IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

R/TAX APPEAL NO. 208 of 2019

FOR APPROVAL AND SIGNATURE:

HONOURABLE MR.JUSTICE J.B.PARDIWALA

and
HONOURABLE MR.JUSTICE A.C. RAO

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1	Whether Reporters of Local Papers may be allowed to see the judgment ?	**NO**
2	To be referred to the Reporter or not ?	**NO**
3	Whether their Lordships wish to see the fair copy of the judgment ?	**NO**
4	Whether this case involves a substantial question of law as to the interpretation of the Constitution of India or any order made thereunder ?	**NO**

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THE PRINCIPAL COMMISSIONER OF INCOME TAX, GANDHINAGAR
Versus
GUJARAT STATE PETRONET LIMITED

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Appearance:
MRS MAUNA M BHATT(174) for the Appellant(s) No. 1
MR B S SOPARKAR(6851) for the Opponent(s) No. 1

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CORAM: **HONOURABLE MR.JUSTICE J.B.PARDIWALA**
and
HONOURABLE MR.JUSTICE A.C. RAO

Date : 09/07/2019

ORAL JUDGMENT
(PER : HONOURABLE MR.JUSTICE J.B.PARDIWALA)

1. This tax appeal under Section 260A of the Income Tax Act, 1961 [for short the Act, 1961] is at the instance of the Revenue and is directed against the order passed by the Income Tax Appellate Tribunal, Ahmedabad 'A' Bench, Ahmedabad in the ITA No.623/AHD/2016, dated 17/10/2018 for the A.Y 2010-11.

2. The Revenue has proposed the following questions of law:-

> *[A] Whether the Appellate Tribunal has erred in law and on facts by not appreciating that the disallowance under section 14A of the Income Tax Act, 1961 can be made on expenditure incurred for earning exempt income even when there is no claim of exempt income?*
>
> *[B] Whether the Appellate Tribunal has erred in law and on facts in deleting the addition of Rs.1,58,31,847/- made by the Assessing Officer under Section 14A of the Income Tax Act read with Rule 8D of the Income Tax Rules?*

3. The tribunal while allowing the appeal preferred by the assessee held as under:-

> *4. We see no reasons to take any other view of the matter than the view so taken by us in assessee's own case. Respectfully following the same, we delete the impugned disallowance of Rs.1,58,31,847/- under section 14A read with Rule-8D. As we do so, we have taken note of the uncontroverted factual position that the Assessing Officer has not shown any dissatisfaction with the disallowance under section 14A read with Rule 8D offered suo motu by the assessee. Learned Department Representative has not disputed this factual aspect. In view of these discussions, the impugned disallowance under section 14A read with Rule 8D, as challenged in appeal before us, stands deleted.*

4. The two questions proposed by the Revenue are squarely covered by the decision of this Court in the case of ***Principal Commissioner of Income Tax, Vadodara-1 Vs. Gujarat State Fertilizer and Chemicals Ltd.; Tax Appeal No.100 of 2019, decided on 18/06/2019***. We quote

the relevant observations, which are as under:-

> *5. Mr. Patel submitted that the Assessing Officer rightly made the disallowance under Section 14A of the Act. He submitted that in a recent decision in the case of Maxopp Investment Limited (supra), the Supreme Court has reiterated that the purpose behind Section 14A of the Act is not to permit deduction of the expenditure incurred in relation to the income which does not form part of the total income. It is to ensure that the assessee does not get double benefit.*
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> *6. He further submitted that this Court, in the case of PCIT-II v. Shreno Limited, (2018)409 ITR 401 (Gujarat), has referred to the decision of the Supreme Court in the case of S.A.Builders Limited v. CIT, (288)ITR 1 and observed that the exposition of law made by the Supreme Court in the case of S.A.Builders Limited (supra) and the observations made therein have been applied by this Court on various occasions particularly in connection with the disallowance to be made under Section 14A of the Act and it has been held that if the assessee can demonstrate the availability of the surplus interest free funds for making the investment generating tax free income, the disallowance under Section 14A of the Act would not be justified.*
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> *7. Mr. Patel submitted that the decision of the Supreme Court in S.A.Builders Limited (supra) is not applicable to the issue involved in the present case as the decision in the case of S.A.Builders Limited (supra) is with respect to Section 36(i)(iii) of the Income Tax Act, whereas in the present case the issue is with regard to the disallowance under Section 14A read with Rule 8D in the context of the assessee having mixed funds, i.e. interest free as well as interest bearing funds. In the case of S.A.Builders Limited (supra), the relevant assessment years were Assessment Years 1990-91 and 1991-92, i.e. prior to the insertion of Rule 8D in the Income Tax Rules by the Income Tax (Fifth Amendment) Rules, 2008 w.e.f. 24th March 2008. It is also submitted that Section 14A has been inserted in the*

Income Tax Act by the Finance Act, 2001, with retrospective effect from 1st April 1962.

8. It is further submitted that after the insertion of Rule 8D, in all the cases of mixed funds, i.e. interest free as well as interest bearing funds, the subsequent decision of the Supreme Court in the case of Maxopp Investment Limited (supra), more particularly para 42 regarding the case of M/s.Avon Cycles Limited, would be applicable for disallowance under Section 14A and such disallowance is required to be assessed as per the provisions of Rule 8D only. The decision of this Court in the case of Shreno Limited, which is based on the prior decision of the Supreme Court in the case of S.A.Builders Limited (supra) is, therefore, not applicable to the cases of mixed funds.

9. On the other hand, this Tax Appeal has been vehemently opposed by Mr.Manish Shah, the learned counsel appearing for the respondent – assessee. Mr.Shah submitted that the decision of the Supreme Court in the case of Maxopp Investment Limited (supra) should not be understood as clinching the issue with regard to the interpretation of Section 14A of the Act and Rule 8D of the Rules. He submitted that in the case of Maxopp Investment Limited (supra), the question before the Supreme Court was, whether the disallowance of expenditure under Section 14A of the Act would be applicable in a case where shares or stocks of a company were purchased for the purpose of gaining control over the said company and incidentally tax free dividend income was generated. He would submit that such an issue does not arise in the present case so as to make the dictum of Maxopp Investment Limited (supra) applicable to the case on hand. He submitted that Maxopp Investment Limited (supra) should not be understood as laying down a proposition of law that the requirement of sub-rule (1) of Rule 8D of the satisfaction to be arrived at by the Assessing Officer before applying the formula given in sub-rule (2) of Rule 8D is done away. He submitted that the decision of the Supreme Court in

Maxopp Investment Limited (supra) does not lay down a proposition that the moment it is demonstrated that the assessee had availed of mixed funds, i.e. interest free as well as interest bearing funds, and utilized them for making investments into securities earning tax free income and the rest applicability of Section 14A read with Rule 8D would be automatic.

15. In Maxopp Investment Limited (supra), the Supreme Court has clarified that the satisfaction has to be recorded by the Assessing Officer to show that the voluntary disallowance of the expenditure made by the assessee on the expenditure incurred for earning exempt income is not in order. The Assessing Officer, in such circumstances, is obliged to assign reasons for he not being satisfied having regard to the accounts maintained by the assessee and the suo motu disallowance made by the assessee under Section14A of the Act. We may reproduce the relevant observations of the Supreme Court in this regard thus:

> *"Having regard to the language of Section 14A(2) of the Act, read with Rule 8D of the Rules, before applying the theory of apportionment, the Assessing Officer needs to record satisfaction that having regard to the kind of the assessee, suo moto disallowance under Section 14A was not correct. It will be in those cases where the assessee in his return has himself apportioned the expenditure but the Assessing Officer did not accept the assessee's apportionment. In that eventuality, he will have to record its satisfaction to this effect. Further, while recording such a satisfaction, the nature of the loan taken by the assessee for purchasing the shares or making the investment in shares is to be examined by the Assessing Officer."*

16. We also refer to and rely upon a decision of this Court in the case of Principal Commissioner of Income Tax v. Shreno Limited, reported in (2018)409 ITR 401 (Gujarat), more particularly paragraphs 16 and 17, which read thus :

> *"16. The primary question which the Supreme Court considered in case of Maxopp Investment Ltd., (Supra) was whether disallowance of expenditure under Section 14A of the Act would be applicable*

in a case where shares or stocks of a company were purchased for the purpose of gaining control over the said company and incidentally tax free dividend income was generated. The assessee had contended that the dominant intention for purchasing the shares was not for earning the dividend but to gain control over the business in the company in which the shares were purchased. The Supreme Court held that the purpose for which the shares were purchased was inconsequential. As long as such investment generated tax free income, disallowance of expenditure for making such investment would be justified. This issue does not arise in the present case. However, it is true that while disposing of bunch of appeals by the said judgment the Supreme Court also considered the correctness of the view of the Punjab & Haryana High Court in case of Avon Cycles Ltd. It was the case in which the Assessing Officer had invoked Section 14A read with Rule 8D and apportion the expenditure between investments made for earning tax free income and the rest. The CIT (Appeals) had deleted the entire disallowance upon which in the appeal filed by the Revenue the Tribunal restored portion of the disallowance observing that the funds utilized by the assessee being mixed funds, the disallowance is confirmed in view of the provisions under Rule 8D(2) of the Rules. This decision of the Tribunal was challenged before the High Court. The Court held that the funds utilized by the assessee were mixed funds and the interest paid by the assessee is also an interest on the investments made, was the finding of fact and therefore, no substantial question of law arises. This judgment was carried in appeal by the assessee. The Supreme Court dismissed the appeal confirming the decision of the High Court.

17. We do not find that this portion of the judgment of the Supreme Court in case of Maxopp Investment Ltd., can be seen as fundamentally changing the understanding and interpretation of Section 14A and Rule 8D of the Rules adopted by this Court and various Courts, noted above. This judgment does not lay down a proposition that the requirement of sub-rule (1) of Rule 8D of the satisfaction to be arrived by the Assessing Officer before applying the formula given in sub-rule (2) of Rule 8D is done away with. In other words, the judgment in case of Maxopp Investment Ltd., does not lay down a proposition that the moment it is demonstrated that the assessee had availed of mixed funds i.e. interest free as well as interest bearing funds and utilized them for making investments into securities earning tax free income and the rest applicability of the Section 14A read with Rule 8D would be automatic. We are conscious that neither in M/s. Max India Ltd., Punjab & Haryana nor in Gujarat State Fertilizer and Chemicals case, this High Court had noticed the judgment of the Supreme Court in case of Maxopp Investment Ltd. Nevertheless in view of the discussion above, in our

opinion the situation would not change on account of the said judgment of the Supreme Court."

17. This Court, in Shreno Limited (supra), has taken the view that Maxopp Investment Limited (supra) cannot be seen or understood to be fundamentally changing the understanding and interpretation of Section 14A and Rule 8D. It went on to hold that the judgment of the Supreme Court does not lay down the proposition that, the requirement of sub-rule (1) of Rule 8D of recording the satisfaction by the Assessing Officer before applying the formula given in sub-rule (2) of Rule 8D is done away with. It clarifies that the judgment in the case of Maxopp Investment Limited does not lay down a proposition that the moment it is demonstrated that the assessee had availed of mixed funds and utilized them for making investment into securities earning tax free income, Section 14A read with Rule 8D would be attracted automatically. The assessee has further relied on the judgment in the case of Principal Commissioner of Income Tax v. Gujarat State Financial Services Limited in the Tax Appeals Nos.1252, 1253 and 1255 of 2018 decided on 15th August 2018, which has followed the decision in the case of Shreno Limited (supra) dealing with the same issue and also an identical argument taken by the department.

18. The language of Section 14A of the Act is plain and clear. Before invoking Rule 8D, the Assessing Officer is obliged to indicate that having regard to the accounts of the assessee, he is not satisfied with the correctness of the claim of the assessee in respect of such expenditure in relation to the income which does not form part of the total income under the Act. To put it in other words, the condition precedent of recording the requisite satisfaction which is a safeguard provided in Section 14A should not be overlooked before going to Rule 8. In such circumstances we are not impressed by the submission canvassed on behalf of the Revenue that once there are

mixed funds, Rule 8 would be attracted automatically.

5. In view of the above, this appeal fails and is hereby dismissed.

(J. B. PARDIWALA, J)

(A. C. RAO, J)

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