

**IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "G", MUMBAI**

**BEFORE SHRI G.S. PANNU, ACCOUNTANT MEMBER AND
SHRI RAM LAL NEGI, JUDICIAL MEMBER**

ITA NO. 4913/MUM/2016 : A.Y : 2012-13

M/s. Elkay Chemical Pvt. Ltd.,
4, Vinay Kunj, Shivaji Park,
Dadar (W), Mumbai 400 028
PAN : AAACE5989K (Appellant)

Vs. ITO-6(2)(3),
Mumbai (Respondent)

**Assessee by : Shri Subhash Shetty
Revenue by : Ms. Anupama Singla**

Date of Hearing : 28/02/2017

Date of Pronouncement : 28/02/2017

ORDER

PER G.S.PANNU, A.M :

The captioned appeal by the assessee is directed against the order of CIT(A)-12, Mumbai dated 06.05.2016, pertaining to the Assessment Year 2012-13, which in turn has arisen from the order passed by the Assessing Officer, Mumbai dated 23.02.2015 under section 143(3) of the Income Tax Act, 1961 (in short 'the Act').

2. The solitary issue in this appeal relates to disallowance sustained by CIT(A) u/s 14A of the Act. Although in the Grounds of appeal the challenge is to the disallowance of Rs.23,10,773/- made by the Assessing Officer, however, at the time of hearing the learned representative for the assessee has confined his arguments with

respect to the disallowance of Rs.21,61,652/-, which has been computed by the Assessing Officer by applying Rule 8D(2)(ii) of the Income Tax Rules, 1962 (in short 'the Rules') on account of interest expenditure. In this background, the relevant facts are that the appellant is a company incorporated under the provisions of the Companies Act, 1956 which is, *inter-alia*, engaged in the business of manufacture of silicone chemicals. The assessee-company was in receipt of an income of Rs.74,39,965/- as share of profits from partnership firm, which was claimed as exempt. The Assessing Officer noted that assessee had claimed expenditure by way of interest and, therefore, he computed the disallowance u/s 14A of the Act by applying Rule 8D(2)(ii) of the Rules and accordingly, disallowed the interest expenditure of Rs.21,61,652/- as interest expenditure incurred in relation to earning of exempt income. The said action of Assessing Officer has since been affirmed by the CIT(A) and accordingly, assessee is in appeal before us.

3. Before us, the learned representative for the assessee pointed out that the Assessing Officer has mechanically applied the computation formula contained in Rule 8D of the Rules without establishing that there was any interest expenditure which could be attributable to the earning of exempt income. It is pointed out that no nexus has been established between the interest expenditure and earning of the exempt income; and, that so far as the year under consideration is concerned, no fresh investments towards capital of the partnership firm has been made and rather, assessee has made a withdrawal of Rs. 25 lacs. In support of the proposition that application

of Rule 8D of the Rules is not automatic, reliance has been placed on the judgment of the Hon'ble Delhi High Court in the case of *Om Prakash Khaitan, 376 ITR 390 (Delhi)* as well as the decision of Mumbai Bench of Tribunal in the case of *Graviss Hospitality Ltd., 53 taxmann.com 63 (Mumbai-Trib.)*. The learned representative also pointed out that the Balance-sheet of assessee-company would show that it has enough own non-interest bearing funds to cover the impugned investments in the partnership firm and, therefore, no interest can be attributable to such investments following the ratio of judgment of Hon'ble Bombay High Court in the case of *Reliance Utility, 313 ITR 340 (Bom)*.

4. On the other hand, the Id. DR appearing for the Revenue has defended the orders of the authorities below and pointed out that post Assessment Year 2008-09, the application of Rule 8D of the Rules to compute the disallowance u/s 14A of the Act cannot be disputed. Accordingly, she has justified the application of Rule 8D of the Rules in order to compute the disallowance out of interest expenditure for the purpose of Sec. 14A of the Act. With respect to the reliance placed by the learned representative on the judgment of Hon'ble Delhi High Court in the case of *Om Prakash Khaitan, 376 ITR 390 (Delhi) (supra)*, it was pointed out that the said decision deals with a situation where no disallowance was made by the assessee whereas in the present case, there was a *suo moto* disallowance made by the assessee with respect to Sec. 14A of the Act.

5. We have carefully considered the rival submissions. As noted earlier, the short point in the present appeal is with respect to

disallowance u/s 14A of the Act on account of interest expenditure. Sec. 14A of the Act prescribes that no deduction shall be allowed in respect of expenditure incurred by assessee in relation to an income which does not form part of the total income under the Act. For the purposes of disallowance of interest expenditure, the Assessing Officer has applied Rule 8D(2)(ii) of the Rules. The action of Assessing Officer is sought to be resisted by the assessee not only on facts, but also in law. As per the assessee, it's capital in the partnership firm stood at Rs.5,21,19,879/- as on 31.3.2012, which comprised of capital introduction of Rs.1,34,28,000/- during the past years from financial year 2002-03 to 2010-11 and accumulation of share of profits of Rs.4,36,41,879/- from financial year 2002-03 till the year ending 31.3.2012. It is also pointed out that during the year under consideration, no capital has been introduced in the partnership firm and rather, assessee has withdrawn an amount of Rs.25 lacs. Before the lower authorities as well as before us, the assessee asserted that the funds borrowed from banks and others have been utilised in the manufacturing business and no part of the loan has been used for making investments in the capital of the partnership firm. In support of such proposition, assessee has also referred to the Balance-sheet as on 31.3.2012 to show the level of Share Capital and Reserves & Surplus vis-a-vis investments in the partnership firm to show that there was enough own funds. Be that as it may, what is abundantly clear from the order of the authorities below is that the aforesaid assertions of assessee have not been negated by the Assessing Officer in any manner, which is a requirement of Sec. 14A(2) of the Act. Quite clearly, Sec. 14A(2) of the Act permits the Assessing Officer to quantify the amount

disallowable u/s 14A of the Act, but lays down a caveat that the Assessing Officer is required to record his satisfaction with regard to the correctness of the claim of assessee in respect of the expenditure in relation to the exempt income. In an identical situation, the Mumbai Bench of the Tribunal in the case of *Graviss Hospitality Ltd.*, 53 *taxmann.com* 63 (Mumbai-Trib.) (*supra*) observed that Rule 8D of the Rules cannot be straightaway applied to compute the disallowance u/s 14A of the Act without complying with the requirement of Sec. 14A(2) of the Act. In the present case, the discussion made by the Assessing Officer does not reflect any satisfaction as to why he disagrees with the claim of assessee that no interest expenditure is relatable to the earning of exempt income and, therefore, in the absence of adherence to the pre-condition contained in Sec.14A(2) of the Act, the disallowance computed by the Assessing Officer by applying Rule 8D(2)(ii) of the Rules is not sustainable. Accordingly, we set-aside the order of CIT(A) and direct the Assessing Officer to delete the addition of Rs.21,61,652/- made u/s 14A of the Act.

6. In the result, appeal of the assessee is partly allowed, as above.

The above decision was pronounced in the open court in the presence of both the parties at the conclusion of hearing on 28th February, 2017.

Sd/-

(RAM LAL NEGI)
JUDICIAL MEMBER

Mumbai, Date : 28th February, 2017

Sd/-

(G.S. PANNU)
ACCOUNTANT MEMBER

Copy to :

- 1) The Appellant
- 2) The Respondent
- 3) The CIT(A) concerned
- 4) The CIT concerned
- 5) The D.R, "G" Bench, Mumbai
- 6) Guard file

By Order

Dy./Asstt. Registrar
I.T.A.T, Mumbai