IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCH ' A '

BEFORE SHRI SUNIL KUMAR YADAV, JUDICIAL MEMBER AND
SHRI JASON P BOAZ, ACCOUNTANT MEMBER

I.T. A. No.877/Bang/2014
(Assessment Year : 2008-09)

M/s. Tata Hitachi Construction Machinery Company Limited,
Jubilee Building, No.45, Museum Road, Bangalore.

…. Appellant.

Vs.

The Dy. Commissioner of Income Tax,
Circle 12(4), Bangalore. ….. Respondent.

Appellant By : Shri Percy Pardiwala, Senior Counsel.
Respondent By : Shri C. H. Sundar Rao, CIT (D.R.)

Date of Hearing : 22.02.2018.
Date of Pronouncement : 20.04.2018.

O R D E R

Per Shri Jason P Boaz, A.M. :

This appeal by the assessee is directed against the order of Commissioner of Income Tax (Appeals)-III, Bangalore dt.14.02.2014 for the Assessment Year 2008-09.

2. Briefly stated, the facts of the case relevant for disposal of this appeal, are as under :-

2.1 The assessee, a company engaged in the business of manufacture, purchase and sale of Hydraulic Excavators, Loaders, mechanical shovels, cranes and spare parts thereof, filed its return of income for Assessment Year 2008-09 on 29.9.2008 declaring total income of Rs.483,41,12,190. The case was selected for scrutiny and in view of international transactions entered into by the assessee with its Associated Enterprises, a reference under Section 92CA of the Income Tax Act, 1961 (in short 'the Act') was made to the Transfer Pricing Officer (TPO) for determination of the Arm's Length Price (ALP) thereof. The TPO vide order under Section 92CA of the Act dt.31.10.2011 has not recommended any TP Adjustment to the ALP of the international transactions entered into by the assessee. The assessment was concluded under Section 143(3) of the Act vide order dt.30.12.2011 wherein the assessee's income was determined at Rs.491,99,25,041 in view of the following additions / disallowances :-

i)	Interest attributable	Rs.4,98,00,000
ii)	Disallowance u/s.14A r.w. Rule 8D	Rs.91,99,658
iii)	Warranty Expenses & Provision	Rs.44,63,000
iv)	R&D Expenditure	Rs.1,32,44,186
v)	Royalty	Rs.91,06,005

2.2 Aggrieved by the order of assessment dt.30.12.2011 for Assessment Year 2008-09, the assessee filed an appeal before the CIT (Appeals) – III, Bangalore. The learned CIT (Appeals) disposed the appeal vide the impugned order dt.14.2.2014 allowing the assessee partial relief.

3.1 Both revenue and the assessee, being aggrieved by the order of the CIT (Appeals) – III, Bangalore dt.14.2.2014 for Assessment Year 2008-09, have filed cross appeals before the Tribunal. Revenue's appeal for Assessment Year 2008-09 has been disposed off by a co-ordinate bench of this Tribunal in its order in ITA No.667/Bang/2014 dt.23.9.2015 allowing the Revenue partial relief.

3.2 Therefore, what is before us is the assessee's appeal for Assessment Year 2008-09, wherein it has raised the following grounds :-

1. That the Learned Commissioner of Income Tax (Appeals), III (CIT-A) erred in confirming the disallowance made by the Assessing Officer (AO) in respect of Appellant's claim u/s 35(1)(iv) read with Sec 35(2)(ia) in a sum of Rs. 2,91,97,333/- incurred towards purchase of Tangible Assets for Research and Development purposes.

2. That both the learned CIT(A) and AO erred in holding that the expenditure on acquisition of tangible capital assets of Rs. 2,91,97,333/- for Research and Development purposes leads to acquisition of rights as contemplated in exclusions contained in second limb of Sec 43(4)(ii).

3. Having regard to the facts in Appellant's case, both the learned CIT(A) and AO ought to have held that the expenditure of Rs. 2,91,97,333/- incurred in acquisition of capital assets is covered within the first limb of Sec 43(4)(ii).

   Viz;*" expenditure incurred on scientific research includes all expenditure incurred for the prosecution, or the provision of facilities for the prosecution of Scientific Research".*

4. That the learned CIT(A) is not justified in her remarks on page 14 of her order that *" the appellant has in his argument **skirted** the issue of whether the research actually yielded the acquisition of rights or not"* and misunderstood the scope of second limb of Sec 43(4)(ii) viz *"expenditure on Scientific Research do not include any expenditure incurred in the acquisition of rights in or arising out of Scientific Research."*

5. That the learned CIT(A) failed to deal with the arguments of the appellant that as per the provisions of Sec 35(3), the learned AO does not have power to disallow on his own, the claim for deduction u/s 35(1)(iv) read with Sec 35(2)(ia), having regard to the fact that the In-House Research and Development Facility of the appellant is approved by the Government of India, Ministry of Science and Technology vide orders dt.22.03.2005 and 27.06.2008, copies of which were furnished to both CIT(A) and AO.

6. That the learned CIT (A), having regard to the facts in Appellants case that the entire Investments were out of own funds, erred in holding that sum of Rs. 36,57,621/- is attributable towards interest expenditure in earning exempt income.

7. That the learned CIT(A) ought to have held that the expenditure towards interest in earning Exempt Income is Rs. Nil, having regard to the fact that the entire Investments by the Appellant were out of own funds.

8. That the CIT(A) erred on facts in stating that the Average Value of Investments was Rs. 1,331.05 Crores (on Page 9 of her order), while the correct Average Value of Investments was Rs. 105.07 Crores (i.e 157.05+53.09 divided by 2) and consequently erred in upholding the disallowance of Rs. 35,57,621/- as interest attributable towards Investments out of borrowed funds.

9. The CIT(A) erred in upholding disallowance of Rs. 52,53,500/- under Rule 8D(2)(iii), while the correct amount of expenditure was only Rs. 73,976/- having regard to facts in Appellant's case.

10. Each of the above grounds are without prejudice to one another.

11. The appellant carves leave to add, amend or alter any of the grounds herein.

12. For these and other grounds that may be urged later, the Appellant prays for appropriate relief.

4. **Ground Nos.1 to 5** : **Disallowance of claim u/s.35(1)(iv) –**

Purchase of Research & Development Assets.

4.1 The Ground Nos.1 to 5 (supra), raised by the assessee challenge the impugned order of the learned CIT (Appeals) in upholding the disallowance / rejection of the assessee's claim under Section 35(1)(iv) r.w.s. 35(2)(ia) of the Act for deduction of an amount of Rs.2,91,97,333 incurred towards purchase of tangible assets for research and development purposes of its in-house R&D facility.

4.2.1 The facts of the matter, as emerge from the record, are that in the course of assessment proceedings the Assessing Officer observed that the assessee had claimed deduction of an amount of Rs.2,91,97,333 on account of purchase of 'assets' for its in-house R&D facility. The Assessing Officer, while examining the issue, personally visited and

inspected the manufacturing and R&D facilities of the assessee at Jamshedpur in Jharkhand for verifying the assessee's claim for deduction under Section 35(1)(iv) r.w.s. 35(2)(ia) of the Act in accordance with report submitted to the DSIR, New Delhi. The assessee was required to substantiate that its activities were revenue in nature and do not create acquisition of rights in or arising out of scientific research as per Sec. 35 r.w.s. 43(4)(ii) of the Act. According to the Assessing Officer the assessee could not substantiate that the above expenses on purchase of assets for utilization in its in-house R&D facility were incurred in accordance with the provisions of Sec. 35 r.w.s. 43(4)(ii) of the Act as its activities resulted in development of new products that give rise to patents, which are intellectual property Rights (IPR) and therefore come under the exclusion clause in the definition of scientific research. In this view of the matter, the Assessing Officer held this expenditure does not qualify to be scientific research expenditure, but rather represents expenditure on intangible assets incurred in connection with acquisition of rights and therefore being in nature of capital expenditure, accordingly disallowed the entire expenditure amounting to Rs.2,91,97,333.

4.2.2 On appeal, the learned CIT (Appeals) concurred with and upheld the Assessing Officer’s finding, holding as under at para 7.2 of the impugned order :-

7.2. I have carefully considered the issue. The main contention of the appellant is that the appellant has acquired only tangible assets and no intangible assets or rights had been acquired. The contention of the AO is that the appellant by this R&D process had acquired substantial rights as covered by Sec 43(4)(ii) of the Act. The AO examined the processes involved in the R&D to find that new processes, products and patents arose as a result of the research, as detailed in a report sent by the appellant to the Ministry, and as reflected in the application for patents under the Patents Act of 1970. On the other hand, the appellant's contention is that the expenses claimed relate to prosecution of scientific research and the provision of facilities for such prosecution and not for the acquisition of right in or arising out of scientific research. From the above, it can be seen that the basic arguments of the appellant company are that the R&D process resulted in certain tangible assets and details of the expenditure had been duly provided to the AO. It is also argued that once the R&D facility is approved by the Ministry, the deduction u/s 35(2AB) cannot be denied.

The appellant's interpretation of Sec 43(4)(ii) is that while encouraging scientific research among Indian companies, Sec 35 r.w.s. 43(4)(ii) envisages denial of deduction only to such expenses as are incurred for registration, legal charges, incidental expenses of advertisement etc. which would not be directly related to the prosecution of scientific research. The arguments of the appellant and the contentions of the AO are considered. I find that the appellant has in his argument skirted the issue of whether the research actually yielded the acquisition of rights or not. Encouraging of scientific research and commercial usage of the rights acquired over the products/processes are two separate issues

involved in this appeal. The appellant has not pointed out how the provisions of Sec 43(4)(ii) do not apply to it, once it is pointed out that the research leads to the acquisition of rights over products, processes and patents. The use of the words "rights in, or arising out of, scientific research" in the Section are clear and unequivocal. The mere fact that tangible assets have resulted out of the R & D process does not mean that there is no acquisition of rights. In para 10.9 of the order, AO has pointed out that assessee has applied for a patent in respect of semi hydrostatic automatic transmission for which an application was made on 11-10-2011. Thus, in the present case, the AO has clearly pointed out that the prosecution of scientific research by the appellant leads to the acquisition of rights over certain processes and products, and for the strengthening and protection of these rights, the appellant has obtained/is in the process of obtaining due patents. In these circumstances, the arguments raised by the appellant are clearly outside the purview of the legal position as laid down in Sec 43(4)(ii). The disallowance made by the AO is found to be in order, and the same is accordingly upheld. This ground is dismissed.

4.3.1 According to the learned Authorised Representative of the assessee, the assessee has set up in-house R&D facility which is recognized by the Department of Scientific and Industrial Research (DSIR), Ministry of Science & Technology, Govt. of India vide order No.TU/IV/2284/2005 dt.22.3.2005 (copy placed at page 1 of paper book) and renewal is extended upto 31.3.2011 vide order dt.27.6.2008 (copy placed at page 2 of paper book). In the year under consideration, the

assessee incurred expenditure of Rs.2,91,97,333 towards acquisition of tangible assets for its in-house R&D facility for carrying out scientific research, the details of which are listed at page 3 of paper book.

4.3.2 It is submitted that when the Assessing Officer visited and inspected the assessee's factory premises at Jamshedpur, he required a copy of the report submitted by the assessee to the DSIR, New Delhi which were made available to him. It is contended that, while no queries were raised by the Assessing Officer when R&D facilities and activities were shown to him by Managing Director, The Chief Design and Development Engineer (R&D) and AGM (R&D), the Assessing Officer's finding in the order of assessment, that the assessee has not been able to substantiate that the aforesaid expenditure on in-house scientific research is related to the assessee's business, is clearly erroneous. It is reiterated that the said expenditure on in-house scientific research is related to the assessee's business and not for any other purposes. It is further contended that the Assessing Officer's view, that the aforesaid expenditure on in-house R&D facility resulted in the assessee acquiring substantial rights in or arising out of scientific research, is factually erroneous as can be seen from the details thereof furnished at page 3 of the paper book which show that they are for upgrading and development of new versions of equipment manufactured by the assessee in the course of its business and not for any other purpose. It was therefore contended that the entire expenditure incurred for its in-house R&D facility is towards scientific research and qualifies for deduction.

4.3.3 It was also submitted that even if the R&D expenditure is to be considered to be capital expenditure, it should be eligible for deduction under Section 35(1)(iv) of the Act. In support of this proportion, the learned Authorised Representative placed reliance on the decision of the co-ordinate bench in the case of (i) Tejas Networks India Pvt. Ltd. (2015) 55 taxmann.com 55 (Bangalore – Trib) and (ii) Resil Chemicals (P) Ltd. Vs. CIT (2014) 51 taxmann.com 250 (Bangalore – Trib); which orders, it was submitted, were rendered on almost similar facts and issues of the allowability of expenditure on R&D in scientific research under Section 35(1)(iv) of the Act even though the expenditure incurred is held to be capital in nature.

4.3.4 In respect of the Assessing Officer's view that the said expenditure does not fall within the definition of 'Scientific Research', as spelt out in Sec. 43(4)(ii) of the Act, the learned Authorised Representative submitted that as can be seen from the break up of the entire expenditure (placed at page 3 of paper book), it is clear that the entire expenditure has been incurred on in-house R&D activity and not arisen out of "acquisition" of rights in or arising out of scientific research. According to the learned Authorised Representative, both the Assessing Officer and the learned CIT (Appeals) have misconstrued the provisions of Sec. 43(4)(ii) of the Act to hold that R&D expenditure resulted in filing of a patent, points to the acquisition of rights.

4.4 Per contra, the learned Departmental Representative for Revenue supported the orders of the authorities below.

4.5.1 We have heard the rival contentions, perused and carefully considered the material on record; including the judicial pronouncements cited. The issue for consideration and adjudication before us is with respect to the interpretation of the definition of "scientific research" as per the provisions of Sec. 43(4)(ii) of the Act and particularly the exclusion to the definition given in clause (ii) to sub-section (4) of Sec. 43 of the Act which states that scientific research expenditure excludes "……. Any expenditure incurred in the acquisition of rights in, on arising out of, scientific research." The contention of the assessee is that the expenditure incurred by it on in-house R&D for improvement and upgrading of products manufactured in the course of its business, does not fall under the exclusion clause provided in Sec. 43(4)(ii) of the Act and is therefore eligible for deduction under Section 35(1)(iv) of the Act. Per contra, Revenue is of the view that expenditure incurred on in-house R&D also needs to be excluded from the definition of "scientific research" since it leads to acquisition of rights in or arising out of 'scientific research'.

4.5.2 We find that this very issue on similar facts has been considered and adjudicated in favour of the assessee and against Revenue by a co-ordinate bench of this Tribunal in the case of Tejhas Networks Ltd. (supra) wherein it followed the decision of the Hon'ble

Karnataka High Court in the case of CIT Vs. Talisma Corpn. (P) Ltd. (2013) 40 taxmann.com 400 (Kar). In that order, in the case of Tejas Networks Ltd. (supra), to which one of us is party, the co-ordinate bench at paras 5.7.1 to 5.7.5 thereof has held as under :-

" **5.7.1** We have heard the rival contentions and perused and carefully considered the material on record, including the judicial decisions cited. The primary issue for consideration/adjudication before us is the interpretation of the definition of "scienitific research" as per the provisions of section 43(4)(ii) of the Act; and particularly the exclusion to the definition given in clause (ii) to sub-section (4) of section 43 of the Act which states that scientific research expenditure excludes " ...any expenditure incurred in the acquisition of rights in, or arising out of, scientific research." The stand of the Revenue seems to be that the expenditure incurred on in-house R&D also needs to be excluded from the definition of "scientific research" if it leads to any intellectual property rights. Per contra, the stand of the assessee is that the expenditure incurred on in-house R&D does not fall under the exclusion clause provided in section 43(4)(ii) of the Act.

5.7.2 We find that this issue has been considered and answered by the Hon'ble Karnataka High Court in the case of *Talisma Corpn. (P) Ltd.* (*supra*). In that case, the Hon'ble High Court had framed the following question of law at para 4 of its order which are as under :ð

"4. The substantial questions of law, which arise for consideration in this appeal, are as under :-

1. Whether the Appellate Authorities were correct in holding that the expenses incurred by the assessee were improvement of capital assets, should be treated as a capital asset as held by the Assessing Officer but also should be given deduction u/s. 35(1)(iv) of the Act, based on an alternative plea raised by the assessee before the Appellate Commissioner for the first time without raising this issue before the Assessing Officer ?

2. Whether the Appellate Authorities were correct in granting relief to the assessee u/s. 35(1)(iv) of the Act, when the Assessing Officer had treated this improvement as a capital asset and had allowed depreciation over it and when such double deduction is not permissible in accordance with section 35(2)(iv) of the Act ?"

The Hon'ble High Court decided the above question of law at para 9 of its order which is extracted hereunder :-

" 9. It is the specific case of the Revenue that, the amount of Rs.10.82 Crores spent by the assessee in acquiring an intellectual property is capitalized in the books. Now further amount of Rs.9,27,34,277 is spent in developing and improving the said product. Therefore, the expenditure on further development of software which is treated as a capital in nature, is also capital in nature. This development is on account of scientific research. The evidence on record shows most of the money is spent towards cost of the employees, who had developed the product "Talisma Enterprise 2.5", multi channel customer relationship management solution, which provides sales, marketing, services, human resources and finance through the medium of e-mail, chat, wireless, fax, phone, etc. to the end users. Therefore, the expenditure in respect of the scientific research, even if it is capital in nature as it was incurred in relation to the business carried on by the assessee under section 35(1)(iv) of the Act, the said expenditure is to be deducted. That is what the Appellate Authority as well as the Tribunal have held.

Accordingly, we answer the substantial questions of law in favour of the assessee and against the Revenue."

5.7.3 In the case of *Talisma Corpn. (P) Ltd.* (*supra*) cited above, the tax payer had acquired Intellectual Property Rights (IPR) which were capitalised in the Books of Accounts. The tax payer spent further amounts in developing and improving the same. The expenditure incurred on improvement were also capitalised in the books of account. While the amount spent on acquiring the IPR were not allowed as deduction u/s. 35 of the Act, the expenditure incurred in-house for improvement of the same was allowed as deduction u/s.35 (1)(iv) of the Act, even though it was capitalised in the Books of Account.

5.7.4 Section 43(4) of the Act defines "scientific Research" for the purposes of the Act and the definition reads as follows :ð

'43(4)(*i*) "scientific research" means any activities for the extension of knowledge in the fields of natural or applied science including agriculture, animal husbandry or fisheries;

(*ii*) references to expenditure incurred on scientific research include all expenditure incurred for the prosecution, or the provision of facilities for the prosecution, of scientific research, but do not include any expenditure incurred in the acquisition of rights in, or arising out of, scientific research;

(*iii*) references to scientific research related to a business or class of business includeð

(*a*) any scientific research which may lead to or facilitate an extension of that business or, as the case may be, all businesses of that class;

(*b*) any scientific research of a medical nature which has a special relation to the welfare of workers employed in that business or, as the case may be, all

businesses of that class;'

From the above definition, it can be seen that u/s.43(4)(ii) of the Act, the expenditure incurred on scientific research does not include "any expenditure incurred in the acquisition of rights in, or arising out of, scientific research." It appears that it is for this reason that the Assessing Officer concluded that the expenditure incurred has resulted in acquisition of rights in or arising out of scientific research.

5.7.5 In the case on hand, the only basis on which the learned CIT(A) sustained the disallowance is the view that the expenditure resulted in the acquisition of rights in or arising out of scientific research. The learned CIT(A) has proceeded on the basis that if the assessee carries out scientific research and is able to obtain IPRs on such research, then he was free to commercially use such IPRs and this is the reason why there is a prohibition u/s.43(4)(ii) of the Act so as to exclude expenditure incurred in the acquisition of rights in or arising out of scientific research. In our view, the aforesaid approach of the authorities below is not correct. The expenditure that is sought to be excluded u/s.43(4)(ii) of the Act is an expenditure which the assessee incurs in acquiring rights in or arising out of scientific research already done by somebody. It is possible that the assessee without carrying out any scientific research, acquires rights in scientific research, arising out of scientific research done by somebody else and claims cost of acquisition of such rights as expenditure on scientific research. It is this kind of expenditure that is sought to be excluded u/s. 43(4)(ii) of the Act in its exclusion clause as " expenditure incurred in acquiring rights in, or arising out of scientific research." It is such type of expenditure carried out by somebody else and such right is acquired by the assessee, that is sought to be disallowed. The objective behind the exclusion clause in section 43(4)(ii) of the Act appears to be that expenditure on scientific research should be on the research actually carried out by the assessee in-house and it should not merely spend money in acquiring rights in OR arising out of scientific research carried out by some other person. If the interpretation sought to be placed by revenue / authorities below is to be accepted, then the benefit sought to be conferred by the provisions of section 35(1)(iv) of the Act would be virtually denied in all cases by invoking the exclusion clause in section 43(4)(ii) of the Act. Such a consequence would never have been intended by the Legislature. As already stated, the object behind the provisions of section 35 of the Act is to encourage scientific research so that the benefit of such research would be available to all. In the given facts and circumstances of the case as discussed above, we are of the view that the claim of deduction under section 35(1)(iv) of the Act is to be allowed. In any event, there is no distinction as to whether the expenditure incurred is capital or revenue, because while the provisions of section 35(1) of the Act allows deduction of revenue expenditure, the provisions of section 35(1)(iv) of the Act allows deduction in respect of capital expenditure. We, therefore, direct the Assessing Officer to allow the deduction claimed by the assessee. Consequently, Ground No.1 of the assessee's appeal is allowed and Ground No.2 of revenue's appeal is dismissed.ò

4.5.3 In the case on hand, the only basis on which the learned CIT (Appeals) sustained the disallowance of the expenditure incurred on assessee's in-house R&D facility was the view that the expenditure resulted in the acquisition of rights in or arising out of scientific research such as patents and it is for this reason there is an exclusion under Section 43(4)(ii) of the Act. In our considered view, the objective behind the exclusion clause in Sec. 43(4)(ii) of the Act appears to be that expenditure on scientific research should be incurred on research actually carried out by the assessee in-house and it should not spend money in acquiring rights in or arising out of scientific research carried on by some other person. If the interpretation sought to be urged by Revenue is to be accepted, then the benefit sought to be conferred by the provisions of Sec. 35(1)(iv) of the Act would virtually be denied in all cases by invoking the exclusion clause in Sec. 43(4)(ii) of the Act. Such a consequence would never have been intended by the Legislature. As already stated, the object behind the provisions of Sec. 35 of the Act is to encourage scientific research. Therefore, respectfully following the decision of the Hon'ble Karnataka High Court in the case of Talisma Corpn (P) Ltd. (supra) and of the co-ordinate bench of this Tribunal in the case of Tejas Networks Ltd. (supra), and in the facts and circumstances of the case, we are of the view and direct the Assessing Officer to allow the deduction claimed by the assessee under Section 35(1)(iv) of the Act on account of expenditure incurred on in-house R&D facility of the assessee. Consequently, grounds 1 to 5 of assessee's appeal are allowed.

5. **Ground Nos.6 to 9 – Disallowance u/s. 14A of the Act**.

5.1 In these grounds (supra), the assessee assails the decision of the learned CIT (Appeals) in holding that an amount of Rs.36,57,021 is attributable towards interest expenditure incurred on earning exempt income under Rule 8D(2)(ii) since the entire investments were made out of own funds. It is further contended that while working out the disallowance u/R 8D (2)(iii), the learned CIT (Appeals) erred in adopting the average value of investments at Rs.1,331.05 Crores whereas the average value of investments ought to be only 105.07 Crores. It was prayed that the disallowance thereunder should be restricted to Rs.73,976 as computed by the assessee and not Rs.52,53,500 as upheld by the learned CIT (Appeals).

5.2.1 We have heard the rival contentions of both the learned Authorised Representative for the assessee and the learned Departmental Representative for Revenue and perused and carefully considered the material on record. The facts of the matter, as emerge from the record is that in the course of assessment proceedings, the Assessing Officer observed that the assessee had earned exempt dividend income of Rs.7,13,70,554 in the year under consideration and in this regard had suo moto disallowed an amount of Rs.73,976 as administrative expenditure incurred for earning the aforesaid income. The Assessing Officer, invoking the provisions of Sec. 14A r.w. Rule 8D computed the total disallowance thereunder at Rs.92,73,634; comprising

disallowance of Rs.40,20,134 under Rule 8D(2)(ii) and Rs.52,53,500 u/Rule 8D(2(iii). On appeal, the learned CIT (Appeals) upheld the disallowance u/Rule 8D(2)(ii) to the extent of Rs.36,57,621 and upheld the entire disallowance of Rs.52,53,500 made by the Assessing Officer under Rule 8D(2)(iii).

5.2.2 Before us, the learned Authorised Representative had submitted that no disallowance of interest was warranted under Rule 8D(2)(ii) as a perusal of the assessee's balance sheet as on 31.3.2008 (copy placed at page 4 of paper book) would show that the assessee had no borrowings during the year and therefore the increase in investments during the year as per Schedule 4 (copy placed at page 6 of paper book) i.e. of approx. Rs.104 Crores would have been met out of own interest free funds without any outflow of interest. The co-ordinate bench of this Tribunal in its order in the assessee's own case for Assessment Year 2008-09, while disposing off Revenue’s appeal in ITA No.667/Bang/2014 vide order dt.23.9.2015, has held that the assessee has generated Rs.229.51 Crores from its operating activity; which in our view is sufficient to cover the assessee's investments during the year in both fixed assets of approx. Rs.117 Crores and approx. Rs.104 Crores in shares, mutual funds, etc. Before us, Revenue has not been able to contradict the aforesaid factual position. In view of the facts and circumstances of the case as discussed above, it is clearly established that the assessee had sufficient interest free own funds to cover the investments in shares, mutual funds, etc. that generated the exempt

dividend and therefore no disallowance under Rule 8D(2)(ii) is called for. We, therefore, direct the Assessing Officer to delete the disallowance of Rs.36,57,621 sustained by the learned CIT (Appeals).

5.2.3 In respect of the disallowance of an amount of Rs.52,53,500 under Rule 8D(2)(iii) upheld by the learned CIT (Appeals), the learned Authorised Representative drew the attention of the Bench to schedule 4 of the assessee's Balance Sheet (copy at page 6 of paper book) to show that the learned CIT (Appeals) at para 5.2 of the impugned order had erroneously taken the figure of average investment of the assessee at Rs.1331.05 Crores; whereas the average figure ought to be Rs.105.07 Crores (i.e. Rs.157.05 + Rs.53.09 divided by 2). It was contended that the assessee had suo moto disallowed administrative expenditure of Rs.73,976 under Rule 8D(2)(iii) and that no further disallowance was called for thereunder. Apart from raising this contention, the assessee was not able to establish before us why the disallowance of administrative expenses be restricted to Rs.73,976 and not be retained at ½%, the average investments as mandated under Rule 8D(2)(iii) which works out to Rs.52,53,500. In our view, taking into consideration the fact that the assessee had earned exempt dividend income of Rs.7,13,70,554, the disallowance as computed under Rule 8D(2)(ii) at Rs.52,53,500; which works out to approx. 7.36% thereof is reasonable in the facts and circumstances of the case in the year under consideration and is therefore upheld.

5.2.4 In the factual matrix of the case as discussed above, we direct the Assessing Officer to delete disallowance under Rule 8D(2)(ii) of an amount of Rs.36,57,621 sustained by the learned CIT (Appeals) and uphold the disallowance made by the authorities below under Rule 8D(2)(iii).

6. **Grounds 10 to 12** are general in nature and therefore no adjudication is called for thereon.

7. In the result, the assessee's appeal for Assessment Year 2008-09 is partly allowed.

Order pronounced in the open court on the 20th day of April, 2018.

Sd/-	Sd/-
(SUNIL KUMAR YADAV)	**(JASON P BOAZ)**
Judicial Member	Accountant Member

Bangalore,
Dt.20.04.2018.

*Reddy gp

Copy to :

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

Senior Private Secretary
Income Tax Appellate Tribunal
Bangalore.