir a company formed and registered under any law for the time being in force in that State; (iii) in the case of any of the Union territories of Dadra and Nagar Haveli, Goa, Daman and Diu, and Pondicherry, a company formed and registered under any law for the time being in force in that Union territory : Provided that the registered or, as the case may be, principal office of the company, corporation, institution, association or body in all cases is in India; Section 2(31) defines a 'person' as follows: (v) an association of persons or a body of individuals, whether incorporated or not, (vi) a local authority, and (vii) every artificial juridical person, not falling within any of the preceding sub-clauses; Explanation - For the purposes of this clause, an association of persons or a body of individuals or a local authority or an artificial juridical person shall be deemed to be a person, whether or not such person or body or authority or juridical person was formed or established or incorporated with the object of deriving income, profits or gains; The assessee corporation clearly fits in the definition of a company and was rightly assessed in the status of a company by the revenue authorities. From the definition of a person under Section 2(31), it is clear that the company and local authority are two different assessable entities. Once a person falls in the definition of a company, it can never fall under the category of local authority. Even on reading the plain provisions of the Incometax Act, it is not possible to accept the contention of the assessee that the assessee is assessable

as a local authority and not as a company.

46. For the reasons stated above, we uphold the order of the CIT(A) in so far as her conclusions that the Assessee is not a 'Local Authority'.

Ground No. 1 is accordingly dismissed.

It is submitted that the CIT(A) wrongly arrived at the conclusion that the Appellant Corporation is not 'Development Authority' within the meaning of Section 10(20A) of the Income Tax Act, 1961 and deprived the Corporation of its legitimate claim of exemption available under the said section, despite strong plea put up by the Corporation.

48. Before we deal with the rival contentions we shall first extract the provisions of Section 10(20A) of the Act which reads as follows: Section 10: Income not included in Total income: In computing the total income of a previous year of any person, any income falling within any of the following clauses shall not be included- (20A) any income of an authority constituted in India by or under any law enacted either for the purpose of dealing with and satisfying the need for housing accommodation or for the purpose of planning, development or improvement of cities, towns and villages, or for both.

49. The learned counsel for the assessee submitted that under the provisions of the VIDC Act, the assessee was to construct hydro-electric power projects and to complete certain irrigation projects. It was also submitted that this would result in making available drinking water as well as power to the public. His further submission was that since water is necessary for development of city, town, villages, the functions performed by the Corporation are developmental functions. He then referred to the provisions of Section 23 whereby any railways lands and roads are required to be realigned for the purpose of carrying out the objects of the assessee and resettlement of any population is rendered necessary, the same has to be done by the assessee. Under Section 50, if any hydro power project or irrigation project is carried out in any area which result in displacement of persons then the assessee has to resettle and rehabilitate them in accordance "with the provisions of Maharashtra Project Affected Persons Rehabilitation Act, 1986. In

the process of the rehabilitation, it is submitted by the learned counsel for the Assessee, that the assessee has to construct houses and has to plan and develop the city, town villages in which the persons displaced have to be rehabilitated. Thus, according to the learned counsel for the assessee, the assessee performs developmental functions and also satisfies the needs of housing accommodation and also does planning, development and improvement to city town and villages. He then referred to the decision of the Hon'ble Supreme Court in the case of Gujarat Industrial Development Corporation v. CIT, 227 ITR 414 wherein the Hon'ble Supreme Court had laid down that the expressions "planning, development or improvement of cities, towns and villages or for both" appearing in Section 10(20A) of the Incometax Act, 1961 should be understood in a wide sense and not in a narrow sense. Thus, according to the assessee, even if indirectly, the functions mentioned in Section 10(20A) of the Act are performed by the assessee, the assessee is entitled to claim the exemption of its income. He also relied on the decision of the Hon'ble Rajasthan High Court in the case of CIT v. Rajasthan Land Devp. Corporation 121 Taxman 573(Raj) wherein it was held that the predominant activities of the corporation were related to agricultural and development activity of the same for the purpose of planned development; and the agricultural land could not be isolated from the development of villages and therefore, the lands fell within the ambit of corporation engaged into the activities of planning, development and improvement of agricultural lands which related to planning, development and improvement of villages.

50. The learned Standing Counsel for the revenue, in reply, submitted that under Section 10(20A), an authority should be constituted under an enactment and the enactment should be for the purpose of dealing with and satisfying the needs for (i) housing accommodation (ii) for the purpose of planning, development or improvement of cities, towns and villages or for both. Referring to the provisions of section VIDC Act, he submitted that the act has been passed for the purpose of mobilizing resources for completing some of the going irrigation projects in Vidarbha area in time bound manner and to promote and operate the said irrigation projects. According to the Standing Counsel for the revenue, the Act was not passed for the purpose of enabling the assessee to perform any of the functions set out in Section 10(20A) of the Incometax Act. With regard to the

rehabilitation of the affected persons by the projects, he pointed out that, as per Section 50 of the VIDC Act, the assessee does not rehabilitate or resettle the affected persons but merely provides fund to the State Government who does rehabilitation and resettlement in accordance with Maharashtra Projects Affected Persons Rehabilitation Act, 1986. His further submission was that even if we are to assume that the assessee performs any of the functions listed in Section 10(20A) of the IT Act, such performance of function is only incidental or ancillary and is only indirect. He also submitted that the reliance placed by the learned Counsel for the assessee on the decision of the Hon'ble Rajasthan High Court in the case of CIT v. Rajasthan Land Development Corporation, 121 Taxman 573 (Raj.), was not proper. He submitted that the Hon'ble Rajasthan High Court considered the definition of the word 'land development' as appearing in Section 2(i) of the Rajasthan Land Development Corporation Act, 1975 and found that the object of the said enactment was planning and development of villages also. He thus, concluded that the decision of the Rajasthan High Court will also not help the case of the assessee as the said decision was on the facts of the said case before the Rajasthan High Court and the facts of the present case are distinguishable.

51. We have considered the rival submissions. We are of the view that the assessee in the present case cannot be said to be an authority constituted by or under any law for the purpose of satisfying housing accommodation or for the purpose of planning, development or improvement of cities, towns and villages or for both, for the following reasons: Firstly, the object of the Act as spelt out in the Preamble is for the purpose of completing certain irrigation projects. Therefore, it cannot be said that the assessee has been established with the objective of satisfying the need for housing accommodation as laid down in the first part of Section 10(20A) of the Incometax Act, 1961. Secondly, the second part of Section 10(20A), deals with corporation established for the purpose of planning, development or improvement of cities, towns and villages. It cannot be disputed that the main purpose of the VIDC Act is for completion of the irrigation projects which are handed over to the assessee for completion by the State Government. There is no planning, development or improvement of cities, towns and villages in carrying out the purposes for which the assessee has been formed. Thirdly. As rightly contended by the learned Standing Counsel, we find that under Section 50

of the VIDC Act, the rehabilitation is to be carried out only by the State Government and not by the assessee.

Whatever planning, development or improvement of cities, towns and villages are done in the process of rehabilitation are done by the State Government and not by the Assessee. Fourthly, the rehabilitation of the displaced persons consequent to any action in performance of any functions of the assessee is too remote and is not incidental to the main purpose for which the assessee was established. We have perused the decision of the Hon'ble Supreme Court in the case of GIDC v. CIT, In the said case, it was found that for the purpose of carrying out the development of an industrial area and industrial estate, the element of planning and development of such area was necessary for development of industries and therefore development of industrial area or industrial estate was held to be development of a place. It was further held in the said case that the developmental activity contemplated in Section 10(20A) need not be necessarily restricted to non industrial activity alone. The said decision is not applicable to the facts of the present case. We have already held that the purpose of enacting the VIDC Act is not to development or improvement of cities, towns and villages but for the purpose of completing the irrigation projects and hydro electric power projects. The decision of the Hon'ble Rajasthan High Court in the case of CIT v. Rajasthan land Devp. Corporation (supra) is again a decision wherein the Rajasthan High Court considered the purpose of the Rajasthan Land Development Act, 1957 and the definition of the word 'land development' contained therein and concluded that the definition was wide enough and the objective of the enactment was wide enough to include development of villages also. We have already held that development of villages, city and town was not under taken by the assessee and that the said objective even assuming it exists, is too remote an objective. It cannot, therefore, be said that the assessee was established by the VIDC Act with the objective of development of city, town or villages. For the reasons set out above, we are of the view that the case of the assessee that its income is exempt under Section 10(20A) is not acceptable. Accordingly, the second ground of the appeal of the assessee is dismissed.

"That the CIT(A) has erred in holding that the Appellant Corporation is not an instrumentality of State and is not 'State' within the meaning of Article 289 of the Constitution of India and thereby "deprived the Appellant Corporation from the benefit of immunity from Income Tax." 53. We have considered the contentions of the learned counsel for the assessee as well as the Standing Counsel for the revenue. This ground was not raised before the Assessing Officer. Under Section 11 of the Income tax Act, 1961, the income derived from the property held under the trust wholly for charitable or religious purposes to the extent to which such income is applied for such purposes or accumulated or set apart to the extent permitted under Section 11 shall not be included in the total income of the previous year. Under Section 12A, an assessee should make an application for registration of the trust before the Commissioner of Income tax. Section 12AA lays down the procedure for registration of the trust. It is only after the registration under Section 12AA is granted, the assessee can seek to claim the exemption under Section 11 of the Incometax Act. The procedure for registration contemplates scrutiny of several requirements as laid down in Section 11 of the Act. A trust deed is one of the basic requirement contemplated underlie provisions of Section 12AA. We fail to understand as to how the assessee can make any claim that it is a trust. The assessee has not come into existence by way of virtue of any trust deed. The assessee has been formed under the provisions of VIDC Act.

Under the provisions of Section 2(17) read with Section 2(26) of the Incometax Act, the assessee would be a company established by or under the said Act. We shall refer to the observations of the Hon'ble Supreme Court in the case of CIT v. U.P. Forest Corporation (Supra) which are as follows: Coming to the question whether the income of the respondent is held for charitable purposes and, therefore, exempt from tax by virtue of Section 11(1) of the Act, we find no such contention was raised by the respondent before the income-tax authorities. In order to take advantage of the provisions of Section 11 of the Act, a trust or institution has to get itself registered. Whether the income of the institution can be regarded as being held for charitable purposes and whether the institution is entitled to registration under Section 12A of the Income-tax Act requires investigation of facts.

In the absence of this contention having been raised before the income-tax authorities, the High Court, in our opinion, ought not to have itself embarked upon examining this issue for the first time and then coming to a conclusion favourable to the respondent. We do realise that the respondent did not raise this contention before the income-tax authorities because it had contended that it was liable to exemption being a local authority. Perhaps a contention in the alternative ought to have been raised, but this was not done. If the High Court had wanted this issue to be decided, the proper course would have been to have remanded the case to the Tribunal or to the assessing authority for a decision. This was perhaps not done because the High Court had already come to the conclusion, in our opinion wrongly, that the respondent was a local authority. Inasmuch as the respondent cannot, in our opinion, be regarded as being a local authority, the interest of justice would demand that the question as to whether its income is liable to be exempted from tax under Section 11(1) of the Act should be investigated and examined by a proper forum under the Act.

These proceedings arise out of the writ petitions which have been filed challenging the correctness of the decision of the Tribunal in respect of the assessment years 1977-78 and 1980-81 and that of the assessing authority for the assessment year 1984-85. In our opinion, the proper course to adopt, while allowing these appeals, would be to require the assessing authority to examine the question as to whether the respondent is entitled to the benefit under Section 11(1) of the Act. Before concluding, we would like to observe that the High Court ought not to have entertained the writ petitions when adequate alternative remedy was available to the respondent. Under the peculiar facts and circumstances of the present case and inasmuch as the litigation between the parties has been going on for a number of years, we do not think it will be appropriate to dismiss these appeals on this ground at this late stage. We, however, emphasise that petitioners should not normally short-circuit the procedure provided by the taxing statute and seek the redress by filing a petition under article 226 of the Constitution of India.

For the aforesaid reasons, these appeals are allowed and the decision of the High Court is set aside. While holding that the respondent is not a local authority whose income is exempted from tax under Section 10(20) of the Act, we, however, direct

the assessing authority to consider the claim of the respondent that its income is not liable to be taxed in view of the provisions of Section 11(1)(a) of the Act. This question should be decided by the assessing authority within six months from today and the liability of the respondent to pay tax would be subject to the outcome of that decision. There shall be no order as to costs.

54. The learned counsel for the assessee relied on the decision of the Supreme Court in the case of ITO v. APSRTC 1986 SC 1054, we are of the view that the said decision will not be applicable in the present case.

The said case arose out of a reference under Section 256(1) of the Income Tax Act, 1961. The question of eligibility to exemption under Section 11 of the Act was made by the Assessee before the Assessing Officer which was rejected and finally allowed by the Supreme Court.

The learned counsel for the assessee sought for the similar direction as made by the Supreme Court in the case of U.P. Forest Development Corporation's case (Supra.). We are of the view that the directions have been given by the Hon'ble Supreme Court under Article 142 of the Constitution of India taking note of the peculiar facts and circumstances of the case. The Tribunal, being a creature of statute does not have any such power to give such direction. The observations of the Supreme Court in the case of U.P. Forest Development Corporation (Supra) extracted above would be enough to dismiss this ground of appeal of the assessee. We accordingly dismiss this ground of appeal of the assessee.

"That the CIT(A) has erred in holding that the Appellant Corporation is not an instrumentality of State and is not 'State' within the meaning of Article 289 of the Constitution of India and thereby deprived the Appellant Corporation from the benefit of immunity from Income Tax." 56. We have considered the submissions of the learned counsel for the assessee as well as the learned Standing Counsel for the revenue. We do not agree with the submissions of the learned counsel for the assessee that the assessee is an instrumentality of the State Government. In the case of Andhra Pradesh State Road Transport Corporation v. ITO, 52 ITR 524, the Hon'ble Supreme Court affirmed the decision of the Hon'ble High Court holding as follows: "The Andhra Pradesh State Road Transport Corporation constituted under

the Road Transport Act, 1950 by a notification issued by the Andhra Pradesh Government, is not immune from liability to income tax on income derived from its trading activities, under Article 289 of the Constitution of India, on the ground that its trading activities were carried on by or on behalf of the government of the State.

Though the majority of its shares are owned by the Andhra Pradesh Government and its activities are controlled by the State, the Corporation has a separate personality of its own, the trading activities are the trading activities of the Corporation and the profit and loss arising therefrom are the profit and loss of the Corporation. The income derived by the Corporation from its trading activities cannot be said to be the income of the Andhra Pradesh State under article 289." The statutory corporation is a separate juristic entity. Whatever may be the control exercised by the State Government on the corporation, the income of the corporation cannot be construed as income of the State. The above being the legal position, we do not think that the assessee can claim any relief under Article 289 of the Constitution of India. This ground of appeal of the assessee is accordingly dismissed as the decision in the case of APSRTC(supra) of the Hon'ble Supreme Court is squarely applicable to the present case also.

57. The grounds of appeal Nos. 5 to 9 and the additional grounds of appeal deal with the merits of the case regarding treatment of interest income, income from house property and claim for set off and carry forward of loss under the head income from business. The facts relating to the above grounds of appeal are as follows: 58. These grounds are connected and, therefore, we deem it proper to decide these grounds of appeals together. During the previous year, the assessee raised funds for the purpose of execution of various irrigation projects by issue of secured non convertible redeemable bonds. The funds raised by issue of these bonds were temporarily invested in short term deposits. On such deposits, the following interest income accrued to the assessee.(1) Interest on FDR(Escrow A/c) Rs. 14,96,548/-(2) Interest on FDR(Collection) Rs. 77,15,384/-(3) Interest on FDR (operation A/c) Rs. 7,90,42,488/- _____ According to the assessee, none of on going projects were completed and ready for the intended use and, therefore, the borrowing costs incurred during the year, namely, bond issuance expenses, interest paid to the bond holders are to be capitalized after deducting

therefrom the interest income received from the temporary investment of borrowed fund. According to the assessee, this was in conformity with the accounting standard No. AS-16 and AS-10. The Assessing Officer, however, was of the view that since the business of the assessee has not commenced, there could be no income or loss from business. He, treated the interest received on temporary investment of borrowed fund as income from other sources. He relied on the decision of the Hon'ble Supreme Court in the case of Challapalli Sugars Ltd. v. CIT 98 ITR 167, Tuticorian Alkali Chemicals & Fertilizers v. CIT, 227 ITR 172 and CIT v. Bokaro Steels, 236 ITR 315 and treated the interest "income as income from other sources." With regard to the interest income received from temporary investment of borrowed funds, the assessee made an alternative plea that in the event of all the interest income being assessed as income from the other sources, the assessee claimed deduction of interest paid to the bond holders during the previous year as an expenditure in connection with the earning of interest under Section 57(iii) of the Incometax Act. The Assessing Officer rejected this contention also.

The State Government had built several residential quarters at various sites where the projects of the assessee were under construction. These residential accommodation were occupied by the employees of the assessee. The assessee collected rents from its employees and also granted House Rent allowance to its employees. The rent charged from the employees was set off against the HRA allowance. A sum of Rs. 18,89,693/-was the house rent recovered from the employees during the previous year. The Assessing Officer treated this as "income from house property." The contention of the assessee with regard to the house rent received was that same was of a capital nature and will go to reduce the overall project cost which will be ultimately capitalized. This contention was not accepted by the Assessing Officer.

Over all submissions of the assessee with regard to interest income as well as other misc. income shown in the profit and loss account including income in the form of rent was that under Section 30 of the VIDC Act, read with Sections 35 and 36 of the said Act, the assessee has to spend all its funds only for the purpose of the objectives of the corporation as mentioned in Section 18 of the VIDC Act.

Thus, according to the assessee, whatever income was earned by the assessee was towards fulfillment of the objects for which the assessee was created. Thus, the interest income as well as the income in the form of rent should all be considered only as income from business or profession. Thus, according to the assessee, this income would go to reduce the cost incurred for setting up of business which is to be capitalized. This submission of the assessee was also rejected by the Assessing Officer. Consequently, the plea of the assessee for carry forward of business losses was also rejected for the reason that the business of the assessee had not commenced and, therefore, there could not be any profit or loss under the head income from business. On appeal by the assessee, the CIT(A) concurred with the view of the Assessing Officer.

58. The Additional issue raised by the Assessed will be decided before other grounds are taken up. The additional issue raised by the Assessed read as follows: The Appellant Corporation started its business on the inception and the Income & Expenditure Account and the Balance Sheet of the year under consideration should be read keeping in view this position.

The Net Deficit after deducting all the allowable business expenditure should be allowed to be recast and worked out and then the resulting losses should be allowed to be carried forward as per the provisions of the Income Tax Act, 1961.

59. Before us, the learned counsel for the assessee has taken a plea that the business of the assessee has started right from its inception in the form of an additional ground. This additional ground of appeal sought to be raised by the assessee can be decided without investigation into any new set of facts and evidence and on the basis of the evidence already on record. We, therefore, deem it proper in the interest of justice, to render a decision on this ground of appeal. His submission was that the assessee was formed for the purpose of completion of 10 selected on going irrigation projects in time bound manner. He referred to the provisions of Section 15 of the VIDC Act under which all the projects and their assets comprising of movable and immovable including irrigation projects, hydro electric power projects, work in construction which vested in the state government and were under the control of the Irrigation Department shall vest in and shall

stand transferred to the assessee corporation. He, then referred to the provisions of Section 2(a) as well as 2(e) of the VIDC Act. Under Section 2(e), irrigation projects mean planning, construction, maintenance and management of major irrigation projects, medium irrigation project and minor irrigation projects including command area development and flood control and allied activities. According to the learned counsel for the assessee, construction of irrigation projects necessarily involve construction of dams, canals, spillways, construction of flanges, erection of gates, filling of gorges, installation of lift irrigation pump, erection and construction of weirs and main canals, distributaries and minor canals structures and linings. According to him, the entire irrigation project consists of carrying out survey where the project is to be set up, feasibility of site, preparation of project report and then carrying out the various construction activity involved in setting up of irrigation project.

Referring to the statement and objects of the VIDC Act, he pointed out that 10 selected irrigation projects which were in various stages were handed over to the assessee. In other words, the submission of the learned counsel for the assessee is that the assessee took up the existing business and is deemed to have started its business right from the date of its inception. The revenue authorities erred in assuming that the business of the assessee had not commenced. Regarding the letter of the assessee before the Assessing Officer, wherein the assessee had stated that the business of the assessee had not commenced and, therefore, the entire expenditure has to be capitalized after deducting therefrom the income in the form of interest and rent, the learned counsel for the assessee submitted that the said letter was only in connection with the status under which the assessee has to be assessed, namely, as a local authority. In any event, if on facts, it can be said that the business of the assessee has commenced, the assessee should be given necessary relief.

60. His next submission was that the object of the assessee is of promotion and operation of some irrigation projects only and the same being undertaken by the assessee without any profit motive, it cannot be said that the income earned by the assessee was of the nature of income from any business or profession. According to him, activities of the assessee can not be construed as business

activity considering the fact that the assessee does not have any profit motive at all.

61. Regarding the income in the form of rent received by the assessee, the learned counsel for the assessee submitted that the residential quarters put up by the State Government with a view to provide accommodation to the staff working in various sites. He submitted that it is a business asset and, therefore, the income derived therefrom has to be assessed only as income from business. He relied on the decision of the Hon'ble Supreme Court in the case of *Universal Plast Industries v. CIT* 237 ITR 454(SC). His further submission was that once it is held that the assessee has commenced its business, the loss arising under the head income from the business has to be allowed to be set off against the income from the house property as well as income from other sources. If it is so set off, then there will be still loss under the head income from business or profession which should be allowed to be carried forward and consequently, there will be no liability to pay any tax by the assessee. The learned counsel for the assessee has also submitted that if it is held that the business of the assessee had commenced, then the assessee should be allowed its claim for depreciation on its depreciable assets which are put to use. Thus, the depreciation will further increase the loss of the assessee under the head income from business and after set off of loss against the income from the house property as well as income from other sources, the net loss should be allowed to be carried forward as per the provisions of the Incometax Act, 1961.

62. The learned Standing Counsel for the revenue submitted that the assessee corporation had not commenced its business. His submission was that the construction of dams, canals erection of gates is not the functions of the VIDC. He referred to the provisions of Section 18 of the VIDC Act which only refers to the promotion and operation of irrigation projects that were handed over to the assessee or in future the projects which will be handed over to the assessee His submission is that the construction of dams, canals and irrigation gates are not the activities of the VIDC. Providing irrigation facility and also generating powers and providing the same to the prospective users is the object of the assessee. Referring to Section 15 and 17 of the VIDC Act, he submitted that Act makes

provisions for vesting of the properties in the assessee only for the purpose of enabling the assessee to provide the water for irrigation and also power for prospective user. Under Section 17, once the object for which the assessee is established is fulfilled, the assessee corporation was to be dissolved and all the properties will vest in the State Government.

According to the learned Standing Counsel for the revenue, these provisions will only go to show that the purpose of handing over Assets is only with a view to enable the assessee to perform its objects, namely, providing facility for irrigation and power for prospective user. His submission in short is that the construction of dams, erection of canal gates etc. are not the business of the assessee. His contention with regard to the claim of the assessee for carry forward of business loss is that under Section 42(2), the net receipt if any in respect of the any of the objects of the assessee shall be solely derived by the State Government. In view of these provisions, he submitted that there can be no loss as far as the assessee is concerned and whatever is the loss, it is the loss of the State Government and not of the assessee.

63. He next contended that the fact that the business of the assessee had not commenced was very categorically admitted by the assessee itself in its letter dated 16.2.2001 filed before the Assessing Officer. He submitted that even to day, the assessee has neither withdrawn the letter nor has explained the reason as to why he made such admission- and as to how the admission by the assessee is not correct. The learned standing counsel submitted that the assessee having given treatment in their books of account as the business not having commenced cannot now seek to put forth an altogether new plea.

64. Regarding the plea of the assessee that the interest income and the income in the form of rent should be assessed as income from business, he relied on the decision of the Hon'ble Supreme Court in the case of Tuticorin Alkali & Chemical(supra). At the time of hearing, it was pointed out by the bench that there is an item of income shown in the profit and loss account, namely, income from sale of water. Under the provision of Section 20 of the VIDC Act, the assessee was empowered to determine and levy water charges in accordance with the

volume of consumption by various users as set out in Section 20 of the VIDC Act.

Query of the Bench was that if there had been sale of water, it only leads to a presumption that the assessee had commenced business notwithstanding the stages of completion of the various irrigation projects under taken by the assessee. The reply of the learned Standing Counsel for the revenue was that there was no explanation from the assessee as to whether the sale of water was through irrigation canals or from other sources like standing water bodies. In the absence of this vital information, he submitted that it cannot be presumed that the assessee had levied the water charges in respect of supply of water through irrigation canals and, therefore, business of the assessee had commenced. The learned Standing Counsel for the revenue also submitted that even assuming it is held that the business of the assessee had commenced, still the income in the form of interest as well as income in the form of rent will have to be assessed under the head income from other sources and income from the house property. In this regard, he relied on the decision of this Bench in ITA Nos. 216/Nag/99 in the case of Forest Development Corporation v. JCIT.65. We have considered the rival submissions. Before we deal with the other contentions of the Learned counsel for the Assessee we shall deal with his submission that the Assessee cannot be said to have carried on any business at all. The provisions of Section 30 of the VIDC Act are relevant in this regard and the said provision reads as follows: (1) The Corporation shall have and maintain its own fund, to which shall be credited,- (a) all the moneys received by the Corporation from the State Government by way of grants, subventions, loans, advances and the loans raised under this Act; (b) all fees, costs and charges received by the Corporation under this Act; (c) all moneys received by the Corporation from the disposal of lands, buildings and other properties, movable and immovable and other transactions; (d) all moneys received by the Corporation by way of water charges, rents and profits or from any other source.

(2) The Corporation may keep current and deposit account with the State Bank of India or any other Bank approved by the State Government in this behalf.

(3) Such accounts shall be operated by such officers of the Corporation as may be authorised by it in this behalf.

(4) Notwithstanding anything contained in Sub-sections (2) and (3), the Corporation may keep on hand, such sum as it thinks fit for its day to day transactions, subject to such limits and conditions as may be prescribed.

The submission of the learned Counsel for the assessee is that the Assessee has been formed for the purpose of carrying out certain objectives mentioned in the act. These objectives cannot be said to be any business at all. According to him the Assessee cannot have any income much less income from business or profession. This argument of the learned counsel for the Assessee cannot be sustained. From a reading of Section 30, it is clear that the Act under which the Assessee was created envisages a situation where the assessee would receive profit and that profit would go to the fund of the corporation.

The important question which needs to be decided before rendering decision on the grounds Nos. 5 to 9 of the grounds of appeal is as to what is the nature of the assessee's business and whether it can be said that the business of the assessee had commenced. In other words the additional ground raised by the Assessee needs to be decided first.

66. With regard to the question as to whether business of the assessee had commenced or not during the previous year, the case of the assessee is that it is involved not only in the business of providing water for irrigation but also in providing the necessary infrastructure like, dams, canals and supply and generation of powers. According to the assessee, it took over from the State Government existing and on going irrigation projects which were at different stages of progress. Thus, according to the assessee, it took over an existing business and ought to be construed as having commenced business from its inception or formation. It was also submitted that the assessee sold water during the previous year and had received a sum of Rs. 1,12,09,306/- on such sale. Thus according to the assessee, the assessee has not only commenced business but has also generated revenue out of the business.

This claim of the assessee is, however, contrary to its own categorical admission before the Assessing Officer that it has not yet commenced its business. This stand of the assessee has also to be judged from the method of accounting regularly employed by the assessee. It is seen from the order of assessment that as per the Tax Audit Report, the system of accounting was stated to be mercantile but cash system of accounting is being followed where receipts are concerned. It was thereafter pointed out by the Assessing Officer that w.e.f. A.Y. 97-98, the assessee can opt for either mercantile or cash system of accounting and hybrid system of was not legally admissible. Thereafter, the assessee by its letter dated 22.1.2001 explained that since no provision has been made in the books for income receivable and expenses payable, the accounting system followed is cash system.

67. Provisions of Section 145 of the Incometax Act as substituted by Finance Act, 1995 w.e.f. 1.4.1997 reads as follows: "145(1)- Income chargeable under the head "profits and gains of business or profession" or "income from other sources" shall subject to the provisions of Sub-section (2), be computed in accordance with either cash mercantile system of accounting regularly employed by the assessee.

(2) The Central Government may notify in the Official Gazette from time to time accounting standards to be followed by any class of assesseees or in respect of any class of income.

(3) Where the Assessing Officer is not satisfied about the correctness or completeness of the accounts of the assessee, or where the method of accounting provided in subsection (1) or accounting standards as notified under Sub-section (2) have not been regularly followed by the assessee, the Assessing Officer may make an assessment in the manner provided in Section 144." Under the cash system of accounting, the entries in the books of account are on actual receipts or on actual payments and the income is determined on the excess of receipts over excess of payments. Under the mercantile system, the income is computed on the basis of income and expenditure relating to a period whether such income is actually received or not. Under this system, receipts are recognized when they became legally due and before it is actually received and expenditure is

recognized when legal liability to pay the same is incurred irrespective of the fact that as to whether they are actually paid. The computation of income is made on the basis of the method of accounting regularly adopted by the assessee. The method of accounting adopted by the assessee may be unscientific or anomalous but the method should be such that the real profits and gains can be properly deduced therefrom.

If the method of accounting adopted by an assessee is such that true income cannot be deduced, then the method of accounting though a well recognized method of accounting can still be rejected by the Assessing Officer. Under Section 5, profits are chargeable when they accrue or arise or are received. The effect of Section 145 is that the assessee's choice of the system of accounting determines whether profits are to be actually charged to tax when they accrue or when they are to be taxed when actually received or at some other point of time. If an assessee's accounts are kept on mercantile basis, the income would be taxable when it accrues or is earned, irrespective of receipt. If the accounts are maintained on cash basis, income would be chargeable only if it is received in the accounting year.

68. It is also settled legal position that an assessee cannot ask for two different methods, one for writing books of accounts for the purpose of his business and another for having his tax liability determined under the Incometax Act. In *Keshav Mills Ltd. v. CIT*, 23 ITR 230(SC), the Hon'ble Supreme Court held that the provisions of Section 13 of 1922 Act (corresponding to Section 145 of 1961 Act) was compulsory on the Incometax authorities and imposed on them an obligation to accept the method of accounting regularly adopted by the assessee except in case when the proviso (Sub-section (3) of Section 145) to that section come into operation.

69. In the light of the above legal provision, we find that the assessee had adopted the method of accounting whereby it did not recognize its business having commenced. The letter dt. 16.2.2001 by the assessee to the Assessing Officer which is crucial reads' as follows: "Till the end of previous year 1997-98, none of the ongoing projects(irrigation, dams & canals etc.) were completed and ready for

their intended use i.e. the qualifying asset was not ready for its intended use. Therefore, all the borrowing cost incurred during the year including 1) Income received from temporary investment of those borrowed funds.

This contention is well supported by the Institute of Chartered Accountants of India -Accounting standard No. AS 16 more particularly, paras 3,4,5,6 & 10 thereof.

Further, provisions of para. 9.3 of AS-10- statement of accounting standards published by the Institute of Chartered Accountants of India which deals about the capitalization of administrative and other general overhead expenses as are specifically attributable to construction of project may be included as part of cost of construction project or as a part of fixed assets.

The expenses incurred on startup and commissioning of the project includes the expenses incurred on test runs and experimental production is usually capitalized as an indirect element of construction cost.

As per these foregoing provisions VIDC has completely capitalized its administrative and direction expenses net of Misc. revenue received from trial activities by way of firstly debiting to Direction and Administration Expenses Account to Profit and Loss account and crediting sale of water to profit and loss account and then by transferring the balancing net loss to works costs.

Has been charged to work account and capitalized according to principles of accounting.

70. From a perusal of the aforesaid letter of the assessee as well as a copy of the balance sheet and income and expenditure account for the year ended 31.3.98, it is apparent that the assessee had followed a method of accounting by which it had not recognized itself as having commenced its business. Even the income from sale of water which is the revenue yielding activity of the assessee had been treated by the assessee as having been generated out of trial activity which will only go to reduce the cost of capitalization of the project cost or say its fixed assets. This is contrary to the cash system of accounting followed by the assessee. Under the cash system, the assessee ought to have treated income

from sale of water as a revenue receipt and income from its business. But what the assessee claimed before the Assessing Officer was that it regards income from sale of water as revenue receipt and income from its business only when all the irrigation projects handed over to it by the State Government are completed. After such completion, income generated by sale of water was alone construed as the point of time when the assessee itself considered it as having commenced business. This is clear from the Income and Expenditure account for the year ended 31.3.98, a copy of which is placed at page 100 of the assessee's paper book. Volume II where the entire expenditure of a revenue nature upto 31.3.98 is capitalised to fixed assets after deducting therefrom the income from sale of water and income in the form of interest received on temporary investment of funds borrowed for the purpose of completing the various irrigation projects. Depreciation has not been claimed by the assessee and the various capital expenditure incurred during the year have been considered as cost of fixed assets. This is clear from the Schedule of fixed assets filed by the assessee before the Assessing Officer, a copy of which is placed at page 101 of Vol. II of the assessee's paper book.

The Assessing Officer accepted this method of accounting followed by the assessee except so far as the claim of the assessee that interest income received from investment of idle funds and rent received from property occupied by the assessee's employees are to be construed as income from business of the assessee and would go to reduce the cost of capitalization of the project. This, the Assessing Officer was entitled to do since the method of accounting employed by the assessee can only determine the mode of computing income but not the range of taxable income or ambit of taxation or the head of income under which an income has to be assessed. The choice to accept a method of accounting employed by the assessee lies with the Assessing Officer but on a proper finding that income cannot be computed properly. The Assessing Officer has accepted the method of accounting adopted by the assessee.

In such circumstances, it is too late in the day for the assessee to contend that the assessee had commenced its business and, therefore, income/loss under the head "income from business" has to be computed as according to its own method

of accounting which has been accepted by the Assessing Officer, it had not commenced its business. There are plethora of court pronouncements where it has been held that provisions of Section 145 are mandatory and the proper method of accounting regularly followed by an assessee is binding on the assessee as well as the Assessing Officer. In CIT v. Sarangpur Cotton Manufacturing Co.

Ltd. (1938) 6 ITR 36(PC), the Privy Council in the context of Section 13 of the Incometax Act, 1922 (equivalent to Section 145 of IT Act, 1961) observed as follows: "Their Lordships are clearly of opinion that the section relates to a method of accounting regularly employed by the assessee for his own purposes- in this case for the purpose of company's business and does not relate to a method of making up the statutory return for assessment of incometax. Secondly, the section makes such a method of accounting a compulsory basis of computation unless in the opinion of the ITO, the income, profits and gains cannot be properly deduced therefrom." In CIT v. A. Krishnaswami Mudaliar, (1964) 53 ITR 122(SC), the Hon'ble Supreme Court reiterated that the ITO is bound to compute the profits by appropriate adjustments from the accounts maintained by an assessee where a system of account is regularly employed: "The only departure made by Section 13 of the Indian I.T. Act from the legislation in England is that whereas under the English legislation, the commissioner is not obliged to determine the profits of a business venture, according to the method of accounting adopted by the assessee, under the Indian IT Act, prima facie, the ITO has for the purpose of Section 10 and Section 12 to compute income, profits and gains in accordance with the method of accounting regularly employed by the assessee. If, therefore, there is a system of accounting regularly employed and by appropriate adjustments from the accounts maintained taxable profit may properly be deduced, the ITO is bound to compute the profits in accordance with the method of accounting. But where in the opinion of the ITO, the profits cannot properly be deduced from the system of accounting adopted by the assessee it is open to him to adopt a more suitable basis for computation of the true profits." We, therefore, hold that the assessee has not yet commenced its business and, therefore, it is not possible to compute income under the head "Income from Business". Thus, the additional ground of appeal of the assessee is dismissed.

71. Ground No. 5: The Assessing Officer has erred in classifying the interest income received by the Appellant on the short term deposits as 'Income from other Sources', instead of proper head 'Income from profits & Gains of Business or Profession' and has brought the amount of interest to tax. The CIT(A) has further wrongly reiterated his view.

72. Ground No. 6. It is wrong on the part of Assessing Officer, to hold the business property as housing property and income received from business assets to be part of 'Income from House Property, despite several decisions to that effect, which have already been referred to during the appeal to the CIT(A) by the Appellant Corporation. Further, the CIT(A) erred in holding the same view of that of the Assessing Officer, and thereby the Appellant Corporation has been levied with unwarranted taxes on the rental income as 'Income from House property'.

73. Ground No. 7. Assuming but not admitting that the Appellant Corporation is a Domestic Company, still, the interest paid on the Bonds should essentially be reduced from the interest income on short term deposits, Under Section 57 of the Income Tax Act. The same was not permitted by the Assessing Officer who isolated the income from interest on short term deposits and without allowing the legitimate deduction, taxed the entire amount of interest income. The CIT(A) also failed give justice and denied to grant the legitimate deduction as per law.

74. Ground No. 8. The Assessing Officer erred in not allowing the accumulated losses to be carried forward and set off against the future income of the Corporation, despite, well aware of the provisions of the Income Tax Act, 1961 particularly Section 70 to 72 thereof. The Appellant Corporation legitimately claimed to allow its losses of Rs. 21.34 Crores to be carried forward and set off against the future profits, if any. But the Assessing Officer denied the claim stating that these are not the business profits and has wrongly classified the income from interest on deposits as well as income from rent under the heads 'Income from other sources' and 'Income from House Property' under the Income Tax Act and brought these amounts to tax. The CIT(A) has reiterated the view of the Assessing Officer and thereby made injustice on the Appellant Corporation.

75. Ground No. 9. The Appellant corporation has not raised the claim of depreciation during the assessment as well as appeal keeping in view the fact that the appellant had claimed exemptions under the various provisions of Income Tax Act. The Appellant be granted legitimate claim of depreciation on its depreciable assets which are put to use by the Appellant. The depreciation will further increase the losses of the Appellant under the head 'Income from Business or profession'. The same may be allowed to be adjusted against the income as arrived by the Assessing Officer under the heads 'Income from House Property as well as 'Income from other sources' and net loss arising thereafter be allowed to be carried forward as per the provisions of Income Tax Act.

76. Ground No. 10. Any other ground that may be raised during the hearing of the case before the Honourable Appellate Tribunal, be allowed to the assessee which specifically remains to be mentioned in the present appeal.

77. Ground No. 5 & 7 can be dealt with together. In respect of Ground No. 5, we are not inclined to accept the submission of the Learned Counsel for the Assessee that since as per the provisions of the VIDC Act whatever income are received by the Assessee goes to the fund of the Assessee which needs to be spent only for the objectives mentioned in the VIDC Act, whatever income earned by the Assessee is to be construed as Business income and not income under any other head.

Whatever might be the provisions of the VIDC Act, while computing the income liable to tax, the provisions of the Income Tax Act, 1961 are only relevant. As per the provisions of the Income Tax Act, 1961, the total income of the Assessee is chargeable to tax under s. 4. The total income has to be computed in accordance with the provisions of the Act.

Section 14 lays down that for the purpose of computation, income of an assessee has to be classified under six head : (A) Salaries. (B) Income from house property. (C) Profits and gains of business or profession. (D) Capital gains. (E) Income from other sources.

The computation of income under each of the above six heads will have to be made independently and separately. There are specific rules of deduction and allowances under each head. No deduction or adjustment on account of any expenditure can be made except as provided by the Act.

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.

Therefore we have to see what is the nature of interest income earned by the Assessee. The Assessee borrowed monies from the public by issue of Secured Non convertible bonds. The money borrowed before it could be used for the purpose for which they were borrowed, were temporarily invested by the Assessee and this investment of funds yielded the interest income in question. Firstly, the business of the Assessee was not investing funds and earning interest. Secondly, there was no business compulsion or inextricable link between the business of the Assessee and the investment of the funds in temporary short-term deposits. Thirdly, the Assessee was free to use these funds in any manner they liked for the purpose of their business. The fact that the Assessee choose to make temporary investments to earn interest will not alter the character of the income into income from business. Fourthly, the fact that it was a prudent accounting policy to reduce the interest cost on borrowed funds by setting off against the cost the interest income earned on temporary investment of borrowed funds is not relevant. The question is by now settled by the decision of the Honourable Supreme Court in the case of Tuticorin Alkali Chemicals & Fertilizers Ltd. v. CIT (227 ITR 172). The next argument of the learned counsel for the Assessee is that the decision of the Honourable Supreme Court in the case of Tuticorin Alkali Chemicals (Supra) is applicable only where the business of the Assessee has not commenced and since in the present case the business of the Assessee has commenced, the interest income will go to reduce the interest payment made on the funds borrowed by the Assessee. We are unable to accept this contention. This Bench has already considered a similar argument in the case of Forest Development Corporation of Maharashtra v. JCIT in ITA 216/nag/99. This bench followed the

decision of the Honourable Madras High Court in the case of South India Shipping Corporation Ltd. v. CIT 240 ITR 24 (Mad). The following are the extract of the decision of this Bench: 23. As to whether the decision in Tuticorin Alkali's case (Supra) will apply where there has been commencement of business or not was considered by the Honourable Madras High Court in the case of South India Shipping Corporation Ltd's case (Supra). The Assessee in the said case sought to set off interest paid on overdraft taken for business against the interest it received from the Bank on deposits.

The decision of the Honourable Supreme Court was sought to be distinguished as not applicable in view of the fact that the Assessee in the case before the Madras High Court had commenced business. The Madras High Court held as follows: The learned counsel for the assessee, however, contended that the decision of the apex Court was in the background of the fact that the assessee therein had not commenced business and, therefore, could not have claimed that the income received on fixed deposits was part of its business income and, therefore, the law laid down therein is inapplicable to the facts of this case. We do not find it possible to agree with the learned counsel that the law laid down in that case is confined to cases where a company has not commenced business. The Court proceeded on the basis that in the usual course, interest received by the company from bank deposits and loan could only be taxed as income under the head 'Income from other sources' under Section 56. The assessee's attempt to claim a right to have its income on bank deposits treated in a different way on the ground that it had not started business was negatived by that Court. The proposition laid down by the Court, therefore, is that interest received by a company which carries on business from bank deposits and loans could only be taxable as 'Income from other sources' and not as 'Business income'.

Under the IT Act, the distinct heads under which the income of an assessee are to be classified are set out in Section 14. The income received by an assessee has to be fitted under one or other head having regard to the source from which that income is derived. The fact that a person carries on business does not lead to the inference that all income received by such a person is business income. The same assessee can have income which may require to be classified under more than

one head. It is the manner in which the income is derived that is relevant and not merely the fact that the person is engaged in a business or in a profession.

All these decision which have held that the interest received on short-term bank deposits by an assessee carrying on business and having the business income are not to be treated as income from other sources but as business income must be held to have been impliedly overruled by the decision of the Supreme Court in the case of Tuticorin Alkali Chemicals & Fertilizers Ltd. (supra).

In the light of this clear verdict of the Honourable Madras High Court the case of the Assessee that the decision of the Supreme Court in Tuticorin Alkali's case will not apply to them as they had commenced their business cannot be accepted. It is not the case of the Assessee that the earning of interest income and the business of the Assessee are inextricably linked. There was no business compulsion which forced the Assessee to make the deposit from which the interest income was derived.

Though we have held that business of the assessee had not commenced yet in view of the above decision of this Bench, we are inclined to dismiss Ground No. 5 of the Grounds of appeal of the Assessee and hold that the revenue authorities were justified in treating the interest income as income from other sources.

78. In Ground No. 7, the Assessee seeks to claim that even if interest income is construed as income from other sources the amount of interest the Assessee pays on the bonds has to be construed as expenditure incurred in connection with earning the interest and deduction under Section 57(iii) of the I.T.Act, has to be allowed while computing the interest income under the head Income from other sources. We are not inclined to accept this contention. Under Section 57 of the I.T.Act, the income chargeable under the head 'Income from other sources' shall be computed after making the following deductions, namely :-

(iii) any other expenditure (not being in the nature of capital expenditure) laid out or expended wholly and exclusively for the purpose of making or earning such income." This section provides for deduction of any other expenditure not being in the nature of capital expenditure laid out or expended wholly or exclusively for the

purpose of making or earning "income from other sources" of Chap. IV-F of the Act. Section 57 allows certain specified deductions on other income referred to in the immediately preceding Section 56 of the Act. The deductions under Section 57 are allowable only if they fall within one or the other of the clauses enumerated in that section and not otherwise.

The borrowings were not made to make investments and earn interest from them. The borrowed amounts kept in short-term deposits undoubtedly yielded interest. The interest income from such deposits was, from such deposits only and was incidental to and was the result of the same. The interest income was totally independent of the borrowings. The expenditure incurred must be for the purpose of making or earning the income; which is not the position in the present case. We are therefore of the view that Ground No. 7 of the Grounds of appeal of the Assessee is without any merit and we accordingly confirm the order of the Revenue authorities.

79. In Ground No. 6 of the grounds of appeal of the Assessee the Assessee has challenged the action of the Revenue authorities in treating the rent received from employees in respect of accommodation provided to them at the various sites where the projects of the Assessee are being worked, as income from House Property. According to the Assessee these are to be construed as Income from business. The further contention of the Assessee was that since these incomes will go to reduce the cost of the project and the amount to be capitalized towards setting up of the project has to be reduced by the income received by the Assessee in the form of rents. The State Government had constructed at various sites of the project now transferred to the Assessee housing accommodation for the employees. The Assessee charges rent in respect of these accommodation. As to whether the employees paid the actual rents or the Assessee made adjustment entries treating the HRA payable to the employees, as rent received is not clear from the order of Assessment. Nevertheless, the fact remains that there resulted an income from rents. The Revenue authorities held that the income is liable to be taxed under the head income from House Property.

The Revenue authorities proceeded on two grounds in holding as above.

Firstly, they held that the business of the Assessee had not commenced and therefore there was no question of treating the rent received as income from business. Secondly, they held that the decision of the Honourable Supreme Court in the case of Tuticorin Alkali Chemicals (Supra) will apply to the facts of the case. We have already held that the business of the Assessee has not commenced and therefore in the light of this finding we shall examine the claim of the Assessee. The law laid down by the decision of the Honourable Supreme Court in the case of Tuticorin Alkali Chemicals (Supra) is to some extent modified by the decision of the Honourable Supreme Court in the case of CIT v. Bokaro Steel Ltd. 236 ITR 315. The Honourable Supreme Court in the latter case had held that even during the period prior to commencement of business, if the Assessee earns some income from utilization of the business assets and such utilization is inextricably linked with the setting up of the business, the income so earned will go to reduce the cost to be capitalized. We are of the view that the claim made by the Assessee deserves to be allowed.

The letting out of residential quarters by the assessee to its employees, in the circumstances of this case, is subservient to and incidental to the main business of the assessee and, therefore, the case comes within the exception of Section 22 of the Income-tax Act. To put it differently the letting out of residential quarters to the employees was incidental to and subservient to the business of the assessee and so it is manifest that the residential quarters were occupied by the assessee for the purpose of the business carried on by it. It follows, therefore, that the rent derived by the assessee from the letting out of the residential quarters to its employees is assessable not under Section 22 of the Income-tax Act but under Section 28 of the income-tax Act, under the head Income from business or profession.

A precisely similar question arose for consideration before the Honourable Patna High Court in Jamshedpur Engineering and Machine Mfg.

Co. Ltd. v. Commissioner of Income-tax 32 ITR 41 (Patna). In that case the assessee company, which carried on the business of manufacturing and selling of agricultural implements, had constructed residential quarters for its employees and

let out the quarters to its employees as incidental to its main business. The assessee incurred expenditure for the repairs and maintenance of the residential quarters and claimed that the expenditure incurred for the repairs and maintenance should be deducted from the profits of the business under Section 10 (2) (xv) of the statute.

It was held by the Division Bench that letting out of the residential quarters was subservient to and incidental to the main business of the assessee and, therefore, section 9 of the Income-tax Act did not apply to the case, and the expenditure incurred by the assessee for the repairs and maintenance of the residential quarters was allowable as deduction from the profits of the business of the assessee under Section 10 (2) (xv). The Honourable Patna High Court in the case of Rohtas Industries Ltd. v. Commissioner Of Income-tax, Bihar & Orissa 41 ITR (524) PAT again considered a similar question. The facts of the case were that Assessee received rents from employees for occupation of its quarters. The Assessee was engaged in business of manufacture and sale of cement, sugar, etc. The Department assessed the income as income from house property. The Court held that Letting out of quarters to employees was incidental and subservient to the carrying on of main business of assessee and therefore the Income was assessable as business income. The letting of the residential quarters to its employee by the assessee is incidental to the main business of the assessee and so the assessment should not be made under income from house property. The rent realised by the assessee company from the buildings of which it is the owner and which have been let out to its employees is assessable under Section 10 of the IT Act and not under Section 9 of the IT Act.

In view of the above decisions we are of the view that the rent received by the Assessee in respect of housing accommodation provided to it's employees at various sites of the project was not to be assessed as income from house property but has to be held as an income which will go to reduce the cost of setting up of business which is to be capitalized. This ground of appeal of the assessee is allowed and the Assessing officer is directed to delete this addition.

80. Ground Nos. 8 and 9 of the grounds of appeal remain to be adjudicated upon. In respect of ground No. 8, the submission of the learned counsel for the assessee is that the loss claimed by the assessee has to be allowed to be set off against the income under the head income from the other sources and income from the house property and the remaining loss if any, should be allowed to be carried forward in accordance with the provisions of Section 70 to 72 of the Income-tax Act, 1961. The learned Standing Counsel for the revenue submitted that under Section 42(2) of the VIDC Act, the net deficit if any in respect of any of the object shall be solely borne by the state government. In view of this provision, he submitted that there can be no loss as far as the assessee is concerned and all the losses are to be absorbed by the state government. Apart from the above submissions, he relied on the orders of the revenue authorities in this regard.

81. We have considered the rival submissions. It is seen from the order of the assessment that the Assessing Officer disregarded the profit and loss account filed by the assessee and completed the assessment on the basis of the principles emerging from the various decisions of the Supreme court referred to in the order of assessment. This was done by the Assessing Officer on the basic assumption that the business of the assessee had not commenced and, therefore, there cannot be computation of income/loss under the head income from the business or profession. We have already held that the business of the assessee had not commenced while deciding the additional ground of appeal of the assessee. In view of the aforesaid finding we are of the view that the action of the Assessing Officer in disregarding the profit and loss account refusing to allow the claim of loss under the head income from the business or profession was proper. We however do not find any force in the contention of the learned Standing Counsel for the assessee that in view of Section 42(2) of the VIDC Act, whatever is the loss of the corporation has to be borne by the state government and, therefore, there can be no loss under the head income from the business or profession as far as the assessee is concerned. So long as the provisions of sections of the Income-tax Act are applied to the assessee, whatever manner in which the loss of the assessee has to be considered in accordance with the statutory provisions contained in the Act by which the assessee was created needs to be disregarded. The assessee was, therefore, well within its right to make the claim for

computation of income from the business or profession in accordance with the provisions of the Incometax Act, 1961.

82. The Ninth ground of appeal of the assessee is with regard to claim for depreciation on depreciable assets which are put to use by the assessee. It is not in dispute that this issue was not raised by the assessee before the Assessing Officer. We have already held that the business of the assessee had not commenced and, therefore, the question of granting depreciation does not arise for consideration as the condition precedent for grant of depreciation is use of an asset for the purpose of the business is not fulfilled by the assessee. This ground of the appeal of the assessee is, therefore, dismissed.

SooperKanoon - India's Premier Online Legal Search - sooperkanoon.com