

**IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH "E" NEW DELHI**

BEFORE SHRI A.D. JAIN, JUDICIAL MEMBER
AND
SHRI SHAMIM YAHYA, ACCOUNTANT MEMBER

I.T.A. No. 4046/Del/2009

A.Y. : 2006-07

Minda Investments Ltd.,
B-64/1, Wazirpur Industrial Area,
Delhi – 110 052

(PAN: AAACL 1433F)

vs. DCIT, Circle 6(1),

New Delhi

(Appellant) (Respondent)

Assessee by : SH. PRADEEP DINODIA AND SH.

R.K. KAPOOR, FCAs

Department by : S h. N.K. Chand, Sr. D.R.

ORDER

PER SHAMIM YAHYA: AM

This appeal by the assessee is directed against the order of the Ld. Commissioner of Income Tax (Appeals) dated 16.7.2009 pertaining to assessment year 2006-07.

2. The issue raised reads as under:- Sub-section (2) and (3) if Section 14A of the Act which has been inserted w.e.f. 1.4.2007 by Finance Act, 2006 is applicable from assessment year 2007-08 onward and not applicable in assessment year 2006-07 under appeal, as such the Ld. Commissioner of Income Tax (Appeals) has erred in directing the Assessing Officer to re-work the amount of disallowance under section 14A of the Act read with Rule 8-D of the Income Tax Rules.

3. In this case the Assessing Officer observed that assessee has earned exempt income in the form of dividend of ` 70,33,453/- u/s 10(33) of the IT Act. Assessing Officer referred to the provision of section 14A which reads as follows:-

“14A. Expenditure incurred in relation to income not includible in total income. – For the purpose 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.”

Hence, Assessing Officer found that expenses incurred to earn this exempt income are to be disallowed. He observed that the contention of the assessee that Assessing Officer has to establish the direct nexus between exempt income and expenses in such case is entirely misplaced & erroneous. He found that contention of the assessee that no expenses have been incurred since dividend and long term capital have been credited in the bank is incorrect. Assessing Officer further observed that assessee has relied upon the Delhi,

ITAT decision in the case of Impulse (India) Pvt. Ltd.. He observed that the argument that no procedure as is given under Rule 8D is available for A.Y. 2006-07 and so no expenses u/s 14A can be disallowed is preposterous.

He held that the legal position as is laid out by section 14A is applicable since 2001. Only the procedure or method of computation has been prescribed from A.Y. 2007-08. The spirit of section 14A of the IT Act has been extant since 1st April, 2001.

He further observed that one of the most of the reason is to adopt the procedure as laid down in Rule 8D for A.Y. 2006-07 since the spirit is the same. He further found alternatively that expenses can be disallowed on an estimate basis (10% or so) or on a pro-rata basis both of which are within boundaries of reasonableness and justice given the intent behind section 14A of the IT Act, 1961. Therefore, he estimated the expenses u/s 14A on a prorata basis (dividend income is 13.22% of total income so expenses are disallowed in same ratio) [Addition of ` 36,45,413/-]

4. Before the Ld. Commissioner of Income Tax (Appeals) the assessee inter-alia filed a working paper, as per rule 8D according to which total disallowance worked out ` 2323449/-. Ld. Commissioner of Income Tax (Appeals) held the working disallowance of ` 23123449/- as given by the assessee is in its submission are erroneous, hence, cannot be relied upon. Ld. Commissioner of Income Tax (Appeals) preferred to rely upon the decision of the Special Bench of the Tribunal in the case of ITO vs. Daga Capital Management P. Ltd. 26 SOT 603 and hence he directed the Assessing Officer to rework the amount of disallowance, as per Section 8D of the IT Rules and specially after satisfying all the documents and records.

5. Against this order the assessee is in appeal before us.

6. We have heard both the counsel and perused the records, in the light of the precedents relied upon. Ld. counsel of the assessee submitted that the decision of Hon'ble Punjab and Haryana High Court in the case of C.I.T. vs. Hero Cycles Ltd. reported in 323 ITR 518 would apply. In this case the facts and decision are as under:-

“The assessee was engaged in manufacture of cycles and parts of two-wheelers in multiple units. It earned dividend income, which was exempted under section 10(34) and (35) of the Income Tax Act, 1961. The Assessing Officer made an inquiry whether any expenditure was incurred for earning this income and as a result of the inquiry made addition by way of disallowance under section 14A(3), which was partly upheld by the Commissioner (Appeals). The tribunal held that there was no nexus between the expenditure incurred and the income generated. Therefore, it held that merely because the assessee had incurred interest expenditure on funds borrowed in the main unit it would not ipso facto invite the disallowance under section 14A, unless there was evidence to show that such interest bearing funds had been invested in the investments which had generated the “tax exempt dividend income”.

On appeal :

Held, dismissing the appeal, that the expenditure on interest was set off against the income from interest and the investment in the shares and funds were out of the dividend proceeds. In view of this finding of fact, disallowance under section 14A was not sustainable. Whether, in a given situation, any expenditure was incurred which was to be disallowed, was a question of fact. The contention of the Revenue that directly or indirectly some expenditure was always incurred which must be disallowed under section 14A and the impact of expenditure so incurred could not be allowed to be set off against the business income which may nullify the mandate of section 14A, could not be accepted.

Disallowance u/s 14A required finding of incurring of expenditure and where it was found that for earning exempted income no expenditure had been incurred, disallowance under section 14A could not stand. Consequently, the disallowance was not permissible.”

6.1 In the light of the above, ld. counsel of the assessee submitted here also the case of the revenue was similar as no direct nexus had been identified between the income and the expenditure. The disallowance has only been made on estimate basis. He further referred that reference by the Ld. Commissioner of Income Tax (Appeals) to decide the issue as per Rule 8D is also not correct in as much as the said rule emanates out of section 14A Sub-section (2) & (3) which were applicable from assessment year 2007-08.

In this regard he referred to ITAT, Delhi Bench decision in the case of Impulse (India) Pvt. Ltd. vs. ACIT 22 SOT 368 wherein it was held that the provisions of sub-section (2) and (3) of Section 14A could not applied preceding the assessment year 2007-08.

6.2 Ld. Departmental Representative on the other hand supported the orders of the Ld. Commissioner of Income Tax (Appeals) and referred the decision of the Bombay High Court in the case of Godrej Boyce Mfg. Co. Ltd. vs. DCIT. In the said case it was held that even when prior to A.Y. 2008-09, when Rule 8D was not applicable, the Assessing Officer has to enforce the provisions of sub-section (1) of Section 14A. For that purpose, the Assessing Officer is duty bound to determine the expenditure which has been incurred in relation to income which does not form part of the total income under the Act. The Assessing Officer must adopt a reasonable basis or method consistent with all the relevant facts and circumstances after furnishing a reasonable opportunity to the assessee to place all germane material on the record.

6.3 We have considered the submissions carefully. We find that in the case of Hero Cycles Ltd., the Hon'ble Punjab and Haryana High Court has held that disallowance u/s 14A required finding of incurring of expenditure and where it was found that for earning exempted income no expenditure had been incurred, disallowance under section 14A could not stand. On the other hand, the Hon'ble Mumbai High Court decision in the aforesaid case of Godrej Boyce Mfg. Co. Ltd. Has held that Assessing Officer can adopt a reasonable basis to identify the expenses in relation to the earning of exempt income. Now in the present case, we find that the matter can not be set aside to the files of Assessing Officer to apply Rule 8 D as the said provision cannot be applicable for the

current assessment year. Secondly, the assessee has urged that no expenditure has been identified to have been incurred to exempt income. Neither the Assessing Officer nor the Ld. Commissioner of Income Tax (Appeals) has rebutted these submission. Assessing Officer has gone into to make the adhoc estimate which is not sustainable in the light of the Hon'ble Punjab and Haryana High Court decision above.

6.4 Under such circumstances, we refer the Hon'ble Apex Court decision in the case of M/s Vegetable Products Ltd. 88 ITR 192, that in the taxing provision if two constructions are possible, one favouring assessee should be adopted.

6.5 Accordingly, following the precedent from the Hon'ble Punjab and Haryana High Court as above, we set aside the orders of the authorities below and decide the issue in favour of the assessee.

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

Order pronounced in the open court on 13/10/2010.

Sd/-
[A.D. JAIN]
JUDICIAL MEMBER

Sd/-
[SHAMIM YAHYA]
ACCOUNTANT MEMBER

Date 13/10/2010