

IN THE INCOME TAX APPELLATE TRIBUNAL, MUMBAI BENCH "E", MUMBAI
BEFORE SHRI SANJAY ARORA, ACCOUNTANT MEMBER AND
SHRI PAWAN SINGH, JUDICIAL MEMBER

ITA No.7437/Mum/2013 for Assessment Year: 2010-11

M/s SNK Investment Pvt. Ltd. 157, Maker Chambers III, Nariman Point, Mumbai-400021. PAN: AAEC8123R	Vs.	ITO 3(3)(3), Room No. 672, 4 th Floor, Aayakar Bhavan, M. K. Road, Mumbai-400020.
(Appellant)		(Respondent)

Assessee by : Shri Sanjay R. Parikh (AR)

Revenue by : Shri Vachaspati Tripathi
(DR)

Date of hearing : 02.06.2016

Date of Order : 26.08.2016

ORDER

PER PAWAN SINGH, JM:

1. The present appeal filed by the assessee against the order of CIT(A)-7, Mumbai, dated 11.09.2013 for Assessment Year (AY) 2010-11. The assessee has raised only one ground of appeal about the additional disallowance of Rs. 10,98,239/- u/s 14A of the Act.
2. Brief facts of the case are that the assessee, who is Non-Banking Financial Company, filed its return of income for AY 2010-11. While framing assessment, the AO observed that assessee has shown dividend income of Rs. 94,71,209/- which is claimed as exempt income. The assessee voluntarily disallowed Rs. 7,87,821/- u/s 14A. During the assessment, the AO asked the

assessee to furnish the details of the disallowance amounting to Rs. 7,87,821/-. The assessee submitted its reply dated 29.10.2012. The reply of assessee extracted by AO in its order which is as under:

“1. Assessee has disallowed and amount of Rs. 7,87,821/- u/s 14A in the return of income Working of the same was already submitted to you.

2. Disallowance u/s 14A offered by assessee is reasonable and based on sound accounting, costing and Taxation principle. The same can be seen from the following calculation:-

(i) During the year assessee has earned dividend income of Rs. 94,71,209/-. The total of the assessee as per Profit & Loss account is Rs. 1,02,64,225/-. Accordingly ratio of dividend income to total income is 92.27%. Hence, assessee has disallowed 92.27% out of the other expenses of Rs. 52,108/- working as under:

DISALLOWANCE U/S 14A

Total Expenses		14,21,018/-
Less: Depreciation	12,746/-	
Interest	<u>13,56,164/-</u>	<u>52,108/-</u>
Disallowance @ 92.30% on 52,108/-		48,096/-
Interest		<u>7,39,725/-</u>
		<u>7,87,821/-</u>

(iii) Balance interest expenses of Rs. 6,16,439/- incurred in respect of interest income of Rs. 7,92,416/- and hence cannot be considered for disallowance u/s 14A.

(ii) Assessee has disallowed Rs. 7,39,725/- out of total interest expenses of Rs. 13,56,164/- being interest paid on borrowed funds used for the purpose of investment working as under:

Interest paid on loan utilized for investments

Loan from Mrs. Arun N. Kampani & 10%

Period for which loan amount Utilized for investments-income of which is exempt	Amount	Amount
From 29-05-2009 to 02-06-2009	15,00,00,000	2,05,479
From 19-06-2009 to 01-07-2009	15,00,00,000	<u>5,34,247</u>
		<u>7,39,726</u>

Interest paid on loan utilized for giving loans to JM financial Services

From 03-06-2009 to 18-06-2009

15,00,00,000

6,16,438

6,16,438

Interest Earned on loan taken utilized for giving loan to JM Financial Services @ 12%.

From 03-06-2009 to 18-06-2009 *15,00,00,000*

7,89,041

7,89,041 ”

The working given by assessee was not accepted by the AO, and AO worked out the disallowance u/s. 14A r.w. Rule 8D of Rs. 17,21,233/- on the basis of .5% of average value of investments. Aggrieved by the order of AO, the assessee filed an appeal before the CIT(A) but without any success. Thus, the present appeal is filed before us.

3. We have heard the Authorised Representative (AR) of the assessee and Departmental Representative (DR) for Revenue and perused the material available on record. AR of the assessee has argued that the assessee has earned exempt income of Rs. 94,71,209/-. The assessee voluntarily disallowed a sum of Rs. 7,87,821/- u/s. 14A of the Act which consist of direct interest expenditure and the other expenses on *pro-rata* basis as per the details made available to the AO during the assessment proceeding. AR further argued that AO has not rejected the books of account nor recorded its dissatisfaction. Ld. AR further submitted that the calculation of voluntary disallowance made by assessee was annexed with the written reply submitted to the AO. Ld. AR of the assessee argued that the additional disallowance made by AO and confirmed by CIT(A) be deleted. Ld. Ld. AR of the assessee further relied upon the decision of ITAT, Delhi in the case of M/s Gillette Group India Pvt. Ltd. vs. DCIT (ITA No.267/Del/2012), Decision of Mumbai Tribunal in AFL P. Ltd. Vs. ACIT (ITA No. 3123/Mum/2011) and decision of Pune Tribunal in ACIT vs. Magarpatta Township Development and Construction Co. Ltd. (2014) taxman.com 284 (Pune-Trib). Ld. DR strongly supported the order of authorities below.

4. We have considered the rival contentions of the parties and perused the material available on record. In Gillette Group India Pvt. Ltd.(supra) the ITAT, Delhi while considering the identical grounds held as under:

“6. From the above, it is evident that as per sub-section (1) of Section 14A, no deduction is to be allowed in respect of expenditure incurred by the assessee in relation to income which does not form part of total income. Sub-section (2) of Section 14A provides the procedure for determination of such expenditure by the Assessing Officer. The Board has also prescribed Rule 8D for determining the expenditure incurred by the assessee for earning of exempt income. Thus, the disallowance can be made under sub-section (1) for the expenditure incurred for earning of exempt income. In the case under appeal before us, from the perusal of the assessee’s profit & loss account, it is evident that the total expenditure incurred was Rs.49,04,028/- only. Thus, the assessee claimed the deduction for the expenditure of Rs.49,04,028/- which is debited to the profit & loss account. The disallowance cannot exceed the expenditure actually claimed by the assessee. We, therefore, accept the assessee’s contention that the disallowance made by the Assessing Officer and sustained by the learned CIT(A) in excess of total expenditure debited to profit & loss account was unjustified. Accordingly, we restrict the disallowance to the extent of expenditure actually claimed by the assessee i.e. Rs. 49,04,028/-.”

Further, Mumbai Tribunal in AFL Pvt. Ltd. the Co-ordinate Bench of this Tribunal held as under:

“In our clear view, therefore, the initial onus to state its case qua the claimed disallowance under section 14A is on the assessee, which is to be made with reference to its accounts and/or other records, with the Assessing Officer obliged to allow the assessee an opportunity to prove the same. Then the Assessing Officer is to examine the same with a view to satisfy himself as to its correctness, stating the reasons for his objective satisfaction, or not so, as the case may be, and proceed accordingly. In the instant case, the said initial onus having been clearly not discharged by the assessee, which finding has been endorsed by us, the disallowance cannot be impugned for want of non-compliance of the procedure laid down under section 14A(2). Again, however, as we observe, none of the parties or their representatives have even as much as cared to look at the facts, which prima facie reflect an apparent case of bank borrowings having been availed for and utilised for specified purposes, so that the interest there on could not be subject to apportionment on the basis of general pool of funds hypothesis, which would otherwise prevail. We can only express our anguish at this clear disregard for facts, which are of prime relevance

in deciding any case; on the contrary, raising a host of irrelevant legal issues before us. The matter must, therefore, travel back to the file of the Assessing Officer to allow the assessee an opportunity to state its case in the matter, who shall decide the same in accordance with the law, issuing definite findings of fact. The relevant grounds are decided accordingly.”

In ACIT vs. Magarpatta Township Development and Construction Co. Ltd. (supra) the Co-ordinate Bench of Pune Tribunal while dealing with the almost identical ground held as under:

“7. We have carefully considered the rival submissions. In so far as the provisions of section 14A of the Act is concerned, it contemplates that for the purposes of computing total income no deduction is to be allowed in respect of any expenditure incurred in relation to an income which does not form part of the total income under the Act. In the present case, assessee was found to have earned exempt income by way of dividend on investments made in the mutual funds. The existence of such exempt income prompted the Assessing Officer to invoke section 14A of the Act while computing the total income of the assessee. Further, the Assessing Officer invoked rule 8D of the Rules to compute the disallowance. Ostensibly, sub-section (2) of section 14A of the Act enables the Assessing Officer to invoke rule 8D of the Rules so as to determine e amount of expenditure incurred in relation to an income which does not form part of the total income. However, the phraseology of sub-section (2) of section 14A of the Act itself brings out that the power of the Assessing Officer to invoke rule 8D of the Rules is subject to the condition that the Assessing Officer, having regard to the accounts of the assessee, is not satisfied with the correctness of the claim of assessee in respect of expenditure incurred in relation to the income which does not form part of the to income i.e. exempt income. It is no longer res-integra that invoking of rule 8D of the Rules in order to compute the disallowance u/s 14A of the Act is neither automatic and nor is dependent merely on the existence of an exempt income in the hands of the assessee. In support of the aforesaid proposition, a gainful reference can be made to the judgement of the Hon'ble Bombay High Court in the case of Godrej & Boyce Mfg. Co. Ltd. (supra) as well as the judgement of the Hon'ble Delhi High Court in the case of Maxopp Investment Ltd. v. CIT [2011] 15 taxmann.com 390/203 Taxman 364. The Pune Bench of the Tribunal in the case of Kalyani Steels Ltd. (supra) has also considered the aforesaid judgements and concluded that section 14A(2) of the Act envisages a condition precedent for invoking rule 8D of the Rules and computing disallowance; and, such condition being that the Assessing Officer records that he is not satisfied with the correctness of the

claim of the assessee in respect of expenditure incurred in relation to income which does not form part of the total income under the Act, having regard to the accounts of the assessee. Notably, the aforesaid precedents also bring out that the satisfaction which is mandated in terms of section 14A(2) of the Act must be based on reasons and on relevant consideration. In other words, the invoking of rule 8D of the Rules in order to compute the disallowance u/s 14A of the Act is to be understood as being conditional on recording of an objective satisfaction by the Assessing Officer with regard to the incorrectness of the claim of the assessee in respect of expenditure in relation to the exempt income, having regard to the accounts of the assessee. In our considered opinion, the aforesaid parity of reasoning in relation to invoking of rule 8D of the Rules read with section 14A of the Act applies to the fact of the present case.

8. In the background of the aforesaid discussion, we may now examine the facts of the present case. As noted earlier, assessee has earned dividend income of Rs. 2,75,483/- on investment in mutual funds. In the course of proceedings before the lower authorities, apart from other assertions, assessee claimed that no expenditure was incurred in relation to earning of such income. Firstly, it was pointed out that the dividend on mutual funds was earned on investment made for about two months only i.e. January and February, 2009 (as found from extract of assessee's submissions to the CIT(A) reproduced in para 3.1 of his impugned order). On the said basis, the case setup by the assessee is that the funds were parked in mutual fund by the bank for a temporary period; and, that it had more than enough non-interest bearing funds by way of share capital and accumulated profits to cover the impugned investment. Thus, no interest was incurred in relation to the investment in mutual funds, which yielded the impugned income. Secondly, it was pointed out that the dividend was credited to the bank account directly by the bank i.e. HDFC and it has also been asserted that the investment in the mutual funds were also made by the same bank. It was therefore contended that there was no direct or indirect expenditure incurred in relation to earning of the impugned exempt income.

9. In para 4.2 of the impugned order, the CIT(A) notes that the Assessing Officer has not examined the availability of interest-free funds and the investments made by the assessee in the mutual funds during the year. The CIT(A) further notes that the Assessing Officer considered interest expenditure of Rs. 3,00,19,761/- as expenditure not directly attributable to any particular income or receipt and subjected the same to disallowance as per clause (ii) of sub-rule (2) of rule 8D of the Rules. As per the CIT(A), the manner and the working for considering Rs.3,00,19,761/- for the purposes of clause (ii) of sub-rule (2) of rule 8D of the Rules has not been recorded by the Assessing Officer in his order. The CIT(A) further records that the Assessing

Officer has not examined the accounts of the assessee so as to arrive at a satisfaction and finding regarding incurrence of direct or indirect expenses in connection with earning of the exempt income as required by sub-section (2) of section 14A of the Act. The CIT(A) also observed that assessee has made the investment from own funds and therefore question of any expense on account of interest for earning of impugned exempt income, "in the given set of facts and circumstances of the case, does not arise."

10. Pertinently, we find no such reasons to distract from the aforesaid findings of the CIT(A) which are clearly borne out by the material on record. In-fact, discussion in the assessment order, which has been referred to by the learned CIT-DR before us does not show as to how the categorical assertions of the CIT(A) are wrong. Though, the Assessing Officer does say that he is "not satisfied with the correctness of the claim 0 expenditure made by the assessee" so however, the same is merely a bald assertion, devoid of any objective analysis of the accounts maintained by the assessee, a mandatory requirement of sub-section (2) of section 14A of the Act. Therefore, in the absence of adherence to the requirements of section 14A(2) of the Act, the Assessing Officer could not have proceeded to invoke rule 8D of the Rules and subject the impugned interest expenditure for disallowance as per clause (ii) of rule 8D of the Rules. Similarly, the CIT(A) records another finding which is to the effect that the dividend receipt has been directly credited into the bank account of the assessee, thus "leaving no scope for incurring any other expenses for earning exempt income" by the assessee. For the said reason, the indirect expenditure sought to be disallowed by invoking clause (iii) to sub-rule (2) of rule 8D of the Rules has also been faulted by the CIT(A). On this aspect, we are in agreement with the CIT(A) that under the given facts and circumstances of the case, the Assessing Officer was not justified in invoking rule 8D of the Rules in order to compute the disallowance U/S 14A(1) of the Act. In view of the aforesaid discussion, we hereby affirm the action of the CIT(A) in deleting the disallowance of Rs.20,66,011/- made by the Assessing Officer invoking section 14A of the Act. Thus, on this aspect, Revenue fails and accordingly the Grounds of Appeal No.1 to 3 are dismissed."

5. Now coming to the facts of the present case. The suo motu disallowance by the assessee company, comprises in the main, interest expenditure (i.e. Rs 7.40 lacs), in respect of which no infirmity has been pointed out by the Revenue despite the assessee furnishing complete details in its respect, i.e., the relevant borrowing and the interest suffered thereon. Similarly for the balance expenditure of Rs.52,108/-, which has been disallowed in the main,

i.e., at Rs.48,096/-. The Revenue has proceeded in matter arbitrarily, and which is precisely the check provided by Sec 14A(2), which is to be satisfied if Rule 8D is to be invoked. We accordingly find no reason to sustain the impugned disallowance. With the above observation, the appeal of assessee is allowed.

6. In the result, the appeal filed by the assessee is allowed.

Order pronounced in the open court on this 26th August, 2016.

Sd/-

(SANJAY ARORA)

ACCOUNTANT MEMBER

मुंबई Mumbai; दिनांक Dated /08/2016

S.K.PS

Sd/-

(PAWAN SINGH)

JUDICIAL MEMBER

आदेशकीप्रतिलिपिअद्येपित/Copy of the Order forwarded to :

1. अपीलार्थी/ The Appellant
2. प्रत्यर्थी/ The Respondent.
3. आयकरआयुक्त(अपील) / The CIT(A), Mumbai.
4. आयकरआयुक्त/ CIT
5. विभागीयप्रतिनिधि, आयकरअपीलीयअधिकरण, मुंबई/ DR, ITAT, Mumbai
6. गार्डफाईल / Guard file.

आदेशानुसार/BY
ORDER,

उप/सहायकपंजीकार
(Asstt.Registrar)
आयकरअपीलीयअधिकरण, मुंबई / ITAT, Mumbai