

आयकर अपीलीय अधिकरण, जयपुर न्यायपीठ, जयपुर
IN THE INCOME TAX APPELLATE TRIBUNAL, JAIPUR BENCH 'B', JAIPUR

श्री विजय पाल रॉव, न्यायिक सदस्य एवं श्री विक्रम सिंह यादव, लेखा सदस्य के समक्ष
BEFORE: SHRI VIJAY PAL RAO, JM & SHRI VIKRAM SINGH YADAV, AM

आयकर अपील सं./ITA No. 74/JP/2019
निर्धारण वर्ष/Assessment Years : 2014-15.

Modern Insulators Limited, A-4, Vijay Path, Tilak Nagar, Jaipur.	बनाम Vs.	The ACIT, Circle-6, Jaipur.
स्थायी लेखा सं./जीआईआर सं./PAN/GIR No. AABCM 0860 G		
अपीलार्थी / Appellant		प्रत्यर्थी / Respondent

निर्धारिती की ओर से / Assessee by : Shri Madhukar Garg (CA)

राजस्व की ओर से / Revenue by : Smt. Runi Pal (JCIT)

सुनवाई की तारीख / Date of Hearing : 04.12.2019.
घोषणा की तारीख / Date of Pronouncement : 06/12/2019.

आदेश / ORDER

PER VIJAY PAL RAO, J.M.

This appeal by the assessee is directed against the order dated 19.11.2018 of Id. CIT (A), Ajmer for the assessment year 2014-15. The assessee has raised the following grounds of appeal :-

1. That the learned CIT (Appeals) has erred in holding that the appellant has not been able to furnish any fund flow statement to show that the interest expenses of Rs. 9,69,03,638/- was incurred for earning taxable income. The said finding is illegal and unjustified.
2. That the learned CIT (Appeals) has erred in holding that the appellant had failed to prove that entire interest of Rs. 9,69,03,638/- was paid only in respect of interest bearing

borrowed funds utilized for business purposes. The said finding is illegal and justified.

3. That the learned CIT (Appeals) has erred in ignoring the decision of Hon'ble Jurisdictional High Court in the case of CIT vs. Deepak Veg Pro Pvt. Ltd., reported in 406 ITR 496. The action of the CIT (Appeals) is illegal and unjustified.
4. That the learned CIT (Appeals) has erred in holding that the Assessing Officer has worked out the disallowance u/s 14A strictly in accordance with Rule 8D and confirming the disallowance of Rs. 3,88,668/- made by the Assessing Officer u/s 14A of the IT Act. The disallowance confirmed is illegal, unjustified and excessive.

The only issue arises in this appeal is regarding disallowance made by the AO under section 14A of the IT Act on account of interest expenses as well as administrative expenses computed as per Rule 8D of the IT Rules.

2. The assessee is a public limited company and filed its return of income on 29.11.2014 declaring Nil income. During the course of assessment proceedings, the AO asked the assessee to show cause as to why disallowance under section 14A in respect of the investments made in the shares should not be made. The assessee contended that no exempt income was earned during the year under consideration and further the assessee's own funds being share capital, reserves and surplus is much more than the investments made in the shares and other securities. The AO did not accept the contention of the assessee and made disallowance of Rs. 3,88,668/- which comprises of disallowance on account of interest expenditure of Rs. 3,28,883/- and disallowance of indirect administrative expenses of Rs. 59,785/-. The assessee challenged the action of the AO before the Id. CIT (A) and contended that the assessee's own interest free funds are more than sufficient to make the

investments. Further, there is no exempt income earned during the year under consideration, therefore, no disallowance is called for under section 14A of the Act. The Id. CIT (A) was not impressed with the contention of the assessee and confirmed the addition/disallowance.

3. Before us, the Id. A/R of the assessee has submitted that there is no fresh investment made in the shares which is the major part of the total investments of the assessee during the year under consideration. Further the AO has not made any disallowance under section 14A of the Act in the preceding year i.e. 2013-14. The Id. A/R has filed a copy of the assessment order dated 22nd March, 2016 and submitted that the AO has not made any disallowance under section 14A of the Act. He has further contended that during the year under consideration the assessee has not earned any exempt income and, therefore, in view of the various decisions, no disallowance is called for under section 14A of the Act. He has also submitted that the assessee's own funds are more than sufficient to source the investments and, therefore, the disallowance made by the AO without considering the fact of availability of assessee's own funds is not sustainable in law. In support of his contention, he has relied upon the decision of Hon'ble Jurisdictional High Court in case of CIT vs. Deepak Vegpro Pvt. Ltd., 406 ITR 496 (Raj.) as well as the decisions of Hon'ble Bombay High Court in case of CIT vs. Reliance Utilities & Powers Ltd. 313 ITR 340 (Bom.), in case of CIT vs. HDFC Bank Ltd., 366 ITR 505 (Bom.) as well as a number of other decisions of the Hon'ble High Courts of Gujarat, Karnataka and Punjab & Haryana. He has referred to the Balance Sheet of the assessee and submitted that the assessee's own funds are more than Rs. 218.92 crores which are many times more to the investments in question and, therefore, no disallowance on

account of interest expenditure is called for. He has also pointed out that the assessee has purchased the shares of M/s. V.S. Lignite Power Pvt. Ltd. under the Power Delivery Agreement dated 25th September, 2008 and as per clause (c) of the said agreement, the assessee has agreed to invest a sum of Rs. 1,12,80,000/- in the share capital of the said company to ensure the un-interrupted power supply. Therefore, the investment was made under the Power Purchase Agreement with M/s. V.S. Lignite Power Pvt. Ltd. The Id. A/R has relied upon the decision of Hon'ble Madras High Court in case of CIT vs. Chettinad Logistics Pvt. Ltd. 248 Taxman 55 (Madras) and submitted that the Hon'ble High Court has upheld the decision of the Tribunal regarding the addition made by the AO under section 14A which was deleted on the ground that the assessee has not earned any exempt income during the relevant year. The Id. A/R has pointed out that the SLP filed by the revenue against the decision of Hon'ble Madras High Court was dismissed by the Hon'ble Supreme Court reported in 257 Taxman 2 (SC). Thus he has contended that the disallowance made by the AO is highly arbitrary and liable to be deleted.

4. On the other hand, the Id. D/R has submitted that the assessee has not bifurcated the use of borrowed funds and, therefore, the mere claim of assessee's own interest free funds is not sufficient until and unless the assessee comes out with the bifurcation of the borrowed funds utilized by the assessee. He has further contended that the shares purchased by the assessee even as per the Power Purchase Agreement cannot be a ground for applicability of section 14A. He has contended that the purpose of investment is not relevant but the income to be earned by the assessee out of the investments is relevant for the purpose of triggering the provisions of section 14A of the IT Act. As regards the assessment

order for the assessment year 2013-14, the Id. D/R has contended that each assessment year is a separate unit and no disallowance of expenditure under section 14A for the assessment year 2013-14 will operate as a res judicata for the AO to consider this issue for the year under consideration. He has relied upon the orders of the authorities below.

5. We have considered the rival submissions as well as the relevant material on record. The AO noted that as per Balance Sheet, the assessee has made investments of Rs. 1,17,10,000/- in the shares and securities and the assessee had also debited interest expenses of Rs. 9,69,03,638/- in the Profit & Loss account. Therefore, the AO proposed to make the disallowance of expenses under section 14A of the Act. The assessee objected to the proposed disallowance under section 14A by taking the plea that the assessee has not earned any exempt income during the year under consideration and further the assessee's own interest free funds are more than sufficient for making such investments. The AO did not accept the contention of the assessee and made the disallowance under section 14A and computed the quantum of disallowance on account of interest at Rs. 3,28,883/- and on account of indirect administrative expenses at Rs. 59,785/- total amounting to Rs. 3,88,668/-. We find from the record that the investments in the shares were made in the preceding year and there is no new investment during the year under consideration. Even the investments as on 31st March, 2013 was Rs. 1,22,04,000/- and as on 31st March, 2014 is Rs. 1,17,10,000/-. Thus there was a reduction in the investments to the extent of Rs. 4,94,000/- during the year under consideration. Once there is no fresh investment during the year under consideration, then the disallowance of interest expenditure has to be considered by taking into account the

availability of funds in the year of investment. The AO for the assessment year 2013-14 has not made any disallowance under section 14A while passing the assessment order under section 143(3) on 22nd March, 2016. Once the AO has accepted the claim of the assessee that no expenditure was incurred towards the investments made in the securities yielding tax free income for the assessment year 2013-14 then the AO cannot take a contrary stand for the year under consideration. Though the principles of res judicata is not applicable in the matter of taxation, however, the rule of consistency has to be followed when there is no change in the facts for the year under consideration in comparison to the facts exist for the assessment year 2013-14. We further note that the assessee's own funds as on 31st March, 2013 was Rs. 204.85 crores which has increased to Rs. 218.92 crores as on 31st March, 2014. Therefore, there is an increase in the assessee's own funds which is on account of reserves and surplus and meaning thereby that the profit of the assessee during the year itself is more than the investments in the shares. Hence in the facts and circumstances, when the AO has not made any addition/disallowance under section 14A for the assessment year 2013-14 and assessee's own funds are more than sufficient for the investments in shares, then the disallowance made by the AO on account of interest expenditure is not called for. The Hon'ble Jurisdictional High Court in case of CIT vs. Deepak Veg Pro Ltd. (supra) as well as various judgments including the judgment of Hon'ble Bombay High Court in case of CIT vs. Reliance Utilities & Powers Ltd. 313 ITR 340 (Bombay) as well as in the case of CIT vs. HDFC Bank Ltd 366 ITR 505 (Bombay) has upheld the finding of the Tribunal that once the assessee's own interest free funds are more than investments in tax free securities, then the presumption would be raised that the investments made by the AO would

be out of interest free funds available with it. Accordingly the disallowance made by the AO is not sustainable and the same is deleted.

5.1. As regards the disallowance on account of indirect administrative expenses, it is settled proposition of law that when there is no exempted income earned by the assessee during the year under consideration, then no disallowance is called for under section 14A. The Hon'ble Madras High Court in case of CIT vs. Chettinad Logistics Pvt. Ltd. (supra) has held in para 9 to 16 as under :-

9. In our opinion Section 14 A of the Act, can only be triggered, if, the Assessee seeks to square off expenditure against income which does not form part of the total income under the Act.

9.1 The legislature, in order to do away with the pernicious practice adopted by the Assessee's, to claim expenditure, against income exempt from tax, introduced the said provision.

10. In the instant case, there is no dispute that no income i.e., dividend, which did not form part of total income of the Assessee was earned in the relevant assessment year.

10.1 Therefore, to our minds, the addition made by the Assessing Officer by relying upon Section 14 A of the Act, was completely contrary to the provisions of the said Section.

10.2 Mr.Senthil Kumar, who appears for the Revenue, submitted that the Revenue could disallow the expenditure even in such a circumstance by taking recourse to Rule 8D.

10.3 According to us, Rule 8D, only provides for a method to determine the amount of expenditure incurred in relation to income, which does not form part of the total income of the Assessee.

10.4 Rule 8 D, in our view, cannot go beyond what is provided in Section 14 A of the Act.

11. Furthermore, we may note that a similar argument was sought to be advanced by the Revenue in the matter concerning, *Redington (India) Ltd. v. Addl. CIT [2017] 77 taxmann.com 257 (Mad.)* which was, subject matter of T.C.A.No.520 of 2016.

11.1 A Co-ordinate Bench of this Court, vide judgment dated 23.12.2016, rejected the plea of the Revenue advanced in that behalf.

11.2 As a matter of fact, a perusal of the judgment would show that the Revenue had sought to argue that because exempt income could be earned in future years, therefore, recourse could be taken to the provisions of Section 14A of the Act, to disallow expenditure. In other words the stand taken by the Revenue was irrespective of the fact whether or not income was earned in the concerned assessment year expenditure under Section 14A could be disallowed against anticipated income.

11.3 Pertinently, the Division Bench in *Redington (India)Ltd. (supra)* case has repelled this precise argument.

12. The Division Bench, in our view, quiet correctly held that, the computation of total income, in terms of Section 5 of the Act, is made qua real income and not, vis-a-vis, notional income.

12.1 The Division Bench went on to hold that Section 4 of the Act brings to tax, that income, which is relatable to the assessment year in issue. The Division Bench, thus, held that where no exempt income is earned in the previous year, relevant to the assessment year in issue, provisions of Section 14 A of the Act, read with Rule 8 D could not be invoked.

12.2 While coming to this conclusion, the Division Bench also took note of the aforementioned Circular, issued by the Board.

12.3 The reasoning of the Division Bench is contained in the following part of the judgment:

"4. The admitted position is that no exempt income has been earned by the assessee in the financial year relevant to the assessment year in issue. The order of assessment records a finding of fact to that effect. The issue to be decided thus lies within the short compass of whether a disallowance in terms of s.14A of the Act read with Rule 8D of the Rules can be contemplated even in a situation where no exempt income has admittedly been earned by the assessee in the relevant financial year.

7. Per contra, Sri. T. Ravikumar appearing on behalf of the revenue drew our attention to the marginal notes of s.14 A pointing out that the provision would apply not only where exempted income is 'included' in the total income, but also where exempt income is 'includable' in total income.

8. He relied upon a Circular issued by the Central Board of Direct taxes in Circular No.5 of 2014 dated 11.2.2014 to the effect that s.14A was intended to cover even those situations whether there is a possibility of exempt income being earned in future. The Circular, at paragraph 4, states that it is not necessary for exempt income to have been included in the income of a particular year for the disallowance to be triggered. According to the Learned Standing Counsel, the provisions of s.14A are made applicable, in terms of sub section (1) thereof to income '*under the act*' and not '*of the year*' and a

disallowance under s.14A r.w.Rule 8D can thus be effected even in a situation where a tax payer has not earned any taxable income in a particular year.

9. We are unable to subscribe to the aforesaid view. The provisions of section 14A were inserted as a response to the judgments of the Supreme Court in *Commissioner of Income Tax v. Maharashtra Sugar Mills Limited* [1971] 82 ITR 452 and *Rajasthan State Ware Housing Corporation v. Commissioner of Income-tax* [2002] 242 ITR 450 in terms of which, expenditure incurred by an assessee carrying on a composite business giving rise to both taxable as well as non-taxable income, was allowable in entirety without apportionment. It was thus that s.14A was inserted providing that no deduction shall be allowable in respect of expenditure incurred in relation to the earning of income exempt from taxation. As observed by the Supreme Court in the judgment in the case of *Commissioner of Income-tax v. Walfort Share and Stock Brokers (P) Ltd.* [2010] 326 ITR 1

'... The mandate of s.14A is clear. It desires to curb the practice to claim deduction of expenses incurred in relation to exempt income against taxable income and at the same time avail of the tax incentive by way of an exemption of exempt income without making any apportionment of expenses incurred in relation to exempt income.'

10. The provision this is clearly relatable to the earning of actual income and not notional or anticipated income. The submission of the Department to the effect that s.14A would be attracted even to exempt income 'includable' in total income would entail the assessment of notional income, assumed to be exempt in the future, in the present assessment year. The computation of total income in terms of s.5 of the Act is on real income and there is no sanction in law for the assessment of admittedly notional income, particularly in the context of effecting a disallowance in connection therewith.

11. The computation of disallowance in terms of Rule 8D is by way of a determination involving direct as well as indirect attribution. Thus, accepting the submission of the Revenue would result in the imposition of an artificial method of computation on notional and assumed income. We believe this would be carrying the artifice too far. (emphasis is ours)"

13. Mr.Senthil Kumar, seeks to distinguish the judgment in *Redington (India) Ltd. case (supra)* based on the fact that Rule 8D had not kicked-in by AY 2007-08, which was the AY being considered in the said case.

14. According to us, this was not the argument, put forth, before the Division Bench. As a matter of fact, the Revenue relied heavily on Rule 8D.

14.1 Mr.Ravikumar, who appeared for the Revenue, in that matter and who is present in this Court, informs us that he had in fact argued that the Rule was

clarifactory in nature and would apply retrospectively, and that, the Division Bench, therefore, discussed the impact of Rule 8D of the Rules.

15. However, it is, our view, as indicated above, independent of the reasoning given in *Redington (India) Ltd.* case (*supra*) that Rule 8D cannot be read in a manner, which takes it beyond the scope and content of the main provision, which is, Section 14 A of the Act.

15.1 Therefore, as adverted to above, Rule 8D, cannot come to the rescue of the Revenue.

15.2 In any event, the Tribunal, via, the impugned judgment has remitted the matter to the Assessing Officer.

15.3 Therefore, for the foregoing reasons, we are of the view, that no interference is called for qua the impugned judgment.

16. To our minds, questions of law, which could have arisen are already covered by the judgment of a Co-ordinate Bench of this Court rendered in *Redington (India) Ltd.* case (*supra*)."

The said decision was challenged by the revenue before the Hon'ble Supreme Court, however, the Hon'ble Supreme Court has dismissed the SLP filed by the revenue reported in 257 Taxman 2 (SC). Accordingly, the disallowance made by the AO under section 14A is deleted.

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

Order pronounced in the open court on 06/12/2019.

Sd/-

(विक्रम सिंह यादव)
(Vikram Singh Yadav)
लेखा सदस्य / Accountant Member

Sd/-

(विजय पाल राँव)
(VIJAY PAL RAO)
न्यायिक सदस्य / Judicial Member

जयपुर / Jaipur

दिनांक / Dated:- 06/12/2019.

das/

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

1. अपीलार्थी / The Appellant-M/s. Modern Insulators Ltd., Jaipur.
2. प्रत्यर्थी / The Respondent-The ACIT Circle-6, Jaipur.
3. आयकर आयुक्त / CIT
4. आयकर आयुक्त / CIT(A)
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, जयपुर / DR, ITAT, Jaipur
6. गार्ड फाईल / Guard File {ITA No. 74/JP/2019}

आदेशानुसार / By order,

सहायक पंजीकार / Asst. Registrar