

आयकर अपीलिय अधिकरण, 'सी' खंडपीठ मुंबई
INCOME TAX APPELLATE TRIBUNAL, MUMBAI "C" BENCH

सर्वश्री महावीर सिंह न्यायिक सदस्य एवं रमित कोचर, लेखा सदस्य
Before S/Sh. Mahavir Singh, JM & Ramit Kochar, AM

आयकर अपील सं./ITA No./6448/Mum/2014,
निर्धारण वर्ष /Assessment Years: 2010-11

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| M/s. Capricon Reality Ltd. Vithaldas Chambers, 3rd Floor 16, Mumbai Samachar Marg, Fort Mumbai-400 001. PAN:AAACC 4297 J | Vs. | The DCIT-Circle -2(1) Room No.542, 5th Floor Aayakar Bhavan, M.K. Road Mumbai-400 020. |
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(अपीलार्थी /Appellant)

(प्रत्यर्थी / Respondent)

Revenue by: Shri G.N. Makwana-DR

Assessee by: Shri K. Gopal &

Ms. Neha Paranjape -AR

सुनवाई की तारीख / **Date of Hearing:** 20/04/2017

घोषणा की तारीख / **Date of Pronouncement:**17/05/2017

आयकर अधिनियम, 1961 की धारा 254(1)के अन्तर्गत आदेश
Order u/s 254(1) of the Income-tax Act, 1961(the Act)

ORDER

लेखा सदस्य, रमित कोचर के अनुसार/ Per Ramit Kochar, AM :

This appeal, filed by the assessee , being ITA No. 6448/Mum/2014, is directed against the appellate order dated 06th August 2014 passed by learned Commissioner of Income Tax (Appeals)- 4, Mumbai (hereinafter called "the CIT(A)"), for the assessment year 2010-11, the appellate proceedings before the learned CIT(A) arising from the assessment order dated 23rd March, 2013 passed by the learned Assessing Officer (hereinafter called "the AO") u/s 143(3) of the Income-tax Act,1961 (Hereinafter called "the Act").

2. The grounds of appeal raised by the assessee in the memo of appeal filed with the Income-Tax Appellate Tribunal, Mumbai (hereinafter called “the tribunal”) read as under:-

“ 1. The learned Commissioner of Income-tax(Appeals) erred in confirming the disallowance of Rs.20,27,472/- under Rule 8D(ii) on account of interest expenses. Your appellants submit that no interest bearing funds have been utilized to earn exempt income and that the said disallowance is not warranted and ought to be deleted.

Without prejudice to the above, your appellants submits that no interest expenses have been claimed by the appellants during the year since the entire interest expenses have been capitalized to the work in progress account.

Without prejudice to the above, your appellants submits that interest if any has to be considered for disallowance should be net of the interest income earned during the year and offered to tax.

2. The learned Commissioner of Income tax(Appeals) has erred in confirming disallowance of Rs.11,45,953/- on account of expenses under Rule 8D(iii) being 0.5% of the average investments. Your appellants submit that the disallowance not warranted and ought to be deleted.

Without prejudice to the above, you appellants submit that have claimed only Rs.14,08,071/- as business expenditure and have taken rest of expenditure amounting to Rs. 3,75,96,844/- to work in progress and that the disallowance if any has to be out of Rs.14,08,071/- which has been claimed by the appellants.”

3. The assessee company is engaged in the business of real estate development. During the course of assessment proceedings u/s 143(3) r.w.s. 143(2) of the 1961 Act, it was observed by the Assessing Officer (A.O.) that the assessee has claimed exemption of dividend income amounting to Rs.97,58,944/-. During the course of assessment proceedings u/s 143(3) r.w.s. 143(2) of the 1961 Act, the assessee was asked to show cause as to

why the disallowance under Section 14A of the 1961 Act read with Rule 8D of the 1962 Rules should not be made. The assessee submitted that no expenses have been incurred by it to earn the said exempted income of dividend of Rs.97,58,944/-.

The AO rejected the contention of the assessee in view of Section 14A of the 1961 Act r.w.Rule 8D of the 1962 Rules and made a disallowance of Rs.31,73,425/- u/r 8D(2)(ii) and 8D(2)(iii) of the 1962 Rules r.w.s 14A of the 1961 Act, vide assessment order dated 23-03-2013 passed by learned AO u/s 143(3) of the 1961 Act.

4.Aggrieved by the assessment order dated 23-03-2013 passed by learned AO u/s 143(3) of the 1961 Act, the assessee filed an appeal before the learned CIT(A). The assessee submitted that investments in shares and securities to the tune of Rs.45,83,81,269/- is ancillary to the main business activities of the real estate development. It was submitted that the funds were borrowed in earlier years for specific purposes but investments have been made in the current financial year. It was submitted that there were no borrowings payable as of 31-03-2010. It was also submitted that interest expenses of Rs.1,20,17,356/- and premium on redemption of debentures to the tune of Rs.1,30,66,409/- was debited to P&L account but were transferred to the work in progress. It was submitted that no interest expenditure can be disallowed as investments are made out of won funds and not borrowed funds. The assessee claimed that no expenses were claimed and hence no disallowance can be made by the assessee. Thus, it was submitted that since no expenses were incurred to earn tax free income

of Rs. 97,58,944/- , no disallowance u/s 14A of the 1961 Act is warranted. It was submitted that the AO has disallowed the expenses without giving any reasons or explanations whatsoever. The assessee claimed that it received Rs.79.30 crores against the sale of flats during the year and these business receipts were the source of making investments in the current year. It is also submitted that no interest was claimed as an expenditure by the assessee as the same was transferred to WIP being the project specific expenses . It was submitted that in any case premium on redemption of debenture shall not be considered for disallowance. It was also argued that the interest to be considered for disallowance should be net of taxable interest income. With respect to disallowance of administrative expenses of Rs.11,45,953/- is concerned , it was submitted that no expenses are incurred for earning exempt income. It was submitted that there are five investments made during the current year , out of which 3 are in mutual funds having a daily dividend plan. It was submitted that investments were made through brokers who were paid commission by these funds and nothing was paid by the assessee for making such investment. It was submitted that these dividends got re-invested itself and does not require any management . On redemption , proceeds got credited to the assessee's bank account directly. It was submitted that it does not require any management. Thus, it was contended that no expenditure were incurred for earning of exempt income. It was submitted that expenses of Rs.3,90,31,159/- was debited in Profit and Loss account and most of the expenses were transferred to work in progress account. It was submitted that the assessee is following project completion method , all project related

expenses stood debited to work in progress and hence the same cannot be disallowed. The assessee submitted list of expenses of Rs. 3,75,96,844/- as expenses which were debited to WIP. It was submitted that there are expenses of Rs.1,63,246/- which were expenses of statutory in nature such as audit fee,workers legal dues, profession tax , rent, rates and taxes which are in no manner related to the exempt income. It was also submitted that there are expenses of Rs.12,44,825/- which are day to day general expenses not related to exempt income incurred by the assessee.Hence ,it was claimed that expenses of Rs. 3,90,04,915/- (Rs. 3,75,96,844/- + Rs.1,63,246/- + Rs.12,44,825/-) under the above three heads cannot be disallowed for the purposes of Section 14A of the 1961 Act. The assessee also submitted that the AO has considered all types of investments for making disallowance u/r 8D(2)(iii) of 1962 Rules r.w.s.14A of the 1961 Act, which included investments in equity shares, mutual funds and debentures. It was submitted that investments in debentures is yielding taxable income and the expenses cannot be disallowed to that effect as it never yielded exempt income.

The learned CIT(A) rejected the contention of the assessee and observed that the assessee has invested Rs.45,83,81,269/- in shares and securities , income from which is not includible in the total income of the assessee. It was observed by learned CIT(A) that the assessee has earned dividend income of Rs.97,58,944/- which was claimed exempt u/s 10(34) of the 1961 Act. It was observed by the learned CIT(A) that assessee was unable to establish nexus between capital of assessee invested in securities and that it was not possible to believe that out of common hotch potch of funds the

entire capital would have gone into business of the assessee and none of the investment has gone into shares and securities. The learned CIT(A) also observed that it was not possible to believe that the entire capital would have been invested in shares and securities especially when the assessee itself was not sure as to how much of the sum had been invested in business of the assessee. It was also observed by the learned CIT(A) that the assessee had not given any details to work out the direct nexus of the interest expenses related to the exempt income which was not includible in the total taxable income. The learned CIT(A) observed that the assessee's case is covered by sub section (3) of section 14A of the Act, because the assessee has claimed before Assessing Officer that no expenditure was incurred by it in relation to the exempt income which did not form part of the total income of the assessee. It was also observed by the learned CIT(A) that assessee's claim was covered by sub section (2) of section 14A of the Act because the Assessing Officer was not satisfied with the correctness of the claim in respect of the expenses incurred in relation to earning of exempt income. The learned CIT(A) observed that for the purpose of disallowance u/s 14A of the 1961 Act, the reference in Rule 8D(2)(ii) is 'Value of Investment' and not the share held as investment and hence even shares held as stock in trade shall also be covered for disallowance. It was the contention of the assessee that it has re-paid all interest bearing loans and borrowings before the last date of the financial year i.e. 31.03.2010 and it was claimed that the assessee received advances from booking of Rs.79.30 crores. The said contention was rejected by the CIT(A) as it was observed by him that the assessee had raised interest bearing loans in earlier years and

investment in shares and securities were made in the current financial year. It was observed by the CIT(A) that although the assessee had repaid interest bearing loans before the end of the relevant financial year but on the dates of investment in shares and securities, of which the income was claimed exempt by the assessee, old interest bearing loans and borrowings stood payable in the books of account of the assessee. The assessee could not produce any evidence to prove that the shares and securities were acquired from interest free loans was the observations of the learned CIT(A). The contention of the assessee that it had debited an expenditure of Rs.3,75,96,844/- in its P&L account for AY 2010-11 in the form of printing and stationery. Filing fee, auditor remuneration, bank charges, employees' salary, bonus, ex-gratia, legal & professional fee retainership fees, rent, rate, taxes, postage and courier, travelling and conveyance, repairs and maintenance, motor car expenses, sundry expenses, telephone expenses, brokerage & commission, interest on loan, premium on redemption of debentures etc. to the work-in-progress were also repelled by the learned CIT(A) who confirmed the assessment order passed by the AO u/s 143(3) of the 1961 Act vide appellate order dated 06-08-2014 passed by learned CIT(A).

5.Aggrieved by the appellate order dated 06-08-2014 passed by learned CIT(A) , assessee filed an appeal before the tribunal. At the outset the Ld. Counsel for the assessee submitted that the assessee had debited amnd transferred an amount of Rs.3,75,96,844/- to work in progress out of expenses incurred by the assessee which found debited in Profit and Loss

Account and hence disallowance cannot be made as the assessee has not claimed any expenditure from the Revenue. It was argued by the Ld. Counsel for the assessee that the assessee has not claimed expenditure of Rs.3,75,96,844/- as revenue expenditure as the same got debited and transferred to work-in-progress. The Ld. Counsel for the assessee further drew our attention to the audited accounts at page-23 of the paper book filed with the tribunal which is profit and loss account and other schedules and said no disallowance can be made on account of interest and hence the order of the Assessing Officer is erroneous. It was submitted that the assessee has not raised fresh loans during the year and the loans were raised in earlier years which were repaid by the assessee during the year under consideration. Our attention was drawn to balance sheet of the assessee which is placed at page-22 of the paper book filed with the tribunal. It was submitted that the assessee has mainly raised funds as advance for booking of flats to the tune of Rs. 79.30 crores which were invested in shares and securities, which are capable of yielding tax free income. It is also submitted that premium on redemption of debentures debited to P & L A/c cannot be disallowed under section 14A as proceeds of debentures were not utilized for making investment in securities which are capable of yielding tax free income as these debentures were issued in earlier years while the investments were made in the current year and these debentures were redeemed during the year. The Ld. Departmental Representative on the other hand relied upon the orders of the learned CIT(A).

6. We have carefully considered rival submissions and perused the material available on record before us. We have observed that the assessee is engaged in the business of real estate development. The assessee has earned dividend of Rs.97,58,944/- which was claimed as exempt from tax u/s 10(34) of the 1961 Act. The assessee claimed that no expenditure was incurred in connection with the earning of the said exempt income and hence no disallowance of expenditure can be made by the AO. The AO invoked Rule 8D(2)(ii) and 8D(2)(iii) of the 1961 Act to make disallowance of Rs.31,73,425/- u/s 14A of the 1961 Act. We have observed that the assessee has made investment of Rs.45,83,81,269/- in shares and securities during the year. The details of the said investment found mentioned in assessment order / page 5 which consisted of investments in shares, debentures and mutual funds. We are agreeable with the proposition of the assessee that investments in Debentures cannot be considered as part of 'Investments' for computing disallowance of expenditure u/s 14A of the 1961 Act as interest income earned from the debentures is taxable under the provisions of the 1961 Act and no exempt income arises from debentures and hence Section 14A of the 1961 Act cannot be invoked. We have observed from the balance sheet of the assessee that the assessee has aggregate own funds in the form of share capital/reserves to the tune of Rs.1.62 cores and also application money received to the tune of Rs.79.30 crores as at 31-03-2010 . The assessee has explained said application money received to be interest-free advances from booking of the flats which the assessee claimed to have invested in shares and securities . The investments were made during the relevant previous

year which were to the tune of Rs. 45.83 crores as at 31-03-2010. The assessee had claimed that advances for booking of flat being application money received to the tune of Rs. 79.30 crores was interest-free which was invested in shares and securities. This claim of the assessee that these advances of Rs. 79.30 crores was an interest free advances from booking of flats which got invested in shares and securities capable of yielding exempt income, needs verification for which we are inclined to set aside and restore the matter back to the file of the Assessing Officer for de-novo determination of the AO. The claim of the assessee that opening interest bearing loans which were in the form of debentures to the tune of Rs. 9.31 crores which were repaid during the year was not invested in shares and securities and hence no disallowance of interest / premium on redemption of debenture can be made u/s 14A of the 1961 shall also be verified by the AO in de-novo proceeding. The Assessing Officer had also made disallowance for administrative expenses under rule 8D(2)(iii) of Income tax Rules 1962 r.w.s. 14A of the 1961 Act being 0.5% of the investments. As held by us in this order earlier, that investments in debentures made by the assessee which give rise to taxable interest shall not be considered as part of 'Investment' for making disallowance u/s 14A of the 1961 Act, which shall be considered by the AO before making disallowance. It is also observed that the assessee is claiming that the other expenses debited to P&L account are in the nature of administrative expenses and the assessee has claimed that same is debited to the work-in-progress account for which necessary details were submitted and hence claim is made that no disallowance should be made u/s 14A of the 1961 Act. We are afraid that the contention of the assessee cannot be

accepted. We have observed from the financial accounts at paper book page-31 wherein method of valuation of inventory is specified to be that the inventory is to be valued at costs or at net realizable value whichever is lower and it also includes directly attributable development expenses and interest cost incurred(net of credits, if any thereon) by the company. The AS-2 issued by ICAI governs the valuation of inventory which is mandatory and which stipulates that inventory is to be valued at cost or net realizable value which ever is lower. Even if we considered that these administrative expenses of Rs. 3.76 crores are directly attributable development expenses to bring inventory to present status which are properly and legitimately debited to work in progress in compliance with AS-2 issued by ICAI, but still the disallowance u/s 14A of the 1961 Act is required to be made . The reason is simple and quite obvious, once the assessee has debited these expenses of Rs. 3.76 crores to the profit and loss account directly attributable development expenses to bring inventory to present status, the assessee has lodged its claim for allowability of these expenses before the Revenue and once these expenses are debited and transferred to work in progress, the same are to be added to work in progress on the credit side of profit and loss account which will enhance work in progress valuation which once allowed by the Revenue in the year of incurring of these expenses will entitles assessee to carried forward the enhance value of work in progress to the subsequent year as part of current assets as closing work in progress and in the immediately succeeding year , it will again enter on the debit side of Profit and Loss account as opening work in progress which will get offset by sale of the stock/inventory or shall be further carried forward as

stock/inventory to the succeeding year if the same is not sold. Thus , these costs are definitely got debited to profit and loss account and disallowance is to be made u/s 14A of the 1961 Act as the claim of work in progress/inventory at the value which is inclusive of these costs are allowed by the AO in the impugned assessment year for rollover to the next year. Thus , this contentions of the assessee cannot be accepted that merely because it got added to closing work in progress , it has neutralized the expenses account on the debit side of Profit and Loss account . We have observed from the perusal of the audited financial statement of the assessee that the “investments” of Rs. 45.83 crores are held as ‘investment’ and not as ‘stock in trade’ and hence the issue of applicability of section 14A of the Act to ‘stock in trade’ do not need require adjudication by us. As per section 14A of the Act where any expenditure is incurred by the assessee in relation to the income which is not includible in total income of the assessee , such expenses shall not be allowed as expenditure. Thus, disallowance of such expenditure incurred in relation to earning of income which does not form part of total income under provisions of this Act shall be computed having regard to accounts of the assessee as provided in section 14A(2) of the Act. Hon'ble Supreme Court in a very recent decision pronounced on 8th May, 2017 in the case of Godrej & Boyce v. DCIT (Civil appeal No.7020 of 2011) wherein the Hon'ble Supreme Court has upheld the disallowance of expenditure incurred in relation to earning of income which is not includible in the total income as is contemplated u/s 14A of the 1961 Act. The primary onus is on the assessee to work out the disallowance of expenditure incurred in relation to earning of the income which is not forming part of

total income of the assessee having regards to the accounts of the assessee. These are facts which are especially in the knowledge of the assessee and primary onus/burden is on the assessee to bring those facts before the AO of having incurred expenditure in relation to earning of income which does not form part of the total income having regards to the accounts of the assessee. Thereafter, the onus shifts to the Assessing Officer to work out the disallowance of expenditure incurred in relation to earning of income which does not form part of total income, having regards to the accounts of the assessee as is contemplated u/s 14A(2) of the 1961 Act . If the Assessing Officer is not satisfied with the correctness of the disallowance of expenditure suo motu offered by the assessee being incurred in relation to earning of income which does not form part of the total income having regards to the accounts of the assessee if the same could not be worked out from the manner in which accounts are made by the assessee, the Assessing Officer can invoke Rule 8D of the 1962 Rules r.w.s. 14A of the 1961 Act and apply method prescribed u/r 8D of the 1962 Rules for making disallowance of expenditure incurred in relation to earning of income which does not form part of the total income. Keeping in view facts and circumstances of the case, in our considered view the matter needs to be set aside and restored to the file of AO for re-computing the disallowance u/s. 14A of the 1961 Act of the expenditure incurred in relation to the earning of income which does not form part of the total income having regards to the accounts of the assessee in accordance with our above directions . The assessee is directed to produce working of disallowance of expenditure incurred in relation to the earning of income which does not form part of the total income having

regards to the accounts of assessee as is contemplated u/s 14A of the 1961 Act. The primary onus/burden is on the assessee to produce such working as the said facts are especially in the knowledge of the assessee. If the AO is not satisfied with the working as is submitted by the assessee as such disallowance cannot be worked out keeping in view accounts of the assessee, the AO will be justified in invoking Rule 8D of the 1962 Rules. Needless to say, proper and adequate opportunity of hearing should be granted by the AO to the assessee in accordance with principles of natural justice. The Assessing Officer is directed to admit necessary evidences and explanation filed by the assessee in its defense which shall be admitted and adjudicated on merits. We order accordingly.

7. In the result, appeal filed by the assessee is partly allowed for statistical purposes.

Order pronounced in the open court on 17th May, 2017.

आदेश की घोषणा खुले न्यायालय में दिनांक 17 मई, 2017 को की गई।

Sd/-

(महावीर सिंह / **Mahavir Singh**)

न्यायिक सदस्य / JUDICIAL MEMBER

मुंबई/Mumbai, दिनांक/Date: 17/05/2017.

व.नि.स. Jv. Sr. PS.

Sd/-

(**Ramit Kochar**)

लेखा सदस्य / ACCOUNTANT MEMBER

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

1. Appellant /अपीलार्थी

2. Respondent /प्रत्यर्थी

3. The concerned CIT(A)/संबद्ध अपीलीय आयकर आयुक्त, 4. The concerned CIT /संबद्ध आयकर आयुक्त;

5. DR A Bench, ITAT, Mumbai /विभागीय प्रतिनिधि, खंडपीठ, आ.अ.न्याया.मुंबई 6. Guard File/गार्ड फाईल

सत्यापित प्रति //True Copy//

आदेशानुसार/ **BY ORDER,**

सहायक पंजीकार **Dy./Asst. Registrar**

आयकर अपीलीय अधिकरण, मुंबई /ITAT, Mumbai.