

IN THE HIGH COURT OF PUNJAB & HARYANA AT CHANDIGARH

ITA-322-2016 (O&M)

Date of Decision: 28.8.2018

Principal Commissioner of Income Tax-I, Chandigarh

....Appellant.

Versus

M/s Vardhman Chemtech Private Limited, Chandigarh

...Respondent.

**CORAM:- HON'BLE MR. JUSTICE AJAY KUMAR MITTAL.
HON'BLE MR. JUSTICE AVNEESH JHINGAN.**

PRESENT: Ms. Urvashi Dhugga, Sr. Standing Counsel for the appellant.

Mr. Surjeet Bhadu, Advocate with
Mr. Raj Kamal, Advocate and
Mr. Veer Singh, Advocate for the respondent.

AJAY KUMAR MITTAL, J.

1. This appeal has been preferred by the revenue under Section 260A of the Income Tax Act, 1961 (in short “the Act”) against the order dated 22.4.2016 (Annexure A-3) passed by the Income Tax Appellate Tribunal, Division Bench, Chandigarh (hereinafter referred to as “the Tribunal”) in ITA No. 488/Chd/2015, claiming the following substantial questions of law:-

1. Whether in the facts and circumstances of the case and in law, the Hon'ble ITAT was right in holding that the provisions of Section 14A as clarified by

CBDT Circular No.5 of 2014, were not attracted as the assessee has not earned any exempt income during the year despite the fact that the assessee had invested a huge sum from which no income was shown while there was a considerable financial outgo on interest/financial charges on borrowed funds?

2. Whether in the facts and circumstances of the case and in law, the Hon'ble ITAT was right in relying on the decision in the case of Lakhani Marketing when the CBDT Circular No.5 of 2014 was not for consideration before the Hon'ble Court at that time?

2. A few facts necessary for adjudication of the instant appeal as narrated therein may be noticed. The assessee filed its return of income on 30.9.2011 declaring an income of ₹ 3,41,50,800/-. The assessment was completed under Section 143(3) of the Act by the Assessing Officer vide order dated 3.1.2014 (Annexure A-1) at an income of ₹ 4,86,08,810/- after making the following additions:-

- (i) ₹ 33,92,141/- on account of disallowance under Section 36(1)(iii) of the Act;
- (ii) ₹ 40,28,526/- disallowance under Section 14A of the Act; and
- (iii) ₹ 64,37,342/- on account of non-deduction of TDS on L/C.

3. Feeling aggrieved, the assessee filed an appeal before the

Commissioner of Income Tax (Appeals) [for brevity “the CIT(A)”] who vide order dated 27.2.2016 (Annexure A-2) upheld addition at Sr. No. (i), deleted the addition at Sr. No. (ii) and remitted back the addition at Sr. No. (iii) to the file of the Assessing Officer. Against the order, Annexure A-2, the assessee filed appeal against addition at Sr. No. (i) whereas the revenue filed appeal against deletion of addition at Sr. Nos. (ii) and (iii). The Tribunal vide order dated 22.4.2016 (Annexure A-3) dismissed the appeal of the revenue whereas the appeal of the assessee was allowed. Hence, the present appeal by the revenue against the deletion of disallowance made under Section 14A of the Act.

4. Learned counsel for the revenue has submitted that the Tribunal has erred in law while upholding the decision of the CIT(A) as it is clarified vide CBDT Circular dated 11.2.2014 that Section 14A of the Act provides for disallowance of expenditure even where taxpayer has not earned any exempt income. In support of her contention, learned counsel has relied upon the following judgments:

- I. Commissioner of Income Tax, West Bengal III, Calcutta v. Rajendra Prasad Moody, Calcutta, AIR 1979 SC 373;**
- II. Maxopp Investment Ltd. v. Commissioner of Income Tax (2018) 402 ITR 640 (SC);**
- III. Commissioner of Income Tax v. Walfort Share and Stock Brokers (2010) 326 ITR 1 (SC); and**
- IV. Godrej and Boyce Mfg. Co. Ltd. v. Deputy Commissioner of Income Tax and another (2010) 328 ITR 81 (Bombay).**

5. On the other hand, learned counsel for the assessee has submitted that the income earned from the investment of equity shares was in the nature of dividend which is an exempt income and therefore, the Assessing Officer was rightly directed not to make disallowance under Section 14A of the Act. Further, it was submitted that the Tribunal had rightly dismissed the appeal of the revenue. Reliance was placed upon the following judgments:-

- I. **CCE, Bolpur v. Ratan Melting and Wire Industries, (2008) 12 STR 416 SC;**
- II. **Commissioner of Income Tax v. Lakhani Marketing Inc. (2014) 111 DTR 149 (P&H);**
- III. **Commissioner of Income Tax v. Holcim India (P) Ltd. (2014) 272 CIT 282 (Del);**
- IV. **Cheminvest Ltd. v. Commissioner of Income Tax (2015) 281 CTR 447 (Del);**
- V. **Redington (India) Ltd. v. Additional Commissioner of Income Tax (2017) 392 ITR 633 (Mad); and**
- VI. **Principal Commissioner of Income Tax v. IL&FS Energy Development Company Limited (2017) 399 ITR 482 (Del).**

6. After hearing the learned counsel for the parties, we do not find any merit in the appeal.

7. Section 14A of the Act reads as under:-

“Section 14A. Expenditure incurred in relation to income not includible in total income.

14A. (1) For the purposes 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.

(2) The Assessing Officer shall determine the amount of expenditure incurred in relation to such income which does not form part of the total income under this Act in accordance with such method as may be prescribed, if the Assessing Officer, having regard to the accounts of the assessee, is not satisfied with the correctness of the claim of the assessee in respect of such expenditure in relation to income which does not form part of the total income under this Act.

(3) The provisions of sub-section (2) shall also apply in relation to a case where an assessee claims that no expenditure has been incurred by him in relation to income which does not form part of the total income under this Act :

Provided that nothing contained in this section shall empower the Assessing Officer either to reassess under section 147 or pass an order enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee under section 154, for any assessment year beginning on or before the 1st day of April, 2001.”

Section 14A of the Act provides for disallowance of expenditure in relation to income not 'includible' in total income.

8. Now, we proceed to examine the judgments relied upon by the learned counsel for the revenue. In **Rajendra Prasad Moody's case (supra)**, the Supreme Court had held as under:-

“The plain and natural construction of the language of Sec. 57(iii) of the Income Tax Act 1961 irresistibly leads to the conclusion that to bring a case within the section, it is not necessary that any income should in fact have been earned as a result of the expenditure. What Sec. 57(iii) requires is that the expenditure must be laid out or expended wholly and exclusively for the purpose of making or earning income. It is the purpose of the expenditure that is relevant in determining the applicability of Sec. 57(iii) and that purpose must be making or earning of income. Sec. 57(iii) does not require that this purpose must be fulfilled in order to qualify the expenditure for deduction. It does not say that the expenditure shall be deductible only if any income is made or earned. There is in fact nothing in the language of Sec. 57(iii) to suggest that the purpose for which expenditure is made should fructify into any benefit.”

9. It was laid down in **Maxopp Investment Ltd's case (supra)** that the provisions of Section 14A of the Act can be applied to the case of a person who was a dealer in shares. It was concluded by the Apex Court in

Walfort Share and Stock Brokers' case (supra) that the basic principle of taxation was to tax the net income, i.e. gross income minus the expenditure and on the same analogy the exemption was also in respect of net income and where the gross income would not form part of total income, its associated or related expenditure would also not be permitted to be debited against other taxable income. Further, it was observed that for the purpose of computing the total income under this Chapter, no deduction shall be allowed in respect of expenditure incurred by the assessee with the main object of earning income which does not form part of the total income under the Act. It was also held that permissible deductions enumerated in Sections 15 to 59 were now to be allowed only with reference to income which was brought under one of the heads of income and was chargeable to tax and if an income like dividend income was not part of the total income, the expenditure/deduction related to such income, though of the nature specified in Sections 15 to 59 could not be allowed against another income which was includible in the total income for the purpose of chargeability to tax. Further, it was pronounced by the Supreme Court in **Godrej and Boyce Mfg. Co. Ltd's case (supra)** that computation of income, disallowance of expenditure incurred in earning income not forming part of total income, Section 14A of the Act was applicable to dividend income and income from mutual funds exempt under Section 10(33) of the Act. None of the aforesaid pronouncements relied upon by learned counsel for the revenue advances the case as set up by it.

10. We now advert to the judicial decisions relied upon by the learned counsel for the assessee. In **Ratan Melting and Wire Industries' case (supra)**, it was held by the Supreme Court that 'circulars and

instructions issued by the Board are no doubt binding in law on the authorities under the respective statutes, but when the Supreme Court or the High Court declares the law on the question arising for consideration, it would not be appropriate for the court to direct that the circular should be given effect to and not the view expressed in a decision of this court or the High Court. So far as the clarifications/circulars issued by the Central Government and of the State Government are concerned they represent merely their understanding of the statutory provisions. They are not binding upon the court. It is for the Court to declare what the particular provision of statute says and it is not for the Executive. Looking at from another angle, a circular which is contrary to the statutory provisions has really no existence in law. In **Lakhani Marketing Inc's case (supra)**, this Court while dismissing the appeal of the revenue had observed that unless and until there is receipt of exempted income for the concerned assessment years, Section 14A of the Act cannot be invoked. Similarly, in **Holcim India (P) Ltd's case (supra)**, the Delhi High Court had laid down that Section 14A of the Act cannot be invoked when no exempt income was earned. Identical view was expressed by Madras High Court in **Redington (India) Ltd's case (supra)**, where it was enunciated that no disallowance under Section 14A read with Rule 8(d) of the Income Tax Rules, 1962 (in short "1962 Rules") can be made in respect of an assessment year in which no exempt income is earned. In **IL&FS Energy Development Company Limited's case (supra)**, the Delhi High Court had expressed that the CBDT Circular dated 11.2.2014 cannot override the express provisions of Section 14A read with Rule 8 D of the 1962 Rules. In **Cheminvest Ltd's case (supra)**, it was

actual receipt of income, which is not includable in the total income during the relevant previous year for purpose of disallowing any expenditure under Section 14A of the Act in relation to said income.

11. Examining the factual matrix, it may be noticed that the Tribunal while relying upon the judgment of this Court in **Commissioner of Income Tax v. Lakhani Marketing Inc. (2014) 111 DTR 149 (P&H)** had held that Section 14A of the Act cannot be resorted to in the year in which no exempt income had been earned. However, the revenue relied upon the CBDT Circular dated 11.2.2014 to contend that Section 14A of the Act can be invoked even in the year in which no exempt income had been earned. Accordingly, the Tribunal had dismissed the appeal of the revenue holding that unless and until there is receipt of exempted income for the concerned assessment year, Section 14A of the Act is not attracted.

12. The Tribunal vide order dated 22.4.2016 regarding the ground of deletion of disallowance amounting to ₹ 40,28,526/- under Section 14A of the Act had recorded as under:-

“We do not find any infirmity in the order of the Ld. CIT (A), who deleted the disallowance made following the decision of the jurisdictional High Court in the case of Lakhani Marketing (supra). The argument of the Ld. DR that the CBDT Circular No.5/2014 dt. 11.02.2014 stating that even in the absence of any exempt income disallowance under Section 14A has to be made, is binding on the Revenue authority, we find has no merit.

13. No illegality or perversity could be demonstrated by learned counsel for the revenue in the aforesaid findings recorded by the Tribunal.

14. No other point was urged by learned counsel for the parties.
15. Thus, substantial questions of law as claimed are answered accordingly and the appeal is dismissed.

(AJAY KUMAR MITTAL)
JUDGE

August 28, 2018
gbs

(AVNEESH JHINGAN)
JUDGE

Whether Speaking/Reasoned	Yes
Whether Reportable	Yes