

**IN THE INCOME TAX APPELLATE TRIBUNAL  
DELHI BENCH 'H' NEW DELHI**

**BEFORE SHRI R.S. SYAL, ACCOUNTANT MEMBER  
AND  
SHRI SUDHANSHU SRIVASTAVA, JUDICIAL MEMBER**

**ITA No. 4144/Del/2011  
AY: 2008-09**

**Yama Finance Ltd.,  
B-6/5, Local Shopping Centre,  
New HDFC Bank,  
Safdarjung Enclave,  
New Delhi.  
(PAN: AAACY1847Q)**

**vs Income Tax Officer,  
Coy. Circle-18(1),  
2<sup>nd</sup> Floor, C.R. Building,  
I.P. Estate,  
New Delhi.**

**(Appellant)**

**(Respondent)**

**Appellant by:** Shri Subodh Gupta, CA  
**Respondent by:** Shri Rajiv Ranka, Sr. DR

**Date of hearing: 27.01.2016**

**Date of pronouncement: 18.04.2016**

**ORDER**

**PER SUDHANSHU SRIVASTAVA, JUDICIAL MEMBER**

The present appeal is preferred by the assessee against the order passed by the Ld.CIT(A)-XXI, New Delhi wherein by the order dated 26.07.2011 the First Appellate Authority has confirmed the action of the Assessing Officer in treating an amount of Rs. 40,04,179/- as business income instead of Capital Gains (as claimed by the assessee) and also upholding the disallowance of Rs. 4,90,274/- u/s 14A of the Income Tax

Act, 1961 (hereinafter called 'the Act'). The appeal pertains to assessment year 2008-09.

2. It is seen from the records that the assessee company had filed its return of income declaring an income of Rs. 35,43,560/- which was processed u/s 143(1) of the Act and the case was later selected for scrutiny. The Assessing Officer noted that the assessee had shown gains from sale of Mutual Funds/Portfolio Management Scheme (PMS) under the head 'Income from Capital Gains'. The Assessing Officer was of the opinion that since the Memorandum of the assessee company authorized the assessee to carry on the business of sale/purchase of securities, the assessee could be said to be carrying on the business of sale/purchase of securities. The Assessing Officer relied on a plethora of case laws and concluded that even a single transaction may constitute trading income and in view of the pattern of investments and frequent transactions of sale/purchase of Mutual funds/ PMS by the assessee company, it could be concluded that the assessee was carrying on a business of sale and purchase with a motive to earn profit and, therefore, the transactions would fall under the purview of section 28 of the Act viz. Business Income and will not be taxable

under 'Capital gains' as claimed by the assessee. The Assessing Officer also relied on the decision of the ITAT Delhi Bench in assessee's own case for Assessment Year 2006-07 wherein in I.T.A. No. 312/Del/2010, the ITAT had held that the assessee's transactions in units of mutual funds were in the nature of business income and were thus chargeable under the head 'Income from Business or Profession' instead of 'Capital Gains'. The Assessing Officer held that since there was no change in the facts and circumstances of the case in the current year, the decision of the ITAT had to be followed. Accordingly, the amount of Rs. 40,04,179/- was treated as business income and after making adjustments for opening and closing stock of investments, the business income was finally calculated at Rs. 31,42,538/- which was added back to the income of the assessee. Secondly, the Assessing Officer noticed that the assessee had earned exempt income by way of dividends amounting to Rs.4,90,274/- and that the assessee had itself added back a sum of Rs. 31,544/- u/s 14A in its computation of income. The Assessing Officer, however, opined that Rule 8D also had to be followed and he accordingly disallowed a further sum of Rs. 4,58,730/- (restricting the disallowance to Rs.

4,90,274/- i.e. the dividend earned) @ 0.5% on the average investments.

3. In appeal, the Ld. CIT (A) confirmed both the disallowances/adjustments and now the assessee is in appeal before us and has raised the following grounds of appeal:-

*“1. The lower authorities have erred and were not justified on facts & circumstances of the case and in law in rejecting the results and accounting treatment of impugned transactions shown in the audited accounts as “investments” in the audited accounts, indicating unambiguously the intentions of making ‘Investments’ and thus the adverse inferences are liable to be rejected.*

*2. On facts and circumstances of the case and in law, the lower authorities have erred and were not justified in treating the net results of gain, amounting to Rs 40,04,179/-, from investments in units of mutual funds & Portfolio Management Scheme (PMS) as ‘Trading’, chargeable under the head ‘Profit & gains of Business of Profession’ as against the claim of the appellant to charge under the head ‘Capital gains’. On the facts and circumstances of the case, it is the case of the appellant that can only be construed as investment in units of mutual funds and not as ‘Business’.*

*3. On facts and circumstances of the case and in law, lower authorities have erred and were not justified in applying rule 8D in an arbitrary manner for determining the disallowance u/s 14A, without any finding the nexus between expenses incurred and dividend income earned and have failed to objectively appraise the*

*ambiguous results of Rule 8D.*

*4. On facts and circumstances and in law, lower authorities have erred and were not justified in making a disallowance of Rs 4,90,274/- as expense incurred in respect of exempt income by invoking section 14A of the Act in an arbitrary manner, which is equivalent to the whole of exempt income, being dividend.*

*5. The above grounds of appeal are independent without prejudice to each other.”*

4. The Ld. AR submitted that the authorities below have followed the decision of the ITAT for Assessment Year 2006-07 in making the adjustments for Assessment Year 2008-09 also. He further submitted that this decision of the ITAT has since been reversed by the Hon'ble Delhi High Court in I.T.A. No. 1658/2010 through the order dated 01.04.2014 which has been placed on record.

5. The Ld. AR submitted that in view of the decision of the Hon'ble Delhi High Court, this year's adjustments also deserve to be reversed as there has been no change in the factual situation as compared to that of AY 2006-07 for which the Hon'ble Delhi High Court has ruled in the favour of the assessee.

6. As regards the other issue in appeal viz. the disallowance u/s 14A of the Act, the Ld. AR submitted that the Assessing Officer has taken all the investments for the purpose of calculation of disallowance whereas the mandate of the Act requires that only those investments which have yielded exempt income ought to be considered for the purpose of calculating the disallowance. He submitted that the assessee company had already added back an amount of Rs. 31,544/- on its own, which was the correct amount of disallowance and, therefore, no further disallowance could be legally sustained.

7. The Ld. DR, in response, relied on the orders of the lower authorities. On the issue of business income vis-à-vis capital gains, the Ld. DR submitted that the Ld. CIT(A) has dealt with this issue on page 8 of the impugned order wherein he has referred to and reproduced the order of the ITAT for Assessment Year 2006-07. As regards the disallowance u/s 14A, the Ld. DR submitted that the assessee has itself not disputed the application of section 14A and hence, the disallowance has been correctly made.

8. We have heard the rival submissions and perused the material on record. As far as the issue of treating capital gains

as business income by the Department is concerned, it is seen that the issue has been settled in favour of the assessee by the Hon'ble Delhi High Court in I.T.A. No. 1658/2010 for Assessment Year 2006-07. We accordingly restore the matter to the file of the Assessing Officer for allowing assessee's claim in terms of the order of the Hon'ble Delhi High Court. The grounds of the assessee on this issue are accordingly allowed.

9. As regards the issue of disallowance u/s 14A of the Act, it is seen that the scheme of section 14A has within it implicit notion of apportionment in cases where the expenditure is incurred for the composite/indivisible activities in which taxable and non-taxable income is received. But when it is possible to determine the actual expenditure in relation to the exempt income or when no expenditure has been incurred in relation to the exempt income, then principle of apportionment embedded in section 14 A has no application. The objective of section 14 A is not allowing to reduce tax payable on the normal exempt income by debiting the expenditure incurred to earn the exempt income. Thus, the expenses incurred to earn exempt income cannot be allowed and the expenses shall be allowed only to the extent they are related to the earning of taxable income. If there is expenditure directly

or indirectly incurred in relation to exempt income, the same cannot be claimed against the income, which is taxable as it is held by the Hon'ble Supreme Court in case of Commissioner of Income-tax v. Walfort Share and Stock Brokers P. Ltd. reported in 326 ITR 1 (SC) that for attracting the provisions of section 14 A, there should be proximate cause for disallowance which as relationship with the tax exempt income. The expenditure incurred in relation to the income which does not form part of total income has to be disallowed. However, it should be the proximate relationship between the expenditure and the income, which does not form part of total income. Once such proximity relationships exist, the disallowance is to be effected. Thus, in order to disallow the expenditure under section 14A, there must be a live nexus between the expenditure incurred and the income not forming part of total income. No notional expenditure can be apportioned for the purpose of earning exempt income unless there is an actual expenditure in relation to earning the income not forming part of total income.

10. On going through the records and hearing the rival submissions, it is seen that the assessee has claimed that expenditure amounting to Rs. 31,154/- had been incurred in

relation to earning of exempt income. The Assessing Officer did not bring any evidence on record to relate the expenditure incurred with the amount of exempt income on one hand and relate the exempt income to the investments yielding exempt income on the other. He simply proceeded to calculate the disallowance under Rule 8D. In the absence of such evidence, it was patently wrong on the part of the Assessing Officer to compute disallowance u/s 14A of the Act by mechanically applying Rule 8D. The Assessing Officer has adopted the formula for estimating expenditure on the basis of investments but the justification for calculating the average investment is missing.

11. The Hon'ble Delhi High Court in the case of Maxopp Investment Ltd. vs CIT (I.T.A. 687/2009) has opined in para 29 of the order as under:-

*"29. Sub-section (2) of Section 14 A of the said Act provides the manner in which the Assessing Officer is to determine the amount of expenditure incurred in relation to income which does not form part of the total income. However, if we examine the provision carefully, we would find that the Assessing Officer is required to determine the amount of such expenditure only 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 the said Act. In other words, the*

*requirement of the Assessing Officer embarking upon a determination of the amount of expenditure incurred in relation to exempt income would be triggered only if the Assessing Officer returns a finding that he is not satisfied with the correctness of the claim of the assessee in respect of such expenditure. Therefore, the condition precedent for the Assessing Officer entering upon a determination of the amount of the expenditure incurred in relation to exempt income is that the Assessing Officer must record that he , is not satisfied with the correctness of the claim of the assessee in respect of such expenditure. Sub-section (3) is nothing but an offshoot of sub-section (2) of Section 14A. Sub-section (3) applies to cases where the assessee claims that no expenditure has been incurred in relation to income which does not form part of the total income under the said Act. In other words, sub-section (2) deals with cases where the assessee specifies a positive amount of expenditure in relation to income which does not form part of the total income under the said Act and sub-section (3) applies to cases where the assessee asserts that no expenditure had been incurred in relation to exempt income. In both cases, the Assessing Officer, if satisfied with the correctness of the claim of the assessee in respect of such expenditure or no expenditure, as the case may be, cannot embark upon a determination of the amount of expenditure in accordance with any prescribed method, as mentioned in sub-section (2) of Section 14A of the said Act. It is only if the Assessing Officer is not satisfied with the correctness of the claim of the assessee, in both cases, that the Assessing Officer gets jurisdiction to determine the amount of expenditure incurred in relation to such income which does not form part of the total income under the said Act in accordance with the prescribed method. The prescribed method being the method stipulated in Rule 8D of the said Rules. While rejecting the claim of the assessee with regard to the expenditure or no expenditure, as the case may be, in relation to exempt income, the Assessing Officer would have to indicate cogent reasons for the same.”*

12. Therefore, on an overall consideration of the facts of the case and respectfully following the ratio of the judgments as aforementioned, we hold that the disallowance u/s 14A was made without due deliberation and analysis by the Assessing Officer and the Ld. CIT (A) was also patently wrong in confirming the disallowance. We, therefore, restore the issue to the file of the Assessing Officer for calculating the quantum of disallowance afresh after considering all the aspects as envisaged in section 14A and Rule 8D after giving due opportunity to the assessee to represent its case. The grounds pertaining to the issue of disallowance u/s 14A are accordingly allowed for statistical purposes.

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

The order is pronounced in the open court on 18.4.2016.

Sd/-

**(R.S. SYAL)**  
**ACCOUNTANT MEMBER**

Sd/-

**(SUDHANSHU SRIVASTAVA )**  
**JUDICIAL MEMBER**

Dated: the 18<sup>th</sup> of April, 2016  
'GS'

Copy of the Order forwarded to:

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

By order

Asstt. Registrar