

IN THE INCOME TAX APPELLATE TRIBUNAL
AHMEDABAD ‘ B ’ BENCH – AHMEDABAD

Before Shri S. S. Godara, JM & Shri Manish Borad, AM.

ITA No. 2138/Ahd/2013
Asst. Year: 2007-08

Zest Aromas Private Ltd., 203, Akashganga, Nr. Vaniya Bhawan, Race course Circle, Vadodara.	Vs.	ACIT, Circle-4, Baroda.
Appellant		Respondent
PAN AAACZ 0601M		

Appellant by	Shri Tushar P. Hemani, AR
Respondent by	Shri James Kurien, Sr. DR.

Date of hearing: 19/01/2017
Date of pronouncement: 31/01/2017

O R D E R

PER Manish Borad, Accountant Member.

This appeal of the assessee for Asst. Year 2007-08 is directed against the order of Id. CIT(A)-III, Baroda, dated 30.05.2013 vide appeal No.CAB/III/-119/09-10 arising out of order u/s 143(3) of the IT Act, 1961 (in short the Act) dated 29.12.2009 framed by Addl. CIT, Range-4, Baroda. Assessee has raised following grounds of appeal :-

- 1.00 On the facts and circumstances of your appellant's case as well as in law, the Id. CIT(A) erred in confirming disallowance of Rs. 5,76,925/- under section 14A of the Act without proving any nexus between the expenditure incurred and exempt income earned.
- 1.01 The Id. CIT (A) further erred in confirming disallowance on account of Portfolio Management Charges amounting to Rs. 4,79,6117-, forming part of total disallowance of Rs. 5,76,9257-, without appreciating the facts that your appellant

has already disallowed such Portfolio Management Charges in the computation of total income.

- 1.02 Your appellant prays before your honour to hold so now and delete the impugned disallowance.
- 2.00 Your appellant craves leave to add, alter and / or amend the ground herein above raised.

2. We find that this appeal is time barred by 8 days and on asking for the reasons for the delay following reasons were provided by the assessee :-

- (i) The impugned order passed by Ld. CIT(A) was received by the assessee on 12.06.13. The said order was handed over to the accountant for passing on the same to the concerned Chartered Accountant for filing appeal before Hon'ble the Income Tax Appellate Tribunal. However, inadvertently, the said accountant forgot to pass on such order to the concerned Chartered Accountant.
- (ii) On inquiry by the concerned Chartered Accountant, the said accountant realized that the impugned order was not passed on for filing an appeal before Your Honors. Upon such facts coming to the knowledge of assessee, impugned order was immediately forwarded to the concerned Chartered Accountant. Thereafter, the said Chartered Accountant prepared Form No.36 along with Grounds of Appeals and forwarded the same to the assessee for signature. Thereafter, the present appeal came to be filed before Your Honors on 19.08.13. In the mean-time, there was a delay of 8 days in filing the appeal.

3. We find that this appeal is barred by mere 8 days due to lapse in performing duty assigned and carelessness of the Accountant, who forgot to pass on the assessment to the concerned Authorized Representative (AR) resulting in delay of 8 days arose. We are of the view that due to the mistake of the Accountant the assessee should not suffer and we, therefore, condone the delay and proceed to adjudicate the appeal.

4. Briefly stated facts of the case are that the assessee is a private limited company engaged in the business of manufacturing industrial fragrance, flavours and perfumes. Return of income was filed on 30.10.2007 showing total income at Rs.1,93,98,830/- and value of fringe benefits at Rs.2,75,925/-. Case was selected for scrutiny assessment. Notices u/s 143(2) of the Act followed by notice u/s 142(1) of the Act were issued. Necessary details including audited financial statement were provided. During the course of assessment proceedings Id. Assessing Officer while examining the provisions of section 14A of the Act observed that assessee received exempt dividend income of Rs. 65.33 lacs and investment as on 31.03.2007 of Rs.9,52 crores. Also interest of Rs.15.52 lacs was paid on the borrowed funds of Rs.1.46 crores. In reply to the show cause notice of Id Assessing Officer about disallowance u/s 14A of the Act, assessee submitted that Rule 8-D r.w.s.14A of the Act has been made applicable w.e.f.24.3.2008 and it is not applicable its case for Asst. Year 2007-08. However, Id. Assessing Officer after taking the details of calculation of disallowance u/s 14A of the Act r.w.r.8-D disallowed a sum of Rs.5,76,925/-. Also addition of Rs.7,94,612/- was made towards differential value of the borrowed funds and loans given. Accordingly, after making addition of Rs.13,71,537/- income was assessed at Rs.2,07,70,367/-.

5. Assessee went in appeal before Id. CIT(A) against the impugned assessment order and got part relief as the impugned disallowance of Rs.7,94,612/- on account of difference of borrowed

funds was deleted whereas disallowance u/s 14A of the Act r.w.r.8-D was sustained by by deciding as follows :-

4.3 I have considered the fact of the case and submission made by the AR of the appellant. As evident from details supplied, appellant has been making fresh investments in tax free securities year after year. Investment decisions are strategic decisions requiring time and effort on part of top management and other employees. Management/maintenance of investment portfolio would also require time and effort besides paper work on part of employees. Attribution of part of employee costs towards investment activities is therefore justified. Once incurring of expenditure towards managerial and administrative purposes for earning of investment income cannot be ruled out, it is a case falling under sub-section (2) of section 14A, i.e. appellant's claim that no expenditure was incurred for earning tax free income is incorrect. But at the same time it is also correct that the expenditure attributable to earning of tax free income is then to be determined in a reasonable manner and not as per Rule 8D for AY 2007-08, as per decision by Mumbai High Court in the case of Godrej & Boyce Manufacturing Co. Ltd.

4.3.1 As regards appellant's contention about investment in tax free income yielding assets being exclusively out of surplus/own funds, appellant has provided some details in support of such contention. But such details are not conclusive as mentioned by the AO in his remand report. Once the common fund is being used for earning taxable as well as tax free incomes, then a part of interest paid has to be attributed to tax free income. Hon'ble Kerala High Court in its decision in the case of [2011] 10 taxmann.com 213 (Ker.), Comm/ss/oner of Income-tax, Thrissur v. Dhanalakshmy Bank Ltd, has held that once no separate accounts are maintained for taxable and non taxable heads of incomes, then disallowance as per rule 8D will have to be made. The onus is on the assessee to establish that the investments made for earning the tax free incomes have been made out of own funds and the borrowed funds.*

4.3,2 At the same time a perusal of the audited accounts of the appellant reveals that the appellant is making investment in tax free securities through Portfolio Management Services and through its own office. The total PMS charges paid during the year is Rs.4,79,611/- during the entire year. This expense is clearly disallowable under section 14A.

4.3.3 The borrowed capital of the appellant is Rs.1.46 crores only as against the investment in securities for Rs.9.52 crore as on 31.03.200/- From the details submitted it is seen that the appellant is also having profits from investments and dividend from investments which are being re-invested in tax free securities. The appellant is also having separate cash credit account for manufacturing purposes. Hence, the disallowance of interest paid in proportion to ratio of investment in tax free securities to total assets is not reasonable. The total disallowance made by the AO is Rs.5,76,925/-. Thus the disallowance made over and above PMS charges is Rs.97,314/-. This amount can be held to be a reasonable amount for making

disallowance out of the interest paid as also administrative expenses incurred by the appellant for making investment through its own office.

4.3.4 Hence, the disallowance made by the AO of Rs.5,76,925/- is upheld on the basis of these discussions and this ground of appeal is dismissed.

5. Aggrieved, assessee is now in appeal before the Tribunal against the impugned disallowance u/s 14A of the Act of Rs.5,76,925/-.

6. Ld. Authorised Representative (AR) submitted that Rule 8D r.w.s. 14A of the Act is applicable from Asst. Year 2008-09 whereas, appellant's case is for Asst. Year 2007-08. Further at this stage, it may be appreciated that Ld. CIT(A), while confirming the disallowance u/s 14A of the Act has observed that appellant has paid total Portfolio Management Services(PMS) charges of Rs.4,79,611/- during the year under consideration and hence, disallowance u/s 14A over and above PMS charges is Rs.97,314/- only (i.e. Rs.5,76,925 - Rs.4,79,611) which is reasonable (Para 4.3.2 & 4.3.3, Pg.14 of CIT(A)'s order). Ld. CIT(A) failed to appreciate that appellant has already offered income from portfolio management as *taxable business income* as is evident from appellant's return of income (Pgs.1-5 @ 2 of P/B). Hence, question of invoking S.14A w.r.t. PMS charges of Rs.4,79,611/- doesn't hold any water since corresponding income has already been offered to tax. As regards balance disallowance of Rs.97,314/- (i.e. Rs.5,76,925 -Rs.4.79,611), assessee's investments in shares at the year-end are to the tune of Rs.9,52,89,090/- (Pgs.33-58 @ 33 of P/B) whereas shareholders' funds available with assessee were Rs.38,41,80,686/- (i.e. Share

Capital Rs.36.00,000 + Reserves Rs.38,05,80,686) (Pgs.33-58 @ 33 of P/B). Thus, interest free funds at appellant's disposal are almost 4.03 times the amount of investments. In such a scenario, no disallowance is called for u/s 14A in respect of interest. Reliance is placed on:

- > CIT vs. Torrent Power Ltd. - 363 ITR 474 (Guj.)
- > CIT vs. Suzlon Energy Ltd. - 354 ITR 630 (Guj)
- > CIT vs. Gujarat Power Corporation Ltd. - 352 ITR 583 (Guj)
- > CIT vs. Hitachi Home & Life Solutions (I). Ltd. - (2014) 41 taxmann.com 540 (Guj)
- > CIT vs. Reliance Utilities & Power Ltd. - 313 ITR 340 (Bom)
- > Munjal Sales Corporation vs. CIT - 298 ITR 298 (SC)

Accordingly, impugned disallowance deserves to be deleted in toto.

7. On the other Id. Departmental Representative (DR) vehemently argued supporting the orders of lower authorities.

8. We have heard the rival contentions and perused the material placed before us and gone through the decisions relied on by the Id. AR. Solitary grievance of the assessee is against the action of Id. CIT(A) confirming the action of Id. Assessing Officer making disallowance of Rs.5,76,925/- u/s 14A of the Act. We observe that assessee had earned exempt dividend income of Rs.65.33 lacs and also paid interest of Rs.15.52 lacs on borrowed funds and assessee's investment as on 31.03.2007 stood at Rs.9.52 crores as against Rs. 10.38 crores as on 31.3.2006. Further amended Rule 8-D with respect to disallowance u/s 14A of the Act came in effect from Asst.

Year 2008-09 whereas in this appeal we are dealing with Asst. Year 2007-08.

9. We further observe that Id. AR referred to the computation of income wherein portfolio management charges(PMS) of 4,79,611/- was paid to look after the affairs of investments in order to give best returns and this amount has been added back to the profit and loss account under the head 'profits and gains' of the business as is appearing in page 2 of the paper book. Further assessee has reduced PMS charges of Rs.4,79,611/- against taxable income from investments of Rs.13,82,979/-. We find force in the arguments of the Id. AR that Id. CIT(A) has failed to appreciate the fact that the assessee has already offered income as taxable income and hence Id. Assessing Officer erred in invoking provisions of section 14A of the Act since corresponding income has already been offered to tax. This fact that Rs.4,79,611/- has been disallowed while calculating the business income has not been disputed by the Revenue and, therefore, this amount of Rs.4,79,611/- stands to be reduced from the gross disallowance of Rs.5,76,925/-.

10. As regards balance disallowance of Rs.97,314/- i.e. (Rs.5,76,925 – Rs.4,79,611) we find that assessee's investment as on 31.03.2007 stands at Rs.9.52 crores whereas interest free funds which included share capital and reserves stood at Rs.38.42 crores as on 31.3.2007 which means that assessee's interest free funds is almost 4 times the investment made. Hon. Jurisdictional High Court in the case of CIT vs. Torrent Power Ltd. 363 ITR 474 (Guj) has held

that if the assessee has sufficient interest free funds to cover up the investment then no disallowance of interest expenses is called for. We, therefore, are of the view that in the present case out of the total disallowance of Rs.5,76,925/- PMS charges of Rs.4,79,611/- has already been disallowed by adding it back to the business income and as far as remaining amount of Rs.97,314/- is concerned, we find that assessee is having sufficient interest free funds to cover up the investments and in this case no disallowance on interest expenses is called for. We accordingly delete the disallowance u/s 14A of the Act of Rs.5,76,925/- and allow the appeal of assessee.

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

Order pronounced in the open Court on 31 st January, 2017
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Sd/-
(S. S. Godara)
Judicial Member

sd/-
(Manish Borad)
Accountant Member

Dated 31/01/2017

Mahata/-

Copy of the order forwarded to:

1.	The Appellant
2.	The Respondent
3.	The CIT concerned
4.	The CIT(A) concerned
5.	The DR, ITAT, Ahmedabad
6.	Guard File

BY ORDER

Asst. Registrar, ITAT, Ahmedabad

1. Date of dictation: 30/01/2017
2. Date on which the typed draft is placed before the Dictating Member: 31/01/2017 other Member:
3. Date on which approved draft comes to the Sr. P. S./P.S.:
4. Date on which the fair order is placed before the Dictating Member for pronouncement: _____
5. Date on which the fair order comes back to the Sr. P.S./P.S.:
6. Date on which the file goes to the Bench Clerk: 1/2/17
7. Date on which the file goes to the Head Clerk:
8. The date on which the file goes to the Assistant Registrar for signature on the order:
9. Date of Despatch of the Order: