

**IN THE INCOME TAX APPELLATE TRIBUNAL
(DELHI BENCH 'A' : NEW DELHI)**

**BEFORE SHRI J.S. REDDY, ACCOUNTANT MEMBER
and
SHRI A.T. VARKEY, JUDICIAL MEMBER**

**ITA No.6291/Del./2013
(ASSESSMENT YEAR : 2010-11)**

M/s. Amar Packagings Pvt. Ltd.,
D – 19/1, Okhla Indl. Area-II,
New Delhi.

vs. ITO, Ward 1 (4),
New Delhi.

(PAN : AAACA5760G)

(APPELLANT)

(RESPONDENT)

ASSESSEE BY : Shri Ved Jain, Advocate
REVENUE BY : Shri S.K. Jain, DR

ORDER

PER A.T. VARKEY, JUDICIAL MEMBER :

This appeal, at the instance of the assessee, is filed against the order of the CIT (Appeals)-IV, New Delhi dated 06.09.2013 for the assessment year 2010-11.

2. The sole ground taken by the assessee before us is against the disallowance u/s 14A of the Income-tax Act, 1961 (hereinafter 'the Act') read with Rule 8D of the Income-tax Rules, 1962 (hereinafter 'the Rules') made by the AO and sustained by the ld. CIT (A).

3. During the year under consideration, the assessee company was engaged in the business of sale and purchase of shares and securities. The assessee filed a return on 15.10.2010 declaring NIL income with a loss of Rs.14,18,360/-. The

assessee has earned exempt income in the form of dividend of Rs.17,56,369/- on the investment of shares and the same was claimed as exempt u/s 10(34) of the Act. The AO observed that Rule 14A is applicable in assessee's case and has also observed that the assessee has incurred direct expenses on account of interest to the extent of Rs.2,35,16,782/-. Thus, the AO computed disallowance @ 0.5% of average value of investment and worked out disallowance of Rs.1,13,77,730/-.

4. Aggrieved, the assessee went in appeal before the Id. CIT (A) who upheld the action of the AO by observing as under :-

“4.3 I have carefully considered the submissions of the Id. AR and perused the order passed by the AO. I find that the appellant has investment of Rs.3,85,88,317.42 as on 31.3.2010 in its balance sheet. The appellant has incurred direct interest expenses of Rs. 2,35,16,7801- The AO has applied Rule 80. The Hon'ble Mumbai High Court in the case of Godrej & Boyce Mfg. Co. Ltd. vs. DCIT [2010] 328 ITR 81 (Bom) has held that the AO is duty bound to make the disallowance where the assessee has made investment income from which is exempt from tax. Similarly, Hon'ble Mumbai ITAT in the case of Stream International Services P. Ltd. v ACIT [2013] 023 ITR (Trib.) 0070 has held that the disallowance u/s 14A is to be made even if no exempt income is realized. The contention of the appellant that the appellant has made investment in shares for appreciation and incurred direct interest expenses of Rs.61,666/- only is not correct. Rule 8D provides the disallowance @ 0.5% of average investment. The AO has correctly applied Rule 8D. In view of the above discussion, I do not find any merit in the submission of the Id. AR. The addition made by the AO is upheld. This ground of appeal is rejected.”

5. The assessee, being aggrieved, is in appeal before us.

6. Ld. AR for the assessee submitted that the assessee has made investment in shares and securities for earning capital appreciation and earning dividend income is incidental to such activities. He submitted that the assessee has incurred interest

expenses to earn taxable income such as trading profit and capital gains. He submitted that the dividend income was not arising on all investment held by the assessee and earning of dividend income was due to holding of investments. He further submitted that the assessee has filed a revised computation claiming expenditure of Rs.61,666/- being incurred for earning income as exempt income. He submitted that assessee had paid salary of Rs.1,20,000/- to one person and DMAT charges of Rs.3,332/- and claimed that 50% of such expenses i.e. Rs.61,666/- (0.50% of Rs.1,20,000/- + Rs.3,332/- = Rs.1,23,332/-) were incurred for earning the exempt income. He submitted that Section 14A is applicable only if some expenditure has actually been incurred by the recipient of tax free income. He further submitted that only expenditure which has been proved to have been incurred in relation to the earning of tax-free income can be disallowed and the section cannot be extended to disallow even expenditure which is assumed to have been incurred for the purpose of earning of tax free income. The word "incurred" refers to the actual spending of the expenditure in relation to the exempt income and does not refer to deemed spending or assumed spending for the purpose. Ld. AR submitted that the AO completely ignored the submissions of the assessee and without recording any satisfaction, straight away applied the provisions of Rule 8D of the Rules and made the disallowance. Ld. AR further submitted that in any case, the disallowance u/s 14A cannot exceed tax free income of the assessee. In this regard, he relied on the following decisions :-

- (i) CIT vs. Taikisha Engineering India Ltd. –370 ITR 338 (Del.);

(ii) ACIT, Circle II, Faridabad vs. NHPC Ltd. – ITA No.424/Del/2013
dated 26th August, 2015

He also relied on a number of decisions in the written synopsis filed by him. Thus, Id. AR pleaded that the orders of the authorities below be set aside and the addition be deleted.

7. Ld. DR for the revenue relied on the orders of the authorities below.

8. We have heard both the sides and perused the records. We find that the assessee had earned exempt income by way of dividend of Rs.17,56,369/- on investment in shares and has claimed it as exempt u/s 10(34) of the Act. The assessee had claimed expenditure to the tune of Rs.61,666/- being incurred for earning the exempt income by filing a revised computation of income. According to the assessee, it had paid a salary of Rs.1,20,000/- to one person and DMAT charges of Rs.3,332/- and claimed 50% of such expenses i.e. Rs.61,666/- incurred for earning the exempt income. However, we find that the AO did not agree with the expenditure shown by the assessee and has stated in the order that, *“the contention of the assessee is gone through and it is not accepted as the interest on the loans taken have been paid by the assessee company”* and went ahead with the calculation as per Rule 8D and disallowed Rs.1,13,77,730/-. The CIT (A) has upheld the addition made by the AO by stating that the assessee had incurred direct interest expenses of Rs.2,35,16,782/- and observed that the AO is duty bound to make the disallowance where the assessee had made investment to earn exempt income. The Id. AR pointed out that a perusal of paper book page 18 would reveal that administrative expenses for the company is only Rs.2,10,245/- and that includes

salary component of Rs.1,20,000/- which is the only expenditure which can be said to be incurred for the year under consideration from which 50% and DMAT expenses has been taken to arrive at Rs.61,666/-. The Hon'ble jurisdictional High Court in the case of CIT vs. Taikisha Engineering India Limited reported in 370 ITR 338 (Del.) has held as under :-

"Section 14A of the Act postulates and states that no deduction shall be allowed in respect of expenditure incurred by an assessee in relation to income which does not form part of the total income under the Act. Under sub Section (2) to Section 14A of the Act, the Assessing Officer is required to examine the accounts of the assessee and only when he is not satisfied with the correctness of the claim of the assessee in respect of expenditure in relation to exempt income, the Assessing Officer can determine the amount of expenditure which should be disallowed in accordance with such method as prescribed, i.e. Rule 80 of the Rules (quoted and elucidated below). Therefore, the Assessing Officer at the first instance must examine the disallowance made by the assessee or the claim of the assessee that no expenditure was incurred to earn the exempt income. If and only if the Assessing Officer is not satisfied on this count after making reference to the accounts, that he is entitled to adopt the method as prescribed i. e. Rule 80 of the Rules. Thus, Rule 80 is not attracted and applicable to all assessee who have exempt income and it is not compulsory and necessary that an assessee must voluntarily compute disallowance as per Rule 80 of the Rules. Where the disallowance or "nil" disallowance made by the assessee is found to be unsatisfactory on examination of accounts, the assessing officer is entitled and authorised to compute the deduction under Rule 80D of the Rules. This precondition and stipulation as noticed below is also mandated in sub Rule (1) to Rule 80 of the Rules."

After going through the other cases also, relied upon by the Id. AR, we find that the AD has not recorded the satisfaction envisaged by the statute before invoking the computation provided for under Rule 80D, which vitiates the impugned order. We also find that in assessee's own case for the previous year also, the Tribunal has deleted the addition made by the AD on this account. Therefore, we uphold the order of the CIT (A) on this issue. This ground of revenue's appeal is dismissed."

We find that the assessee has earned exempt income to the tune of Rs.17,56,369/- and has suo motu disallowed Rs.61,666/- u/s 14A of the Act. We find that the AO has invoked Rule 8D without pointing out any reason for not being satisfied with the computation made by the assessee in respect of expenditure incurred for earning exempt income. The Hon'ble jurisdictional High Court in CIT vs. Tikisha Engineering India Ltd. (supra) has held that without recording the objective satisfaction as required under sub-section (2) to section 14A that the AO is not satisfied with the correctness of the claim of the assessee in respect of expenditure in respect of exempt income, the AO cannot invoke Rule 8D to compute the said disallowance under the said Rule. Therefore, we find substance in the argument of the Id. AR and so, we find that without recording satisfaction as envisaged by the statute before invoking the computation provided for under Rule 8D has vitiated the impugned order. In this case we also note that exempt income is to the tune of Rs.17,56,369/- whereas the disallowance is to the tune of Rs.1,13,77,730/- which is 647% of the exempt income, which cannot be the interpretation for computing disallowance as per section 14A or Rule 8D as held recently by the Hon'ble jurisdictional High Court in the case of Joint Investment Pvt. Ltd. vs. CIT – (2015) 372 ITR 694 (Del.) wherein it has been held *“By no stretch of imagination, can section 14A or Rule 8D be interpreted so as to mean that the entire tax exempt is to be disallowed. The window for disallowance is indicated in section 14A, and is only to the extent of disallowing expenditure “incurred by the assessee in relation to the tax exempt income”. This proportion or portion of the tax exempt income surely cannot swallow the entire amount as has happened in this case.”* Therefore,

we direct deletion of the addition made by the AO and which was sustained by the CIT (A) in his impugned order. This ground of the assessee succeeds and the appeal is allowed.

9. In the result, the appeal of the assessee is allowed.

Order pronounced in open court on this 11th day of March, 2016.

**Sd/-
(J.S. REDDY)
ACCOUNTANT MEMBER**

**sd/-
(A.T. VARKEY)
JUDICIAL MEMBER**

**Dated the 11th day of March, 2016
TS**

Copy forwarded to:

- 1.Appellant
- 2.Respondent
- 3.CIT
- 4.CIT(A)-IV, New Delhi.
- 5.CIT(ITAT), New Delhi.

**AR, ITAT
NEW DELHI.**