

IN THE INCOME TAX APPELLATE TRIBUNAL,  
KOLKATA 'B' BENCH, KOLKATA  
Before Shri Pramod Kumar (Accountant Member),  
and Shri Mahavir Singh (Judicial Member)

I.T.A. No.: 666/ Kol. / 2012  
Assessment year: 2008-09

*Deputy Commissioner of Income Tax*  
*Circle 6, Kolkata*

.....Appellant

*Vs.*

*Gulshan Investment Co Ltd.*  
*9, Ezra Street, Kolkata 700 001*  
*[ PAN : AACCG0597R ]*

.....Respondent

**Appearances by:**

L K S Dahiya and K N Jana, *for the appellant*  
Girish Sharma, *for the respondent*

Date of concluding the hearing : March 6, 2013

Date of pronouncing the order : March 11, 2013

**ORDER**

**Per Pramod Kumar:**

1. By way of this appeal, the Assessing Officer has challenged correctness of learned Commissioner (Appeals)'s order dated 21<sup>st</sup> January 2011, in the matter of assessment under section 143(3) of the Income Tax Act, 1961 (hereinafter referred to as 'the Act') for the assessment year 2008-09, on the following ground:

That on the facts and circumstances of the case, learned CIT(A) erred in law in holding that the disallowance under section 14 A of the Income Tax Act, read with rule 8D of the Income Tax Rules, is not applicable in the case of the assessee since the shares were kept as stock in trade. The CIT(A) should have upheld the disallowance made by the AO.

The appeal is time barred by 10 days, but the Assessing Officer has moved a condonation petition, duly supported by an affidavit. Learned

counsel for the assessee does not object to the prayer for consolidation. In this view of the matter, and having regard to the material on record, we condone the delay and proceed to take up the matter on merits.

3. The issue in appeal lies in a very narrow compass of undisputed material facts. The assessee is engaged in the business of share trading. During the course of scrutiny assessment proceedings, the Assessing Officer noticed that while the assessee has earned dividend income of Rs 18,91,556, the assessee has not made any disallowance under section 14 A in respect of "expenses relatable to the above exempt income". The Assessing Officer also noticed that the assessee had paid interest of Rs 10,34,315. On these facts, the Assessing Officer computed the disallowance under section 14 A r.w.r. 8 D as follows:

**Disallowance under section 14A :**

During the relevant year, the assessee had earned dividend income of Rs.18,91,556/-. It was found that the expenses relatable to above exempt income has not been included back to the total income for taxation. (2) Assessee paid interest for Rs.10,34,315/-. As per point 2 of Rule 8D Rs.7,97,762/- is disallowed. As per point (3) disallowance is worked out as section 14A read with Rule 8D of the I.T. Act as under :-

Opening value of stock-in-trade	:	Rs.20,17,95,911
Closing value of stock-in-trade	:	Rs.33,72,25,080
Average stock-in-trade	:	Rs.26,95,10,496
½% of average stock-in-trade	:	Rs. 13,47,552
Total addition under section. 14A	:	Rs. 21,45,314
		(i.e. Rs.13,47,552 + Rs.7,97,762)

2. Aggrieved by the stand so taken by the Assessing Officer, assessee carried the matter in appeal before the CIT(A). Learned CIT(A), after elaborately reproducing the written submissions of the assessee, concluded as follows:

I have duly considered the observations of the Assessing Officer and submissions of the assessee. The assessee did not show any expenditure on the exempted income or disallowance under section 94(7) in the return of income. There cannot be any income without any kind of expenses or labour howsoever, small it may be. Therefore, the Assessing Officer was justified in calculating the disallowance on the exempted income. During the appellate proceedings the appellant was asked

to file the details of share dividend earned and calculation of loss disallowable as per the provisions of section 94(7). The appellant submitted the details of all the shares and has calculated an amount of Rs.1,57,227/- to be disallowable as loss against the dividend income under provisions to section 94(7) of the I.T. Act, 1961. The assessee does not have any investments and all the shares are being held as stock in trade only. Therefore, the assessee submitted that no deduction can be made on account of expenses. Following the judgments of Hon'ble Kerala High Court in CIT -vs.- Leena Ramchandran (Kerala High Court) - ITA No. 1784 of 2009 and Hon'ble ITAT, Mumbai in the case of Yatish Trading Co. P. Ltd. -vs.- ACIT (ITAT Mumbai)- ITA No. 456/Mum./2009(10.11.2010) relied upon by the assessee in the written submissions, it is held that Rule 8D is not applicable in the case of assessee since there are no investments and all the shares were kept as stock in trade only and further no interest expenses have been incurred for investments. However, section 14A is still applicable where it provides that no deduction in respect of expenditure incurred by the assessee in relation to exempted income will be allowed. There are expenses incurred for earning dividend income as well as earning of the business income. The dividend income may not involve separate/ direct expenses but indirect expenses are there in purchasing those shares and other administrative expenses in the earning of income. The section 14A does not take care of only direct expenses but indirect expenses are also to be allocated to the exempted income. There may not be any investments for making Rule 8D applicable in the facts of the appellant. Rule 8D is a method prescribed when the dividend income is earned from investments. Therefore, in the facts and circumstances of the case of the assessee the expenditure is estimated to be @10% of the dividend earned, as fair and reasonable estimation. Therefore, an expenditure of Rs.1,89,155/- is disallowed in addition to an amount of Rs.1,57,227/- as disallowance under section 94(7) in relation of earning of dividend income. This ground of appeal is partly allowed.



3. The Assessing Officer is aggrieved of the relief so granted by the CIT(A) and is in appeal before us.
4. We have heard the rival contentions, perused the material on record and duly considered factual matrix of the case as also the applicable legal position.
5. We consider it appropriate to begin with reproducing Rule 8 D of the Income Tax Rules, which is as follows:

*Method for determining amount of expenditure in relation to income not includible in total income.*

**8D(1)** Where the Assessing Officer, having regard to the accounts of the assessee of a previous year, is not satisfied with-

- (a) the correctness of the claim of expenditure made by the assessee; or
- (b) the claim made by the assessee that no expenditure has been incurred, in relation to income which does not form part of the total income under the Act for such previous year,

he shall determine the amount of expenditure in relation to such income in accordance with the provisions of sub-rule (2).

**(2)** The expenditure in relation to income which does not form part of the total income shall be the aggregate of following amounts, namely:-

(i) the amount of expenditure directly relating to income which does not form part of total income;

(ii) in a case where the assessee has incurred expenditure by way of interest during the previous year which is not directly attributable to any particular income or receipt, an amount computed in accordance with the following formula, namely:-

$$\frac{A \times B}{C}$$

Where A = amount of expenditure by way of interest other than the amount of interest included in clause (i) incurred during the previous year;

B = the average of value of investment, income from which does not or shall not form part of the total income, as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year;

C = the average of total assets as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year;

(iii) an amount equal to one-half per cent of the average of the value of investment, income from which does not or shall not form part of the total income, as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year."

**3.** For the purposes of this rule, the 'total assets' shall mean, total assets as appearing in the balance sheet excluding the increase on account of revaluation of assets but including the decrease on account of revaluation of assets.

6. A plain look at the above rule shows that 8 D(2)(ii) and (iii) can only be applied in the situations in which shares are held as investments, and that this rule will not have any application when the shares are held as stock in





trade. It is so for the elementary reason that the one of the variables on the basis of which disallowance under rules 8D(2)(ii) and (iii) is to be computed is the value of "investments, income from which does not or shall not form part of total income", and, when there are no such investments, the rule cannot have any application. When no amount can be computed in the light of the formula given in rule 8 D(ii) and (iii), no disallowance can be made under rule 8D (2)(ii) and (iii) either. As held by Hon'ble Supreme Court in the case of **CIT Vs B C Srinivas Shetty ( 128 ITR 294)**, when computation provisions fail, the charging provisions cannot be applied, and by the same logic, when the computation provisions under rule 8 D (2) (ii) and (iii) fail, disallowance under the said provisions cannot be made either as the said provision is rendered unworkable.

7. However, that does not exclude the application of rule 8 D(2)(i) which refers to the **"amount of expenditure directly relating to income which does not form part of total income"**. In other words, in a case where shares are held as stock in trade and not as investments, the disallowance even under rule 8 D is restricted to the expenditure directly relatable to earning of exempt income. Consequently, while Section 14 A will still apply in the cases whether shares are held as stock in trade or as investments, and that is precisely what a Special Bench of this Tribunal has held in the case of **ITO Vs Daga Capital Management Pvt Ltd ( 117 ITD SB 169)**, the disallowance to be made under section 14 A read with rule 8 D will be restricted to direct expenses incurred in the earning of dividend income.

8. It is also important to bear in mind the fact that, in the case of **Godrej & Boyce Mfg Co Ltd Vs DCIT (328 ITR 81)** and dealing with a period when rule 8 D was not applicable, Hon'ble Bombay High Court has not only held that **"the Assessing Officer has to enforce the provisions of sub section (1) of Section 14A, and for that purpose, the Assessing Officer is duty bound to determine the expenditure which has been incurred in relation to income which does not form part of total income under the Act"**, but further

while remitting the matter to the Assessing Officer for computation of disallowance under section 14 A, that the Assessing Officer shall examine whether " **any expenditure (direct or indirect)**" [ Emphasis by underlining supplied by us] in relation to exempt income is incurred and that disallow the same. As a corollary to the above legal position, so far as disallowance under section 14 A in a situation in which the exempt income yielding asset, such as shares in question, is held as stock in trade, and not as investment, the disallowance will be of related direct and indirect expenditure, whereas disallowance under rule 8 D will be restricted to disallowance of only direct expenses. Revenue thus derives no advantage from invoking rule 8 D in such cases; on the contrary, the scope of disallowance is only minimised in such a situation.

9. So far as the case before us is concerned, as will be clearly discernible from the observations of the learned CIT(A) extracted earlier in this order, learned CIT(A) has upheld disallowance under section 14 A in respect of even indirect expenditure, but he has merely held that the provisions of rule 8 D do not come into play in this case as the shares are not held as 'investments'. As learned counsel rightly contends the provisions of rule 8 D can never be applied in a case where exempt income yield assets are not held as investments, and that the related assets, i.e. shares, having been held as stock in trade all along, there is no occasion to invoke rule 8 D. There is no infirmity in this approach, nor do revenue authorities stand to lose anything by this approach canvassed by the assessee. Quite to the contrary of what learned Departmental Representative perceives to be advantageous to the Assessing Officer, in case the application of rule 8 D was to be upheld, there would have been no disallowance at all since not only that no investments were held by the assessee, admittedly there are no direct expenses are incurred on earning of the dividends and as such in all the three segments of disallowance under rule 8D(2) i.e. 8D (2) (i), (ii) and (iii), there will be zero disallowance. As against this zero disallowance under rule 8 D, the CIT(A) has upheld disallowance to the extent of Rs 1,57,227 in respect of indirect

expenses attributed to the earning of dividends, and it has even the case of revenue that this disallowance for indirect expenses is unfair or unreasonable.

10. In view of the above discussions, while uphold the conclusions arrived at by the learned CIT(A), we also make it clear that, in our humble understanding, the provisions of Section 14A are indeed attracted whether or not the shares are held as stock in trade or as investments, even though the provisions of rule 8D(2)(ii) and (iii) cannot be invoked in such a case, and even though the provisions of rule 8 D(2)(i) are much narrower in scope than the scope of Section 14 A *simplicitor*. With these observations, we confirm the conclusions of the learned CIT(A) and decline to interfere in the matter.

11. In the result, the appeal is dismissed. Pronounced in the open court today on 11 th day of March, 2013

Sd/xx

**Mahavir Singh**  
(Judicial Member)

Sd/xx

**Pramod Kumar**  
(Accountant Member)

**Kolkata, the 11<sup>th</sup> day of March, 2013**

Copies to : (1) The appellant  
(2) The respondent  
(3) CIT  
(4) CIT(A)  
(5) The Departmental Representative  
(6) Guard File



By order etc

Assistant Registrar  
Income Tax Appellate Tribunal  
Kolkata benches, Kolkata