

IN THE INCOME TAX APPELLATE TRIBUNAL
Mumbai "A" Bench, Mumbai.

Before Justice (Retd.) C.V. Bhadang (President) and Shri B.R. Baskaran (AM)

I.T.A. No. 4834/Mum/2019 (A.Y. 2014-15)
I.T.A. No. 4835/Mum/2019 (A.Y. 2015-16)

Adi Lim Bilimoria, 3 rd Floor, Rakhi Mahal, Dinshaw Vatcha Road Mumbai-400 021. PAN : AADPB0971C (Appellant)	Vs.	DCIT-4(1)(1) 6 th Floor Aayakar Bhavan M.K. Road Mumbai-400 020. (Respondent)
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Assessee by	Shri Porus Kaka & Shri Manish Kanth
Department by	Shri Manoj Kumar Sinha
Date of Hearing	16.01.2024
Date of Pronouncement	15.03.2024

ORDER

Per B.R.Baskaran (AM) :-

Both the appeals filed by the assessee are directed against the orders passed by the learned CIT(A)-9, Mumbai and they relate to A.Ys. 2014-15 & 2015-16. Common issue urged in both the appeals relate to the disallowance made under section 14A of the Act in relation to exempt income earned by the assessee.

2. Both these appeals were earlier disposed of by a common ex-parte order passed on 28.11.2022. Subsequently, pursuant to the miscellaneous applications filed by the assessee, the above said common ex-parte order was recalled, vide order dated 05-09-2023 passed in MA Nos. 375 & 376/Mum/2023 filed by the assessee. Accordingly, both the appeals have come up for adjudication again.

3. We shall first take up the appeal relating to A.Y. 2014-15. The assessee is carrying on stock broking business, for which separate books of account have been maintained. The Learned AR submitted that the assessee has maintained separate accounts for his investment activity, i.e., the business activity and investment activity are distinct and separate. During the year relating to A.Y. 2014-15, the assessee earned following exempt income :-

Share of income from partnership firm	: Rs. 87,647/-
Long term capital gains	: Rs. 17,35,882/-
Dividend other exempt income	: <u>Rs. 2,72,945/-</u>
	Rs. 31,28,898/-
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The assessee did not disallow any expenditure as per requirements of section 14A of the Act. It is pertinent to note that, under section 14A of the Act, the expenditure incurred in relation to exempt income is required to be disallowed. Hence, the Assessing Officer asked the assessee the reasons for not disallowing any expenditure relatable to exempt income. The assessee submitted that

- (a) he has held investments over the last 30 to 40 years and the dividend income was earned from those investments.
- (b) investment activity is distinct and separate and is not connected with the business activity carried on by him.
- (c) no part of business income or business capital has been used to purchase the shares and hence there was no connection between the business activity and personal investment activity.

Accordingly it was submitted that no expenditure relating to investment activity was incurred and hence no disallowance of expenditure is called for.

4. The Assessing Officer was not convinced with the explanations of the assessee. He noticed that the assessee has held investment to the tune of Rs. 4.97 crores and Rs. 6.39 crores as on 31.3.2013 and 31.3.2014 respectively. Accordingly he took the view that the disallowance under section 14A of the Act is required to be made by applying the provisions of Rule 8D. Accordingly he disallowed a sum of Rs.29,77,790/- under Rule 8D

of I T Rules in AY 2014-15, which consisted of interest disallowance of Rs. 26,93,364/- u/r 8D(2)(ii) and expenditure disallowance of Rs. 2,84,426/- u/r 8D(2)(iii).

5. In the appellate proceedings, the assessee contended before Ld CIT(A) that the Assessing Officer has resorted to Rule 8D without recording his dissatisfaction over the claim made by the assessee that no expenditure was incurred in earning exempt income. Accordingly it was contended that the Assessing Officer was not justified in computing disallowance as per rule 8D of the IT Rules. In the alternative it was submitted that the disallowance cannot exceed exempt income.

6. The learned CIT(A) noted the exempt income as Rs. 28,58,953/-. With regard to the contention that the Assessing Officer has not recorded his dissatisfaction, the learned CIT(A) held that the assessee did not support his claim with any evidence and hence the Assessing Officer was justified in computing disallowance as per rule 8D. However, he accepted the alternative contention of the assessee and directed the Assessing Officer to restrict the disallowance u/s 14A of the Act to Rs. 28,55,953/- equivalent to the exempt income as noted by him.

7. The main grievance of the assessee is that the learned CIT(A) was not justified in rejecting the contention of the assessee that the Assessing Officer did not record his dissatisfaction over the claim of the assessee, before proceeding to invoke Rule 8D of I T Rules. The Learned AR submitted that, as per sec.14A(2) of the Act, the Assessing Officer would get the power to compute the disallowance under rule 8D of the I.T. Rules, only if he records his dissatisfaction over the correctness of the assessee's claim that too having regard to the accounts of the assessee. He submitted that non-recording of dissatisfaction would vitiate the addition made by the AO. In this regard, the learned AR took support of the decision rendered by Hon'ble

Bombay High Court in the case of DCIT Vs. Godrej & Boyce Mafg. Co. Ltd. (2023) 149 taxman.com 222. The Learned AR also invited our attention to the paper book to substantiate the contention of the assessee that he has maintained separate books of account for his business. He submitted that the assessee has maintained separate bank account for his investment activity. He further submitted that the Profit and Loss account is debited with the expenses exclusively related to the business activity only. Inviting our attention to the capital account of the assessee placed at page No. 8 of the paper book, the learned AR submitted that the assessee was meticulous in maintaining the accounts, i.e., whenever any business expenditure involved personal element, that portion of the expense relating to personal purposes is directly debited his Capital account without claiming it in the Profit and Loss account. Even though all these factual details were furnished before the AO, yet the Assessing Officer did not record dissatisfaction over the claim so put forth by the assessee. Accordingly he submitted that the disallowance made by the AO is liable to be deleted.

8. On the contrary, learned DR supported the order passed by the learned CIT(A).

9. We heard the rival contention and perused the record. The provisions of sec.14A read as under:-

“14A (1) For the purposes of computing the total income under this Chapter, no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to income which does not form part of the total income under this Act.

(2) The Assessing Officer shall determine the amount of expenditure incurred in relation to such income which does not form part of the total income under this Act **in accordance with such method as may be prescribed, if the Assessing Officer, having regard to the accounts of the assessee, is not satisfied** with the correctness of the claim of the assessee in respect of such expenditure in relation to income which does not form part of the total income under this Act.”

As per sec. 14A(2) of the Act, the AO is entitled to resort to the method prescribed under Rule 8D of I T Rules, only if the AO, having regard to the accounts of the assessee, is not satisfied with the correctness of claim of the assessee. Hence recording of dissatisfaction over the submissions of the assessee, that too having regard to the accounts of the assessee, is a mandatory condition. The above said legal position has been explained by Hon'ble Bombay High Court in the case of Godrej & Boyce Mfg Co Ltd (supra) as under:-

“11. In the present case, the assessee has earned an exempt income of Rs.84,30,37,423/- from shares and mutual funds and submitted a computation of inadmissible expenditure u/s 14A amounting to Rs.13,66,635/-. The assessee claimed that the disallowance made u/s 14A was as per the books of account attributable to earning of exempt income. On a perusal of the assessment order we find that there is no discussion by the AO with regard to the computation of inadmissible expenditure made by the assessee forming part of the return of income. Further, the AO has not recorded any satisfaction that the working of inadmissible expenditure u/s 14A is incorrect with regard to the books of account of the assessee. The provision u/s 14(2) (sic. 14A(2)) does not empower the AO to apply Rule 8D straightaway without considering the correctness of the assessee's claim in respect of expenditure incurred in relation to the exempt income. We agree with the view of the ITAT that in the present case the AO has neither examined the claim in respect of expenditure incurred in relation to exempt income of the assessee nor has recorded any satisfaction with regard to the correctness of assessee's claim with reference to the books of account. Consequently, the disallowance made by applying the Rule 8D is not only against the statutory mandate but contrary to the legal principles laid down....”

10. In the instant case, we noticed that the assessee has maintained separate books of account for his business activities. The exempt income has been accounted separately in another bank account and it is not mixed up with the business activities. In the books of business also, we noticed that the personal portion of various expenses viz., Entertainment expenses, Sales promotion, Motor Car, Telephone, Travelling etc have been debited to the Capital account, i.e., the same were not claimed as business expenditure. This action of the assessee proves that he was meticulous in maintaining his books of accounts. We notice that the assessee has not claimed any expenditure against exempt income. The question of making disallowance out of expenditure debited to the profit and loss account will arise, only if the

taxable income and exempt income are accounted together. This is not the case here. Hence, there is merit in the contentions of the assessee that no disallowance u/s 14A of the Act is called for, since no part of business expenditure is related to the exempt income. However, we noticed that the AO did not examine the above said explanations of the assessee with reference to the books of account and did not record his dissatisfaction over the claim of the assessee, which is a mandatory condition prescribed u/s 14A(2) of the Act. Hence the AO could not have resorted to apply the provisions of Rule 8D in the facts of the present case. We notice that the Ld CIT(A) has placed burden upon the assessee in this regard to prove the negative, while it is the duty of the AO to examine the books and record his dissatisfaction. Accordingly, following the decision rendered by Hon'ble Bombay High Court in the case of Godrej & Boyce Mfg Co Ltd (supra), we hold that the disallowance u/s 14A of the Act made by the AO by applying the provisions of Rule 8D of the Act is against the statutory mandate and is liable to be deleted. Accordingly, we set aside the order passed by Ld CIT(A) on this issue and direct the AO to delete the disallowance made u/s 14A of the Act.

11. We shall now take up the appeal filed for AY 2015-16. In this year also, the assessing officer computed disallowance u/s 14A of the Act by applying Rule 8D at Rs.22,15,530/- and Ld CIT(A) restricted the disallowance to the extent of exempt income amounting to Rs.15,70,420/-. The Ld A.R submitted that the facts prevailing in this year are identical with that prevailed in AY 2014-15. In this year also, the AO did not examine the books of account and record dissatisfaction over the claim of the assessee that the business books of account are maintained separately and the expenditure claimed therein are not related to the exempt income. Hence the AO could not have resorted to the provisions of Rule 8D of I T Rules. Accordingly, following the decision rendered by Hon'ble Bombay High Court in the case of Godrej & Boyce Mfg Co Ltd (supra), we hold that the

disallowance u/s 14A of the Act made by the AO by applying the provisions of Rule 8D of the Act in this year also is against the statutory mandate and is liable to be deleted. Accordingly, we set aside the order passed by Ld CIT(A) on this issue and direct the AO to delete the disallowance made u/s 14A of the Act.

12. In the result, both the appeals of the assessee are allowed.

Order pronounced on 15.3.2024.

Sd/-
(Justice (Rtd.) C.V. Bhadang))
President

Sd/-
(B.R. Baskaran)
Accountant Member

Mumbai.; Dated : 15/03/2024

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent
3. The CIT(A)
4. CIT
5. DR, ITAT, Mumbai.
6. Guard File.

//True Copy//

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BY ORDER,

(Assistant Registrar)
ITAT, Mumbai