

**In the Income-Tax Appellate Tribunal,  
Delhi Bench 'A', New Delhi**

**Before : Shri Bhavnesh Saini, Judicial Member And  
Shri L.P. Sahu, Accountant Member**

**ITA No. 3987/Del/2015  
Assessment Year: 2010-11**

Indraprastha Sehkari Bank Ltd., A-101, Wazirpur Group Industrial Area, Delhi. PAN: AAAJI 0005P <b>(Appellant)</b>	<b>vs.</b>	ACIT, Circle 19(1), New Delhi.  <b>(Respondent)</b>
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<b>Appellant by</b>	Sh. Ved Jain, Advocate
<b>Respondent by</b>	Sh. Amit Katoch, Sr. DR

<b>Date of Hearing</b>	06.02.2019
<b>Date of Pronouncement</b>	13.02.2019

**ORDER**

**Per L.P. Sahu, A.M.:**

This is an appeal filed by the assessee against the order of ld. CIT(A)-12, New Delhi dated 25.02.2015 for the assessment year 2010-11 on the following grounds :

1. *On the facts and circumstances of the case, the order passed by the learned Commissioner of Income Tax (Appeals) {CIT(A)} is bad both in the eye of law and on facts.*
  
2. *On the facts and circumstances of the case, the learned Commissioner of Income Tax (Appeals) (CIT(A)} has erred both on facts and in law in sustaining the disallowance of Rs. 18,35,948/- to the returned income of Rs.3,47,04,820/- declared by the assessee.*

3. *(i) On the facts and circumstances of the case, the learned Commissioner of Income Tax (Appeals) (CIT(A)) has erred both on facts and in law in confirming the disallowance of an amount of Rs. 18,35,948/- made by the Ld.AO by invoking the provision of Section 14A of the Act, read with Rule 8D.*

*(ii) That the above addition has been confirmed after arbitrarily rejecting the explanation and evidences brought on record by the assessee.*

4. *On the facts and circumstances of the case, the learned Commissioner of Income Tax (Appeals) (CIT(A)) has erred both on facts and in law in confirming the disallowance made u/s 14A of the Act, ignoring the fact that the owned funds being more than the investments, no disallowance on account of Interest can be made."*

2. The brief facts of the case are that the assessee filed return on 22.09.2010 declaring income at Rs.3,47,04,820/-. The assessee is a registered cooperative society which is carrying on banking activities including providing credit facilities to its Members. The case was selected for scrutiny and statutory notices were issued to the assessee. During the course of assessment proceedings, the Id. Assessing Officer noticed that the assessee has declared dividend income of Rs.18,76,025/-, which did not form part of the total income of the assessee and the Assessing Officer also noticed that the assessee had claimed expenditure from taxable income and no further expenditure have been disallowed by the assessee towards earning the exempted income. Accordingly, the Assessing Officer issued show cause notice as to why the expenses in relation to exempt income should not be disallowed as per section 14A of the IT Act read with Rule 8D of the ITAT Rules. In reply, the assessee submitted as under :

*'The assessee is a banking organization and has invested its surplus liquidity in mutual funds by way of making original subscription in various mutual funds schemes. Such subscriptions are made in liquid funds for short term to deploy the surplus funds available with the bank. Such a subscription in mutual funds does not entail any direct or indirect cost. Further whenever the mutual fund is encashed, the payment to the assessee is made through RGTS directly to the account of the bank and no expenditure is incurred for its realization. The assessee has paid-up capital & free reserves to the tune of Rs. 1822 lacs as on 31.03.2010, whereas the investments made in the mutual funds as at the close of the year is only Rs.671 lacs.*

*Hence the assessee has not incurred any expenditure in relation to dividend income earned on the investments in mutual funds schemes, so no disallowance on this account is warranted. ”*

From the above submissions of the assessee, the Assessing Officer was not satisfied and calculated the disallowance as per Rule 8D(2)(ii) and 8D(2)(iii) and made total disallowance u/s. 14A to the tune of Rs.18,35,948/-. Aggrieved from the above additions, the assessee appealed before the Id. CIT(A), where he made detailed written submissions and relied on many case laws. The Id. CIT(A) after considering the detailed submissions of the assessee and also relying on some case laws, upheld the action of the Assessing Officer. Aggrieved by the impugned order, the assessee is in appeal before the ITAT.

3. The Id. AR of the assessee submitted a written synopsis which is as under :

1. This is assessee's appeal preferred against the order of Id. CIT(A) dated 25.02.2015, in which the Ld. CIT(A) has confirmed addition of Rs. 18,35,948/- made by the Ld. AO u/s 14A of the Income Tax Act, read with Rule 8D of the Income Tax Rules.
2. The brief facts of the case are that the assessee is a Registered Cooperative Society which is engaged in Banking Business including providing credit facilities to its Members.

3. The assessee filed its return of income on 22.09.2010 declaring an income of Rs. 3,47,04,820/-
4. Thereafter, assessee's case was selected for scrutiny and notice u/s 143(2) and 142(1) of the Act was issued to assessee.
5. During the year under consideration, the assessee had invested in Mutual Funds amounting to Rs. 6,71,27,181/-, on which assessee earned dividend income of Rs. 18,76,025/- and claimed as exempt from tax as per section 14A read with rule 8D of the Act.
6. However, the Ld. AO during the assessment proceedings had alleged that the assessee did not declare any expenditure in relation to the said exempt income and issued a show cause notice asking why the expenses in relation to the exempt income should not be disallowed.
7. In response to the above, the assessee vide reply dated 13.02.2013 (**PB Page 26**), submitted that since assessee is a banking organization, it has invested the surplus liquid funds in various mutual funds scheme. The subscription in such mutual funds schemes does not entail any expenditure and encashment is made through RTGS directly to the account of the bank. Therefore, no expenditure is incurred for realization as well.
8. However, the Ld. AO did not consider the submissions made by the assessee and made the addition in the hands of the assessee invoking Rule 8D as under:

**A. Addition under Rule 8D(ii) is computed as under:**

(i). Amount of interest paid during the year	Rs.6,34,71,270/-
(ii). Average value of investments	Rs.3,35,63,591/-
(iii). Average value of a	Rs.1,27,70,72,677/-
(iv). Net Amount of addition made by the A.O. applying Rule 8D(ii) of the Act	<b>(A)</b> Rs.16,68,130/-

**B. Addition under Rule 8D(iii) is computed as under:**

0.5% of Average value of investments	<b>(B)</b>	Rs.1,67,818/-
<b>Total disallowance made by the AO (A) + (B)</b>		<b>Rs.18,35,948/-</b>

9. The Ld. AO also alleged that since the payments to Mutual Funds have been made from the bank account with Bank of Baroda, which is a designated currency chest by RBI, therefore it was interest bearing fund and the contention of the assessee that investment was made out of interest free funds cannot be accepted.
10. Aggrieved by this, assessee filed an appeal before the Ld. CIT(A) and submitted that

the investment in these shares were made out of the own funds of the assessee and therefore addition made by the AO under section 14A is unwarranted.

11. It was also submitted that, the assessee owned surplus interest free funds as under:

(i) Paid up share capital	Rs. 3,33,80,150/-
(ii) Balance in Reserve funds	Rs. 14,88,43,047/-
(iii) Profit & loss account	Rs. 2,56,71,519/-
(iv) Balance in current deposits	Rs. 11.53.74,812/-
TOTAL	Rs. 32,32,69,528/-

From the above balances, it is obvious that the assessee's own funds and current account balance is much more than the investments in the Mutual funds which is Rs. 6,71,27,181/-. In other words investments in mutual funds is out of own funds.

12. However, learned CIT(A) disagreeing with the submissions and explanations made by the assessee confirmed the addition made by the AO.

13. The Ld. CIT(A) also sustained the additions made by the Ld. AO on the ground that the investment made out of Bank of Baroda account which is a designated currency chest of RBI, is not an interest free fund and therefore, there are no sufficient interest free funds.

14. It is pertinent to mention here that, Currency Chest is not an interest bearing fund, and interest had been paid on the amount of fixed deposits & other deposits of the customers as appearing in the balancesheets. Therefore the contention of the assessee that there are sufficient interest free funds available with the assessee cannot be held wrong.

15. It is an undisputed fact by the AO as well as CIT(A) that the own funds of the assessee are more than the investments made by the assessee. It is a well settled law that where the assessee has sufficient own funds to make the investments then it would have to be presumed that the investment made by the Assessee would be out of the interest-free funds available with the Assessee. **Reliance in this regard is placed on the following catena of judgements:**

i. **Hon'ble High Court of Punjab and Haryana in the case of CIT v. Max India Ltd. in ITA No. 186 of 2013 dated 06.09.2016**

*"Merely because the interest free funds with the assessee have decreased during any period, it does not follow that the funds borrowed on interest were utilized for the purpose of investing in assets yielding exempt income. If even after the decrease the assessee has interest free funds sufficient to make the investment in assets yielding the exempt income, the presumption that it was such funds that were utilized for the said investment remains. There is no reason for it not to. The basis of the presumption as we will elaborate later is that an assessee would invest its funds to*

*its advantage. It gains nothing by investing interest free funds towards other assets merely on account of the » interest free funds having decreased. In that event so long as even after the decrease thereof there are sufficient interest free funds the presumption that they would be first used to invest in assets yielding exempt income applies with equal force. ”*

**ii. CIT versus HDFC Bank Ltd in ITA No. 330 of 2012 dated 23 July 2014 (Bombay High Court) / [2014] 366 ITR 505 (Bombay)**

*“5. We find that the facts of the present case are squarely covered by the judgment in the case of Reliance Utilities & Power Ltd. (supra). The finding of fact given by the IT AT in the present case is that the Assessee's own funds and other non-interest bearing funds were more than the investment in the tax-free securities. This factual position is not one that is disputed. In the present case, undisputedly the Assessee's capital, profit reserves; surplus and current account deposits were higher than the investment in the tax-free securities. In view of this factual position, as per the judgment of this Court in the case of Reliance Utilities & Power Ltd. (supra), it would have to be presumed that the investment made by the Assessee would be out of the interest-free funds available with the Assessee. We therefore, are unable to agree with the submission of Mr Suresh Kumar that the Tribunal had erred in dismissing the Appeal of the Revenue on this ground. We do not find that question (A) gives rise to any substantial question of law and is therefore rejected. ”*

**iii. Gujarat High Court in the case of CIT vs Suzlon Energy Ltd. (2013) 354 ITR 630**

In this case the High Court explicitly approved the decision of ITAT holding that disallowance u/s 14A is not justified where the assessee's own funds far exceeds the investment made.

**H.T. Media Ltd. vs Principal Commissioner of Income Tax-IV, New Delhi- 2017] 399 ITR 576 (Delhi)**

*“51. In the present case, the Assessee has been able to demonstrate that the AO has failed to establish any direct nexus between the investments made by the Assessee and the interest expenditure incurred. On the other hand, the Assessee was able to show that any interest expenditure incurred was in respect of various bank loans during the course of the AY in question. The AO also failed to deal with the assertion of the Assessee that it had sufficient own funds and, as such, had no occasion to use borrowed interest bearing funds for that purpose. ”*

**ITAT Delhi in the case of NATH BROS. EXIM INTERNATIONAL LTD. VERSUS THE ACIT, ITA No. 5547/Del./2012, C.O.No.95/Del./2013 And ITA.No.6030/Del./2015**  
*“11. After considering the rival submissions, we are of the view that addition of € 2,19,561/- is not justified. The assessee has own sufficient funds which are more than the investment made by the assessee. Therefore, no interest is to be disallowed. Further, A.O.*

*has not made out a case if any borrowed funds have been used for the purpose of making investment to earn exempted income. In the absence of any nexus between the borrowed funds and the funds invested to earn exempt income, the disallowance of interest is not permissible. We, accordingly, set aside the orders of the authorities below and delete the addition of f 2,19,610/-."*

ITAT Delhi in the case of **CHINA TRUST COMMERCIAL BANK VERSUS ADIT, INTERNATIONAL TAXATION, ITA No. 1257/Del/2011** order dated 26.12.2017 "*We have carefully considered the rival contentions and also perused the orders of the coordinate bench in assessee's own case for Assessment Year 2003-04 to 2005-06 in ITA No. 212-214/Del/2016, wherein, it has been held that even in the remand proceedings the assessee failed to furnish any corroborative evidence to show how investment were made by it and through which funds. Therefore, it was held that in absence of discharge of onus the expenditure had to be disallowed. Therefore, the disallowance of Rs. 752494/- were disallowed in that year. For this year, the assessee has relied on the decision of Hon'ble Bombay High Court in C/7 Vs. HDFC Bank Ltd 366 ITR 505 wherein it has been held that if assessee is having more interest free funds then interest bearing funds , presumption would be available that investment in tax free securities has been made from interest free funds and no disallowance would be permissible u/s 14A of the Income Tax Act on account of interest. The above decision was not available before the coordinate bench while deciding issues in earlier years, no such grounds was also raised therein, During the year assessee has made investment in HUDCO of Rs. 2 crores as mentioned at page No. 3 of the assessment order whereas, interest free funds available with the assessee of share capital and reserve and surplus of Rs. 42.28 crores as at 31.03.2006. Further, as at 31.03.1999 the available interest free funds in the form of share capital and reserve and surplus was Rs. 35.14 crores. In view of this the presumption would lie in favour of the assessee that assessee has made investment out of its own tax free funds. Therefore, following decision of the Hon'ble Bombay High Court in HDFC Bank Ltd Vs. DCIT 383 ITR 529 we reverse the finding of the lower authorities and direct the Ld AO to delete the disallowance of f 364206/- on account of interest expenses being allegedly paid on pro rata basis relating to earning of tax free interest income of f 15.50 lacs on tax free HUDCO bonds of Rs. 2 crores. In the result ground No. 1 of the appeal is allowed."*

16. Regarding the disallowance of Rs. 1,67,818/- made by the Ld. AO as per Rule 8D(iii) of the Income Tax Rules, it is submitted that the Ld. A.O. has not controverted the claim of the assessee that investment and encashment of mutual funds has been made through RTGS directly through the account of Bank and accordingly no expenditure is incurred for either investment or its realization. The expenses incurred on account of various administrative expenses such as legal & professional charges, postage, telegram and telephone charges and other expenditure etc. are normal allowable Business expenditure. It is submitted that none of these expenses have direct nexus between the earning of dividend income and were incurred for the purpose of smooth & efficient running of business operations and therefore did not call for any disallowance U/s 14A of the Act.

There is no nexus between the exempted income earned and the expenditure disallowed by the Ld. AO.

17. Thus, in view of the above facts, the additions made by the Ld. AO and sustained by CIT(A) is liable to be deleted.”

4. On the other hand, the ld. DR relied on the order of the lower authorities and submitted that the lower authorities have examined the issues. Therefore, the order of the ld.CIT(A) does not call for any interference.

5. After hearing both the sides and perusing the entire materials available on record, we notice that the AR of the assessee had submitted that the assessee had sufficient own funds for making investment in mutual funds of Rs.6.71 crores. While going through the balance sheet of the assessee for the last year placed at page 6 to 8 of the paper book , we notice that the assessee’s own funds was only Rs.18.26 crores for the preceding year as paid up capital plus reserves and surplus, whereas in the current year, the own funds was increased to Rs.20.79 crores and balance in current deposit accounts have been reduced by 0.60 crores (Rs.11.54 crores – Rs.12.14 crores). Accordingly, the net increase in the own funds is by Rs.2.53 crores and the assessee has admittedly invested Rs.6.71 crores during this year. Therefore, the contention of the assessee cannot be accepted that the entire investment of Rs.6.71 croes made during this year was out of own funds and current deposit account interest free because the own funds and current deposits interest free available with the assessee in the preceding year stood invested in the assets as shown in the balance sheet itself. Therefore, in our opinion, the matter should be sent back to the Assessing

Officer to examine whether the assessee had sufficient own funds and balance in current deposit account interest free on the date of making investments. The assessee is directed to produce material evidence to support his contention that the impugned investment of Rs.6.71 crores was made out his own funds and current deposit account interest free. Needless to say, the assessee shall be given reasonable opportunity of being heard. Accordingly, the appeal of the assessee deserves to be partly allowed for statistical purposes.

6. In the result, the appeal is allowed for statistical purposes.

Order pronounced in the open court on 13.02.2019.

Sd/-

**(Bhavnes Saini)**  
**Judicial member**

Sd/-

**(L.P. Sahu)**  
**Accountant Member**

Dated: 13.02.19

*\*aks\**

*Copy of order forwarded to:*

(1) <i>The appellant</i>	(2) <i>The respondent</i>
(3) <i>Commissioner</i>	(4) <i>CIT(A)</i>
(5) <i>Departmental Representative</i>	(6) <i>Guard File</i>

*By order*

*Assistant Registrar  
Income Tax Appellate Tribunal  
Delhi Benches, New Delhi*