IN THE HIGH COURT OF PUNJAB AND HARYANA
AT CHANDIGARH

ITA No. 436 of 2019
Date of decision: 15.1.2020

Pr. Commissioner of Income Tax-1, Ludhiana
.. Appellant

v.

M/s Rico Auto Industries Ltd.
.. Respondent

CORAM: HON'BLE MR. JUSTICE AJAY TEWARI
HON'BLE MR. JUSTICE AVNEESH JHINGAN

Present: Mr. Rajesh Katoch, Senior Standing Counsel and
Ms. Pridhi Jaswinder Sandhu, Junior Standing Counsel
for the appellant.

...

AVNEESH JHINGAN, J.

The revenue is in appeal under Section 260A of the Income Tax Act, 1961 (for short, 'the Act') against the order dated 2.5.2019 passed by the Income Tax Appellate Tribunal, Chandigarh (for short, 'the Tribunal'). Following substantial questions of law have been claimed:

"(i) Whether on the facts and circumstances of the case and in law, the Hon'ble ITAT was justified in giving directions to the A.O. to compute the disallowance only on those investments which have yielded exempt income, ignoring the clear mandate of Rule 8D 2(iii) which unambiguously computes disallowance u/s 14A equal to one half percent of the average value of investment, income from which does not or shall not form part of total income.

(ii) Whether on the facts and circumstances of the case and in law, the Hon'ble ITAT was justified in giving directions to the A.O. to compute the disallowance only on those investments which have yielded exempt income, ignoring the clear mandate of Rule 8D 2(ii) which unambiguously computes disallowance u/s 14A by taking the average of value of investment, income from which does not or shall not form part of total income as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year?"

The facts relevant for the present appeal are that the assessment year involved is 2013-14. The assessee made investments in the equity of domestic group companies, some of which yielded exempt dividends. The assessee had significant borrowed funds which were almost equal to non-interest bearing funds. The assessee itself computed disallowance of ₹3,35,66,806/- under Section 14A of the Act read with Rule 8D of the Income Tax Rules, 1962 (for short, 'the Rules'). During the assessment proceedings, the assessee contended that disallowance was inadvertent mistake, as the investments were made out of non-interest bearing funds and regular cash profit of the company. The Assessing Officer refused withdrawal of voluntary disallowance. The assessment was framed vide order dated 25.11.2016. The Commissioner of Income Tax (Appeals) [for short, 'CIT (A)'] vide order dated 23.3.2018 allowed the appeal of the assessee with regard to withdrawal of voluntary disallowance. Further, it was directed that disallowance under Section 14A of the Act read with Rule 8D of the Rules be made as per the amendment made w.e.f. 2.6.2016. The revenue preferred an appeal, the Tribunal vide order dated 2.5.2019 partly allowed the appeal and held that the amended Section 14A of the Act and Rule 8D of the Rules would not be applicable for the relevant assessment year as the amendment was prospective. However, the Assessing Officer was directed to compute disallowance on the investments which yielded exempt income. The relevant portion of the order of the Tribunal is reproduced below:

> "Regarding the ruling that the Assessing Officer shall account on those investments which have yielded exempt income, we find strength by the orders of the special Bench of ITAT in the case of Vreet Investment Pvt. Ltd. 188 TTJ 001 (Del-Trib.) and also the order in the case of Prime Property Development Corp Pvt. Ltd. in ITA No. 7402/Mum/2016 dated 16.11.2017. We direct the Assessing Officer to compute the disallowance accordingly."

The present appeal is filed raising a grievance against the direction of the Tribunal.

Learned counsel for the revenue argued that the Tribunal erred in directing to compute disallowance only considering the investments which yielded exempt income. However, he was not in a position to dispute that this Court in number of cases held that the amount of disallowance under Section 14A of the Act is to be restricted to the amount of exempt income only and not at a higher figure.

Further, the Supreme Court in **Maxopp Investment Ltd. v. Commissioner of Income Tax, New Delhi, 2018(402) ITR 640** held as under:

> "40. We note from the facts in the State Bank of Patiala cases

that the AO, while passing the assessment order, had already restricted the disallowance to the amount which was claimed as exempt income by applying the formula contained in Rule 8D of the Rules and holding that section 14A of the Act would be applicable. In spite of this exercise of apportionment of expenditure carried out by the AO, CIT(A) disallowed the entire deduction of expenditure. That view of the CIT(A) was clearly untenable and rightly set aside by the ITAT. Therefore, on facts, the Punjab and Haryana High Court has arrived at a correct conclusion by affirming the view of the ITAT, though we are not subscribing to the theory of dominant intention applied by the High Court. It is to be kept in mind that in those cases where shares are held as 'stock-in-trade', it becomes a business activity of the assessee to deal in those shares as a business proposition. Whether dividend is earned or not becomes immaterial. In fact, it would be a quirk of fate that when the investee company declared dividend, those shares are held by the assessee, though the assessee has to ultimately trade those shares by selling them to earn profits. The situation here is, therefore, different from the case like Maxopp Investment Ltd. where the assessee would continue to hold those shares as it wants to retain control over the investee company. In that case, whenever dividend is declared by the investee company that would necessarily be earned by the assessee and the assessee alone. Therefore, even at the time of investing into those shares, the assessee knows that it may generate dividend income as well and as and when such dividend income is generated that would be earned by the assessee. In contrast, where the shares are held as stock-in-trade, this may not be necessarily a situation. The main purpose is to liquidate those shares whenever the share price goes up in order to earn profits. In the result, the appeals filed by the Revenue challenging the judgment of the Punjab and Haryana High Court in State Bank of Patiala also fail, though law in this respect has been clarified hereinabove."

[Emphasis supplied]

There is no dispute raised that computation of disallowance under Section 14A of the Act and Rule 8D of the Rules would be only with regard to the amount of exempt income. In such circumstances, the direction of the Tribunal calls for no interference as it only tantamounts to remand the matter to the Assessing Officer to compute disallowance as per the law and in view of the rules applicable in the relevant year.

The appeal is dismissed.

(AVNEESH JHINGAN)
JUDGE

(AJAY TEWARI)
JUDGE

15.1.2020
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Whether speaking/reasoned: Yes/No
Whether reportable: Yes/No