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

+ **ITA 1467/2018**

Date of decision: 18th December, 2018

THE PR. COMMISSIONER OF INCOME TAX-9 Appellant

Through: Mr. Ruchir Bhatia, Sr. Standing
Counsel with Mr. Sanampreet Singh,
Adv.

Versus

VEDANTA LIMITED. Respondent

Through: Mr. Sachit Jolly and Mr. Siddharth
Joshi, Advs.

CORAM:

HON'BLE MR. JUSTICE SANJIV KHANNA

HON'BLE MR. JUSTICE ANUP JAIRAM BHAMBHANI

SANJIV KHANNA, J. (ORAL)

CM APPL. 53243/2018(for condonation of delay) in ITA 1467/2018

This is an application for condonation of delay of 59 days in filing of the appeal. The application is not opposed by counsel for the respondent. Accordingly the application is allowed and delay is condoned.

ITA 1467/2018

This appeal by the Revenue under Section 260A of the Income-tax Act 1961 (for short 'Act') in the case of Vedanta Ltd (Formerly known as Madras Aluminium Co. Ltd.) relates to the assessment year 2010-2011 and arises from the order dated 10th April, 2018 passed by the Income-Tax Appellate Tribunal ('Tribunal', for short).

2. The issue raised by the Revenue relates to the disallowance under Section 14A of the Act. It is an accepted and admitted position that the respondent assessee had earned dividend income of Rs.8.97 crores which was exempted under Section 10(34) of the Act. The said dividend was paid by group companies. The assessee had made self disallowance of Rs. 9,07,453/-.

3. The assessing officer, without examining and referring to the disallowance or recording his dissatisfaction on disallowance made, had invoked and applied Rule 8D of the Income Tax rules, 1962('Rules', for short) as if it was mandatory. This is clear from the relevant portion of the assessment order under the heading expenditure incurred in relation to income not includible in total income under section 14A read with Rule 8D, which for the sake of completeness and clarity is reproduced below:-

“The assessee company filed its return electronically on 28.09.2010 admitting an income of Rs. 81,99,030/- under normal computation and Rs. 168,14,36,980/- u/s 115B of the Act, The return was e-processed U/s 143(1) of the I.T. Act. The case was selected for scrutiny and notice u/s 143(2) of the I.T. Act was issued on 29.08.2011 which was duly served on the assessee company on 06.09.2011.

In response to the above notice and subsequent hearing notice, Sh. Rajkumar Bashak, authorized representative of the assessee company attended from time to time and produced books of account and other details called for. The books of account and details produced were examined.

The assessee company has income from business and income from Short Term Capital Gains during the financial year. The assessee had also claimed

deduction u/s 80IA of the I.T. Act on the income generated from eligible unit limited to business income. It is further observed during the examination of books of account that the assessee had not worked out deduction as per Section 14A read with Rule 8D with regard to the expenditure in relation to dividend income on which exemption u/s 10(34) has been claimed. Therefore, the total income as per regular computation has been assessed as follows:-

Expenditure Incurred In Relation To Income Not Includible In Total Income Under Section 14A Read With Rule 8D:-

(i)	<i>Direct Expenditure</i>	<i>Rs. 9,07,453/-</i>
(ii)	<i>Interest Expenditure to the extent not directly attributable to any particular Income(A)</i>	<i>Rs.12,26,00,000</i>
	<u>Average Value of Investment (B)</u>	
	<i>Average value of investment in exempted income as Per the balance sheet as on 01.04.2009 and 31.03.2010</i>	
	<i>Investment in exempted income as on 01.04.2009</i>	<i>Rs. 72,91.40.000/-</i>
	<i>Investment in exempted income as on 31.03.2010</i>	<i>Rs. 107,03,70,000/-</i>
	<i>Total</i>	<i>Rs. 179,95,10,000/-</i>
	<u>Average Value of Investment (B)</u>	
	<u>Average Value of Total Assests(C)</u>	
	<i>Value of total assets as Rs. 693,77,70,000/- On 01.04.2009</i>	
	<i>Value of total assets as Rs. 756,35,60,000/- On 31.03.2010</i>	
	<i>Average Value of total assets (C)</i>	<i>Rs.1450,13,30,000</i>
		<i>Rs.725,06,650,000</i>
	<i>Therefore interest expenditure to be disallowed</i>	
	$A \times B / C = \frac{12,26,00,000 \times 89,97,55,000}{725,06,65,000}$	<i>=Rs.1,52,13,771</i>

(iii) *Half percentage of average value of Investment(B)* = Rs. 44,98,775

Aggregate of (i), (ii) and (iii)=
907453+15213771+4498775 = Rs.2,06,19,999

Therefore, audition to the tune of Rs.2,06,19,999/- is made to the income of assessee company. ”

4. The Commissioner of Income-Tax (Appeals) deleted the said addition on two accounts; firstly, he held that the Assessing Officer had failed to record his objective satisfaction whether the disallowance made by the assessee was appropriate and in accordance with law. He observed that the Assessing Officer had mechanically applied Rule 8D without recording any satisfaction for invoking the said rule. The Rule 8D can be applied only if the assessing officer is not satisfied with the correctness of the claim made by the assessee in respect of the expenditure which the assessee claims to have been incurred in relation to income which does not form part of his total income.

5. The second reason given by the Commissioner of Income-Tax (Appeals) was facts specific. He had recorded the following findings:-

“Further I found disallowance has been worked out mechanically without considering the submissions or referring to the accounts of the assessee. I have examined the annual report of the appellant and it is seen that

- As on 31st March, 2010 the appellant had the total investment in assets giving rise to tax free income at Rs. 107.03 crores and against that the appellant had own funds of Rs. 22.50 crores as share capital and Rs. 493.41 crores as reserves and surplus. Thus own funds/interest free funds amounting to Rs. 515.91 crores*

are much more as compared to investments of Rs. 107.03 crores yielding tax free income.

- Further during the current year the investments have increased from Rs. 72.91 crores as on 31.03.2009 to Rs. 107.03 crores as 31.03.2010 however there is no corresponding increase in loans. In fact loans have declined from Rs. 4.46 crores as on 31.03.2009 to Rs. 1.04 crores as on 31.03.2010. Thus it cannot be said that borrowed funds had been used to make fresh investments.
- The interest expenses of Rs. 12.26 crores debited to the profit and loss account. Out of this a sum of Rs. 12.02crores is interest paid to Tamilnadu Electricity Board and interest paid on cash credits is Rs. 8.9 lakhs. Thus, it is clear that, interest paid is used for business purposes as the bifurcation of the interest cost in the following table shows:

<i>Particulars</i>	<i>Rs. Million</i>
<i>Interest provides as per supreme Court order on Belated Payments made to Tamilnadu Electricity Board</i>	<i>120.21</i>
<i>Interest on cash credit accounts of Bank grid other misc interest</i>	<i>0.89</i>
<i>Bank Charges</i>	<i>1.50</i>
<i>Total interest considered by AO</i>	<i>122.60</i>

”

6. Commissioner of Income Tax (Appeals) on examining facts had held that the assessee had not used interest bearing funds for making investment that had yielded tax free income. He referred to decisions of different High

Courts. Reference was also made to clause (iii) to Rule 8D(2) to observe that the assessing officer had not examined the question whether the disallowance of Rs. 9,07,453/- was sufficient and in accordance with law. The final finding recorded by the Commissioner of the Income-Tax (Appeals) was:

“Thus respectfully relying of the above referred decision of Hon’ble ITAT, it is held that the rejection of appellant’s claim by A.O. u/s 14A is not as per law as no satisfaction is recorded for invoking Rule 8D and the rejection of appellant’s claim is not supported by material evidence that expenses debited to the accounts of the appellant have proximate connection with the earning of the exempt income. Therefore, the disallowance of expenses under Rule 8D(2) is not in accordance with law and is liable to be deleted.”

7. The Tribunal adopts and accepts the reasoning given by first appellate authority, holding that the findings did not call for any interference.

8. It is apparent that the Assessing Officer without examining, commenting and rejecting the disallowance made by the respondent-assessee had applied Rule 8D as compulsory and universally applicable rule where the assessee has earned exempt income. However, Rule 8D cannot be invoked and applied unless the Assessing Officer records his dissatisfaction regarding correctness of the claim made by the assessee in relation to expenditure incurred to earn exempt income. This is the mandate and pre-condition imposed by sub-section (2) to Section 14A of the Act. Rule 8D is in the nature of best judgment determination i.e. determination in default and on rejection of the explanation of the assessee in relation to expenditure

incurred to earn exempt income. Rule 8D is not applicable by default but only if and when the Assessing Officer records his satisfaction and rejects the explanation of the assessee regarding the disallowance of expenditure. In the present case the assessment order proceeds on a wrong assumption that Rule 8D would apply to all cases and is mandatory. Finding of the Tribunal affirming the order of the Commissioner of Income Tax (Appeals) is in accordance with the law.

9. Legal principle and ratio is no longer *res integra* and is settled by the judgment of the Supreme Court in ***Godrej & Boyce Manufacturing Co. Ltd. Vs. Deputy Commissioner of Income-Tax and another*** [2017] 394 ITR 449 (SC) in which it has been held as under:-

“37. We do not see how in the aforesaid fact situation a different view could have been taken for Assessment Year 2002-2003. Sub-sections (2) and (3) of Section 14-A of the Act read with Rule 8-D 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 8-D 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 Sections 14-A(2) and (3) read with Rule 8-D of the Rules or a best judgment determination, as earlier prevailing, would become applicable.”

10. As the legal issue is settled, no substantial question of law arises for consideration in the present appeal, which is dismissed.

SANJIV KHANNA, J

ANUP JAIRAM BHAMBHANI, J

DECEMBER 18, 2018/rr