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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

+ **ITA 277/2018**

THE PR. COMMISSIONER OF INCOME TAX -5..... Appellant

Through: Mr. Puneet Rai, Standing Counsel

versus

KESHAV POWER LTD.

..... Respondent

Through: Mr. Simran Mehta, Advocate

CORAM:

HON'BLE MR. JUSTICE SANJIV KHANNA

HON'BLE MR. JUSTICE CHANDER SHEKHAR

ORDER

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07.09.2018

Revenue has preferred this appeal under Section 260A of the Income Tax Act, 1961 ('Act' for short) against order dated 01.09.2017, passed by the Income Tax Appellate Tribunal ('Tribunal' for short) in the case of Keshav Power Ltd. in ITA No. 4277/DEC/2015, pertaining to Assessment Year 2011-12.

2. The assessee has earned exempt/dividend income of Rs.88,83,863/-. The assessee applying Section 14A of the Act in the return filed had made disallowance of Rs.1,04,90,253/-. This factual position is not disputed.

3. The Assessing Officer held that Rule 8D of the Income Tax Rules, 1962 ('Rules' for short) was mandatory and applying the Rule, the disallowance was increased to Rs.4,15,24,709/-. The reasoning given by the Assessing Officer is as under:-

"2. The brief facts of the case are that the assessee company is engaged in the business of generation and distribution of power. The company had taken a 27 MW Thermal Power Plant on Operating Lease w.e.f. March 2005 at Dalmiapuram,

Distt. Tiruchirapalli and is operating the same. The assessee e-filed return of income declaring NIL income on 26/09/2011, which was processed u/s 143(1) of the Income Tax Act, 1961 (hereinafter referred as the Act). Later on, the case was selected for scrutiny under CASS, notice u/s 143(2) of the Act dated 07/08/2012 was issued and served upon the assessee. Due change incumbent, notices u/s. 143(2) & 142(1) of the Act along with a detailed questionnaire dated 24/12/2013 were issued fixing the case for hearing and requiring the assessee to file necessary details. In response, the AR of the assessee company attended the proceedings from time to time and furnished the requisite certain information. AO observed that Section 14A of the I.T. Act, 1961 regulates the expenditure which was incurred in relation to exempt income. By virtue of this section no deduction shall be allowed in respect of expenditure incurred by the assessee on account of income which does not form part of the total income under the Act. 'The CBDT has notified rule 8D to avoid ad-hoc disallowance to impart visibility to the expenditure incurred for earning exempt income. Moreover, procedure for computation of disallowance has been provided in sub-sections (2) and (3) of section 14A of the I T Act. The ITAT, Special Bench, New Delhi in the case of MIS Cheminvest Ltd. ITA no 87/De1/2008 has also held that the disallowance u/s 14A is to be made even if no income has resulted or earned by the assessee in the year under consideration. Therefore, in view of the specific

provisions for quantification of disallowance as contained in sub-sections (2) and (3) of section 14A, which are procedural. The disallowance is strictly to be made in terms of the specific provisions of Rule 8D. The assessee has offered the total dividend income as disallowance u/s 14A but it is not acceptable as computation under rule 8D. The assessee has not established with the necessary documentary evidence that it had not incurred any Interest expenditure for the investment which has yielded dividend or shall yield such income and any other expenditure for earning exempted Dividend Income. The assessee has incurred interest expenditure and other expenditure during the year as well as earlier years and the exact quantum of expenditure for the year as well as earlier years could not be worked out. The disallowance u/s- 14A and as per Rule 8D is being made in the assessee's case year after year as noted from the assessment orders of the previous years. This year as well, the assessee has earned dividend income of Rs.88,83,863/-. Therefore, the disallowance was made as per Rule 8D under sec-14A of the Act at Rs.5,04,08,572/- and deduction of disallowance made by the assessee u/s. 14A Rs. 88,83,863/- in the computation of income which comes to total disallowance as per Rule 8D at Rs.4,15,24,709/- and assessed the income of the assessee at Rs.4,37,12,090/- vide order dated 21.2.2014 passed u/s 143(3) of the Act.”

4. The enhanced disallowance was deleted by the Commission of Income Tax (Appeals) observing that the assessee had made disallowance Rs.1,04,90,253/- under Section 14 A, which was more than the exempt income of Rs.88,83,863/-. The disallowance made by the assessee being reasonable no further disallowance was necessary.

5. The Tribunal, vide impugned order, has upheld the findings recorded by the Commission of Income Tax (Appeals).

6. This appeal has no merit as Assessing Officer had not recorded necessary and required satisfaction, in terms of sub section (2) to Section 14A of the Act for invoking Rule 8D making the addition of Rs.4,15,24,709/-. Rule 8D is not mandatory and would come into play only when the Assessing Officer comes to the conclusion and records his satisfaction that he was not satisfied with the correctness of the disallowance made by the assessee, having regard to the accounts placed before him. This is a necessary and mandatory precondition for the Assessing Officer to invoke and apply Rule 8D of the Rules. Thus, Rule 8D cannot be applied unless this satisfaction is recorded by the Assessing Officer. This is clear and lucid from the judgment of the Supreme Court in ***Godrej & Boyce Manufacturing Company Ltd. versus Deputy Commissioner of Income Tax***, (2017) 394 ITR 449 in which it has been observed as under :-

“37. We do not see how in the aforesaid fact situation a different view could have been taken for the Assessment Year 2002-2003. Sub-sections (2) and (3) of [Section 14A](#) of the Act read with Rule 8D of the Rules merely prescribe a formula for determination of expenditure incurred in relation to income which does not form part of the total income under the Act in a

situation where the Assessing Officer is not satisfied with the claim of the assessee. Whether such determination is to be made on application of the formula prescribed under Rule 8D or in the best judgment of the Assessing Officer, what the law postulates is the requirement of a satisfaction in the Assessing Officer that having regard to the accounts of the assessee, as placed before him, it is not possible to generate the requisite satisfaction with regard to the correctness of the claim of the assessee. It is only thereafter that the provisions of [Section 14A\(2\)](#) and (3) read with Rule 8D of the Rules or a best judgment determination, as earlier prevailing, would become applicable.”

7. In the present case the Assessing Officer has not recorded his satisfaction regarding the correctness of the self disallowance made by the assessee under Section 14A, as is mandatory in terms of sub section (2) of Section 14A of the Act to invoke and take recourse to Rule 8D of the Rules. Thus, the Assessing Officer, did not act as per and in terms of the statute.

8. In view of the aforesaid position, appeal by the Revenue must fail and is accordingly dismissed without any order as to costs.

SANJIV KHANNA, J

CHANDER SHEKHAR, J

SEPTEMBER 07, 2018/PB