

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

BEFORE SHRI N.V. VASUDEVAN, VICE PRESIDENT
AND SHRI B R BASKARAN, ACCOUNTANT MEMBER

ITA No.2302/Bang/2019
Assessment year:

M/s. Pai & Pai Enterprises, # 438/1, 20 th Main, 1 st Block, Rajajinagar, Bengaluru – 560 010. PAN: AABFP 0658G	Vs.	The Assistant Commissioner of Income Tax, Circle 2(2)(1), Bengaluru.
APPELLANT		RESPONDENT

Appellant by	:	Shri Pranav Krishna, Advocate
Respondent by	:	Shri Priyadarshi Mishra, Jt.CIT(DR)(ITAT), Bengaluru.

Date of hearing	:	24.06.2020
Date of Pronouncement	:	26.06.2020

ORDER

Per N.V. Vasudevan, Vice President

This appeal by the assessee is against the order dated 20.08.2019 of the CIT(Appeals)-2, Bengaluru relating to assessment year 2013-14.

2. The only issue that needs to be adjudicated in this appeal is with regard to the correctness of the quantum of sum disallowed u/s. 14A of the Income-tax Act, 1961 [the Act].

3. The assessee is a partnership firm engaged in the business of trading in packing materials. The AO noticed that the assessee received dividend income of Rs.4,93,472 which did not form part of total income under Chapter III of the Act. In view of the provisions of section 14A of the Act, any expenditure in earning income which does not form part of the

total income under Chapter III of the Act should be disallowed and added to the total income of assessee.

4. The AO computed the disallowance u/s. 14A of the Act by applying the formula laid down in Rule 8D(2)(ii & (iii) of the Income-tax Rules, 1961 [the Rules] as follows:-

Total amount of interest debited in P&L account		17,40,670
Value of investment as on 31.03.2012	1,94,83,523	
Value of investment as on 31.03.2013	1,99,66,163	
Average value of investments [A]	1,97,24,843	
Assets as on 31.03.2012	6,10,81,044	
Assets as on 31.03.2013	7,84,75,331	
Average value of assets [B]	2,97,78,188	
0.5% of the average value of investments [A * 0.5%]		98,624
Proportionate Interest on B		4,92,051
Total interest disallowed u/s. 14A		5,90,675

5. Before the CIT(Appeals), the assessee submitted that there cannot be any disallowance in terms of Rule 8D(2)(ii) of the Rules towards interest expenses because the assessee had sufficient interest-free funds which were much more than the investments which would yield exempt income. With regard to disallowance under Rule 8D(2)(iii) of the Rules, the contention of assessee was that only those investments which yielded exempt income should be taken into consideration for the purpose of arriving at the average value of investments before applying the formula under Rule 8D(2)(iii) of the Rules. The CIT(A), however, did not deal with the contention of assessee, but gave relief to the assessee by restricting the disallowance u/s. 14A of the Act to the extent of exempt income earned by the assessee i.e., Rs.4,93,477 as against the disallowance made by the AO u/s.14A at Rs.5,90,675.

6. Aggrieved by the order of the CIT(Appeals), the assessee is in appeal before the Tribunal.

7. We have heard the rival submissions. We have also perused the balance sheet of the assessee as on 31.3.2012 & 31.3.2013, a copy of which is placed at page 12 of the assessee's PB. A perusal of the same would show that own funds available with the assessee is a sum of Rs.5.58 crores (approx.), whereas the total value of the investments is only a sum of Rs.1,99,66,164. It is thus clear that interest-free own funds available with the assessee was much more than the value of investments. The Hon'ble High Court of Karnataka in the case of *CIT v. Micro Labs Ltd.*, 383 ITR 490 (Kar) has taken the view that if interest-free own funds are much more than the value of investments, then for the purpose of disallowance u/s. 14A of the Act it has to be presumed that own funds were used for the purpose of making investments and therefore no disallowance in terms of Rule 8D(2)(ii) of the Act should be made towards interest expenses. In view of the aforesaid decision of the Hon'ble High Court of Karnataka, we are of the view that the disallowance in terms of Rule 8D(2)(ii) of the Rules should be deleted. We hold and direct accordingly.

8. Insofar as disallowance in terms of Rule 8D(2)(iii) of the Rules is concerned, the limited prayer made by the Id. counsel for the assessee is that for working out the average value of investments before applying formula in terms of Rule 8D(2)(iii), only the investments which yielded tax-free exempt income should be considered and not the entire value of investments. In support of this stand, reliance was placed on the decision of the Delhi Special Bench of the ITAT in the case of *ACIT v Vireet Investments Pvt Ltd.*, 58 ITR (Trib) 313 / 165 ITD 25 (SB)(Del).

9. We have considered the submissions made on behalf of the assessee and the Id. DR. In the case of *Vireet Investments Pvt Ltd.*

(*supra*), one of the questions that arose for consideration was, whether for applying Rule 8D only dividend yielding investments should be taken into consideration for computing the average value of investments. The Special Bench held that only those investments which yielded exempt income should be considered for computing the average value of investments while applying formula under Rule 8D(2)(iii) of the Rules.

10. In view of the aforesaid decision of the Special Bench, we direct the AO to make disallowance in terms of Rule 8D(2)(iii) of the Rules by taking only the investments which yielded exempt income while computing the average value of investments.

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

Pronounced in the open court on this 26th day of June, 2020.

Sd/-
(B R BASKARAN)
ACCOUNTANT MEMBER

Sd/-
(N V VASUDEVAN)
VICE PRESIDENT

Bangalore,
Dated, the 24th June, 2020.

/Desai S Murthy /

Copy to:

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR, ITAT, Bangalore.

By order

Assistant Registrar
ITAT, Bangalore.