

IN THE INCOME TAX APPELLATE TRIBUNAL
“A” BENCH : BANGALORE

BEFORE SHRI N.V. VASUDEVAN, JUDICIAL MEMBER
AND SHRI ABRAHAM P. GEORGE, ACCOUNTANT MEMBER

ITA No.622/Bang/2014
Assessment year : 2011-12

M/s. MPL Enterprises, Syndicate House, Manipal – 576 104. PAN : AABCM 3221B	Vs.	The Additional Commissioner of Income Tax, Udupi Range, Udupi – 576 103.
APPELLANT		RESPONDENT

Appellant by	:	Smt. Sheetal Borkar, Advocate
Respondent by	:	Shri P. Dhivahar, Jt. CIT (DR)

Date of hearing	:	12.02.2015
Date of Pronouncement	:	27.02.2015

ORDER

Per N.V. Vasudevan, Judicial Member

This is an appeal by the assessee against the order dated 17.3.2014 of the CIT(Appeals), Mysore relating to assessment year 2011-12.

2. The assessee is a company, engaged in the business of dealing in properties, foreign currency and insurance agency related services. The Assessing Officer noticed that the assessee had shown in the balance sheet as on 31.3.2011 investment in shares of Rs.92,34,050. The

assessee also earned dividend income of Rs.1,15,584 which was claimed as exempt in the computation of income.

3. Under the provisions of section 14A of the Act, any expenditure incurred in earning income (dividend income) which does not form part of total income u/s. 10A of the Act, should be disallowed. According to assessee, only a sum of Rs.2,890 in the form of administrative expenses had to be disallowed u/s. 14A of the Act.

4. The AO was of the view that disallowance of expenses of earning exempt income had to be worked out in accordance with Rule 8D of the I.T. Rules. The assessee, in reply to the query of AO in this regard submitted as follows:-

“As per our opinion there are no amount disallowable u/s 14A. The reasons are given below:

- a. As on 31st March, 2010, the total borrowed funds of the Company was Rs.9,19,00,000/-, whereas the investment held was Rs. 1,00,42,530/-. The borrowed fund represents, the amount raised by way of debentures, which was used to make the payment towards demerger dues of M/s ICDS Limited. The whole of the demerger dues of M/s ICDS Limited was incurred to acquire the assets as stock in trade and no portion of the same is allocable to the investments in shares.
- b. Further, during the year ending 31st March, 2011, there are no new investments. The whole of the debentures raised Rs. 16,00,00,000/- was used to make the repayment towards demerger of dues of M/s ICDS Limited.
- c. Thus no portion of the borrowed fund is allocable to the investments and accordingly there is no disallowance of interest u/s 14A.

d. Further no portion of the expenses allocable to earning of Dividend. None of the expenses were incurred to earn Dividend. However the Company has on its own disallowed a sum of Rs. 2,890/- towards the same, being amount incurred towards collection of cheques etc. Thus there are no further disallowances of expenses u/s 14A.”

5. The AO did not verify the aforesaid claim of the assessee, but observed that disallowance u/s. 14A of the Act r.w. Rule 8D of the Rules had to be made and he worked out the disallowance as follows:-

“4.6 Hence, in the light of the above judgments and for the reasons stated in paras above, disallowance u/s. 14A has to be done. Hence, the disallowance in accordance with Rule 8D(2) is worked out as under:

Rule 8D(2)(i)	:	NIL
Rule 8D(2)(ii)	:	$A \times \frac{B}{C}$
A. Interest expenses	:	Rs. 1,52,68,865
B. Average value of investment	:	Rs. 96,38,290
C. Average of total assets	:	$[28,19,40,678+27,24,29,698/2]$ = Rs. 27,71,35,188
		$\frac{1,52,68,865 \times 96,38,290}{27,71,35,188} =$ Rs. 5,30,929
Rule 8D(2)(iii)	:	$\frac{1}{2} \%$ of average value of investment Rs. 96,38,290 x 0.5% = Rs. 48,191
Rule 8D(2)(i)	:	NIL
Rule 8D(2)(ii)	:	Rs. 5,30,929
Rule 8D(2)(iii)	:	<u>Rs. 48,191</u>
		<u>Rs.5,79,120</u>

In view of the above, an amount of Rs. 5,79,120/- as worked out above is added to the total income of the assessee u/s 14A r.w. rule 8D of the IT Rules being the expenditure for

earning the exempted income for which the AR of the assessee vide order sheet noting dated 12.12.2013 has agreed.”

6. Before the CIT(A), the assessee reiterated the contentions as were put forth before the AO. The CIT(A), however, upheld the order of AO. Hence the assessee's appeal before the Tribunal.

7. The Id. counsel for the assessee filed before us a copy of the Annual Report for 2010-11 and pointed out that the own funds of the assessee as on 31st of March, 2010 & 2011 were much more than the investments in shares. It was pointed out by him that share capital reserves and surplus were Rs.2,84,03,000 and Rs.69,45,722 respectively as on 31.3.2010 and Rs.2,84,03,000 and Rs.74,75,780 respectively as on 31.3.2011. The value of investments in shares as on 31.3.2010 was Rs.1,00,42,530 and as on 31.3.2011 it was Rs.92,34,050. The Id. counsel for the assessee accordingly submitted that own funds were much more than the investment in shares and therefore no disallowance ought to have been made u/s. 14A of the Act r.w. Rule 8D of the Rules. The other submissions made before the AO were also reiterated before us.

8. The Id. DR relied on the order of the AO.

9. We have given a very careful consideration to the rival submissions. In our view, the disallowance u/s. 14A of the Act r.w. Rule 8D of the I.T. Rules insofar as it relates to application of Rule 8D(2)(ii) of the Rules cannot be sustained. As is clear from the financial statements, the

assessee had own funds which were sufficient to make investment in shares. In the circumstances, the conclusion of AO that borrowed funds were used for making investments in shares cannot be sustained.

10. As far as disallowance under Rule 8D(2)(iii) of the Rules is concerned, the same deserves to be remanded back to the AO for fresh consideration. The assessee had claimed before the AO that general expenses incurred for earning tax free dividend was only Rs.2,890. This explanation has not been found to be false by the AO. Whenever an assessee makes a claim regarding expenditure incurred for earning exempt income, it is incumbent upon the AO to consider such a claim and reject the same objectively and only thereafter AO can resort to invoking Rule 8D(2)(iii) of the Rules. In the set aside proceedings, the AO will examine the claim of assessee and thereafter decide the issue in accordance with law.

11. In the result, the appeal of the assessee is partly allowed.

Pronounced in the open court on this 27th day of February, 2015.

Sd/-
(ABRAHAM P. GEORGE)
Accountant Member

Sd/-
(N.V. VASUDEVAN)
Judicial Member

Bangalore,
Dated, the 27th February, 2015.

/D S/

Copy to:

1. Appellant
2. Respondents
3. CIT
4. CIT(A)
5. DR, ITAT, Bangalore.
6. Guard file

By order

Assistant Registrar /
Senior Private Secretary
ITAT, Bangalore.