

**IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH 'F', NEW DELHI**

**Before Dr. B. R. R. Kumar, Accountant Member
Sh. Yogesh Kumar US, Judicial Member**

ITA No. 4971/Del/2015: Asstt. Year2011-12

ITA No. 4972/Del/2015 : Asstt. Year2012-13

M/s RJ Corp Ltd. (formerly known as M/s Arctic Drinks Ltd.), F-2/7, Okhla Industrial Area, Phase-I, New Delhi-110020	Vs.	ACIT, Central Circle-7, New Delhi
(APPELLANT)		(RESPONDENT)
PAN No. AAACA2573R		

ITA No. 5310/Del/2015 : Asstt. Year2011-12

ITA No. 5311/Del/2015 : Asstt. Year2012-13

DCIT, Central Circle-7, New Delhi	Vs.	M/s RJ Corp Ltd. (formerly known as M/s Arctic Drinks Ltd.), F-2/7, Okhla Industrial Area, Phase-I, New Delhi-110020
(APPELLANT)		(RESPONDENT)
PAN No. AAACA2573R		

Assessee by : Sh. Rajat Jain, CA&

Sh. Akshat Jain, CA

Revenue by : Sh. T. Kipgen, CIT DR

Date of Hearing:01.08.2022

Date of Pronouncement: 25.08.2022

ORDER

Per Dr. B. R. R. Kumar, Accountant Member:

The cross appeals filed by the assessee and the Revenue are directed against the orders of Id. CIT(A)-24 dated 08.06.2015.

ITA No. 5310/Del/2015 : A.Y. 2011-12 (Revenue Appeal)**Revised grounds filed on 26.07.2022**

"2. On the facts and circumstances of the case, the CIT(A) has erred in law in deleting the addition of Rs. 6,71,96,845/- made by the AO on account of disallowance u/s 14A of the I.T. Act, 1961.

3. On the facts and circumstances of the case, the CIT(A) has erred in ignoring the prescribed method under rule 8D for calculating the disallowance u/s 14A of I.T. Act, 1961, once it is established that claim of the assessee is not correct.

4. On the facts and circumstances of the case, the CIT(A) has erred in ignoring the fact that section 45(2) is applicable on conversion of investment to stock in trade of Rs. 1,79,14,46,369/- which was on 01.04.2010 as per submission of the assessee. Thus, the Id. CIT(A) has failed to enhance that capital gain arising from conversion of capital asset into stock in trade as per section 45(2) of the Act 1961."

ITA No. 4971/Del/2015 : A.Y. 2011-12 (Assessee Appeal)

2. Following grounds have been raised by the assessee:

"1. That on the facts and in circumstances of the case and in law, the Ld. Commissioner of Income Tax (Appeals) has erred by not appreciating the facts that loan given to M/s Arctic International (P) Ltd., Mauritius (AE) was out of the shareholders fund and not out of any interest bearing borrowed fund.

1.1 That the finding of the Commissioner of Income Tax (Appeals) on disallowance of Rs.1,83,35,019/- are self contradictory and bad in law.

2. That on the facts and in circumstances of the case and in law, the Ld. Commissioner of Income Tax (Appeals) has erred by not appreciating the facts of the case that the said loan was given for the direct/indirect participation, control and management of the AE's and no income accrue or arise to assessee on notional basis.

3. That on the facts and in circumstances of the case and in law, the Ld. Commissioner of Income Tax (Appeals) has erred in upholding the disallowance of Rs.89,32,232/- u/s 14A of the Income Tax Act read with clause (iii) Rule 8D of the Income Tax Rules, 1962 made by the Ld. Assessing Officer.

3.1 That the Ld. Commissioner of Income Tax (Appeals) grossly erred in law by not appreciating the facts that Ld. AO has applied Rule 8D straight away without recording his satisfaction about the claim of the appellant that no expenses were incurred related to exempt income, the disallowance upheld by the Commissioner of Income Tax (Appeals) is bad in law.

4. That on the facts and in circumstances of the case and in law, the Ld. Commissioner of Income Tax (Appeals) has erred by not appreciating the facts that the entire investment was converted into stock in trade as on 01.04.2010 and the appellant has already considered the said amount of Rs.18,85,98,890/- as trading profit on sale of the unquoted shares in its profit and loss account as well as return of income and discharged tax liability as per the provisions of the Income Tax Act.

4.1 That without prejudice, the Commissioner of Income Tax (Appeals) failed to appreciate that if the transaction on sale of shares was not to treated as trading transaction then the profit included in trading profit needs to be excluded."

3. Ground Nos. 1 & 2 of assessee appeal not pressed.

Disallowance u/s 14A:

Ground No. 2 & 3 of Revenue appeal and

Ground No. 3 of Assessee appeal

4. During the year, the assessee has earned Rs.50,000/- of dividend income which has been reflected under the head "other income" in the P&L account. The AO disallowed an amount of Rs.14,12,51,908/- u/s 14A of the Income Tax Act, 1961.

5. The Id. CIT(A) determined the disallowance @ 0.5% of the average investment.

6. Aggrieved, the Revenue filed appeal before us against the deletion of disallowance to the tune of Rs.6,71,96,859/- by the Id. CIT(A) and by the assessee for upholding disallowance of Rs.89,32,232/-. The Id. DR submitted his arguments in writing which are as under:

"In the above case, it is humbly submitted that the following submission may kindly be considered with regard to Section 14A of I.T. Act.

Submission on Section 14A

a. Section 14A of the Income-tax Act, 1961 ('Act') was into the Income Tax Act, 1961 vide Finance Act 2001, with retrospective application from 1.4.1962. It provides for disallowance of expenditure in relation to income not "includible" in total income. Over a period of time, there have been several cases decided on this issue by various High Courts.

CBDT issued a Circular no. 5/2014 on 11th February 2014, clarifying, inter alia, as follows:

"A controversy has arisen in certain cases as to whether disallowance can be made by invoking section 14A of the Act even in those cases where no income has been earned by an assessee which has been claimed as exempt during the financial-year."

3. *It is pertinent to mention that section 14A of the Act was introduced by the Finance Act, 2001 with retrospective effect from 01.04.1962. The purpose for introduction of section 14A with retrospective effect since inception of the Act was clarified vide Circular No. 14 of 2001 as under:*

"Certain incomes are not includible while computing the total income, as these are exempt under various provisions of the Act. There have been cases where deductions have been claimed in respect of such exempt income. This in effect means that the tax incentive given by way of exemptions to certain categories of income is being used to reduce also the tax payable on the non-exempt income by debiting the expenses incurred to earn the exempt income against taxable income. This is against the basic principles of taxation whereby only the net income, i.e., gross income minus the expenditure, is taxed. On the same analogy, the exemption is also in respect of the net income. Expenses incurred can be allowed only to the extent they are relatable to the earning of taxable income." Thus, legislative intent is to allow only that expenditure which is relatable to earning of income and it therefore follows that the expenses which are relatable to earning of exempt income have to be considered for disallowance, irrespective' of the fact whether any such income has been earned during the financial-year or not.

4. *The above position is further clarified by the usage of term 'includible' in the Heading to section 14 A of the Act and also the Heading to Rule 8D of I.T. Rules, 1962 which indicates that it is not necessary that exempt income should necessarily be included in a particular year's income, for disallowance to be triggered. Also, section 14A of the Act does not use the word "income of the year" hut "income under the Act". This also indicates that for invoking disallowance under section 14A, it is not material that assessee should have earned such exempt income during the financial year under consideration.*

5. *The above position is further substantiated by the language used in Rule 8D(2)(ii) & 8D(2)(iii) of I.T. Rules.....*

6. *Thus, in light of above, Central Board of Direct Taxes, in exercise of its powers under section 119 of the Act hereby clarifies that Rule 8D read with section 14A of the Act provides for disallowance of the expenditure even where taxpayer in a particular year has not earned any exempt income."*

The issue therefore, is if section 14A (1) would stand attracted even if such income, i.e., income not includible in the total income, is not actually earned, subject to expenditure relatable to such income having been incurred. The CBDT Circular 5/2014, after explaining the rationale of the provision of section 14A (with reference to Circular 14 of 2001), i.e., to curb the practice of reducing the tax liability on taxable income (i.e., income forming part of the total income) by claiming expenditure incurred in earning tax-exempt income against taxable income, goes on to state that the legislative intent is that the expenditure relatable to earning such income shall have to be considered for disallowance. In that event i.e., expenditure relating to earning tax-exempt income having been incurred, it would become irrelevant if the exempt income has actually materialized or not, so that the disallowance of the said expenditure u/s. 14A would follow. The same therefore is only a continuation of Circular 14 of 2001, taking the premise of section 14A to its logical conclusion. The purpose of these Circulars and the legislative intent is to apply the basic principle of taxation, i.e., that it is only the net income - taxable or non-taxable, i.e., net of all expenditure incurred for earning the same, that could be subject to tax or, as the case may be, exempt from tax.

The later Circular, which is in consonance with the Memorandum explaining the provisions of Finance Bill, 2001 (introducing section 14A) as well as the Notes to the Clauses presented along with the said Bill, has been noted with approval by the Hon'ble Supreme Court in CIT v. Walfort Share & Stock Brokers (P.) Ltd, [2010] 192 Taxman 211/326 ITR 1 (SC), holding as under:

"The insertion of section 14A with retrospective effect is the serious attempt on the part of Parliament not to allow deduction in respect of any expenditure incurred by the assessee in relation to income, which does not form part of the total income under the Act against the taxable income (see Circular No. 14 of 2001 dated November 22,2001). In other words, section 14A clarifies that expenses incurred can be allowed only to the extent they are relatable to the earning of taxable income. In many cases the nature of expenses incurred by the assessee may be relatable partly to the exempt income and partly to the taxable income. In the absence of section 14A, the expenditure incurred in respect of exempt income was being claimed against taxable income.

"The mandate of section 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 exemption of exempt income without making any apportionment of expenses incurred in relation to exempt income. The basic reason for insertion of section 14A is that certain incomes are not includible while computing total income as these are exempt under certain provisions of the Act."

The issue, thus, considered in perspective, is not if the income not forming the part of the total income (the tax-exempt income) is earned or not, but if expenditure relatable to such income has been incurred. If such expenditure stands incurred, section 14A(1) becomes applicable.

The decision by the Apex Court in the case of CIT v. Walfort Share & Stock Brokers (P.) Ltd. (supra) stands followed in Godrej & Boyce Mfg. Co. Ltd. v. Dy. CIT [2017] 81 taxmann.com 111 (SC) where the Hon'ble Supreme Court, while considering whether deduction of expenditure incurred in earning dividend income which is not includible in the total income of the Assessee by virtue of the provisions of Section 10(33) of the Income Tax Act, 1961 as in force during the Assessment Year i.e. 2002-2003, was admissible or otherwise, made the following observations:

"32. A brief reference to the decision of this Court in Walfort Share and Stock Brokers (P.) Ltd. (supra) may now be made, if only, to make the

discussion complete. In Walfort Share and Stock Brokers (P.) Ltd.(supra) the issue involved was: "whether in a dividend stripping transaction the loss on sale of units could be considered as expenditure in relation to earning of dividend income exempt under Section 10(33), disallowable under Section 14A of the Act?"

"33. While answering the said question this Court considered the object of insertion of Section 14A in the Income Tax Act by Finance Act, 2001, details of which have already been noticed. Noticing the objects and reasons behind introduction of Section 14A of the Act this Court held that:

"Expenses allowed can only be in respect of earning of taxable income."

"In paragraph 17, this Court went on to observe that:

"Therefore, one needs to read the words "expenditure incurred" in section 14A in the context of the scheme of the Act and, if so read, it is clear that it disallows certain expenditure incurred to earn exempt income from being deducted from other income which is includible in the "total income" for the purpose of chargeability to tax."

"The views expressed in Walfort Share and Stock Brokers (P.) Ltd. (supra), in our considered opinion, yet again militate against the plea urged on behalf of the Assessee."

The expenditure is incurred to produce or generate or in anticipation of, income, whether taxable or non-taxable. In fact, the classification as to tax status (i.e., taxable or non-taxable) has nothing to do with the income generating process; an income being, as a matter of fiscal incentive, being granted tax exempt status under the Act, for the time being. The fact of having incurred expenditure for earning income - tax-exempt (or non-exempt), which is largely a question of fact, would thus remain, and not undergo any change, irrespective of whether it has resulted in any income (whether tax-exempt or non-exempt). The principle is well-settled, representing a fundamental concept of taxation, i.e., the allowability (or otherwise) of an expenditure would not depend upon whether it has in fact resulted in an income, i.e., positive income, which is in any case a matter subsequent, and that the mere fact that expenditure

stands incurred for the purpose is sufficient for its admissibility, as explained by the Apex Court in CIT v. Rajendra Prasad Moody [1978] 115ITR 519 (SC).

The Apex Court was in that case examining the true interpretation of section 57(iii), which employed the words 'any expenditure (not being in the nature of capital expenditure) laid out or expended for the purpose of making or earning such income', the question of law raised before it reading as under:

"Whether, on the facts and in the circumstances of the case, interest on money borrowed for investment in shares which had not yielded any dividend is admissible under s. 57(iii)?"

The revenue's contention in the above case was that the making or earning of income was a sine qua non to the admissibility of the expenditure u/s. 57(iii). And, therefore, where no income resulted, no expenditure would be deductible. The Apex Court rejected the revenue's contention, and held that to bring a case within the section, it is not necessary that any income should in fact have been earned as a result of the expenditure and therefore, the interest paid on money borrowed for investment in shares, which had not yielded any dividend, was admissible under section 57(iii). The ratio decidendi of the judgment of Hon'ble Supreme Court in CIT v. Rajendra Prasad Moody (supra) can be applied to say, by the same analogy, that the expenditure incurred to earn an exempt income is subject to its admissibility in accordance with the provisions of the Income Tax Act, 1961 including those of section 14A irrespective of whether there is a receipt or income or not during the year under consideration.

In sum, the principle that it is the net income, i.e., net of expenditure relatable thereto, which is subject to tax and, correspondingly, not liable to tax, i.e., where it does not form part of the total income, is well established. It follows, therefore, that once an income is liable (or not liable) to tax, all expenditure relatable thereto is to be reckoned, and it matters little that the said expenditure has indeed resulted in a positive income. This principle, i.e., to exclude all expenditure relatable to the earning of income not forming part of the total income, irrespective of its

quantum, has also been noted with approval by the Hon'ble Apex Court in the case of Maxopp Investment Ltd. reported in [2018] 91 taxmann.com 154 held vide order dated 12.02.2018 Hon'ble Supreme Court has observed in para 3 and 32 the following:

"3. Though, it is clear from the plain language of the aforesaid provision that no deduction is to be allowed in respect of expenditure incurred by the assessee in relation to income which does not form part of the total income under the Act, the effect whereof is that if certain income is earned which is not to be included while computing total income, any expenditure incurred to earn that income is also not allowed as a deduction. It is well known that tax is leviable on the net income. Net income is arrived at after deducting the expenditure incurred in earning that income. Therefore, from the gross income, expenditure incurred to earn that income is allowed as a deduction and thereafter tax is levied on the net income. The purpose behind Section 14A of the Act, by not permitting deduction of the expenditure incurred in relation to income, which does not form part of total income, is to ensure that the assessee does not get double benefit. Once a particular income itself is not to be included in the total income and is exempted from tax, there is no reasonable basis for giving benefit of deduction of the expenditure incurred in earning such an income. For example, income in the form of dividend earned on shares held in a company is not taxable. If a person takes interest bearing loan from the Bank and invests that loan in shares/stocks, dividend earned therefrom is not taxable. Normally, interest paid on the loan would be expenditure incurred for earning dividend income. Such an interest would not be allowed as deduction as it is an expenditure incurred in relation to dividend income which itself is spared from tax net. There is no quarrel upto this extent."

"32. In the first instance, it needs to be recognized that as per section 14A(1) of the Act, deduction of that expenditure is not to be allowed which has been incurred by the assessee "in relation to income which does not form part of the total income under this Act". Axiomatically, it is that expenditure alone which has been incurred in relation to the income which is (not) includible in total income that has to be disallowed. If an expenditure incurred has no causal connection with the

exempted income, then such an expenditure would obviously be treated as not related to the income that is exempted from tax, and such expenditure would be allowed as business expenditure. To put it differently, such expenditure would then be considered as incurred in respect of other income which is to be treated as part of the total income."

The Hon'ble Supreme Court, in the judgment in the case of Maxopp Investment Ltd. reported in [2018] 91 taxmann.com 154 (SC), has also affirmed the view that the dominant purpose for which investment into shares is made by assessee may not be relevant as section 14A applies irrespective of whether shares are held to gain control or as stock-in-trade and further interpreted the dominant purpose test and upheld the theory of apportionment, in following words:

"33.....The entire dispute is as to what interpretation is to be given to the words in relation to in the given scenario, viz. where the dividend income on the shares is earned, though the dominant purpose for subscribing in those shares of the investee company was not to earn dividend. We have two scenarios in these sets of appeals. In one group of cases the main purpose for investing in shares was to gain control over the investee company. Other cases are those where the shares of investee company were held by the assessee as stock-in-trade (i.e. as a business activity) and not as investment to earn dividends. In this context, it is to be examined as to whether the expenditure was incurred, in respective scenarios, in relation to the dividend income or not.

"34. Having clarified the aforesaid position, the first and foremost issue that falls for consideration is as to whether the dominant purpose test, which is pressed into service by the assessee would apply while interpreting Section 14A of the Act or we have to go by the theory of apportionment. We are of the opinion that the dominant purpose for which the investment into shares is made by an assessee may not be relevant. No doubt, the assessee like Maxopp Investment Limited may have made the investment in order to gain control of the investee company. However, that does not appear to be a relevant factor in

determining the issue at hand. Fact remains that such dividend income is non-taxable. In this scenario, if expenditure is incurred on earning the dividend income, that much of the expenditure which is attributable to the dividend income has to be disallowed and cannot be treated as business expenditure. Keeping this objective behind Section 14A of the Act in mind, the said provision has to be interpreted, particularly, the word 'in relation to the income' that does not form part of total income. Considered in this hue, the principle of apportionment of expenses comes into play as that is the principle which is engrained in Section 14A of the Act. This is so held in Walfort Share & Stock Brokers (P.) Ltd., relevant passage whereof is already reproduced above, for the sake of continuity of discussion, we would like to quote the following few lines therefrom.

"The next phrase is, "in relation to income which does not form part of total income under the Act". It means that if an income does not form part of total income, then the related expenditure is outside the ambit of the applicability of section 14A.

.....

The theory of apportionment of expenditure between taxable and non-taxable has, in principle, been now widened under section 14A."

"35. The Delhi High Court, therefore, correctly observed that prior to introduction of Section 14A of the Act, the law was that when an assessee had a composite and indivisible business which had elements of both taxable and non-taxable income, the entire expenditure in respect of said business was deductible and, in such a case, the principle of apportionment of the expenditure relating to the non-taxable income did not apply. The principle of apportionment was made available only where the business was divisible. It is to find a cure to the aforesaid problem that the Legislature has not only inserted Section 14A by the Finance (Amendment) Act, 2001 but also made it retrospective, i.e., 1962 when the Income Tax Act itself came into force. The aforesaid intent was expressed loudly and clearly in the Memorandum explaining the provisions of the Finance Bill, 2001. We, thus, agree with the view taken by the Delhi High Court, and are not inclined to accept the opinion

of Punjab & Haryana High Court which went by dominant purpose theory. The aforesaid reasoning would be applicable in cases where shares are held as investment in the investee company, may be for the purpose of having controlling interest therein. On that reasoning, appeals of Maxopp Investment Limited as well as similar cases where shares were purchased by the assesseees to have controlling interest in the investee companies have to fail and are, therefore, dismissed.

36. There is yet another aspect which still needs to be looked into. What happens when the shares are held as 'stock-in-trade' and not as 'investment', particularly, by the banks? On this specific aspect, CBDT has issued circular No. 18/2015 dated November 02, 2015.

37. This Circular has already been reproduced in Para 19 above. This Circular takes note of the judgment of this Court in Nawanshahar case wherein it is held that investments made by a banking concern are part of the business or banking. Therefore, the income arises from such investments is attributable to business of banking falling under the head 'profits and gains of business and profession'. On that basis, the Circular contains the decision of the Board that no appeal would be filed on this ground by the officers of the Department and if the appeals are already filed, they should be withdrawn. A reading of this circular would make it clear that the issue was as to whether income by way of interest on securities shall be chargeable to income tax under the head 'income from other sources' or it is to fall under the head 'profits and gains of business and profession'. The Board, going by the decision of this Court in Nawanshahar case, clarified that it has to be treated as income falling under the head 'profits and gains of business and profession'. The Board also went to the extent of saying that this would not be limited only to co-operative societies/Banks claiming deduction under Section 80P(2)(a)(i) of the Act but would also be applicable to all banks/commercial banks, to which Banking Regulation Act, 1949 applies.

38. From this, Punjab and Haryana High Court pointed out that this circular carves out a distinction between 'stock-in-trade' and 'investment' and provides that if the motive behind purchase and sale of shares is to earn profit, then the same would be treated as trading profit and if the object is to derive income by way of dividend then the

profit would be said to have accrued from investment. To this extent, the High Court may be correct. At the same time, we do not agree with the test of dominant intention applied by the Punjab and Haryana High Court, which we have already discarded. In that event, the question is as to on what basis those cases are to be decided where the shares of other companies are purchased by the assessee as 'stock-in-trade' and not as 'investment'. We proceed to discuss this aspect hereinafter.

39. In those cases, where shares are held as stock-in-trade, the main purpose is to trade in those shares and earn profits therefrom. However, we are not concerned with those profits which would naturally be treated as 'income' under the head 'profits and gains from business and profession'. What happens is that, in the process, when the shares are held as 'stock-in-trade', certain dividend is also earned, though incidentally, which is also an income. However, by virtue of Section 10 (34) of the Act, this dividend income is not to be included in the total income and is exempt from tax. This triggers the applicability of Section 14A of the Act which is based on the theory of apportionment of expenditure between taxable and non-taxable income as held in Walfort Share & Stock Brokers (P.) Ltd. case. Therefore, to that extent, depending upon the facts of each case, the expenditure incurred in acquiring those shares will have to be apportioned."

Hence, the Hon'ble Supreme Court, in the judgment in the case of Maxopp Investment Ltd. has held as under:

(i) Only that expenditure which is in relation to earning dividends can be disallowed under section 14A and rule 8D.

(ii) The dominant purpose for which investment into shares is made by assessee may not be relevant as section 14A applies irrespective of whether shares are held to gain control or as stock-in-trade. However, where shares are held as stock-in-trade, main purpose is to trade in those shares and earn profits therefrom and, in process, certain dividend is also earned which is tax exempt under section 10(34); expenditure attributable to exempt dividend income will have to be apportioned to be disallowed under section 14A.

(iii) Rule 8D is prospective in nature and could not have been made applicable in respect of assessment years prior to 2007 when this rule was inserted.

Amendments of Finance Bill 2022.

The Finance Bill 2022, has introduced an amendment to clarify that expense disallowance under the said section shall apply and shall be deemed to have always applied even in a case where the exempt income has not accrued or arisen or has not been received during a particular year.

The amendments which are introduced with the use of words 'for removal of doubts', 'shall be deemed always to have meant' or to explain an existing provision, are normally considered to be clarificatory or declaratory amendments.

These amendments are expected to provide for an obvious omission or clear up doubts in the interpretation of an existing legislation. As a general rule, such clarificatory amendments are considered to have a retrospective effect. This applies even if such amendments are made applicable from a prospective date in the Finance Bill (See Justice GP Singh's Principles of Statutory Interpretation and CIT v. Vatika Township (P) Ltd [2014] 49 taxmann.com 249 (SC)).

In the case of Vatika Township (P) Ltd (supra), the Hon'ble Supreme Court discussed the general principles concerning retrospectively, an extract of which is as under:

- *"A legislation, be it a statutory Act or a statutory rule or a statutory Notification, may physically consists of words printed on papers. However, conceptually it is a great deal more than an ordinary prose. There is a special peculiarity in the mode of verbal communication by a legislation. A legislation is not just a series of statements, such as one finds in a work of fiction/non-fiction or even in a judgment of a Court of law. There is a technique required to draft a legislation as well as to understand a legislation. Former*

technique is known as legislative drafting and latter one is to be found in the various principles of 'Interpretation of Statutes'. Vis-a-vis ordinary prose, a legislation differs in its provenance, lay-out and features as also in the implication as to its meaning that arise by presumptions as to the intent of the maker thereof. [Para 30]

- *Of the various rules guiding how a legislation has to be interpreted, one established rule is that unless a contrary intention appears, a legislation is presumed not to be intended to have a retrospective operation. The idea behind the rule is that a current law should govern current activities. Law passed today cannot apply to the events of the past. One principle of law is known as *lex prospicit non respicit*: law looks forward not backward. As was observed in *Philips v. Eyre* [1870] LR 6 QB 1 a retrospective legislation is contrary to the general principle that legislation by which the conduct of mankind is to be regulated when introduced for the first time to deal with future acts ought not to change the character of past transactions carried on upon the faith of the then existing law. [Para 31]*
- *Thus, legislations which modified accrued rights or which impose obligations or impose new duties or attach a new disability have to be treated as prospective unless the legislative intent is clearly to give the enactment a retrospective effect; unless the legislation is for purpose of supplying an obvious omission in a former legislation or to explain a former legislation. [Para 32]*
- *For the sake of completeness, that where a benefit is conferred by a legislation, the rule against a retrospective construction is different. If a legislation confers a benefit on some persons but without inflicting a corresponding detriment on some other person or on the public generally, and where to confer such benefit appears to have been the legislators object, then the presumption would be that such a legislation, giving it a purposive construction, would warrant it to be given a retrospective effect. This exactly is the justification to treat procedural provisions as retrospective. [Para 33]"*

Hence, the rule is different when it comes to substantive amendments which modify existing rights, or which impose new obligations or impose new duties or attach a new disability. Such amendments are presumed to have prospective effect unless there is an express legislative intent to give retrospective effect.

It is my humble submission therefore alongwith the aforesaid judgments of Hon'ble Supreme Court which constitute an authority in law on the issue whether an expenditure incurred in relation to a tax-exempt income attracts disallowance u/s 14A irrespective of whether such tax-exempt income has been earned during the year or not or earned incidentally with business income, the Finance Bill 2022 has sought to put matters at rest by laying down in no uncertain terms and in a crystal clear manner the dominant intention of the statute. The same intention which was sought to be redressed by the CBDT vide Circular no.5/2014 dated 11/02/2014. For the sake of repetition, it is stressed again that the intention of the statute is that expense disallowance under the said section shall apply and shall be deemed to have always applied even in a case where the exempt income has not accrued or arisen or has not been received during a particular year. It does not talk about income earned during a particular year but income earned under the Income Tax Act. Most importantly the clarification has not modified accrued rights or imposed obligations or imposed new duties or attached new disabilities but only sought to reinforce the spirit behind the law which was the stand of the Law makers from the date of introduction of the section 14A vide Finance Act 2001, with retrospective application from 1.4.1962.

In the instant case of the appellant, as the amendments are applicable retrospectively the disallowance made by the AO deserves to be confirmed."

7. As the facts reveal that the assessee has earned Rs.50,000/- only as dividend, relying on the judicial pronouncements mentioned below and the settled position of law, we hold that no disallowance is called for more than the amount earned as dividend.

(i) Joint Investments Pvt. Ltd. Vs. CIT (59 com 295) – it was held that disallowance u/s 14A of the Act is to be restricted to the tax exempt income.

(ii) Daga Global Chemicals Pvt. Ltd. Vs. ACIT [2015-ITRV-ITAT-MUM-123) – has held that disallowance u/s 14A r.w.Rule 8D cannot exceed the exempt income.

(iii) M/s. Pinnacle Brocom Pvt. Ltd. Vs.ACIT (ITA No.6247/M/2012) – has held that disallowance u/s 14A cannot exceed the exempt income.

(iv) DCM Ltd. v. DCIT (ITA No.4567/Del/2012) – held that the disallowance u/s 14A of the Act cannot exceed the exempt income.

8. We have gone through the submissions of the Id. DR and find that the amendment has been brought by the Finance Bill 2022 which is prospective in nature. Hence, we hold that, the amount of disallowance u/s 14A of the I.T.Act needs to be restricted to the extent of exempted income earned (Rs. 50,000/-) during the relevant assessment year. The appeal of the Revenue on this ground is dismissed and the appeal of the assessee is allowed.

Conversion of Investments:

Ground No. 4 in ITA No. 4971/Del/2015 (Assessee appeal)

Ground No. 4 in ITA No. 5310/Del/2015 (Revenue appeal)

9. The detailed facts pertaining to this issue are as under:

“The appellant company was holding investment amounting to Rs.179,14,46,369/- and Nil in shares of various companies as on 31/03/2010 and 31/03/2011 respectively. The appellant company has transferred the entire investment to Stock-in-Trade with effect from 01/04/2010. The appellant company has

shown the sale of Quoted shares of Rs.18,81,966/- Unquoted shares of Rs. 59,39,27,500/- and Mutual Funds of Rs. 1,29,65,649/- under the head sales in its Profit & loss account during the financial year under consideration. The appellant company shown profit on sales of unquoted shares of Rs 18,85,98,890/- in its profit & loss account.

10. Before the Assessing Officer, the assessee submitted details of sales of quoted shares, unquoted shares and mutual funds

made during the financial year under consideration. The AO questioned to explain why the said proceeds have been credited in the P & L Account instead of being taken into consideration for capital gains. The appellant company submitted that it was engaged in investment in shares till 31.03.2010 and such shares were held as investment and were shown accordingly in the audited balance sheet as at 31.03.2010. The appellant also submitted that the board of directors in their meeting held on 01.04.2010 decided to hold the investments in equity shares and units of mutual funds as Stock in Trade with immediate effect. The reference of the same was also given in Note no. 19 of schedule 21 of the Audited Accounts. The appellant also submitted that the entire investments held as on 01.04.2010 consisting of 64696536 Nos. of equity shares / units of Mutual Funds costing Rs.1,79,14,46,369/- were transferred to Stock in trade. The appellant vide the said reply also submitted the scrip-wise share trading chart for Financial Year 2010-11 and Financial Year 2011-12 showing the complete details of shares transferred from investment account, their cost and number of shares transferred, purchases made showing quantity and value and

the sale made showing the quantity and value and closing stock of share. The appellant also submitted that the profit made on trading in shares has been duly shown as business income in the computation of income for the assessment year 2011-12 and 2012-13.

11. The Assessing Officer has completed the assessment under section 153A read with section 143(3) by making addition of Rs.18,85,98,890/- as income from capital gain from sale of unquoted shares of sister concerns by rejecting the books of account / book results without appreciating the fact that the appellant has already considered trading profit on sale of the said unquoted shares in its profit & loss account as well as return of income and discharged tax liability as the provisions of the Income tax Act, 1961. The AO held as under:

"From the details of shares purchased and sold, it is seen that substantial receipts are from sale of unquoted shares of sister concerns. Out of the total sale proceeds of Rs. 60,87,75,114/- of shares sold, the unquoted shares of sister concerns sold amount to Rs. 59,39,27,500/-. The balance of only Rs. 1,48,47,615/- is from Quoted shares and Mutual funds. The conversion on paper has been carried out only to camouflage the actual trading results and to avoid payment of capital gains by setting off expenses against the sale proceeds of shares.

In view of the above discussion the sale of unquoted shares is taken as sale of investment for the purposes of capital gains."

12. Thus, the AO made addition of Rs. 18,85,98,890/- on account of capital gain of sale of shares etc. which has been considered as business income.

13. Before us, the assessee submitted that the action of the AO which has been confirmed by the Id. CIT(A) is not tenable as income from capital gain from sale of unquoted shares of sister concerns has duly considered in the P&L account as well as in the return of income and discharged the tax liabilities as per the provisions of Income Tax Act, 1961.

14. The Id. DR supported the order of the Id. CIT(A).

15. We have gone through the relevant portion of the order of the Id. CIT(A) in toto.

"4.5.3 I have considered the submissions of the AR and the assessment order. As noted earlier at ground Nos. 1 to 5, AO has treated the unquoted shares held by the appellant as investment and brought to tax the same as capital gain. While doing so he has taken out Rs. 59,39,27,500/- from the credit side of P&L account (sale proceeds of unquoted shares) and brought to tax the same under the head capital gains after deducting the cost of the shares.

4.5.4 It is noted here that as per the appellant, the investments were converted into stock-in-trade on 01.04.2010 i.e. during the Present Previous Year itself. As per section 2(47)(iv) of the Act, transfer includes conversion of capital assets into stock- in-trade. Further, as per section 45(2) of the Act the capital gains arising from conversion of capital asset into stock-in-trade is chargeable to tax in the previous year in which such stock-in-trade has been sold or otherwise transferred. In the present case since the investments, according to the appellant, were converted into stock-in-trade during the present Previous Year itself, it is liable to offer for tax, the capital gain on conversion of such investments into stock-in-trade. The assessee has not shown any capital gain arising on such conversion. Thus even if one goes by the appellant's version, an

amount equal to market value of the unquoted shares as on 01.04.2010 minus their cost becomes chargeable to tax during the present Previous Year under the head capital gains. The balance amount i.e. the difference between the sale price and the price at which the conversion of investment took place would be chargeable under the head income from business. Since, the conversion and subsequent sale have taken place during the same previous year, the sale proceeds become taxable under the head capital gain, unless the appellant has adopted different rates for conversion & subsequent transfers.

4.5.5 However as pointed out by the AO from the seized documents (page 60 & 61 of annexure A-3 referred to at pages 12 to 15 of the assessment order) and the statement of Sh. Rajesh Chopra Director of the company dated 27.02.2014 (referred to at page 15 of the assessment order) there is no truth in the appellant's submission that the investments were in fact converted into stock-in-trade on 01.04.2010. Further all these are unquoted shares which in fact are investments and not meant for earning profit by resorting to trading in them. Mere book entry of conversion into stock-in-trade, in the given circumstances, cannot result in the investments actually becoming stock-in-trade. It is noted here that the appellant has not made any arguments on the AO's findings in this regard. Therefore, there is merit in AO's action in bringing to tax the proceeds from the sale of unquoted shares under the head capital gains. However, he has not stated whether the capital gain is taxable as long term capital gain or short term capital gain and he has also not given the indexation benefit to the appellant. Further he has to adopt the correct cost in respect of the shares transferred at each stage. He is directed to recompute the capital gain in the above manner. In the result ground is partly allowed."

16. Thus, we find that the Id. CIT(A) has affirmed the action of the AO in treating the amount of Rs.18,85,98,890/- as income from capital gains. Since, the arguments put forward before us are similar to the arguments before the Id. CIT(A), after going through the entire issue, we hereby confirm the action of the Id. CIT(A). However, we find that the revenue has taken up a ground with regard to the applicability of Section 45(2) which do not emanate either from the order of the Id. CIT(A) or from the Assessment Order. Since, we have confirmed the orders of the revenue, no adjudication on the ground no. 4 is called for.

17. In the result, the appeal of the assessee on this ground is dismissed.

ITA No. 5311/Del/2015 : A.Y. 2012-13 (Revenue Appeal)

18. Following grounds have been raised by the revenue:

"1. On the facts and circumstances of the case, the Id. CIT(A) has erred in law in deleting the addition of Rs.15,74,16,144/- made by the AO on account of disallowance u/s 14A of the Income Tax Act, 1961.

2. On the facts and circumstances of the case, the Id. CIT(A) has erred in ignoring the prescribed method under rule 8D for calculating the disallowance u/s 14A of the Income Tax Act, 1961, once it is established that claim of the assessee is not correct."

ITA No. 4972/Del/2015 : A.Y. 2012-13 (Assessee Appeal)

19. Following grounds have been raised by the assessee:

1. That on the facts and in circumstances of the case and in law, the Ld. Commissioner of Income Tax (Appeals) has erred by not accepting the revised

surrendered income of Rs. 1,75,66,829/- shown in the return of income filed in response to notice issued u/s 153A as additional interest income instead of Rs.10,00,00,000/- surrendered during post search proceedings by applying the principal of estoppel.

1.1 That the Ld. Commissioner of Income Tax (Appeals) was grossly erred in law holding that principal of estoppel apply to surrender during the search.

1.2 That Ld. Commissioner of Income Tax (Appeals) erred in law in holding that an assessee cannot revisit the surrender made during search even if there was a bonafide cause for such retrieval.

1.3 That the findings of the Commissioner of Income Tax (Appeals) on surrender are contradictory to his own findings about rejections of the books of accounts and findings on surrender are bad in law. Once books of accounts are accepted as that then revised surrender should also have been accepted.

2. That on the facts and in circumstances of the case and in law, the Ld. Commissioner of Income Tax (Appeals) has erred by not appreciating the facts that the entire investment was converted into stock in trade as on 01.04.2010 and the appellant has already considered the profit on sale of the unquoted shares in its profit and loss account as well as return of income and discharged tax liability as per the provisions of the Income Tax Act.

2.1 That without prejudice, the Commissioner of Income Tax (Appeals) failed to appreciate that if the transaction on sale of shares was not to treated as trading transaction then the profit included in trading profit needs to be excluded.

3. That on the facts and in circumstances of the case and in law, the Ld. Commissioner of Income Tax (Appeals) has erred in upholding the disallowance of Rs.97,36,816/- being done by the Ld. AO u/s 14A of

the Income Tax Act read with clause(iii) Rule 8D of the Income Tax Rules, 1962.

3.1 That the Ld. Commissioner of Income Tax (Appeals) grossly erred in law by not appreciating the facts that Ld. AO has applied Rule 8D straight away without recorded his satisfaction about the claim of the appellant that no expenses were incurred related to exempt income, the disallowance upheld by the Commissioner of Income Tax (Appeals) is bad in law."

ITA No. 5311/Del/2015

Disallowance u/s 14A:

20. The ratio laid down in ITA No. 4971/Del/2015 and 5310/Del/2015 for the A.Y. 2011-12 in this order stands applicable. During the year, the assessee has earned dividend income of Rs. 1,00,000/- and hence the disallowance is restricted to the dividend earned.

21. As a result, the appeal of the Revenue is dismissed and Ground No. 3 of the appeal of the assessee is allowed.

ITA No. 4972/Del/2015

Conversion of Investments:

22. The ratio laid down in ground No. 4 in ITA No. 4971/Del/2015 in this order stands applicable. The appeal of the assessee on this ground is dismissed.

Addition on account of Surrendered Income:

23. During the year, the Assessing Officer mad addition under the head "income from capital gains" of Rs.5,81,46,845 and disallowance u/s 14A which amounts to Rs.15,74,16,144/-. Both

the additions have been dealt in the preceding paras of this order.

24. Further, the Id. CIT(A) held that the assessee has gone back on the surrender of Rs.10 Cr. made during the post search proceedings and the same was not completely honoured. The Id. CIT(A) held that the assessee has only surrendered Rs.1,75,66,829/- being the interest on loan given to Australian AE and taxed an amount of Rs.8,24,33,171/-. While enhancing the addition, the Id. CIT(A) held as under:

"4.1.4.....that during the search proceedings the appellant had surrendered Rs.10 crore as additional income "on account of disallowance of expenses and others". Based on its surrender, the IT Authorities had stopped the investigation into the affairs. Thereafter, the appellant has gone back on its surrender. The action of the AO in rejecting books of account is being negated for the reasons that no adverse evidences could be found from the books of accounts. However, the same does not mean that the appellant's affairs are in order in all respects especially when the appellant himself had surrendered the income during search action that to towards disallowance of expenses. It is noted that the previous year relevant to the present assessment year was about to end as on the date of search (27.03.2012). The appellant best knows his true affairs. It is not the case of surrendered of undisclosed income and its immediate retraction thereafter. But the retraction has occurred after a considerable gap of time. Examination of books cannot be a proper substitute for full thronged investigation which takes place during search & post search proceedings, which was stopped due to surrender of income by the appellant. The doctrine of estoppel operates here. On the basis of appellant's surrender, the investigation was stopped. Therefore, appellant is stopped from

going back on its surrender/promise. It is noted here that the scheme of the act does recognize the act of surrender of any undisclosed income at the time of search. Such surrender is one of the significant events of in any search and post search proceedings and it greatly influences the post search investigation. By surrendering the undisclosed income the appellant stops the investigating officer from continuing with investigation on that issue on the principle that a fact accepted by the other party need not be proved. Here the surrender was "on account of disallowance of expenses and others". After a long gap, it is very easy to say that there are no discrepancies in the documents. The party has got ample time to set right the weaknesses, if any, in his affairs and also to take care of any deficiencies that could be linked to the contents of the seized papers including third party affairs. Thus any retraction from surrendered income, that too after a considerable time period, only points towards lack, of bonafide on the party of the appellant. This is also against the rule of estoppel. A person who by his statement has induced another to believe his words and act in a particular manner, cannot go back and say that what he stated was incorrect. He is estopped from doing so. Therefore, I hold that addition be restricted to Rs. 8,24,33,171 (Rs. 10 crores-1,75,66,829) and the balance addition is hereby deleted. In the subsequent grounds relating to 14A disallowance-and capital gain on sale of shares I am partly confirming the AO's action. The additional income resulting from part confirmation of those grounds would also be telescoped into the above stated Rs. 8,24,33,171/- as the same is covered by the narration of the surrendered income."

25. We find that this is an ad-hoc enhancement made by the Id. CIT(A) which is not backed up by any material found and seized during the search.

26. We have gone through the Circular of the CBDT with regard to surrender taken in the statement recorded u/s 132(4).

F. No. 286/2/2003-IT (Inv)
GOVERNMENT OF INDIA
MINISTRY OF FINANCE & COMPANY AFFAIRS
DEPARTMENT OF REVENUE
CENTRAL BOARD OF DIRECT TAXES

*Room No. 254/North Block,
New Delhi, the 10th March, 2003*

To
All Chief Commissioners of Income Tax, (Cadre Contra)
&
All Directors General of Income Tax Inv.

Sir
Subject: Confession of additional Income during the course of search & seizure and survey operation -regarding

Instances have come to the notice of the Board where assesseees have claimed that they have been forced to confess the undisclosed income during the course of the search & seizure and survey operations. Such confessions, if not based upon credible evidence, are later retracted by the concerned assesseees while filing returns of income. In these circumstances, on confessions during the course of search & seizure and survey operations do not serve any useful purpose. It is, therefore, advised that there should be focus and concentration on collection of evidence of income which leads to information on what has not been disclosed or is not likely to be disclosed before the Income Tax Departments. Similarly, while recording statement during the course of search it seizures and survey operations no attempt should be made to obtain confession as to the undisclosed income. Any action on the contrary shall be viewed adversely.

Further, in respect of pending assessment proceedings also, assessing officers should rely upon the evidences/materials gathered during the course of search/survey operations or thereafter while framing the relevant assessment orders.

*Yours faithfully,
Sd/-
Under Secretary (Inv. II)*

27. Further, the Hon'ble Supreme Court in the case of CIT Vs. Mantri Share Brokers (P.) Ltd. 96 taxmann.com 280 held that *"where except statement of Director of assessee company offering additional income during survey in his premises, there was no other material either in form of cash, bullion, jewellery or document in any other form to justify said statement, addition made of said income in hands of assessee under section 69B was to be deleted."*

28. Since, the specific query put to the revenue authorities as to the existence of any material or any credible evidence, did not elucidate any tangible indication as to the undisclosed income determined by the Id. CIT(A), keeping in view the CBDT instruction and respectfully following the judgment of the Hon'ble Apex Court, we hereby hold that the action of the Id. CIT(A) cannot be affirmed.

29. In the result, the appeal of the assessee on this ground is allowed.

30. In the result, the appeals of the assessee are partly allowed and that of the Revenue are partly allowed.

Order Pronounced in the Open Court on 25/08/2022.

Sd/-

(Yogesh Kumar US)
Judicial Member

Dated: 25/08/2022

Subodh Kumar, Sr. PS

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(Appeals)
5. DR: ITAT

Sd/-

(Dr. B. R. R. Kumar)
Accountant Member

ASSISTANT REGISTRAR