

आयकर अपीलीय अधिकरण, जयपुर न्यायपीठ, जयपुर
IN THE INCOME TAX APPELLATE TRIBUNAL, JAIPUR BENCHES, JAIPUR

श्री कुल भारत, न्यायिक सदस्य एवं श्री विक्रम सिंह यादव, लेखा सदस्य के समक्ष
BEFORE: SHRI KUL BHARAT, JM & SHRI VIKRAM SINGH YADAV, AM

आयकर अपील सं./ITA No. 854/JP/2016
निर्धारण वर्ष/Assessment Year : 2012-13.

M/s Lakhani Shoe Co. Pvt. Ltd. Plot No. 130, Sector-24, Faridabad – 121005	बनाम Vs.	Asst. Commissioner of Income Tax, Circle-2, Alwar.
स्थायी लेखा सं./जीआईआर सं./PAN No. AAACL 2991 A		
अपीलार्थी / Appellant		प्रत्यर्थी / Respondent

निर्धारिती की ओर से / Assessee by : Shri S.C. Vasudeva (C.A)
राजस्व की ओर से / Revenue by: Shri S.L. Chandel (Addl.CIT)

सुनवाई की तारीख / Date of Hearing : 25.08.2017.
घोषणा की तारीख / Date of Pronouncement : 18/09/2017.

आदेश / ORDER

PER SHRI KUL BHARAT, JM.

This appeal by the assessee is directed against the order of Ld. CIT (A)-22,
Alwar dated 15.07.2016 pertaining to Assessment Year 2012-13.

The assessee has raised the following grounds of appeal:-

- "1. That the Ld. CIT(A) while sustaining the addition of Rs. 8,91,810/- out of the addition of Rs. 9,05,772/- as made by the Ld. Assessing Officer, under section 14A of the Act read with Rule 8D, has failed to consider the fact that no satisfaction has been recorded by the Ld. Assessing Officer for making the aforesaid disallowance.
2. That in this connection, the Ld. CIT(A) has not considered the fact that since no exempt income has been earned by the appellant, disallowance under section 14A of the Act read with Rule 8D is not warranted.
3. (a) That in this connections, the Ld. CIT(A) has erred in law and on facts in sustaining the aforesaid addition u/s 14A of the Act read with Rule 8D, without giving credence to the fact that investment of Rs.

2,26,75,000/- made in Lakhani Footwear Pvt. Ltd., was as a result of the family settlement/arrangement pursuant to the order of the Company Law Board (CLB) dated 22.05.2008 for which there was no outflow of funds as well as fact that such settlement/ arrangement took place in the earlier years by virtue of the said order.

(b) that further in this connection the Ld. CIT(A) has misinterpreted the provisions of law inasmuch as, he has himself stated in his order that there has been a quid-pro-quo to settle the family dispute for which the payment was not made in cash but would have been made in kind. Accordingly, there being no outflow of funds, there cannot be a presumption that interest bearing funds have been utilized for the purpose of the said investment and accordingly, no disallowance under section 14A of the Act read with Rule 8D is warranted.

4. That the appellant craves leave to add, amend and/or alter the grounds of appeal at a later date."

2. Grounds no. **1 to 3** are against invoking the provisions of Section 14A of the Income Tax Act, 1961 (hereinafter referred to as the Act) read with Rule 8D of the Income Tax Rule, 1962.

3. Briefly stated the facts are that the case of the assessee was picked up for scrutiny assessment and the assessment u/s 143(3) of the Income Tax Act, 1961 (hereinafter referred to as the Act) was framed vide order dated 24/12/2014. During the assessment proceedings, the Assessing Officer observed that on perusal of note 9 of balance sheet it was gathered that the assessee had investment to the tune of Rs. 3,00,000/- in 14500 equity shares of HFC, investment of Rs. 55,000/- in 1000 equity shares of M/s Auto Pin (India) Ltd., investment of Rs. 2,26,75,000/- in 22,67,500/- shares of M/s Lakhani Footwear Private Limited. Thus total such investments comes to Rs. 2,30,30,000/- and no income from the above investment has been included to the total income of the assessee. On the other hand the assessee was paying interest to the banks. The above investment attracts the

disallowance 14A read with Rule 8D. Hence, the Assessing Officer applied provision of Section 14A read with Rule 8D and made addition of Rs. 9,05,772/-. Appeal from addition made on account of disallowance of interest paid on unneeded loss.

4. Aggrieved by this order, assessee preferred an appeal before Ld. CIT(A), who after considering the submissions partly allowed the appeal. Thereby, the Ld. CIT(A) deleted the addition made on account of disallowance of interest of Rs. 50,31,326/- and restricted the addition made by invoking the provisions of Section 14A to the tune of Rs. 8,91,810/- out of addition of Rs. 9,05,772/-. Ld. Counsel for the assessee reiterated the arguments as made in the written arguments. The arguments of the Ld. Counsel for the assessee are reproduced as under:-

"The only issue involved in the appeal before the Hon'ble Bench is with regard to sustaining of an addition of Rs. 8,91,810/- by CIT(A) out of the addition of Rs. 9,05,772/- made by the learned Assessing Officer for the above assessment year under section 14A of the Income-tax Act 1961 (The Act) read with Rule 8D of Income-tax Rules, 1962.

The above addition of Rs. 9,05,772/- has been made out of the interest paid by the appellant to the extent to Rs. 1,19,26,519 on the bank borrowings. In paragraph 5.1 of the order of the Ld. Assessing Officer has stated as under:-

"It was gathered that the assessee has investment to the tune of Rs. 3,00,000/- in 14500 equity shares of HFC, investment of Rs. 55,000/- in 1000 equity shares of M/s Auto Pin (India) Limited; investment of Rs. 55,000/- in equity shares of M/s Auto Pin (India) Limited; investment of Rs. 2,26,75,000/- in 22,67,500/- shares of M/s Lakhani Footwear Private Limited. Thus total such investments come of Rs. 2,30,30,000/- and no income from the above

investments has been included to the tune of the assessee. On the other hand the assessee was paying interest to the banks. The above investment attracts the disallowance 14A read with Rule 8D."

The disallowance has been computed under Rule 8D of the Income Tax Rules, 1962. The computations in respect of such disallowance are contained in paragraph 5.4.9 of the assessment order.

In reply to show cause notice of Ld. Assessing Officer, the appellant had explained that investment to the extent of Rs. 3,55,000/- in shares of Haryana Financial Corporation (3,00,000/-) and Auto Pins (India) Ltd. Rs. (55,000) had been made in financial year 1995-96 and 1996-97 respectively. The company had enough accruals of Rs. 82.25 lakhs for financial year 1995-96 and Rs. 114.33 lakhs for financial year 1996-97 in which the aforesaid investment had been made. It was also explained to the Ld. Assessing Officer that as far as the investment of the Rs. 2,26,75,000/- in M/s Lakhani Footwear Pvt. Ltd. is concerned, this investment has arisen out of family settlement and arrangement. No funds were actually utilized. It is only a book entry and there was no outflow of funds. During Ass. Year 2011-12 also this investment was reflected in the books of account and no addition u/s 14A of the Act read with Rule 8D was made.

It was further explained to the Ld. AO that no addition has ever been made u/s 14A of the Act for any of the past assessment years taking into account has facts as stated above. The appellant had also cited various decisions of the High Court and the Tribunal wherein it has been held that no disallowance can be made, if nexus between the tax free income and amount of interest paid is not proved. However, the Ld. AO relying on the decision of the special Bench of the Hon'ble Tribunal in the case of Cheminvest Ltd. vs. ITO as well as few other decisions quoted by him in the assessment order in

paragraph 5.4.7, has given his finding in paragraph 5.4.8 and disallowed amount of interest computed in paragraph 5.4.9 of his order.

The appellant filed an appeal before Ld. CIT(A) who after going through the various submissions and upheld the addition of Rs. 8,91,810/- out of Rs. 9,05,772/- by holding that provisions of section 14A of the Act would not be applicable to investments made in the shares of Haryana Finance Corporation and Auto-pins amounting to Rs. 3,55,000/- as these have been made out of internal accruals but with regard to investment in shares of Lakhani Footwear Ltd. amounting to Rs. 2,26,75,000 there has been a quid pro-quo between two family members to settle the family dispute and the consideration for such shares stated to have not been paid in cash but would have been paid in the form of forgoing rights in certain other companies investment of the family and therefore, investment in these shares cannot be said to be free. In view thereof, the Ld. CIT(A) held that provisions of Section 14A of the Act read with rule 8D are applicable as regards the investment in shares of Rs. 2,26,75,000/-. Accordingly the addition of Rs. 9,05,772 was proportionally reduced by 6 Ld. CIT(A) and an addition of Rs. 8,91,810 was upheld.

It is humbly submitted that the Sub-section (1) of section 14A of the Act reads as under:-

“For the purpose of computing the total income under this chapter, no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to income which does not form part of the total income under this Act.”

It would be observed from the above section that disallowance is required to be made under section 14A of the Act is with reference to the expenditure incurred by an assessee in relation to income which does not form part of the total income under the Act. The Ld. AO has to be satisfied after going

through the account books, that amount of interest has been incurred in relation to a n income which does not form part of the income and that there is evidence to show that interest bearing funds have been utilized for making investment, income in respect of which is exempt from tax. The AO in this case has neither recorded his satisfaction nor has led any evidence that there was any nexus between the interest paid on borrowings and the exempt income. His observations in paragraph 5.1 of his order provide clear indication that he had made up his mind to disallow interest u/s 14A of the Act.

In this regard the Ld. CIT(A) has also failed to appreciate that the investment in shares of Lakhni Footwear Ltd. has been made by passing a book entry in the books of account for the year ended 31.3.2011 (page 53 of the Paper Books). The issue of quid pro-quo has no relevance and in case any amount of interest has not been paid by the appellant for earning any exempt income no disallowance can be made under section 14A of the Act. Both Ld. AO and Ld. CIT(A) have failed to appreciate that there is no nexus between the interest bearing funds with the investment in shares of Lakhni Footwear Ltd. The observations of the Ld. CIT(A) that only selected pages of the order of the Hon'ble Company Law Board had been filed before him seems to have been made without appreciating that the order of the Hon'ble Company Law Board had 17 enclosures having 91 pages. A reference to this has also been made in the order of the Hon'ble Company Law Board (page 17 of the Paper Book). Therefore, only relevant pages of the enclosures were filed with Ld. CIT(A) so that the volume of paper book is reduced. Nothing prevented him to ask the appellant to file a complete copy of the order along with enclosures which would have been filed without any difficulty.

It is humbly submitted that the provision of section 14A of the Act are not attracted in this case as the Ld. Assessing Officer has not recorded satisfaction having regard to the correctness of claim of the appellant with

reference to the accounts of appellant. Further, both the lower authorities failed to provide any evidence that there is a nexus between the interest bearing funds having been utilized for making investments income in respect of which is exempt from tax. In any case, there being no tax free income in the relevant year from the investments referred to by the Ld. AO and CIT(A), provision of section 14A of the Act would not be applicable in this case. The observations of the Ld. AO in paragraph 5.1 state that no income has been earned by the appellant from the investments in shares held by the appellant.

(A) The following case law supports the contention that the AO has to record his satisfaction that expenditure has been incurred and claim of the appellant is not maintainable.

- 1. Godrej and Boyce Manufacturing Co. Ltd. vs. DCIT and another (328 ITR 81) (Bombay)**
- 2. CIT vs. Taikisha Engineering India Ltd. (370 ITR 338) (Delhi)**
- 3. CIT- I, Ludhiana vs. Abhishek Industries Ltd. (2015) 56 taxmann.com 391 (Punjab & Haryana)**

(B) The following case law supports the contention that there has to be nexus between the interest bearing funds and the investment in shares.

- 1. Commissioner of Income-tax, Faridabad vs. Lakhani Marketing Inc. (2014) 49 taxmann.com 257 (Punjab & Haryana)**
- 2. Assistant Commissioner of Income-tax, Circle-1 v. Ercon Composites (2014) 49 taxmann.com 489 (Jodhpur-Trib.)**
- 3. Commissioner of Income-tax v. Hero Cycles Ltd. (2010) 323 ITR 518 (P&H)**
- 4. Commissioner of Income-tax –III v. Gujarat Narmada Valley Fertilizers Co. Ltd. (2014) 42 taxmann.com 270 (Gujarat)**

(C) It has also been held that in case no income has been earned from investment in respect of which interest is sought to be disallowed u/s 14A of the Act, no disallowance of interest can be made under the aforesaid section. Following cases support the above contention.

- 1. Redington (India) Ltd. vs. Additional Commissioner of Income-tax, Co. Range-V, Chennai (2017) 77 taxmann.com 257 (Madras)**
- 2. Ms. Amita Verma vs. Assistant Commissioner of Income-tax, Central Circle-13, New Delhi (2016) 71 Taxmann.com 91(Delhi-Trib.)**
- 3. Joint Investment (P.) Ltd. vs. Commissioner of Income-tax (2015) 59 taxmann.com 295 (Delhi)**
- 4. Assistant Commissioner of Income-tax, Company Circle-I (2) Chennai v. M. Baskaran (2014) 50 taxmann.com 138 (Chennai –Trib.)**
- 5. Cheminvest Ltd. V. Commissioner of Income-tax (2015) 378 ITR 33 (Delhi).**
- 6. CIT IV vs. Holcim India P. Ltd. (57 taxmann.com 28) (Delhi)**
- 7. CIT vs. Winsome Textile Industries Ltd. (319 ITR 204) (P&H)**
- 8. CIT – I vs. Corrttech Energy (P) Ltd. (2014) 45 taxmann.com 116 (Gujarat)**
- 9. CIT vs. Shivam Motors (P) Ltd. (2015) 55 taxmann.com 262 (Allahabad).”**

5. Per contra Ld. D/R opposed the submissions, and supported the order of authorities below.

6. We have heard the rival contentions, perused the material available on record and gone through the order of the authorities below. The assessee has challenged

the correctness of the decision of the Ld. CIT(A) holding that the provision of Section 14A of the Act, read with Rule 8D of the Income Tax Rules, 1962 is applicable with regard to the allotment of shares to the appellant to the tune of Rs. 2,26,75,000/-. The contention, of the assessee is that the shares have been allotted under a family settlement, no fund was transferred. It is also contended that the AO has not recorded satisfaction with regard to the claim of the assessee that no expenditure was incurred.

There is no dispute with regard to the fact that the investment of Rs. 2,26,75,000/- was made in M/s Lakhani Footwear Pvt. Ltd. this investment is in pursuance of family settlement. Further, revenue has not disputed the contention of the assessee that no tax free income is earned from the investment in question. We find merit into the contention that as per provision of Section 14A, the AO is empowered to make disallowance of expenditure in relation to income which does not form part of the total income under the Act. By this provision of the Act, it cannot be construed that merely investment made in such assets, on sale of such asset would fetch surplus in future, which would not be taxable, in our view, even in that situation no disallowance can be made by invoking the provision of Section 14A. For making disallowance u/s 14A, there has to be income which does not form part of total income. In the year under appeal it is not the case of the AO that the assessee has earned income out of the investment, moreover it is not the case where the assessee has claimed loss. Therefore, in our considered view, the authorities below were not justified in making disallowance of Section 14A of the Act. More particularly in view of the Judgment of the Hon'ble Delhi High Court in the case of

Joint Investment Pvt. Ltd. vs. Commissioner of Income-tax has held that - the window for disallowance was indicated in Section 14A and was only to the extent of disallowing expenditure "incurred by the assessee in relation to the tax exempt income". This proportion or portion of the exempt income cannot be swallowed the entire amount as has happened in this case.

Therefore, respectfully following the ratio laid down by the Hon'ble Delhi High Court, we direct the AO to delete the addition.

7. **Ground no. 4** is general in nature and needs no separate adjudication.
8. In the result, appeal of the assessee in ITA No. 854/JP/2016 is allowed.

Order pronounced in the open court on Monday, the 18th day of September 2017.

Sd/-
(विक्रम सिंह यादव)
(VIKRAM SINGH YADAV)
लेखा सदस्य / Accountant Member
Jaipur

Sd/-
(कुल भारत)
(KUL BHARAT)
न्यायिक सदस्य / Judicial Member

Dated:- 18/09/2017.

Pooja/

आदेश की प्रतिलिपि अग्रेषित / Copy of the order forwarded to:

1. The Appellant- M/s Lakhani Shoe Co. Pvt. Ltd., Faridabad.
2. The Respondent- ACIT, Circle-2, Alwar.
3. The CIT(A).
4. The CIT,
5. The DR, ITAT, Jaipur
6. Guard File (ITA No. 854/JP/2016)

आदेशानुसार / By order,

सहायक पंजीकार / Assistant. Registrar

