IN THE INCOME TAX APPELLATE TRIBUNAL
AHMEDABAD "**B**" BENCH*AHMEDABAD*

आयकरअपीलीयअधिकरण, अहमदाबादन्यायपीठ'बी'

Before: ShriAnil Chaturvedi, Accountant Member
ShriKul Bharat, Judicial Member

ITA No. 2120/Ahd/2011 Assessment Year :2008-09

The ACIT, Circle-4, Ahmedabad, Navjivan Trust Bldg., Off. Ashram Road, Ahmedabad.	**V/s.**	HariOrgochem Pvt. Ltd. 1, Avadh Apartment, Nr. Parimal Railway Crossing, Paldi, Ahmedabad - 380007
(Appellant)	..	(Respondent)

AND

C.O. No. 197/Ahd/2011 Assessment Year :2008-09

HariOrgochem Pvt. Ltd. 1, Avadh Apartment, Nr. Parimal Railway Crossing, Paldi, Ahmedabad - 380007	**V/s.**	Dy. CIT, Circle – 4, Ahmedabad
PAN No. AAACH7088L		
(Appellant)	..	(Respondent)

राजस्वकीओरसे/By Revenue	ShriNarendra Singh,Sr. D.R.
आवेदककीओरसे/By Assessee	Shri P. M. Mehta with Shri G. M. Thakor, A.R.
सुनवाईकीतारीख/Date of Hearing	28.08.2015
घोषणाकीतारीख/Date of Pronouncement	30.09.2015

O R D E R

PER : Kul Bharat, Judicial Member

Both the Revenue and assessee have challenged the order of CIT(A)-VIII, Ahmedabad, dated 15.06.2011 pertaining to assessment year 2008-09 by filing appeal and Cross Objection respectively. Both the appeal and Cross Objection are taken up together and are being disposed of by way of this consolidated order for the sake of convenience.

2. First we take up the Revenue's appeal in ITA No.2120/Ahd/2011.

3. Briefly stated facts are that the case of the assessee was taken up for scrutiny assessment and the assessment u/s.143(3) of the Income Tax Act, 1961 (hereinafter referred to as 'the Act') was framed vide order dated 24.12.2010. While framing assessment, the Assessing Officer (AO in short) made disallowance of Rs.8,61,908/- by applying Rule 8D of the Income Tax Rules, 1962, disallowance of fees and legal expenditure of Rs.12,00,000/- and disallowance on employees contribution to Provident Fund amounting to Rs.2,23,715/-. Assessing Officer also rejected the book profit adopted by the assessee and adopted the same at Rs.5,44,57,207/-.

4. Assessee feeling aggrieved by the order of the Assessing Officer, preferred an appeal before the ld. CIT(A), who after considering the submissions of the assessee partly allowed the appeal thereby the ld. CIT(A) confirmed the addition. In respect of disallowance of Rs.12 lacs, the ld. CIT(A) deleted on the ground that the disallowance was merely on the basis of presumption and in respect of the disallowance of employees contribution deleted the addition. In respect of book profit, the ld. CIT(A) deleted the addition.

5. Now, both the Revenue and the assessee have challenged the order.

6. The first ground of deletion of addition of Rs.12 lacs made on account of disallowance out of fees and legal expenses. Ld. Sr. D.R., Shri Narendra Singh vehemently argued that ld. CIT(A) was not justified in deleting the addition. He submitted that the Assessing Officer had given finding on the basis of that payments have been recently introduced. The agreement between the two concerns under the same management is loosely worded and does not have any outlined detailed nature, purpose and justification of the amount in question. He submitted that the Assessing Officer has observed that assessee has not submitted any detail of services rendered by the employees other than mentioning in general that the secretarial work of the company has increased. Further, it has also not been evidenced that the employees are solely at the disposal of the assessee company. On the contrary, ld. Counsel for the assessee submitted that the finding of the Assessing Officer is misplaced. Ld. Counsel reiterated the submissions as were made before the CIT(A).

7. We have heard the rival contentions and perused the material available on record. We find that the ld. CIT(A) has decided the issue in para-5.2 by observing as under:

> *"5.2 I have carefully considered the Assessment Order, finding of Assessing Officer and the submission of the Appellant. The Assessing Officer has disallowed 50% of fees and legal expenses paid by Appellant to DCPL mainly on the ground that payment is to related concern and said related company is incurring loss hence payment made by Appellant is excessive. The Appellant both at the time of assessment proceedings and appellate proceedings submitted Moll entered between both the parties and submitted that as production of current Assessment Year has been increased as well as it required more persons for legal and secretarial work, some of the employees referred herein above have worked for Appellant Company for which it has made payment of Rs. 1 lacs per month. In the present case, Assessing Officer has never denied that appellant has not used the services of employees and considering it, AO has allowed 50% of payment made by Appellant. Even DCPL is making payment of round about Rs. 1.75 lacs to 1.80 lacs to persons used by Appellant for DCPL has charged Rs. 2 per month which cannot be termed as excessive, more particularly when Assessing Officer has not disputed the work carried out by such persons. Similar disallowance was*

made in A.Y. 2007-08 and in appeal, vide my order dated 22nd October, 2010 in Appeal No. CIT(A)-VIII/DC-4/749/09-10 I have deleted disallowance made by the Assessing Officer. Considering this, the disallowance made by Assessing Officer on presumption is not justified and it is deleted and related ground of appeal is allowed."

7.1. The Assessing Officer made disallowance on the basis that the payments have been recently introduced. The agreement between two concerns under the same management is loosely worded and does not have any outlined detailed nature, purpose and justification of the amount in question. Further, the Assessing Officer observed that no supporting evidence has been placed on record. Service rendered by aforesaid employees of Dharnidhar Chemicals Pvt. Ltd. and proceeded to hold that the fees for services of the employees of the Dharnidhar Chemicals Pvt. Ltd. as excessive by 50% of the amount paid to the associate concern of the assessee was disallowed and added back to the total income of the assessee. However, the ld. CIT(A) deleted the same on the basis that in earlier year similar disallowance was made and predecessor of the CIT(A) in A.Y. 2007-08 had deleted the disallowance. This fact has not been disputed by the Revenue. Ld. Counsel for the assessee had pointed out that the co-ordinate Bench of this Tribunal in ITA No. 45/Ahd/2011 has confirmed the finding of the ld. CIT(A). We find that the co-ordinate Bench in ITA No. 45/Ahd/2011 for A.Y. 2007-08 has confirmed the order of ld. CIT(A) in para 13 by observing as under:

"13. We find that no specific mistake in the findings of the Ld.CIT(A) could be pointed out by the Ld. DR. We find that the genuineness of the payment is not in dispute. The Assessing Officer after observing about the loss incurred by the assessee company has brought no material on record after making investigation to show that the assessee has not received the services for which payments were made by the assessee. Rather, on the other hand, the allowance »f deduction at the rate of 50% shows that the Assessing Officer also agreed that services of the staff of the payee company were utilized by the assessee company for its business purpose. No material was brought on record to show that the consideration for services received by the assessee was so excessive as to warrant any disallowance out of the same. It is also observed that the amount of consideration paid was as per Memorandum of Understanding entered into by the assessee with the payee company. In view of the above facts and circumstances, we do not find any good reason to interfere with the order of the Ld.CIT(A), hence this ground of appeal of the Revenue is dismissed."

7.2 The revenue has not pointed out any change into facts and circumstances. Therefore, taking a consistent view, this ground of Revenue's appeal is rejected and the order of the ld. CIT(A) is confirmed.

8. Ground no.2 is against deletion of addition of Rs.2,23,705/- on account of disallowance of employees contribution to Provident Fund u/s.36(1)(via). Ld. Counsel for the assessee fairly conceded that this issue has been decided against the assessee in A.Y. 2007-08 by co-ordinate Bench in ITA No. 45/Ahd/2011. We find that co-ordinate Bench at para 18 has decided the issue by following the judgment of Hon'ble Gujarat High Court in case of CIT vs. Gujarat State Road Transport Corporation as under:

> *"18. The Ld. DR filed before us copy of the order of Hon'ble Gujarat High Court in the case of CIT Vs. Gujarat State Road Transport Corporation (2014) 41 taxmann.com 100 (Guj.) and submitted that the Hon'ble High Court has held that with respect to the sum received by the assessee firm from any of his employees to which provisions of sub-clause (x) of clause (24) of section (2) applies, the assessee shall be entitled to deduction in computing the income referred to in section 28 with respect to such sum credited by the assessee to the employees' account in the relevant fund or funds on or before the "due date" mentioned in explanation to section 36(1)(va)."*

8.1. Therefore, following the judgment of Hon'ble Gujarat High Court and the decision of the co-ordinate Bench, we hereby set aside the order of ld. CIT(A) on this issue and confirmed the order of Assessing Officer. This ground o Revenue's appeal is allowed.

9. Ground nos. 3 & 4 are general in nature need no separate adjudication.

10. In the result, appeal of the Revenue is partly allowed.

11. Now, we take up the assessee's C.O. No. 197/Ahd/2011 (arising out of ITA No.2120/Ahd/2011 – Revenue's appeal).

11.1 The concised grounds raised in Cross Objection are as under:

> *1. In law and in the facts and circumstances of the respondent's case, the Ld. CIT(A) erred in confirming the disallowance u/s.14A read with Rule 8D for*

Rs.7,61,9087-, when no such disallowance is called for. He ought to have deleted the entire addition of Rs.8,61,908/-.

2. *In law and in the facts and circumstances of the respondent's case, the Ld. CIT(A) erred in solely relying on the decision of Godrej & Boyce Manufacturing Co. Ltd. vs. DCIT and Another, by not considering the ratio laid down by other judicial pronouncements available on the issue on which the appellant had relied. In view of the various judicial pronouncements cited by the appellant before the CIT(A), the confirmation of addition of Rs.7,61,9087- made by him U/S.14A r.w. Rule 8D, deserves to be deleted.*

3. *The respondent craves leave to add, alter, amend and/or withdraw any ground or grounds either before or during the course of hearing of the appeal.*

12. The only effective ground is against the confirmation of disallowance made u/s.14A read with Rule 8D of Rs.7,61,908/-. Ld. Counsel for the assessee submitted that authorities below were not justified in making disallowance and confirming the same. Ld. Counsel for the assessee reiterated the submissions made in the statement of fact-cum-synopsis. Ld. Counsel for the assessee submitted that the assessee was having sufficient interest free funds. On the contrary, ld. Sr. D.R. supported the order of the authorities below and submitted that there is no infirmity into the order of the authorities below.

13. We have heard rival contentions and perused the material on record. We find that the contentions of the assessee against the disallowance as submitted in statement of facts-cum-synopsis are as under:

"1. The brief facts of the case giving rise to the present cross-objections are that the Assessing Officer made following three disallowances in his order passed u/s. 143(3) of the Act:-

(i) Disallowance u/s. 14A r.w. Rule 8D	*8,61,908*
(ii) Disallowance of fees & legal Expn.	*12,00,000*
(iii) Disallowance u/s.36(1)(va)	*2,23,715*

1.1 The Ld.CIT(A) has confirmed the disallowance made u/s.14A amounting to Rs.7,61,908 by solely relying on the decision of Godrej & Boyce Mfg. Co. Ltd. vs. DCIT and Another. However, he deleted the administrative expenses of Rs.1,00,000 already shown by the appellant relating to its investments in shares and Mutual funds etc.

2. *As regards the disallowance made u/s.14A, at the very outset, the appellant would like to submit that provisions of sec.14A provide that no deduction shall*

be made in respect of expenditure incurred by the assessee in relation to income which does not form the part of the total income. For better appreciation of the legal position, the relevant parts of section 14A are reproduced below:-

"Expenditure incurred in relation to income not includible in total income.

14A.[(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.]***

[(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"

[Emphasis supplied]

From perusal of the above, it can be inferred that section 14A is applicable only when:

(i) The taxpayer generates an income which is exempt from tax.
(ii) For earning such income some expenditure has been incurred.
(iii) Provisions of Rule 8D can be invoked only when having regard to the accounts of the assessee, the Assessing Officer is not satisfied with the correctness of the claim of assessee in respect of such expenditure.

In the above context, the appellant would like to submit that the impugned disallowance of expenditure was made by the Assessing Officer, which was confirmed by the Ld. CIT(A), by simply assuming that the appellant had incurred some expenditure to earn exempt income, however, while doing so, he has failed to establish a pre-requisite nexus between the expenditure disallowed and the investments made from which the income derived is exempt from tax. In such circumstances, it is most respectfully submitted that there cannot be any presumption that the borrowings were made for the purpose of making investments. Further, as required in Clause (2) of Sec. 14A, the Assessing Officer has not recorded any proper satisfaction about the correctness of the claim in respect of such expenditure. The Assessing Officer had even failed to acknowledge the fact of incurring of administrative expenses of Rs.1,00,000 shown by the appellant.

3. ***In the case of Godrej & Boyce Mfg. Co. Ltd. V/s. DCIT – 43DTR 178 (2010)*** *- the Hon. Bombay High Court in paras 24 & 25 of their judgment had explained the scope of applicability of Sub-s. (2) of Sec.14A of the Act in*

detail; the relevant extracts of which are reproduced here below for better appreciation of the facts:-

"What merits emphasis is that the jurisdiction of the AO to determine the expenditure incurred in relation to such income which does not form part of the total income, in accordance with the prescribed method, arises if the AO is not satisfied with the correctness of the claim of the assessee in respect of the expenditure which the assessee claims to have incurred in relation to income which does not form part of the total income. Moreover, the satisfaction of the AO has to be arrived at, having regard to the accounts of the assessee. ***Hence, sub-s.(2) does not ipso facto enable the AO to apply the method prescribed by the rules straightaway without considering whether the claim made by the assessee in respect of the expenditure incurred in relation to income which does not form part of the total income is correct.*** *The AO must, in the first instance, determine whether the claim of the assessee in that regard is correct and the determination must be made having regard to the accounts of the assessee.* ***The satisfaction of the AO must be arrived at on an objective basis.*** *It is only when the AO is not satisfied with the claim of the assessee, that the legislature directs him to follow the method that may be prescribed."*

[Emphasis supplied]

3.1 From perusal of the aforesaid observations of the Hon. Mumbai High Court, it would be seen that Sub-s. (2) of sec.14A does not ipso facto enable the AO to apply the method prescribed by the Rule straightaway without considering whether the claim made by the assessee in respect of the expenditure incurred in relation to income which does not form part of the total income is correct. The satisfaction of the Assessing Officer must be arrived at on the objective basis. In the light of the aforesaid observation of the court, it would be seen that the Ld.CIT(A) casually followed the decision of Mumbai High Court cited supra without considering the detailed observations given in the judgment. In fact, the aforesaid Mumbai High Court decision is normally quoted and relied upon in the following two areas:-

(i) ***The provisions of Sub-ss. (2) & (3) of Sec. 14A are constitutionally valid*** *and the provisions of Rule 8D of the IT. Rules are not ultra-virus the provisions of Sec.14A and do not offend Article 14 of the Constitution;*

(ii) The provisions of Rule 8D of the I.T. Rules which have been notified with the effect from 24th March 2008 shall apply w.e.f. A.Y. 2008-09 and not prior to that.

4. The appellant submits that various courts have been taking a consistent view that disallowance u/s.14A can be made only if there is an actual nexus between tax-free income and expenditure incurred on the same. In this connection reliance may be placed on the following judicial pronouncements:-

1. CIT vs. Hero Cycles Ltd. [2010] 189 Taxman 50 (P & H High Court)

Even under Rule 8D of S. 14A, disallowance can be made only if there is actual nexus between tax-free income and expenditure

The assessee earned dividend income on shares which was exempt from tax. The AO took the view that the investment in shares was made out of borrowed funds on which interest expenditure was incurred and consequently made a disallowance u/s 14A. This was partly upheld by the CIT (A). On further appeal by the assessee, the Tribunal deleted the disallowance by noting that ***the assessee had proved that the investment in shares was made out of non-interest bearing funds. It held that unless there was evidence to show that the interest - bearing funds had been invested in the tax - free investments and the nexus was established by the Revenue, s. 14A could not be applied on mere presumption.*** *The Revenue appealed to the High Court and claimed that in view of* ***s. 14A (2) and Rule 8D (1) (b), a disallowance could be made even if the assessee claimed that no expenditure had been incurred in respect of the tax - free income.*** *HELD, dismissing the appeal:*

(i) If the investment in the shares is out of the non-interest bearing funds, disallowance u/s 14A is not sustainable;

(ii) The contention of the revenue that directly or indirectly some expenditure is always incurred which must be disallowed u/s 14A cannot be accepted;

(iii) ***Disallowance u/s 14A requires a finding of incurring of expenditure. If it is found that for earning exempted income no expenditure has been incurred, disallowance u/s 14A cannot stand;***

[Emphasis supplied]

2. Maruti Udhyog Limited Vs. DCIT 92 ITD 119 (Delhi IT AT)

From the Head Notes:

Section 14A, read with section 36(1)(iii) of the Income-tax Act, 1961 - Expenditure incurred in relation to income not includible in total income - Assessment year 1999-2000 - Assessee had paid interest to certain parties on advances, deposits, etc. - It had also invested in shares yielding tax-free income -Assessing Officer, relying on section 14A, calculated interest on total investment in shares and made disallowance -Commissioner (Appeals) also held that there was direct nexus between funds borrowed and investment in shares yielding tax-free income but, made disallowance on day to day working product method ***- Whether nexus between borrowed funds and investment can be said to be established only where it is shown that interest free fund are not available with assessee - Held, yes - Whether since Commissioner(Appeals) had merely picked up sources on which interest was paid by assessee and had completely ignored other***

sources and further that interest free funds were available to assessee for making investment which far exceeded investment in shares order of Commissioner (Appeals) was to be set aside and, addition was to be deleted - Held, yes.

[Emphasis supplied]

On perusal of the above judicial decisions , it may be concluded that It ***is the onus of the Assessing Officer to establish a nexus between the expenditure incurred and the source of exempt income, in the event he wants to disallow u/s 14A of the Income Tax Act, 1961.*** *In the facts of the case, no nexus whatsoever has been established by the Assessing Officer. Thus, disallowance made by assessing officer u/s 14A requires to be deleted.*

5. ***Without prejudice to what is stated herein above,*** *and with regard to disallowance of interest expenditure, the appellant submits that appellant has got following interest-free funds available with it to cover investments made in shares and mutual funds:*

Share Capital	*:*	*Rs. 32,00,200*
Reserve & Surpluses	*:*	*Rs. 28.38,41,330*
Total	*:*	*Rs. 28,70,41,530*

It can be seen from aforesaid details that as appellant had sufficient interest free funds, proportionate disallowance of interest expenditure is not justified. Reliance is placed on the ratio of ***Hon'ble Supreme Court's decision in case of Munjal Sales Corporation V/s Commissioner of Income-Tax 298ITR 298****; wherein the Apex Court has observed that the assessee had advanced interest free loan to its sister concern amounting to Rs.5,00,000/-; whereas the opening balance of interest free funds as on 1 April, 1994 was Rs.1.91 crores, which is sufficient to cover the impugned loan of Rs.5 lacs. Hence, there cannot be any disallowance of interest under Section 36(1)(iii) of the Act. Apart from above, following decisions also support the case of assessee:*

(i) Torrent Financiers Vs. ACIT 73 TTJ 624, Ahmedabad;
(ii) CIT Vs. Radico Khaitan Limited 142 Taxman 681, Allahabad High Court

5.1 The appellant also relies on the following decisions in support of its claim that no disallowance u/s 14A is required to be made as far as interest expenditure is concerned.

(a) Decision of the Bombay High Court in CIT v. Reliance Utilities and Power Ltd. (313 ITR 340):

From the Head Notes:

"INTEREST ON BORROWED CAPITAL — ***INVESTMENTS BY APPELLANT — FINDING THAT INVESTMENTS WERE FROM INTEREST-FREE FUNDS AVAILABLE WITH APPELLANT —***

BORROWED CAPITAL USED FOR PURPOSES OF BUSINESS — INTEREST DEDUCTIBLE— INCOME-TAX ACT, 1961, S.36(1)(iii).

The appellant claimed deduction of interest on borrowed capital. The Assessing Officer recorded a finding that the sum of Rs. 213 crores was invested out of its own funds and Rs. 147 crores was invested out of borrowed funds. Accordingly he disallowed interest amounting to Rs. 4.40 crores calculated at 12 per cent per annum for three months from January, 2000 to March, 2000. ***The Commissioner (Appeals) found that the appellant had enough interest-free funds at its disposal for investment and accordingly deleted the addition of Rs. 4.40 cores made by the Assessing Officer*** *and directed him to allow the deduction under section 36(1)(iii).* ***The order of the Commissioner (Appeals) was upheld by the Tribunal. On appeal to the High Court:***

Held, dismissing the appeal, ***that if there were funds available both interest-free and overdraft and/or loans taken, then a presumption would arise that investments would be out of the interest-free funds generated or available with the company, if the interest-free funds were sufficient to meet the investments.*** *In this case this presumption was established considering the finding of fact both by the Commissioner (Appeals) and the Tribunal. The interest was deductible.*

EAST INDIA PHARMACEUTICAL WORKS LTD. v. CIT [1997] 224 ITR 627 (SC) and WOOLCOMBERS OF INDIA LTD. v. CIT [1982] 134 ITR 219 (Cat) relied on."

[Emphasis supplied]

(b) *Decision of the ITAT,* ***Ahmedabad, in ACIT v Hipolin Ltd. (ITA No. 4259/Ahd/2007):***

"2. The brief facts of the case are that the appellant is engaged in the business of manufacturing of washing powder, detergent cakes, tooth paste, etc. in the name of 'Hipolin'. During the year under consideration, the Assessing Officer found that the appellant claimed interest of Rs.16.78 lacs as bank charges. The Assessing Officer, further, found that the appellant has shown investment of Rs. 26, 71,053/- as on 31-03-2004 as compared to Rs.19, 49,725/- as on 31/03/2003. Thus, the appellant has made new investment of Rs. 7,21,238/- in shares. The dividend income on the above mentioned investment was examined. The Assessing Officer sought to disallow proportionate interest out of the interest claimed. ***It was explained to the Assessing Officer that the appellant has made investment in shares out of the huge interest-free funds available in the form of paid upshare capital and accumulated reserves****. The total investment in shares is less than 1% of the said interest-free funds. The Assessing Officer, however, did not agree with the appellant and disallowed proportionate expenses which amounted to Rs.53,027/- which included interest of Rs.9,403/- and administrative expenses of Rs.43,624/-.*

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6. On the other hand, the Learned Authorised Representative of the appellant submitted that the Hon'ble Bombay High Court in the case of CIT vs. Reliance Utilities Power Ltd. 313 ITR 340 (Bom) has held that ***it has to be first presumed that the investment were made out of interest-free funds available with the appellant. Therefore, no disallowance is called for****. It is an undisputed fact that the appellant has substantiate share capital and reserves. Therefore, it cannot be said that investments in shares were made out of interest bearing funds. After hearing the parties, we decline to interfere with the order of the Learned CIT (Appeals), which is confirmed. Hence, this ground of Revenue is dismissed."*

[Emphasis supplied]

5.2 Apart from above, Assessee submits that as against interest expenditure of Rs. 2,25,918, it has earned interest income of Rs. 10,65,299 and as interest income being in excess of expenditure, no disallowance under Section 14A is required for proportionate interest expenditure.

6. With regard to ***disallowance of administrative expenditure u/s.14A****, it is submitted that administrative expenditure incurred during the current year are mainly for the purpose of assessee's main business. However,* ***in all fairness, the appellant itself has shown Rs.1,00,000 expenditure incurred in investments made by it in the shares and mutual funds*** *and the income earned there from. In fact, the Ld.CIT(A) has not negativated the claim of the appellant relating to expenses of Rs. 1,00,000. Not only this, the Assessing Officer has not challenged the correctness of the said claim with facts & figures and the Ld.CIT(A) has also considered the said expenditure of Rs.1,00,000 and deleted to the above extent, out of the addition of Rs.8,61,908, which resulted into confirmation of addition of Rs.7,61,908. Here the Assessing Officer was required to find out and quantify the expenses incurred by the appellant for earning exempted income by establishing a proper nexus between the two. In fact, there was no need of application of Rule 8D, as the appellant had already shown the administrative expenditure incurred during the year at Rs.1,00,000. The appellant relies on the following two decisions available on the matter-*

(1) Decision of Third Member division of Delhi ITAT in case of Wimco Seedlings Vs. DCIT 109 TTJ 462;

(2) Decision of Delhi ITAT in case of Malwa Investments Limited Vs. DICT 3 DTR 455

Considering this, no disallowance of administrative expenses is justified.

7. As regards the Grounds of Appeal taken by the Department against the deletion of the addition of Rs.12,00,000 made on account of disallowance out of fees and legal expenses, and deletion of the addition of Rs.2,23,715 made by the Assessing Officer on account of disallowance of employees' contribution to Provident Fund u/s. 36(1)(va) of the Act, the appellant would file a detailed reply at the time of hearing of the appeal before your honour.

8. In the light of the factual and legal position brought out above, it is prayed that the disallowance of Rs.7,61,908confirmed by the CIT(A) may kindly be deleted and the Grounds of Appeal raised by the Department against the relief given by the CIT(A) to appellant may kindly be dismissed."

13.1 The Assessing Officer made disallowance by invoking the provisions of Section 14A r.w. Rule 8D of the Income Tax Rules. As per assessee, the AO has not established any nexus between the expenditure disallowed and investment made from which the income denied is exempt from tax. Secondly, the AO has not recorded any proper satisfaction about the correctness of the claim in respect of such expenditure. There is no dispute with regard to the fact that the assessment year under appeal being 2008-2009, therefore, any disallowance u/s.14A would be in accordance with the method prescribed under Rule 8 D of the Income Tax Rules, 1962. For the sake of clarity, the relevant provisions of section 14A are reproduced hereinbelow:

Section-14A :- Expenditure incurred in relation to income not includible in total income.

[(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:]

[Provided that nothing contained in this section shall empower the Assessing Officer either to reassess under section 147 or pass an order enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee under section 154, for any assessment year beginning on or before the 1st day of April, 2001.]

[(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.]

13.2. From the conjoint reading of the above provision, it is evident that making of disallowance by applying Rule 8-D of the Income Tax Rules, 1962 is not automatic. The AO has to first find out what was the expenditure incurred by the assessee in relation to the income which does not form past of the total income under the Act (hereinafter refer to as the exempt income). Therefore, firstly the AO is required to find out the nexus between the expenditure incurred and exempt income. If the expenditure is not related to the exempt income, in our considered view the AO is not empowered to make disallowance u/s.14A of the Act by applying Rule 8D of the Income Tax Rules. Thus, first requirement of law is that the expenditure should be related to the exempt income. In case, where the assessee makes a claim that 'x' amount is related to the exempt income or otherwise no expenditure is related to the exempt income, in that event, the AO has to satisfy himself about the correctness of the claim having regard to the accounts of the assessee before proceeding to apply Rule 8 D of the Income Tax Rules, 1962 for computing disallowance. Hence, another requirement of law is that the AO has to satisfy himself about the correctness of the claim of the assessee having regard to the accounts of the assessee. The provision of section 14A mandates the AO to examine the accounts of the assessee before proceeding to apply Rule 8D of the IT Rules. In the present case, the AO has made disallowance on account of interest expenditure and administrative expenses. Since on both the counts, the AO has failed to record his finding, we are of the considered view that disallowance as made by the AO cannot be sustained. Hence, AO is hereby directed to delete the disallowance. Thus, grounds raised in the cross-objection are allowed.

14. In the combined result, the appeal of the Revenue is partly allowed, whereas cross-objection filed by the assessee is allowed.

This Order pronounced in open Court on 30/09/2015

Sd/-	Sd/-
(Anil Chaturvedi)	**(Kul Bharat)**
Accountant Member	**Judicial Member**

Ahmedabad, Dated : 30/ 09/2015

S.K.Sinha

आदेशकीप्रतिलिपिअग्रेषित / Copy of Order Forwarded to:-

1. अपीलार्थी / Appellant
2. प्रत्यर्थी / Respondent
3. संबंधितआयकरआयुक्त/ Concerned CIT
4. आयकरआयुक्त- अपील / CIT (A)
5. विभागीयप्रतिनिधि,आयकरअपीलीयअधिकरण, अहमदाबाद/ DR, ITAT, Ahmedabad
6. गार्डफाइल / Guard file.

By order/आदेशसे,

//True Copy//

उप/सहायकपंजीकार
आयकरअपीलीयअधिकरण,अहमदाबाद।