

**IN THE INCOME TAX APPELLATE TRIBUNAL "B", BENCH KOLKATA**

**BEFORE SHRI A. T. VARKEY, JM & DR. A.L.SAINI, AM**

**आयकरअपीलसं./ITA No.172, 173 & 174/Kol/2016**

**(निर्धारणवर्ष / Assessment Years: 2008-09, 2009-10 & 2010-11)**

<b>ITO, Wd-12(1), Kolkata</b> Aayakar Bhawan, P-7, Chowringhee Square, Kolkata – 700 069.	<b>Vs.</b>	<b>M/s Bonanza Trading Company (P) Ltd.</b> B-103, Rai Enclave, 7/1A, Sunny Park, Kolkata – 700 019.
स्थायीलेखासं./जीआइआरसं./PAN/GIR No. : AABCB 0175 D		
<b>(APPELLANT)</b>	<b>..</b>	<b>(RESPONDENT)</b>

Appellant by : Shri Saurabh Kumar, Addl. CIT(DR)

Respondent by : Shri Asim Choudhury, Advocate.

सुनवाईकीतारीख/ **Date of Hearing** : **13/11/2017**

घोषणाकीतारीख/**Date of Pronouncement** : **10/01/2018**

**आदेश / O R D E R**

**Per Dr. Arjun Lal Saini, AM:**

The captioned three appeals filed by the Revenue, pertaining to assessment years 2008-09, 2009-10 & 2010-11, are directed against the orders passed by the Id. Commissioner of Income Tax (Appeals)-9, Kolkata, in Appeal Nos. 588/589/ and 590/CIT(A)-9/Wd-12(1)/2014-15/Kol, which in turn arise out of assessment orders passed by the Assessing Officer u/s.143(3) of the Income Tax Act, 1961 (hereinafter referred to as the 'Act').

2. Since, these three appeals relate to same assessee, different assessment years, identical issues are involved, therefore, these have been clubbed and heard together and a consolidated order is being passed for the sake of convenience and brevity. Revenue's appeal in ITA No.172/Kol/2016, Assessment Year 2008-09, is taken as the lead case.

3.The Revenue has raised the following grounds of appeal (in lead case in ITA No.172/Kol/2016, Assessment Year, 2008-09) are as follows:

*“1.That in the facts & circumstances of the case and in law, the Id. CIT(A) has erred by allowing relief to the assessee in respect of the disallowance made u/s 14A of the I.T. Act r.w.r 8D(2)(ii) of I.T. Rule whereas, the assessee failed to establish the fact in course of assessment that its interest being funds were not utilized for investments which yielded exempt income which was the onus upon the assessee to prove as observed by the Hon’ble Calcutta High Court in the case of Dhanuka and Sons [ITA No.633 of 2004 dated 19.04.2011].*

*2.That in the facts & circumstances of the case and in law, the Id. CIT(A) has erred on the issue of disallowance made under Rule 8D(2)(iii) as because offering of short term capital gain for tax on sale of investments does not mean that such investments has lost its nature to yield dividend income and should not be considered to be included in computation of average value of investments for disallowance under the said Rule.*

*3.That the appellant craves for leave to add delete or modify any of the grounds of appeal before or at the time of hearing.”*

4.In this appeal, the main grievance of the Revenue is that the Id. CIT(A) has erred by allowing relief to the assessee in respect of the disallowance made u/s 14A of the I.T Act and r.w.r. 8D(2)(ii) and Rule 8D (2) (iii) of I.T. Rules.

5.The brief facts qua the issue are that during the assessment proceedings under section 143(3), the assessing officer noticed from the Profit & loss Account of the assessee as well as computation sheet that assessee had earned Dividend Income of Rs.13,18,618/- and claimed the same as exempt u/s 10 of the I.T Act,1961. The assessee has also claimed long term capital gain of Rs.48,41,068/- as exempt u/s 10(38) of the I.T. Act,1961. The assessee was asked to file a detail of disallowable expenditure in terms of section 14A r.w.r 8D of I.T. Rules.

During the assessment proceedings the assessee submitted before the AO that he earned dividend income amounting to Rs.13,81,618/- and also earned income from long term capital gain amounting to Rs.48,41,068/-. It was clarified to AO that no expenditure was incurred by the assessee which is directly related to earning of these incomes. However, the assessee himself disallowed Rs. 6,43,032/- related to earning of exempted income.

Thereafter, the AO observed from the computation of "income from Business or Profession" that the assessee has made an addition under the head "Expenses debited to profit & loss account which relate to exempt income" an amount of Rs. 6,43,032/-. However, on further perusal of details, the AO noted that the said amount was an aggregate of STT amounting to Rs.2,61,895/-, Share transfer of Rs.1,05,000/-, Payment to portfolio Manager for Rs. 2,76,037/- and Rs. 100/- relating to Demat charges. Now, this may be mentioned that STT payment is expressly disallowable u/s. 40(a)(ib) of the I.T.Act,1961 and hence it is not a disallowance u/s 14A of the Act, but 40(a)(ib) of the Act. The payments related to portfolio manager is also not an allowable deduction under the head capital gain and so it is also not allowable otherwise. Hence, it was noted by AO that in true sense, the assessee has disallowed only Rs.1,05,100/- u/s 14A of the I.T.Act,1961.

Again, the assessee was asked to file a computation in terms of rule 8D.

In response to that the assessee had filed a detail on 29/12/2010 computing total disallowance as per rule 8D at Rs.1,05,383/-. The assessee had also put a note below such computation which reads as under:

1. Expenditure on interest is attributable to the business of the assessee and, as such, has not been considered for the purposes of amount inadmissible u/s. 14A.
2. All the investment other than those stated above have not been considered for the purpose of average investment u/s. 14A as the same had been offered for short term capital gain in assessment year 2008-09 and

2009-10. Moreover, the unquoted investment shall be offered for taxation in the year of sale.

Regarding details of use of borrowed fund, the assessee has submitted that the borrowed fund during the year increased by Rs.12,72,95,212/-. It was submitted that the fund was used for business purpose only. The borrowed fund was utilized for purchase of space on ownership Rs. 9,10,12,500/-, for purchase of other assets Rs.34,69,153/- and for working capital of Rs. 3,38,95,637/-. It was stated by the assessee that the borrowed fund was used for the purpose of business and not for investment.

The Assessing officer observed that the assessee had simply stated that no direct expenditure was incurred for earning of exempt income but nothing had been stated about indirect expenses in the form of Administrative and other expenses incurred by the assessee, so was the case with expenditures incurred as interest. The AO noted that in the case of S.G. Investment & industries Ltd, Vs. DCIT 89 ITD 44 Hon'ble ITAT, Kolkata had opined that the word "in relation to" is of much wider import and not only encompasses direct & indirect expenditure but also those expenditures which are proximate to any income not chargeable to tax. Hence, expenditures relating to exempt income are liable to be disallowed. Actually, the assessee had disallowed certain expenditures u/s. 14A, most of which are otherwise also not allowable. The AO Noted that subsequently, the assessee had filed a computation with notes which has no basis or relevance, as the assessee has picked up certain investment leaving others without any reason although exempt income arises or shall arise from those investments also. The AO observed that it was evident from the nature of business of the assessee and accrual of dividend income that part of administrative as well as interest expenses attributable to exempt income, the provisions of section 14(2) read with rules 8D would be applicable to the assessee. The AO also, relied on the judgment of Hon'ble ITAT "Special Bench" Mumbai in the case of M/s. Daga Capital Management Pvt. Ltd. Vs. ITO 6(2)(2), Mumbai in ITA No. 8057/Mum/03, ratio of which is mostly approved by the

Hon'ble High Court Bombay (except retrospective application of rule 8D), therefore, Rule 8D would be applicable to the assessee. This may further be mentioned that the submission of the assessee that interest is totally used for business purpose is also not correct in view of the fact that the assessee is not maintaining separate bank accounts for investment purpose and business purpose, so that the interest element could be apportioned. The AO noted that it was apparent from record that the assessee is carrying on with huge loan fund which was standing at Rs. 8,99,69,473/- as on 01/04/2007 and Rs.21,72,67,379/- as on 31/03/2008. As far as use of most of the fund for purchase of assets are concerned, it is true for the loan fund pertaining to loans taken during the relevant previous year but such loans were taken in the fag end of the year and does not bears much interest, therefore, AO held that interest attributes to investments as well as business and hence, the same should also be considered for computation of disallowance. The assessee was also not correct in taking only minimum investment leaving others with a note that short term capital gain was paid on such investment as dividend arose or shall arise from such investments also. Based upon the above discussion, the AO made the disallowance as per Rule 8D as under:

As per Rule 8D(i) : Rs.100/- (as per assessee's computation)

As per Rule 8D(2)(ii):  $A \times B \div C = 1,09,83,149 \times 9,99,72,533 \div 25,04,47,228 = \text{Rs.}43,84,210/-$ .

(This is to be mentioned that the notations A,B& C are having the same meaning as assigned to them under Rule 8D)

As per Rule 8D(2)(iii): Investment in Shares as on 01/04/2007: Rs.6,52,43,631/-

Investment in Shares as on 31/03/2008: Rs.13,47,01,434/-

Average value of investment : Rs.9,99,72,533/-

½ of above: : **Rs.4,99,863/-**

The AO disallowed Rs.48,84,173/- (Rs.43,84,210 + 4,99,863 + 100). Since the assessee had already disallowed Rs.1,05,100/-, therefore net disallowance was made by AO at Rs.47,79,073/- (Rs.48,84,173 - Rs.1,05,100).

6. Aggrieved by the addition made by the AO under Rule 8D(2)(ii) and 8D(2)(iii), the assessee filed an appeal before the Id. CIT(A) who has allowed the appeal of the assessee. During the appellate proceedings, the counsel submitted before the Id. CIT(A) that AO did not consider that the shares which had been invested, was over a period of time. The assessee submitted before the Id. CIT(A) that he had purchased shares from his surplus funds, as the sale proceeds of shares were utilized to buy new shares. The assessee had also invested in their subsidiary company, as strategic investment to expand their real estate business. The Id CIT(A) after going through the month-wise sale and purchase details of investments, observed that there was surplus funds for investment from which exempt income was being earned. The Id CIT(A) also noted that there was no disallowance of interest in the earlier years and perusal of the month-wise details of purchase and sale of investment for FY 2006-07 also showed that the assessee had surplus fund on the sale of investments which was used to purchase further investments. Further assessee had made strategic investment in wholly owned subsidiaries from which the assessee had submitted that no dividend income had been earned from the same till date. On the verification of the Memorandum of Association, it was also found that Real Estate Development and Real Estate Investment was one of the main objects of the company. Thus, the Id. CIT(A) found that the case is covered by the decision of the Punjab & Haryana High Court in the case of CIT vs. Hero Cycle Limited 323 ITR 518, wherein it was held that if sale proceeds from investment is enough to be used for the purpose of purchase of investment then it is clear that the assessee has surplus fund

and no disallowance under 14A can be made. This way, the Id. CIT(A) allowed the appeal of the assessee and deleted the addition made by AO.

7. Not being satisfied with the order of the CIT(A), the Revenue is in appeal before us. The Id. DR for the Revenue has submitted before us that Id CIT(A) was wrong in allowing relief to the assessee in respect of disallowance made by AO, as the assessee failed to establish the fact in the course of assessment proceedings that its interest bearing funds were not utilized for investments which yielded exempt income which was the onus upon the assessee to prove and therefore, the order of the CIT(A) was erroneous and not based on the facts. The Id. DR for the Revenue had submitted that under Rule 8D(2)(ii), the assessee had failed to establish the fact that interest bearing funds were not utilized for investment which yielded exempt income.

8. On the other hand, the Id. Counsel for the assessee submitted that assessee is engaged in real estate investment and investment in share and securities. The assessee company has its own surplus funds to invest in share and security. Therefore, disallowance under Rule 8D(2)(ii) should not be made. Apart from this, the Id. Counsel also submitted that disallowance under Rule 8D(2)(iii) in order to compute average investment only dividend bearing securities/shares should be taken into account for disallowance. In addition to this, the counsel for the assessee has relied on the judgment of ITAT Kolkata in the case of REI Agro Ltd. vs. DCIT reported in [2013] 35 taxmann.com 404, wherein it was held that in order to compute average investment, only dividend bearing securities/shares should be taken into account for disallowance.

9. Having heard the rival submissions and perused the materials available on record, we note that under Rule 8D(2)(iii), it is not the total investment at the beginning of the year and at the end of the year, which is to be considered but it is the average of the value of investments which has given rise to the income which does not form part of the total income, is to be

considered. In respect of the provisions of rule 8D(2)(iii), which is the subject-matter of the appeal, a perusal of the said provision shows that what is disallowable under rule 8D(2)(iii), is the amount equal to ½ percentage of the average value of investment the income from which does not or shall not form part of the total income. Thus under sub-clause (iii), what is disallowed is ½ percentage of the numerator B in rule 8D(2)(ii). Again this is to be calculated in the same line as mentioned earlier in respect of Numerator B in rule 8D(2)(ii) of the Act. Therefore, not all investments become the subject-matter of consideration when computing disallowance u/s 14A r.w.r 8D. The disallowance u/s 14A r.w.r. 8D is to be in consideration to the income which does not form part of the total income and this can be done only by taking into consideration the investment which has given rise to this income which does not form part of the total income.

We note that, so far the disallowance under Rule 8D(2)(ii) is considered, the assessee company has proved that it has sufficient funds to invest in shares and securities, therefore, no disallowance is warranted. Therefore, we are of the view that disallowance u/s 14A r.w.r. 8D(2)(ii) should not be made in the case of the assessee under consideration because the assessee had its own funds to invest in shares and securities and some of the investments were made by the assessee in subsidiary companies for strategies purpose.

Hence, we confirm the order passed by the Id CIT(A), so far the disallowance under Rule 8D (2) (ii) is concerned.

For disallowance under Rule 8D(2)(iii), the assessee had suo-moto disallowed Rs.1,05,100/-, however, we note that in order to compute the disallowance under Rule 8D (2) (iii), only dividend bearing securities should be considered. Therefore, we direct the AO to compute disallowance after taking consideration the investment which was given rise to the exempt income, that is, dividend bearing shares and securities, as per the method suggested in the judgment of REI Agro Ltd. vs. DCIT reported in [2013] 35 taxmann.com 404 (supra) and the disallowance so computed should be



reduced by Rs.1,05,100/-, the suo moto amount disallowed by the assessee.

10. In the result, the appeal filed by the Revenue (ITA No.172, 173 & 174/kol/2016) are partly allowed.

Order pronounced in the open court on this 10/01/2018.

**Sd/-**

**(A. T. VARKEY)**

न्यायिक सदस्य / JUDICIAL MEMBER

कोलकाता /Kolkata; दिनांक Dated 10/01/2018

RS, SPS.

**Sd/-**

**(DR. A.L.SAINI)**

लेखा सदस्य / ACCOUNTANT MEMBER

आदेशकीप्रतिलिपिअग्रेषित/Copy of the Order forwarded to :

1. The Appellant – ITO, Wd-12(1), Kolkata
2. प्रत्यर्थी/ The Respondent-M/s Bonanza Trading Company (P) Ltd.
3. आयकरआयुक्त(अपील) / The CIT(A), :Kolkata.
4. आयकरआयुक्त/ CIT
5. विभागीयप्रतिनिधि, आयकरअपीलीयअधिकरण, कोलकाता/ DR, ITAT, Kolkata
6. गार्डफाईल / Guard file.  
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By Order

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Head of Office/D.D.O,  
I.T.A.T, Kolkata Benches,  
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