

आयकर अपीलिय अधीकरण, न्यायपीठ – “D” कोलकाता,
*IN THE INCOME TAX APPELLATE TRIBUNAL
KOLKATA BENCH “D” KOLKATA*

Before **Shri Waseem Ahmed, Accountant Member** and
Shri S.S.Viswanethra Ravi, Judicial Member

ITA No.213/Kol/2016
Assessment Year:2008-09

DCIT, Circle-11(1), P-7, Chowringhee Square, Kolkata-69	बनाम / V/s.	M/s Development Constultant Pvt. Ltd., 24, Park Street, Kolkata-16 [PAN No.AAACD 8900 F]
अपीलार्थी /Appellant	..	प्रत्यर्थी /Respondent

C.O. No.21/Kol/2016
(a/o ITA No.213/Kol/2016)
Assessment Year: 2008-09

M/s Development Constultant Pvt. Ltd., 24, Park Street, Kolkata-16	बनाम / V/s.	DCIT, Circle-11(1) P-7, Chowringhee Square, Kolkata-69
Co-objector	..	प्रत्यर्थी /Respondent

आवेदक की ओर से/By Assessee	Shri Anup Biswas, FCA
राजस्व की ओर से/By Respondent	Shri Arindam Bhattaharjee, Addl. CIT-DR
सुनवाई की तारीख/Date of Hearing	05-10-2017
घोषणा की तारीख/Date of Pronouncement	06-12-2017

आदेश /O R D E R

PER Waseem Ahmed, Accountant Member:-

This appeal as well as Cross Objection (CO) by the Revenue and assessee is directed against the order of Commissioner of Income Tax (Appeals)-9, Kolkata dated

01.12.2015. Assessment was framed by DCIT, Circle-11, Kolkata u/s 143(3) of the Income Tax Act, 1961 (hereinafter referred to as 'the Act') vide his order dated 29.12.2010 for assessment year 2008-09.

Shri Arindam Bhattacharjee, Ld Departmental Representative appeared on behalf of Revenue and Shri Anup Biswas, Ld. Authorized Representative appeared on behalf of assessee.

First we take up Revenue's appeal in ITA No.213/Kol/2016.

2. Solitary issue raised by Revenue in its appeal is that Ld. CIT(A) erred in deleting the addition made by the Assessing Officer for ₹78,94,597/- only for the expenses u/s 14A r.w.s. Rule 8D of the IT Rules, 1962.

3. Briefly stated facts are that assessee is a private limited company and engaged in activity of consultancy engineering. The assessee during the year under consideration besides the income of its consultancy engineering business also earned dividend income for ₹33,73,356/- only which was claimed as exempted u/s. 10(34) of the Act. The assessee *sum motu* offered a disallowance u/s. 14A of the Act in respect of divided income for ₹3,37,335/- being 10% of dividend income as expenditure incurred in relation to it. The disallowance was made by the assessee in the light of earlier year disallowance and as per the order of appellate authority. However, the AO observed certain facts and deficiency with the amount of disallowance made by the assessee in respect of dividend income as detailed under:-

- a) Assessee has disallowed *suo motu* expenses in relation to dividend income which implies that the assessee has incurred the expenses in the connection of dividend income.
- b) There was no justification filed by the assessee for making the disallowance @ 10% of the dividend income. The claim of the assessee that disallowance was in line of earlier year disallowance and as per the order of appellate authority cannot be applied to the present facts of the case as Rule 8D of IT Rules came into force with effect from Assessment Year 2008-09 as held by the Hon'ble Bombay High Court in the case of *Godrej & Bye Mfg. Co. Ltd. Vs. DCIT & Another* reported in 328 ITR 81(Bom).

Thus The disallowance is required to be made after having regard the books of account but in the instant case, no such reference was made by the assessee. Thus, the disallowance offered @ 10% u/s 14A of the Act does not justify the amount of disallowance. In view of above, the Assessing Officer invoked the provision of Rule 8D r.w.s 14A of the Act and made the disallowance as under:-

i) Direct expenses	nil
ii) Interest expense	Rs.76,78,824
iii) Administrative expense	<u>Rs. 2,15,773</u>
	Rs.78,94,597
iv) Amount already disallowed	Rs. 3,37,336
v) Total disallowance	Rs.75,57,261

The AO made the disallowance of the aforesaid amount and added to the total income of assessee.

4. Aggrieved, assessee preferred an appeal before Ld. CIT(A). The assessee before Ld. CIT(A) submitted as under:-

- 1) No amount of disallowance should be made u/s 14A of the Act. However, the disallowance being 10% of dividend income was offered on the basis of earlier appellate order and to avoid unnecessary / further litigation;
- 2) All the investments were made by the assessee long time back in the year 1985 to 2005 except an amount of investment of ₹29.30 lacs made during the year in mutual fund;
- 3) No part of borrowed fund was utilized in the impugned investment. Moreover, the loan funds are representing the term loan, cash credit and short term loan which were exclusively used for the purpose of business. Therefore the consideration of interest expenditure for ₹307,15,295/- for the purpose of disallowance u/s 14A of the Act is not justifiable.
- 4) The own fund of assessee is exceeding more than the investment. Therefore a presumption can be drawn that the own fund was utilized in the impugned investment.

- 5) The dividend income was earned from the subsidiary company and long term investment except for a sum of ₹50,400/- which was from other company. Therefore, the impugned investments which have given rise to the dividend income represent the strategic investment. Thus no disallowance is warranted.
- 6) Without prejudice to the above, it was also submitted that the investment which have given rise to the dividend income during the year should only to be considered for the purpose of disallowance u/s. 14A of the Act.
- 7) The AO erred in considering the net current asset instead of total of the balance-sheet while making disallowance u/s.14A of the Act Ld.

The Id. CIT(A) after considering the submission of the assessee deleted the addition made by the AO after having reliance on the order of Ld. CIT(A) for the preceding Assessment Year 2010-11 which reads as under:-

“ 4.2 I have considered the submissions of the AR and perused various judicial decisions cited before me in support of the appellant’s claim and the decisions available on this particular subject in the public domain. I have also examined the impugned order wherein the disallowance u/s.14A has been made by invoking Rule 8D of the IT Rules, 1962. From the details furnished on record, I note that the appellant had invoked Rule 8D and disallowed a sum of ₹11,86,541/- under Section 14A of the Act. It is however noted that no cogent reasons were recorded by the AO for regarding or rejecting the calculation of the appellant. Although the AO has held that Rule 8D is applicable in the relevant AY 2008-09, but he has not recorded any satisfaction nor has pointed out specific infirmity in the claim of the appellant. Section 14 clearly lays down that the AO has to record objective satisfaction in respect of the disallowance offered by the assessee having regard to its books of accounts. The AO has not considered the specific facts involved in the assessee’s case before making the disallowance. The AO seems to have mechanically ignored the explanation stating that the submissions was untenable in law and unacceptable. There is a clear lack of recording of objective satisfaction of the part of the AO before making further disallowance u/s.14A of the Act.

4.3 Nevertheless, I now proceed to consider the specific facts brought before me by the assessee in support of his claim for no-application of Rule 8D. From the audited accounts it is apparent that the average cost of investments during the relevant year was ₹446.35 lacs whereas the appellant’s net owned funds in the form of share capital & reserves were ₹3068.86 las. As such it is apparent that the assessee’s net owned funds both at the beginning and at the closing of the

relevant year were substantially higher than the cost of investments. It is also apparent that the unsecured loans have been repaid and there are no unsecured loans outstanding at the end of the year. As such it could not be said that for making investments use of borrowed funds was necessary. The AR had stated that the secured loans were obtained by the appellant for specified business purposes and nothing was brought on record by the AO to prove that the secured loans obtained for specified purposes were diverted by the assessee for acquiring investments. I also note that the assets acquired out of secured funds borrowed for specified purposes corresponded to the secured loan amounts. In the circumstances in absence of any finding on Assessing Officer's part substantiating diversion of fund, one has to accept that secured loans were utilized only for specified purposes and not utilized for acquiring investments. I also find that the investments as at the end of the relevant year were substantially brought forward from the earlier years and in the earlier years disallowance was not made by establishing any correlation between use of borrowed funds and acquisition of investments. Instead an estimated figure of 10% of exempt income was disallowed by my predecessors. On these facts therefore I find merit in the submissions of the AR that when the assessee has both own funds and borrowed funds then the presumption would be that the investments were acquired out of own funds. This proposition finds support in the decision of the ITAT, Kolkata in the case of *H.S.IL Limited vs. Addl. CIT (ITA No.83/Kol/2012) dated 05.08.2014*. Since the assessee's net own funds substantially exceeded the cost of investments and the AO not having established any proximate cause between use of secured loans and acquiring investments, disallowance was not justified simply on presumption. For the reasons set out in the foregoing, therefore, I do not find merit in the AO's action of disallowing interest of ₹9,66,502/- and the same is directed to be deleted.

4.4 Similarly the AO disallowed 0.5% of the average investments by invoking Rule 8D(2)(iii). From the AO's working I note that the disallowance was made at 0.5% of average investments which inter alia included strategic investments in group & subsidiary companies. In the first instance I find that the AO did not identify any specific item of expenditure which he found to be relatable to earning of tax free income. As pointed out by the AR the dividend only on two occasions was received by ECS mode without incurring any collection or bank charges. Whatever little administrative expenses incurred for accounting of the expenses, the appellant had disallowed ₹1,46,866/-. Moreover no disallowance out of administrative expenses was permissible where the investments were made in subsidiaries for strategic but purposes. These investments were made with business motive and not to earn dividend income. The Delhi High Court in the case of *Oriental Structure Engineers Pvt. Ltd. (216 taxmann 92)* has held that where the assessee had made investments in shares of subsidiaries on the principle of commercial expediency and with a view to achieve business objective and not for the purposes of earning dividend simplicitor then no disallowance u/s. 14A is warrant. A similar view has been adopted by the ITAT, Mumbai Bench in the case of *Garware Wall Ropes Limited (5408/Mum/2012)*.

Furthermore the ITAT, Kolkata in the case of REI Agro Ltd (ITA No.1331/Kol/2011) date 19.06.2013 has held that disallowance under section14A read with rule 8D is to be in relation to the income which does not form part of the total income and this can be done only by taking into consideration the investment which has given rise to this income which does not form part of the total income. In the circumstances only the expenses incurred in relation to investments which yielded exempt income amounting to ₹51.66 lacs, that the expenses could have been disallowed u/s.14A. On the contrary I find that the assessee itself had suo moto disallowed expenses of ₹1,46,868/-. Such expenditure being offered for disallowance is therefore held to be disallowable u/s.14A of the Act. The AO is accordingly directed to delete the disallowance of ₹2,20,039/- made under Rule 8D(2)(iii).”

The Revenue, being aggrieved, is in appeal before us.

5. Ld. DR before us submitted that the disallowance has to be made as per Rule 8D of the IT Rules as it came into force with effect from Assessment Year 2008-09. He fairly supported the order of AO.

On the other hand, Ld AR filed a paper book which is running from pages 1 to 84 and stated that own capital of assessee exceeds the amount of investment. Therefore no disallowance of interest expense can be made under Rule 8D(2)(ii) of the IT Rules, 1962. He cited case law of Hon'ble Bombay High Court in the case of *CIT vs. Reliance Utilities and Power Ltd.* reported in (2009) 313 ITR 340 (Bom) and *CIT vs. HDFC Bank Ltd.* Income Tax Appeal No. 330 of 2012 dated 23.07.2014.

Ld.AR further submitted that the disallowance towards administrative expense can be made under Rule 8D(2)(iii) of the IT Rules, in respect of the investment which have given rise to the dividend income during the year.

Ld. AR also contained the major dividend income was received from the subsidiary company. Therefore no disallowance can be made in respect of dividend income received from subsidiary company. The relevant details of the dividend income detailed as under:-

(i)	Subsidiary Company	Amount of dividend Amount (Rs)	
	DC Industrial Plant services Pvt. Ltd.	14,39,940	
	Kontest Chemicals	<u>15,66,900</u>	
		<u>30,06,840</u>	30,06,840
(ii)	Non-subsidiary company		
	Investech Securities Pvt. Ltd.	<u>50,400</u>	
		50,400	50,400

Total 30,57,240

In this regard, Ld. AR has relied on the order of Chennai Tribunal in the case of *EIH Associated Hotels Ltd. vs. DCIT* in ITA No.1503 & 1624/Mds/2012 dated 17.07.2013 for the assessment year 2008-09. Lastly, Ld. AR relied on the order of Ld. CIT(A).

6. We have heard the rival contentions of both the parties and perused and carefully considered the materials on record; including the judicial pronouncements cited and placed reliance upon. In the instant case, the disallowance was made by AO as per Rule 8D of the IT Rules in respect of dividend income earned by assessee during the year and assessee claimed to have earned dividend income as detailed under:-

<i>Particulars</i>	<i>Amount (Rs)</i>
<i>Income from investment as per P&L</i>	<i>40,42,886.00</i>
<i>Less: Dividend not eligible for exemption</i>	<u><i>6,69,630.00</i></u>
	<i>33,73,356.00</i>
<i>Dividend (exempt) as above</i>	<i>33,73,356.00</i>
<i>Less: Deduct estimated expenditure @ 10%</i>	
<i>As per CIT(A) order</i>	<u><i>3,37,335.00</i></u>
<i>Total [see note below]</i>	<i>30,36,020.00</i>

Note: dividend not eligible for exemption would be Rs.9,85,646/- instead of Rs.6,69,630/- mentioned above and consequently the "dividend eligible for exemption" would be Rs.30,57,240/- [40,42,886 – 9,85,646] as against claim of exemption of Rs.30,36,020/- in the return. This is because the contention of the appellant that no expenditure has been incurred in relation to the dividend income of Rs.30,57,240/-

The disallowance was made by the AO under Rule 8D(2) (iii) and Rule 8D(2)(iii) of IT Rules, 1962. As regards to the disallowance made by the AO on account of interest expense, we note that the own capital of assessee exceed amount of investment as demonstrated under:-

Own fund position vis-à-vis investment

As on the last date of the previous year relating to assessment year 2008-09 i.e. 31.03.2008, the position of shareholder fund was as follows:

<i>Own fund</i>	<i>Rs. In lakhs</i>
<i>Share capital – opening</i>	<i>120.00</i>
<i>Reserve & surplus-opening</i>	<u><i>1780.29</i></u>
	<i>1900.29</i>

Deduct:

<i>Revaluation reserve-opening</i>	<u>690.33</u>
<i>Own fund at the beginning of the year</i>	<u>1209.96</u>

<i>Add: Profit of F.Y 2007-08 after tax</i>	<u>558.14</u>
(A)	<u>1768.10</u>

Investments

<i>Total investment at the beginning of the year</i>	416.75
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<i>Less: Total investment at the end of the year</i>	<u>446.35</u>
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<i>Investment made during the year (B)</i>	<u>29.60</u>
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<i>Net owned fund position as on 31.03.08 (C) [A-B]</i>	<u>1738.50</u>
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Submission: 1. Investment of Rs.29.60 lakh was made during the year under Appeal in mutual fund etc.

2. own fund of the appellant is far more than the total cumulative investment.

From the above details we observed that there is no ambiguity with regard to own fund available with the assessee. In such facts and circumstances a presumption can be drawn that investment has been made out of own fund of assessee. Therefore no disallowance on account of interest expense should be made under Rule 8D(2)(ii) of IT Rules. In holding so, we draw our support and guidance from the judgment of Hon'ble Bombay High Court in the case of *Reliance Utilities and Power Ltd.* (supra) wherein it was held as under:-

"The principle therefore would be that if there are funds available both interest-free and overdraft and/or loans taken, then a presumption would arise that investments would be out of the interest-free fund generated or available with the company, if the interest-free funds were sufficient to meet the investments. In this case this presumption is established considering the finding of fact both by the CIT(A) and Tribunal"

6.1 Similarly the ld. AR also relied on the order of the Hon'ble Bombay High Court in the case of *CIT vs HDFC Bank Ltd* reported in 366 ITR 505 (Bom). The relevant extract of the order is reproduced below :-

"Where assessee's capital, profit reserves, surplus and current account deposits were higher than the investment in tax-free securities, it would have to be presumed that investment made by the Assessee would be out of the interest-free funds available with Assessee and no disallowance was warranted u/s 14A."

In view of above proposition, we hold that no disallowance of interest expense claimed by the assessee can be made under the provision of Section 14A of the Act r.w.r 8D of IT Rules.

Now coming to the disallowance made by the AO in respect of administrative expense we note that the investment which have given rise to the dividend income during the year can only be considered for the purpose of disallowance under Rule 8D(2)(iii) of IT Rules.

In holding so we find guidance & support from the order of Coordinate Bench of this Tribunal in the case of *REI Agro Ltd. v. Dy. CIT* [2013] 35 taxmann.com 404/144 ITD 141 (Kol.) which was also affirmed by the Hon'ble Calcutta High Court vide Order dated 09.04.2014 in GA No. 3581 of 2013, wherein it was held that the disallowance as per Rule 8D shall be made by taking into consideration only those shares, which have yielded dividend income in the year under consideration. Therefore we direct the AO to make the disallowance under rule 8D after considering the investments which have yielded the dividend income during the year.

7. We also find that the assessee has made investment in subsidiary company from which the dividend income was earned by it during the year. In this regard, we observed that the assessee has made strategic investment in its subsidiary company to control the interest in the company and not with the object to earn dividend income. The dividend income is merely incidental from the subsidiary company. Therefore no disallowance of whatsoever can be made in respect of dividend income earned from the subsidiary company. In holding so, we find support and guidance from the order of the Hon'ble Tribunal in the case of *Electrosteel Casting Limited Vs. DCIT* reported in 58 ITR (Trib) 5 wherein it was held that no disallowance shall be made against the dividend income if it arises from the strategic investment. The relevant extract of the order reads as under:-

“141. We have considered the aforesaid submissions of the learned counsel for the assessee and are of the view that in the light of the decisions referred to above, in computing the disallowance under section 14A of the Act read with rule 8D(2)(ii) and (iii) of the Rules, the Assessing Officer while adopting the average value of investments has to consider only those investments which yielded dividend income during the previous year. Similarly, in computing the disallowance under section 14A of the Act read with rule 8D(2)(ii) and (iii) of the Rules, the Assessing Officer while adopting the average value of investments has to exclude the investments which are strategic investments.”

Thus, the strategic investments need to be excluded for the purpose of the disallowance under section 14A read with rule 8D of Income Tax Rules. The Id. DR before us has not brought anything contrary to the argument of Id. AR that the impugned investments are not strategic investments. Thus in the above proposition and respectfully following the order of this Tribunal in the case of *Electrosteel Casting Limited* (supra) we reverse the order of lower authorities.

In view of the above, we hold that the investments made in the non-subsiary company which have yielded dividend income can only be considered for the purpose of the disallowance under section 14A r.w.r. 8D(2)(iii) of Income Tax Rules 1962. Thus the appeal filed by Revenue is partly allowed. Accordingly, AO is directed.

Coming to assessee's CO No.21/Kol/2016.

8. As far as CO filed by assessee is concerned, the first aspect to be considered is the condonation of 16 days delay in filing the CO which is explained as owing to holidays followed with Saturday and Sunday. Considering the reasons given, we deem it fit to condone the delay in filing the CO of assessee.

9. Grounds raised by assessee in its CO are as under:-

"1. For that on the facts and in the circumstances the Learned Commissioner of Income Tax (Appeals) was wrong in not considering the fact that during assessment proceeding the appellant had contended that although no expenditure was incurred in earning the dividend income, the appellant, to avoid unnecessary litigation on this matter, had offered in it return disallowance @ 10% on the basis of an earlier year CIT(A) order amounting to Rs.3,37,335.

2. For that the Learned Commissioner of Income Tax (Appeals) had erred in not considering the third limb of Rule 8D(2) of the IT Rules towards 0.5% of average value of investments from which exempt income has been earned [0.5% of 15,74,990 (excluding subsidiary)] so much so that he sustained the additions of Rs.3,37,335, disputed by the appellant during the course of assessment, in place of Rs.7,875/- being 90.5% of Rs.15,74,990.

3. The Appellant craves the opportunity to adduce further grounds as additional grounds before and/or at the time of hearing."

10. The effective issue raised in both the ground of assessee's CO is that Ld. CIT(A) erred in not giving direction to make the disallowance under Rule 8D(2)(iii) of the IT Rules after excluding the dividend income earned from the subsidiary company.

11. At the outset, we find that the impugned issue is well settled by the various Benches of ITAT as discussed above. Respectfully following the same and taking a consistent view, we hold that while making the disallowance under Rule 8D(2)(iii) of IT Rules in the instant case the dividend income earned from subsidiary company should be excluded for the purpose of disallowance. Hence, assessee's CO is allowed.

12. **In the result, appeal of Revenue is partly allowed and that of CO of assessee is also allowed.**

Order pronounced in open court on 06/12/2017

Sd/-

(न्यायिक सदस्य)

(S.S.Viswanethra Ravi)
Judicial Member

Sd/-

(लेखा सदस्य)

(Waseem Ahmed)
Accountant Member

*Dkp, Sr.P.S

दिनांक:- 06/12/2017 कोलकाता / Kolkata

आदेश की प्रतिलिपि अग्रेषित / Copy of Order Forwarded to:-

1. आवेदक /Assessee-M/s Development Constultant Pvt. Ltd., 24, ParkStreet,Kolkata-16
2. राजस्व/Revenue-DCIT, Cir-11(1), P-7, Chowringhee Square, Kolkata-69
3. संबंधित आयकर आयुक्त / Concerned CIT
4. आयकर आयुक्त- अपील / CIT (A)
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण कोलकाता / DR, ITAT, Kolkata
6. गार्ड फाइल / Guard file.

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By order/आदेश से,

Sr. Private Secretary
Head of Office/DDO
आयकर अपीलीय अधिकरण,
कोलकाता