IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCHES "D", MUMBAI

BEFORE SHRI SANJAY ARORA, A. M. AND SHRI VIJAY PAL RAO, J. M.

ITA No.: 5491/Mum/2011
Assessment Year: 2008-09

Rainy Investments Pvt. Ltd. C/o. M/s. Akali and Akali, Chartered Accountants, 1/102 Vatsaladevi CHS, V. N. Purav Marg, Chunabhatti (E), Mumbai - 400 022 [PAN NO.: AACCR 6374 H]	Vs.	Asstt. Comm. of Income Tax – 9(3), Mumbai
(Appellant)		(Respondent)

Appellant by : Shri Rajrattansingh H. Akali
Respondent by : Dr. Manjunath Karkihalli

Date of hearing : 09.01.2013
Date of Pronouncement : 16.01.2013

O R D E R

Per Sanjay Arora, A.M.:

This is an Appeal by the Assessee directed against the Order by the Commissioner of Income Tax (Appeals)–20, Mumbai ('CIT(A)' for short) dated 21.06.2011, partly allowing the assessee's appeal contesting its assessment for the assessment year (A.Y.) 2008-09 u/s.143(3) of the Income Tax Act, 1961 ('the Act' hereinafter) vide order dated 30.08.2010.

2. The brief facts of the case are that the assesse-company, engaged in the business of investment in shares and securities, returned its income for the year at Rs.26,95,408/- on 27.09.2008. As the profit and loss account, filed along with, disclosed dividend income at Rs.50,000/-, which had been claimed exempt by the assessee per its return, section 14A

r.w.r. 8D was attracted. In fact, the assessee had itself made a disallowance to the extent of Rs.1,09,783/- u/s.14A. As per the Assessing Officer (A.O.), the same, however, worked out to Rs.10,30,481/- in terms of rule 8D (of the Income Tax Rules, 1962), so that he framed the assessment accordingly. The same having been since confirmed by the ld. CIT(A), the assessee is in second appeal.

3. Before us, the assessee's principal contention was that it did not dispute the invocation of section 14A r/w r. 8D, but it's application; the disallowance in the facts of the case exceeding the amount of income earned, even after its restriction to Rs.4,19,150/- by the ld. CIT(A), upon accepting the assessee's Ground No. 2 before him in view of the disallowance u/s.14A as already made by the assessee itself. With regard to the infirmity in the application of rule 8D, the ld. AR would, taking us through the relevant working, contend that the authorities below had included the amount of 'share application money' as a part of the investments yielding tax-free income while applying the proportion in terms of rule 8D (ii), as well as the appropriate percentage under rule 8D (iii), even as 'share application money' did not yield any tax-free income. On being enquired about the details of the same, the ld. AR could not show us any, conceding to the same being not on record. Again, on being questioned as to how could the 'share application money' continue from year to year, and that if there was any stipulation in law with regard to the time period by which the said offer money had to be either refunded or adjusted against the allotment of shares, he could not furnish any satisfactory answer; though, however, would show us, with reference to the assessee's submissions before the first appellate authority, that it had made a specific plea that only investments that generated tax-free income could be considered for the purpose of working out the disallowance u/s.14A r/w r. 8D, to however no finding by him.

The ld. DR, on the other hand, relied on the orders of the authorities below, stating that irrespective of the quantum of the tax-free income, the provision read with rule 8D being mandatory, would have to be applied. The ld. CIT(A) has, in any case, given appropriate relief in the matter, so that no further relief is called for.

4. We have heard the parties, and perused the material on record. Section 14A r/w r. 8D is mandatory in its application where the assessee earns income which is claimed tax-exempt, as dividend income in the instant case. In fact, there is no doubt with regard to this; the assesse itself conceding to the same before us and, besides, being engaged in the business of making investments and earning dividend income as an integral part thereof. The only option, therefore, if it considers the application of the provision as operating to its detriment, is to forfeit its right to exemption from tax in its respect.

Qua merits, we find much force in the assessee's argument that 'share application money', to the extent it is actually so, so that it only represents amount/s paid by way of application for allotment of shares, the same cannot be regarded as an investment in shares, or an asset (or asset class) yielding tax-free income, and neither is it capable of yielding any tax-free income. The same would, therefore, in our clear view, have to be excluded in working out the disallowance u/r. 8D. Further, though the Revenue has not disputed the sums reflected as 'share application money' in the assessee's balance-sheet, the AO, to whom the matter is to be in any case restored for working out the disallowance by excluding the same, shall, in the set aside proceedings, also examine the veracity of the assessee's claim with regard to the same being 'share application money'. This is in view of the pertinent questions raised by the Bench in its respect, to which no satisfactory answer was forthcoming during hearing, nor – to be fair to the ld. AR, could possibly be in the absence of any details on record. We state so as the 'share application money' would ordinarily only be 'public money' and, thus, except perhaps where toward shares of private limited companies, subject to stringent procedure, as is generally in place for such funds. We may further clarify that the exclusion of 'share application money', as opined by us, is not in the least for the reason that it did not yield any tax-free income for the relevant year, but for the reason that it is incapable of any such income. The same is only in the nature of application (offer) money, which would though, on allotment, get adjusted against the cost of the said shares, and only whereupon any rights in the investee company inure to the allottee. No rights, not even inchoate, in the share capital of the issuing company arise on the payment of the share application money, irrespective of the

time period for which it may outstand. The same may at best yield interest income (for which a special procedure though has to be followed by the company concerned), which is in any case taxable, so that there is no scope for application of sec. 14A thereon.

As such, upon verification of the assessee's claim with regard to the share application money as on 31.03.2007 and 31.03.2008, as appearing in its balance-sheet/books of account, so that no shares had actually been allotted in its respect as at the relevant dates, the same shall be excluded by the AO from the qualifying amount in reckoning the average investment in working out the disallowance under rules 8D (ii) and 8D(iii). The A.O. will decide the matter per a speaking order, allowing the assessee a reasonable opportunity to present its case before him.

We may further clarify that we having, subject to the necessary verification, accepted the assessee's said contention, and no other infirmity in the application of rule 8D having been brought to our notice, the A.O. shall restrict the disallowance u/s.14A to the amount so determined. The assesse shall, nevertheless, be at liberty to withdraw its claim for exemption u/s. 10 on the dividend income, in which case, there is no scope for application of s. 14A and, consequently, of any disallowance being made with reference thereto. We decide accordingly.

5. In the result, the assessee's appeal is allowed for statistical purposes.

Order pronounced on this 16th day of January, 2013

Sd/-	Sd/-
(VIJAY PAL RAO) JUDICIAL MEMBER	(SANJAY ARORA) ACCOUNTANT MEMBER

MUMBAI, Dated: 16.01.2013

Copy forwarded to:

1. The Appellant.
2. The Respondent.
3. The C.I.T.
4. CIT (A)
5. The DR, 'D' Bench, ITAT, Mumbai

BY ORDER

ASSISTANT REGISTRAR
ITAT, Mumbai Benches, Mumbai

Roshani