

Interest accrued from investment in 'Kisan Vikas Patra' is taxable on accrual basis, rules HC

Summary – The High Court of Gujarat in a recent case of Sureshchandra M. Shah, (the Assessee) held that interest from investment in Kisan Vikas Patra is taxable on accrual basis.

Facts

- On scrutiny, the Assessing Officer noticed that the assessee had shown investment in Kisan Vikas Patras (KVP) of Rs. 1 crore but had not shown any income from accrued interest on such KVPs in return filed.
- The Assessing Officer did not accept the contention of the assessee that the KVPs are the capital asset under section 214 and will be accounted for when matured at the cost indexation and instead added a sum of Rs. 21.09 lakhs to the total income of the assessee as accrued interest on the KVPs during the year under consideration.
- On appeal, the Commissioner (Appeals) rejected the assessee's appeal.
- On second appeal, the Tribunal rejected the appeal of the assessee upholding the order of the Assessing Officer that the accrued interest on KVP is taxable.
- On further appeal, the appellant contended that the KVP was nothing but a promissory note and the entire amount with interest was promised to be paid over at the end of maturity period. There was nothing to suggest that the interest would accrue during such period. He contended that the KVP should be considered as an asset under section 214, therefore, gain should be taxed on maturity with the benefit of indexation.

Held

- The revenue authority as well as the Tribunal, on the basis of the terms and conditions of which KVPs were issued and the Departmental Circular came to the conclusion that the interest would accrue year after year and had to be accounted for in the accounts, which the assessee maintain in the mercantile system.
- KVP Rules of 1988 provide for terms and conditions on which such certificates were issued. Rule 12 thereof pertains to encashment on maturity and provide *inter alia* that the maturity period of a certificate of any denomination shall be five and half years commencing on the date of the certificate, and provided that for a certificate purchased on or after 1-3-2003, its maturity shall be eight years and seven months. The amount, inclusive of interest, payable on encashment of the certificate at any time after expiry of its maturity period shall be Rs. 2,000 for a denomination of Rs. 1,000. Rule 13 pertains to premature encashment and permit such premature encashment, notwithstanding anything contained in rule 12, on the death of the holder of the certificate; on forfeiture by a pledgee being Gazetted Government Officer, or when ordered by the Court of law. Sub-rule (2) of rule 13 provides that when a certificate is encashed within a period of one year from

the date of the certificate, only the face value of the certificate shall be payable. Under sub-rule (3), if the encashment is after expiry of one year but before the expiry of two years and six months from the date of certificate, the holder would receive face value of the certificate together with simple interest at the rate applicable from time to time to the account holders under the Post Office Savings Account Rules, 1981. Sub-rule (4) of rule 13 provides for different rate of returns for any premature encashment after expiry of two years and six months; depending upon the date of purchase of KVP. The instant case is governed by sub-rule (4) of rule 13, since admittedly; KVPs were purchased after 1-3-2003.

- It could thus be seen that on the grounds specified in rule 13, premature encashment before 2 years and six months of the date of the certificate is envisaged under the rules. However, after completion of such maturity lock-in period of two years and six months, an investor could at his option, encash the certificate and would receive the return at the rates specified in different rules; depending upon the date of purchase of the certificate.
- Under the circumstances, the Tribunal was correct in confirming the opinion that the KVP did not amount to a promissory note and which, at the end of the period, the authority promise to pay a fixed sum of money only. It was a case where even premature exit from the scheme was permissible. After completion of two years and six months from the date of issuance of the certificate, the investor could withdraw his investment at the rate of return specified in the rules.
- In this context, the authorities correctly relied on circular no. 687 dated 19-8-1994 in which it was stated that, 'the interest on Kisan Vikas Patras has to be assessed to income tax on accrual basis, the amount of interest accrued on these patras during initial two and half years has to be determined in consultation with the department of Economic Affairs. The amount of interest accrued on investment in Kisan Vikas Patra by an assessee is to be calculated on the basis of table received from the Department of Economic Affairs wherein rates of interest and maturity amount for Rs. 1000 denomination of Kisan Vikas Patra are given.'
- Therefore, the authorities correctly recorded that the assessee was entitled to encash KVPs after two years and six months and in the present case, such period was over.
- In the result, Tax Appeal was dismissed.