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IN THE HIGH COURT OF DELHI AT NEW DELHI

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ITA No. 136/2017

EICHER MOTORS LTD.

..... Appellant

Through: Mr.Ajay Vohra, Sr.Advocate with
Mr.Gaurav Jain, Mr.Aniket D.Agrawal,
Advocates.

versus

COMMISSIONER OF INCOME-TAX-III

..... Respondent

Through: Mr.Zoheb Hossain, Sr.Standing
Counsel.

**CORAM: JUSTICE S. MURALIDHAR
JUSTICE PRATHIBA M. SINGH**

ORDER

15.09.2017

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1. This is an appeal by the Assessee under Section 260A of the Income Tax Act, 1961 ('Act') against an order dated 4th January 2016 passed by the Income Tax Appellate Tribunal ('ITAT') in ITA No. 2561 & 2386/Del/2013 for the Assessment Year ('AY') 2009-10.

2. Admit.

3. The following questions are framed for consideration:

“(i) Whether on the facts and in the circumstances of the case, the Tribunal exceeded jurisdiction in setting aside the claim of weighted deduction under Section 35 (2AB) of the Act to the file of the assessing officer to re-examine the issue on grounds,

which were not even subject matter of appeal before the Tribunal?

(ii) Whether on the facts and in the circumstances of the case, the Tribunal erred in law in not deleting the disallowance made under section 14A of the Act, despite holding that the assessing officer had failed to (i) record his satisfaction in terms of Section 14A(2)/(3) and (ii) establish direct/ proximate nexus of expenses with the earning of exempt dividend income?”

4. The facts in brief are that the Assessee, which is engaged *inter alia* in the manufacture of motorcycles, filed its return of income for the AY in question on 29th September, 2009 declaring an income of Rs. 150,38,49,972/- claiming book profit of Rs. 34,27,02,218/- under Section 115JB of the Act. Since the tax liability under the normal provisions of the Act was higher than the tax liability on book profits, the tax liability was determined under Section 115JB.

5. During the AY in question, the Assessee had in-house Research and Development (‘R&D’) centres at Pithampur and Chennai which were duly approved by the Department of Scientific and Industrial Research (‘DSIR’) in accordance with Section 35 (2AB) of the Act. Accordingly, the Assessee claimed weighted deduction of Rs.19,57,26,863/- being 150% of all the research expenses incurred in the in-house R&D facilities under Section 35 (2AB) of the Act.

6. The Assessee had also earned dividend income of Rs. 6.39 crores from investments in subsidiary companies and mutual funds that were exempt under Section 10 (33) and (34) of the Act. The Assessee, however, did not disallow any expenditure in respect of the earnings of the above exempt

income.

7. The return was picked up for scrutiny. The Assessing Officer ('AO') in the assessment order dated 28th December 2011 granted 100% deduction on both capital and revenue expenditure incurred on the two R&D centres but disallowed the additional weighted deduction of 50% amount of Rs. 6,52,42,288/-.

8. The AO further invoked Section 14A of the Act and computed disallowance of Rs. 1,02,73,361/-. The reason that weighed with the AO in making the above disallowance as regards the exempt income was that the AO observed that Section 14A was straightaway attracted but no expenses were claimed. The AO then surmised that certain expenses ought to have been incurred for earning the dividend income like purchase of raw materials, salaries, etc. The AO proceeded to apply Rule 8D (2) and (3) of the Income Tax Rules as applicable at the relevant time and worked out the disallowance as Rs. 1,02,73,361/-.

9. In the appeal filed by the Assessee before the Commissioner of Income Tax (Appeals) ['CIT (A)'], on the question of the expenses incurred on the R&D Centres, the CIT (A) held that the Assessee was entitled to weighted deduction for the entire expenditure incurred. It was held that the disallowance made by the AO was "not based on correct appreciation of facts and position in law". As far as the issue relating to the disallowance under Section 14A of the Act is concerned, the CIT (A) restricted the disallowance to Rs. 20,24,169/-.

10. Both the Revenue as well as the Assessee went in appeal before the ITAT. By the impugned order dated 4th January 2016, on the first issue regarding expenses incurred on the R&D centres, the ITAT concurred with the Assessee but paradoxically remanded the matter to the AO to decide the issue afresh on the ground that the AO had not returned a finding on the revenue and capital nature of the said expenditure.

11. As regards the issue concerning disallowance under Section 14A for earning exempt income, the ITAT again concurred with the Assessee that the AO had failed to record reasons for disagreeing with the Assessee that it had not incurred any expenditure in relation to earning of exempt income. Nevertheless, on this issue again, the ITAT remanded the matter to the CIT (A) to decide the issue afresh. A direction was issued to the CIT (A) to call for a remand report from the AO and “to record his satisfaction and cogent reasons before invoking the provisions contained u/s 14A read with Rule 8D of I.T. Rules.”

12. The Court is unable to concur with the impugned order of the ITAT on both the aspects. Having held that the R&D expenditure as claimed by the Assessee ought to have been allowed, there was no question of remanding the matter to the AO for returning a finding on whether the expenditure was of revenue or capital nature. This is because, under Section 35 (2AB) of the Act, both revenue and capital expenditure are allowable in their entirety, excluding expenditure in the nature of cost of any land or building. There was going to be no purpose served in analysing whether the expenditure was of revenue or capital nature. In fact, the AO himself had allowed 100% of

the expenditure both of revenue and capital nature and the disallowance was only the additional 50% amount which, again, the CIT (A) had found and correctly so, in the opinion of this Court, ought not to have been disallowed. Recently, this Court in W.P.(C) 9306/2015 **Maruti Suzuki India Limited Vs. UOI & Anr**, by its decision dated 4th August, 2017 has held "The legislative intent behind this provision is to encourage innovation, research and development in India and non-grant of the benefit under Section 35 (2AB) defeats the legislative intent." In that view of the matter, the Court has no hesitation in holding that the Assessee is entitled to the full benefit of Section 35 (2AB) and that the ITAT was in error in remanding this issue to the AO for a fresh decision.

13. As regards the disallowance of expenditure for earning exempt income in terms of Section 14A of the Act, the settled legal position is that the AO had to record reasons for disagreeing with the submission of the Assessee that it had incurred no expenditure for earning such exempt income. This is plain even from Rule 8D (1) which requires the AO to mandatorily record his satisfaction that the claim made by the Assessee that no expenditure has been incurred is incorrect "having regard to the accounts of the assessee." In this case, a perusal of the AO's reasoning shows that the AO has merely conjectured that *there is an inbuilt cost even in passive investment as also incidental expenditure like collection, telephone, follow up etc.*, The AO thus concludes that the expenses are embedded as indirect expenses. This is not as per the requirements of Rule 8D. There is no satisfaction recorded 'based on the accounts of the assessee'. The AO simply presumes that since the exempt income exists and is being claimed by the Assessee, some

portion of the expenses ought to be added back. This is not sufficient as per the law. Once this mandatory requirement is itself not fulfilled, in terms of the law explained by this Court in *Maxopp Investment Ltd. v. CIT*, [2012] 347 ITR 272 (Delhi), the question of remanding the matter to the CIT(A) and to call for a remand report from the AO for the purposes of rectifying this jurisdictional defect simply did not arise. In this context, the Court also notices that in the order passed by the AO on 28/30th December 2016 pursuant to the impugned order of the ITAT on remand, the AO had simply repeated his entire assessment order passed in the first instance. Be that as it may, the Court is of the view that the ITAT erred in overlooking the correct legal position in remanding the matter to CIT (A).

14. Accordingly, both the questions are answered in favour of the Assessee and against the Revenue. The impugned order of the ITAT and the consequential order of the AO dated 28/30th December 2016 are hereby set aside but without any order as to costs.

S. MURALIDHAR, J.

PRATHIBA M. SINGH, J.

SEPTEMBER 15, 2017/ 'anb'