

आयकर अपीलीय अधीकरण, न्यायपीठ – “वि” कोलकाता,
IN THE INCOME TAX APPELLATE TRIBUNAL “B” BENCH: KOLKATA
(समक्ष)Before श्री महावीर सिंह, न्यायीक सदस्य एवं/and श्री, सी.डी.राव लेखा सदस्य)
[Before Shri Mahavir Singh, JM & Shri C. D. Rao, AM]

आयकर अपील संख्या / I.T.A No. 47/Kol/2012

निर्धारण वर्ष / Assessment Year: 2008-09

Hindusthan Paper Corporation Ltd.
(PAN: AAACH9463K)
(अपीलार्थी/Appellant)

Vs. Deputy Commissioner of Income-tax
Circle-5, Kolkata.
(प्रत्यर्थी/Respondent)

Date of hearing: 30.05.2012

Date of pronouncement: 22.08.2012

For the Appellant: Shri D. S. Damle

For the Respondent: Shri L. K. S. Dahiya

आदेश/ORDER

Per Mahavir Singh, JM (महावीर सिंह, न्यायीक सदस्य)

This appeal by assessee is arising out of order of CIT(A)-VI, Kolkata in Appeal No. 129/CIT(A)-VI/Cir-5/10-11/Kol dated 30.09.2011. Assessment was framed by DCIT, Circle-5, Kolkata, u/s. 143(3) & 115WE(3) of the Income-tax Act, 1961 (hereinafter referred to as the “Act”) for AY 2008-09 vide his order dated 29.12.2010.

2. This only issue in this appeal of assessee is against the order of CIT(A) in confirming the disallowance of interest expenditure by invoking the provisions of section 14A of the Act read with Rule 83(2)(ii) of the Income-tax Rules, 1962 (hereinafter referred to as the “Rules”) and also Rule 8D(3) of the Rules at Rs.1,02,59,650/-. For this, assessee has raised following three effective grounds:

“1. For that on the facts and in the circumstances of the case and in law, the CIT(A) erred in upholding the disallowance of Rs.1,08,65,937/- u/s. 14A read with Rule 8D under the I. T. Act, 1961.

2. For that on the facts and in the circumstances of the case and in law, the Ld. CIT(A) failed to correctly appreciate the details and explanations furnished by the assessee in support of the claim that no expenditure had been incurred in relation to earning exempt income in terms of Section 14A of the Act and without assigning cogent reasons upheld the disallowance made by the AO.

3. For that on the facts and in the circumstances of the case and in law, the disallowance u/s. 14A of the I. T. Act be deleted and/orreduced.”

3. Brief facts leading to the above issue are that the assessee is engaged in the business of manufacturing of paper. The assessee filed its return of income on 30.09.2008. Subsequently, assessee's case was selected for scrutiny u/s. 143(2) of the Act. During the course of assessment proceedings, AO noticed from the audited accounts of the assessee that it has invested huge amount of capital in unquoted shares specially shares of subsidiary companies and earned exempted income at Rs.12.38 cr. Accordingly, AO invoked the provisions of section 14A of the Act r.w.s. Rule 8D of the Rules and made following disallowances:

"The disallowance u/s. 14A as per Rule 8D is as under:

(i) *Rule 8D(2)(ii) – axb/c*

Here, a = amount of expenditure by way of interest other than the amount of interest included in clause (i) incurred during the previous year – Rs.31,19,00,000/-.

b = the average of value of investment, income from which does not or 'shall not' form part of the total income, as appearing to the balance sheet of the assessee, on the first day and last day of the previous year – Rs.205,19,30,000/-.

c = the average of the total assets as appeared in the balance sheet of the assessee, on the first day and the last day of the previous year – Rs.10,55,26,23,500/-.

So, $a \times b/c = Rs.6,06,287/-$

(ii) *Rule 8D(iii) – An amount = 1/2% of the average of value of investment, income from which 'does not' or 'shall not' form part of the total income, as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year.*

1/2% of Rs.205,19,30,000/- = Rs.1,02,59,650/-

Therefore, total of Rs.1,08,65,937/- is considered and disallowed as expenditure related to earning of exempt income u/s. 14A, as per method provided under Rule 8D."

Aggrieved, assessee preferred appeal before CIT(A), who also confirmed the disallowance of prorata interest expenditure. The CIT(A) held that the assessee has huge investment for which there are different types of expenses incurred by it i.e. interest and other expenses. According to CIT(A), funds of the assessee are going from common kitty and there is no distinction of own funds and borrowed funds. According to CIT(A), assessee cannot take the plea that at that particular time it had its own free funds and because of that borrowed funds were not utilised for investment in shares from where exempted income was earned. The CIT(A) finally held that the transactions includes investment yielding exempted income, which are integral part of

the business of the assessee. Hence, he confirmed the addition made by AO. Aggrieved, now assessee is in appeal before us.

4. Before us Ld. Counsel for the assessee Shri D. S. Damle narrated the facts that the assessee during the year earned dividend income of Rs.12.38 cr. from shares held of its subsidiary Hindusthan Newsprint Ltd. and the same was exempted u/s. 10(33) of the Act and accordingly, the same was claimed as exempt. Ld. Counsel stated that the assessee has made investments in two subsidiaries i.e. Nagaland Pulp & Paper Co. Ltd. (NPPCL) and Hindusthan Newsprint Ltd. (HNL). He explained the background of investment made and stated that the Govt. of India nationalised loss making NPPCL brought under the administrative control of the assessee by way of subsidiary. According to him, the newsprint division was converted into its wholly owned subsidiary at the instance of Govt. of India and it functioned under the administrative control of Ministry of Industries, who required the control operations of these two subsidiary companies. According to Ld. Counsel, the Govt. exercises control over its subsidiaries through the agencies of the assessee. He narrated that even financial assistance and funding provided by the Central Govt is routed through the assessee to these two companies. Even the entire investment in these two subsidiaries was made out of capital contribution received from Govt. of India. He drew our attention to audited accounts and took us to fresh investments made at Rs.17.46 cr. with HNL. He stated the fact that the said investment was made as per advice of Govt. of India vide letter dated 8(15)/2005-PE7 dated 18.05.2006, which is enclosed at assessee's paper book at pages 6 & 7. He drew our attention to clause (2) specifically wherein it is categorically mentioned that out of the proceeds investment in HNL of Rs.718.80 cr. was made, the assessee also invested a sum of Rs.60 cr. out of its internal accruals. The relevant para 2 reads as under:

“2. The project cost of Rs.718.8 crore will be met by the Company through a term loan of Rs.500.00 crore from Banks and Financial Institutions and the balance amount of Rs.218.8 crore out of internal accruals of HPC (Rs.60.00 crore) and HNL (Rs.158.80 crore) without any budgetary support or guarantee from GOI. HNL: has paid up equity of Rs.82.54 crore against the authorised equity capital of Rs.100 crore. HPC would contribute Rs.17.46 crore towards the remaining equity. The balance assistance of Rs.42.54 crore would be given by HPC through leasing of an equipment/component to be purchased for EDP towards which lease rental would be charged by HPC from HNL.”

Ld. Counsel stated that even this fact is clear from the P&L Account drawn as on 31.03.2008 which shows that the profit after tax, which assessee earned during the year at Rs.91.83 cr. and there is sufficient profit available with the assessee to cover up the cost of fresh investment of

Rs.17.46 cr. He also drew our attention to Schedule 1A of the annual financial statement for the year ending 31st March, 2008 which shows that during FY 2007-08 the Govt. of India infused capital fund of Rs.54.60 cr. in the assessee company and this was infused in the month of September 2007. Ld. Counsel stated that it means that the assessee was having Govt. of India funds to the extent of Rs.54.60 cr. in September, 2007 and as on 31.03.2008 the profit earned during the year amounting to Rs.91.83 cr.. He stated that assuming but not accepting that the internal accruals were not utilised for making fresh investments even though the fresh capital infused by Govt. of India during September, 2007 fund had a clear nexus with the investment made during the year and subsidiary company HNL from where it earned dividend of Rs.12.38 cr. He also narrated that the cost of investment Rs.21,392.30 lacs whereas assessee's own funds available are at Rs.87981.12 lacs. In such facts, Ld. Counsel stated that there is no need for AO to make disallowance under Rule 8D(2) of the Rules as there was no nexus between borrowed funds and acquisition of investment which gives exempted income to the assessee. According to Ld. Counsel the interest expenditure of Rs,6,06,287/- disallowed and confirmed by lower authorities should be deleted in full. He also stated that administrative expenses disallowed by AO at Rs.1,02,59,650/- as alleged by AO that this expenditure is in relation to earning exempt income is preposterous and illogical. Ld. Counsel for the assessee stated that there cannot be any expenditure to earn such dividend income because the dividend is from a subsidiary company HNL and the investment was made in earlier years not in this year. He stated that for collecting dividend warrant the assessee has not to incur any expenditure reason being the dividend warrant is directly being credited to the bank of the assessee company. Even in collecting there is no expenditure incurred by assessee. In view of these facts, the Ld. Counsel for the assessee stated that the disallowance of administrative expenses however establishing any proximate cost or nexus of the same with the exempted income is without any basis. Hence, it deserves to be deleted.

5. On the other hand, the Ld. CIT, DR Shri L. K. S. Dahiya first of all relied on the orders of the lower authorities i.e. the orders of AO as well as the CIT(A). Ld. CIT, DR stated that the assessee has invested a sum of Rs.214 cr. approximately in investments i.e. in acquiring the shares of subsidiary particularly HNL whereas its own fund was to the tune of Rs.880 cr. Shri Dahiya argued that the funds of the assessee are from common kitty and there is no distinction of own funds or borrowed funds and assessee cannot take the plea that at that particular time it had its own free funds because the borrowed funds were utilised for the purpose of investment.

According to him, all the transactions including investments yielding exempted income, are integral part of the business of the assessee. Ld. CIT, DR drew our attention to the provisions of section 14A of the Act r.w.s. 8D and stated that Rule 8D applies to the relevant assessment year 2008-09 and Rule 8D has prescribed a formula where the funds are common and cannot draw distinction between the borrowed funds and assessee's own funds in that eventuality Rule 8D will be applied for computation of disallowance. The AO has adopted the same and there is no other way out to compute the disallowance except as provided in Rule 8D of the Rules. With respect to disallowance on administrative expenses, Ld. CIT, DR Shri Dahiya stated that the assessee has made huge investment rendering into crore of rupees and that also Rs.214 cr. in acquiring shares of its subsidiaries which requires a lot of advisory consultation including payment of fees, technical deliberations, strategic investment, decision by the management which has a cost. Ld. CIT, DR also relied on the decision of Hon'ble Calcutta High Court in the case of Dhanuka & Sons Vs. CIT (2011) 339 ITR 319 (Cal). He also relied on 203 Taxman 639, He also relied on the decision of Hon'ble Calcutta High Court in the case of CIT Vs. Smt. Leena Ramachandran (2011) 339 ITR 296 (Cal) and the decision of ITAT Delhi Bench in the case of Technopak Advisors (P) Ltd. Vs. Addl. CIT (2012) 50 SOT 31 (Del. Bench).

6. In reply, Ld. Counsel for the assessee Shri Damle relied on the provision of section 14A (1) and (2) of the Act wherein the provision talks of nexus of borrowed fund utilised for tax free income and in case there is no nexus the disallowance cannot be made or the provisions of section 14A read with Rule 8D of the Rules cannot be invoked. He drew our attention to Rule 8D(1) of the Rules wherein the AO's satisfaction in respect to correctness of the claim of the assessee in relation to income which does not form part of the total income is must. Ld. Counsel stated that in the present case before us neither the AO nor the CIT(A) has tried to establish any nexus of borrowed funds with the investment bearing exempted income. In such case, no disallowance can be made. Ld. Counsel for the assessee relied on the case law of Hon'ble Bombay High Court in the case of Godrej & Boyce Mfg. Co. Ltd. vs. DCIT [2010] 328 ITR 81 (Bom.).

7. We have heard rival submissions and gone through facts and circumstances of the case. We find from the P&L Account of the assessee company for the year ended 31.03.2008 that it has earned dividend from subsidiary company at Rs.12.38 cr. The assessee's investments which are declared in assessee's Balance Sheet Schedule 6, which is enclosed at assessee's paper book page 5 are as under:

SCHEDULE : 6 INVESTMENTS – AT COST		As at 31.03.2008	(Rs. In Lakh) As at 31.03.2007
Long Term Investments :			
(i)	Nagaland Pulp & Paper Company Limited 11,39,231 Equity shares of Rs.1000/- each	11,392.31	11,392.31
(ii)	Hindustan Newsprint Limited 9,99,99,900 Equity Shares of Rs.10/- each	9,999.99	8,253.99
Total		21,392.30	19,646.30

It means that during the year the assessee has made investment in acquiring shares of HNL and total investment during the year was 17.74 cr. We further find from the documents placed before us at page 6 of the assessee's paper book that this investment of Rs.17.46 cr. on the advice of Govt. of India vide letter dated 18.05.2006 as reproduced above. As per Schedule 1A of the Annual Financial Statement as on 31.03.2008 it is evident that during the FY 2007-08 Govt. of India infused capital fund of Rs.54.60 cr. in the month of September, 2007. It is also a fact that the assessee acquired shares of HNL in the month of September, 2007, it means that the fresh investment in the shape of acquiring of shares of HNL by the assessee was out of fresh capital infused by Govt. of India. As per the argument of Ld. Counsel and going through the P&L Account for the year ended 31.03.2008, we find that the profit after tax was at Rs.91.83 cr. which is also available to the assessee for making investment in purchase of shares and subsidiary HNL. These facts clearly establishes that the fresh investment in HNL by assessee was out of interest free funds and no borrowed funds were utilised. But taking the argument of Ld. CIT, DR Shri Dahiya that the funds of the assessee are going from common kitty and there is no distinction of own fund and borrowed fund and assessee cannot take the plea that at that particular time it had its own fund because borrowed funds were still there. According to Shri Dahiya, the transactions of investments yielding exempted income are integral part of the business of the assessee, but in any case, the AO has to prove the nexus between the borrowed funds and investments made by assessee for earning dividend income. Further, as regards to disallowance of administrative expenses, the assessee's contention was that there is only one dividend and which has been sent through ECS directly in the assessee's bank account by HNL. We find that the facts are clear that the dividend warrant was only one and HNL sent the dividend through banking channel i.e. through ECS and it seems that there is no expenditure involved in it. Even otherwise to substantiate that there requires same disallowance on account of pro rata interest and also administrative expenses. AO has to find

out the nexus which is the very essence for invocation of the provisions of section 14A of the Act. The relevant provision of section 14A reads as under:

“14A. ³⁸[(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.]

³⁸[(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 :]

Rule 8D(1) is also reproduced as under:

“8D. (1) Where the Assessing Officer, having regard to the accounts of the assessee of a previous year, is not satisfied with –

- (a) the correctness of the claim of expenditure made by the assessee; or*
- (b) the claim made by the assessee that no expenditure has been incurred, in relation to income which does not form part of the total income under the Act for such previous year, he shall determine the amount of expenditure in relation to such income in accordance with the provisions of sub-rule (2). “*

8. We find from the above factual and legal position, that we have already taken a view exactly on similar facts in the case of M/s. Balarampur Chini Mills Ltd. Vs. DCIT ITA No.504/K/2011 for AY 2008-09 dated 29.07.2011, wherein it is held as under:

“8. Here in the present case, there is no linkage or nexus between the funds borrowed by assessee and the impugned investments, hence, no interest expenditure can be disallowed by mechanically applying the Provisions of Rule 8D of the Rules. The assessee has explained that the share capital and reserves, that is its own funds, were utilised for the purpose of investment in shares for earning dividend income and this has not been negated by lower authorities i.e. neither CIT(A) nor AO. The assessee has explained each and every investment with sources of funds and its utilization as well as opening application of funds and closing application of funds as noted above. It is an admitted position in law that expenditure can be disallowed U/s.14A of the Act if and only if it is incurred in relation to income which does not form part of total income. From the facts of the present case, it is clear that there is no link with expenditure for earning of dividend income incurred by the assessee and once the facts are clear, no disallowance can be made by invoking rule 8D of the Rules. Neither the AO nor CIT(A) has recorded any finding that having regard to the account of the assessee, they are not satisfied with the correctness of the claim of expenditure made by assessee or the claim made by assessee that no expenditure has been incurred in relation to income which do not form part of the total income under the Act for the relevant assessment year. In the absence of any such finding, facts of the present case shows that the investment in shares was made out of own capital employed and not from borrowed funds, no disallowance on account of interest expenditure can be made by invoking rule

8D of the Rules. Accordingly, in the given facts and circumstances, we delete the addition and allow this issue of assessee's appeal."

We find from the above that the issue is squarely covered in favour of the assessee and hence, we allow the claim of assessee and this issue of assessee's appeal is allowed.

9. In the result, appeal of assessee is allowed.

10. Order pronounced in the open court on 22.08.2012.

Sd/-

Sd/-

सी.डी.राव लेखा सदस्य
(C. D. Rao)
Accountant Member

महावीर सिंह, न्यायीक सदस्य
(Mahavir Singh)
Judicial Member

(तारीख) Dated : 22nd August, 2012

वरिष्ठ निजि सचिव Jd.(Sr.P.S.)

आदेश की प्रतिलिपि अग्रेषित:- Copy of the order forwarded to:

1. अपीलार्थी/APPELLANT – Hindusthan Paper Corporation Ltd., 75C, Ruby Building, Park Street, Kolkata-700 016.
2. प्रत्यर्थी/ Respondent – DCIT, Circle-5, Kolkata.
3. आयकर कमिशनर (अपील)/ The CIT(A), Kolkata
4. आयकर कमिशनर/ CIT Kolkata
5. विभागीय प्रतिनीधी / DR, Kolkata Benches, Kolkata

सत्यापित प्रति/True Copy,

आदेशानुसार/ By order,

सहायक पंजीकार/Asstt. Registrar.