IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO.487 OF 2015

Pr. Commissioner of Income-Tax-3,
Aayakar Bhavan, M.K. Road,
Mumbai – 400 020. .... Appellant

- Versus -

M/s. Reliance Capital Asset Management Ltd., One Indiabulls Center, Tower-I, 12th Floor, Jupiter Mills Compound, Senapati Bapat Road, Elphinstone Road,
Mumbai-400 013. .... Respondent

Mr. Suresh Kumar with Ms Samiksha Kanani for the Appellant.

Mr. R. Murlidhar with Mr. Rajesh Shah i/by M/s. Rajesh Shah & Co. for the Respondent.

CORAM: S.C. DHARMADHIKARI &
PRAKASH D. NAIK, JJ.

DATE : SEPTEMBER 19, 2017

ORAL ORDER (Per Shri S.C. DHARMADHIKARI, J.**):**

1. By this appeal, the Revenue questions the order passed by the Income Tax Appellate Tribunal, Bench at Mumbai,

dated 17-10-2014.

2. The Bench had before it two appeals of the assessee for the Assessment Years 2007-08 and 2008-09 being Income Tax Appeal Nos.8625 of 2010 and 4459 of 2012.

3. There was also an Income Tax Appeal No.4795 of 2012 by the Revenue for the Assessment Year 2008-09.

4. A common order was passed by the Tribunal because all these appeals were heard together.

5. As far as the assessee is concerned, for the Assessment Year 2007-08, it raised two grounds in its appeal. The first was: disallowance of software expense; and the second was, disallowance made under Section 14A of the Income Tax Act, 1961 ("the Act" for short).

6. As far as the Revenue's appeal before us is concerned, it is restricted only to the disallowance under Section 14A of the Act.

7. Mr. Suresh Kumar would submit that this appeal raises the following substantial question of law:-

> *"Whether on the facts and in the circumstances of the case, the Hon. Income Tax Appellate Tribunal was justified in restricting the disallowance u/s 14A to Rs.3,50,000/- as against Rs.1,46,78,090/- made by the Assessing Officer u/s 14A r.w. Rule 8D without appreciating the fact that for invoking disallowance u/s 14A, it is not material that the assessee should have earned such exempt income during the financial year under consideration as per CBDT circular No.5/2014 dated 11.02.2014?*

Thus, the disallowance made under Section 14A was an issue which the Revenue has projected before us. From the record it appears that the assessee's appeal for the Assessment Year 2008-09 is dismissed, and the assessee's appeal for the Assessment Year 2007-08 and the Revenue's appeal for the Assessment Year 2008-09 were partly allowed.

8. The Revenue is in appeal before us insofar as Assessment Year 2008-09.

9. Even in the Revenue's appeal which was partly

allowed, the issue is same and in respect of disallowance made under Section 14A of the Act.

10. Mr. Suresh Kumar, appearing on behalf of the Revenue, would submit that the facts are not very much in dispute. It is true that the assessee is the Asset Manager of Reliance Mutual Fund. The Assessing Officer noted that the assessee received dividends on two occasions and further the said dividends were also directly credited to the Bank account. The assessee disclosed dividend income of Rs.8,33,46,239/- and long term capital gains of Rs.68,88,582/- and claimed both the income as exempt. In its return of income, the assessee worked out a sum of Rs.1,25,605/- as expenditure incurred in earning the above incomes. However, the Assessing Officer took the view that the disallowance under Section 14A should be worked out as per the provisions of Rule 8D of the Income Tax Rules, 1962 ("the Rules" for short). The Assessing Officer has accepted that there was no requirement of making any disallowance out of interest expenditure. However, he disallowed part of indirect expenses calculated at 0.5% of the average value of investments,

which worked out to Rs.1,46,78,090/-. This was in terms of Rule 8D and accordingly, the Assessing Officer enhanced the disallowance made by the assessee to the above figure.

11. The assessee approached the Commissioner of Income Tax (Appeals) and argued that it had substantiated the reasonableness of the working of expenses in para 2.5 of its submission dated 19-3-2010 (to the extent of Rs.1,25,605/-). There are 27 entries of dividends. All are by way of credit and no receipts are by cheque. Eight receipts are by way of direct credit and balance 19 entries were received in the form of dividend reinvestment. The total number of entries in the nature of transactions in respect of long term capital gains (STT) paid are four in number. It is in these circumstances, the assessee submitted that the working of the Assessing Officer in accordance with Rule 8D is unreasonable and excessive and the assessee's working is reasonable.

12. That is how the matter was decided and after both sides were heard, the Commissioner restricted the disallowance

to Rs.1,25,66,793/- as against the amount of Rs.1,45,52,785/- disallowed by the Assessing Officer. Aggrieved, both sides went in appeal to the Tribunal.

13. Mr. Suresh Kumar would submit that the reasons from paras 8 to 8.2 of the Tribunal's order are totally vitiated by non-application of mind. The Assessing Officer was right for once he was satisfied in terms of Section 14A that having regard to the accounts of the assessee, the claim of the assessee in respect of expenditure incurred in relation to income not includible in total income under the Act was not justified, then, he was obliged to go to Rule 8D and in the submission of Mr. Suresh Kumar, Rule 8D {sub-rule (2)(iii)} would have to be invoked and applied in this case. On facts, in terms of this sub-rule, 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, shall be the expenditure in relation to income which does not form part of the total income. Thus, according to

Mr. Suresh Kumar, Rule 8D(2), sub-rule (iii) would enable the Assessing Officer to act in accordance therewith. Even the First Appellate Authority has not accepted the version of the assessee, as would be apparent from para 7 of the Tribunal's order. In the circumstances, the conclusion reached by the Tribunal in para 8.2 is erroneous, both on facts and law. All the more when the Tribunal has not accepted the version of the assessee in its entirety but modified the order of the Commissioner of Income Tax (Appeals) and restricted the disallowance made under Section 14A of the Act to Rs.3,50,000/-. Mr. Suresh Kumar would, therefore, submit that the present appeal be admitted.

14. On the other hand, Mr. Murlidhar, learned counsel appearing for the assessee in the appeal, would submit that there is no merit in the appeal. Mr. Murlidhar would submit that Section 14A, sub-section (2), which has been invoked in this case, mandates that 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 the Act in accordance with such method as may be prescribed. However,

Mr. Murlidhar submits that this is conditional upon the satisfaction of the Assessing Officer. 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 which is incurred and in terms of Section 14A, then alone he can fall-back on the said sub-rules and apply Rule 8D. Mr. Murlidhar invites our attention to the order of the Assessing Officer and particularly his conclusion that the assessee disputes the quantum of disallowance and once Section 14A is attracted, the disallowance is to be made as per Rule 8D only which has been prescribed by the Legislature.

15. Mr. Murlidhar would submit that this understanding of the Assessing Officer was totally incorrect. The position is that he has to be dissatisfied with the correctness of the claim of the assessee having regard to the assessee's account. Even the Commissioner of Income Tax (Appeals) has found that the Assessing Officer has not specifically rejected the working and has not provided any reason for doing so.

16. The Commissioner, however, committed a further mistake and which was sought to be corrected by the Tribunal. The Commissioner, in his fairly detailed order, according to Mr. Murlidhar, has agreed with the appellant's working of disallowance of Rs.1,25,66,793/- instead of the Assessing Officer's disallowance of Rs.1,45,52,785/-. That is how the Commissioner only partly allowed the assessee's appeal.

17. However, the Tribunal found and rightly that the assessee has allotted the expenses but in relation to investments made in various schemes of Reliance Mutual Fund. The assessee made investments and of the figure set out in para 8 of the Tribunal's order. Thus, out of aggregate investments of Rs.68.25 crores, the investments made in other companies were only Rupees Eight Crores. The remaining investments are mainly in various schemes of Reliance Mutual Fund only and also in other group concerns. Once there is no dispute that the investments made in the various schemes of Reliance Mutual Fund and also in other group concerns are usually made out of business policy, then, bearing in mind the Investment Schedule provided in the

Balance Sheet, the Tribunal should have, in fact, deleted the entire disallowance as worked out. However, even if the Tribunal has restricted the disallowance to be made under Section 14A to Rs.3,50,000/-, it has essentially confirmed the approach of the Commissioner of Income Tax (Appeals). Thus, on the point of applicability of Rule 8D(2) there is a concurrent finding, according to Mr. Murlidhar. Hence, he would submit that the appeal be dismissed.

18. With the assistance of Mr. Suresh Kumar and Mr. Murlidhar, we have perused the order of the Assessing Officer, that of the First Appellate Authority and the Tribunal. We have perused Chapter IV of the Income Tax Act which contains Section 14A. The relevant part of Section 14A reads thus:-

> *"(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."

19. The Assessing Officer did not specifically record that he is not satisfied with the correctness of the claim of the assessee in respect of the expenditure in relation to the income which does not form part of the total income under the Act. However, he felt obliged and going by the presence of Rule 8D that once Section 14A is attracted, the disallowance is to be made as per Rule 8D only which has been prescribed by the Legislature. The Assessing Officer has not adverted to the plain language of sub-section (2) of Section 14A.

20. It is that mistake committed by the Assessing Officer which was partially corrected by the First Appellate Authority. The First Appellate Authority agreed with the assessee that the Assessing Officer has not commented upon the correctness or otherwise of the appellant's working of the claim. He has not specifically rejected that working and has not provided any reason for doing so. The Commissioner was of the view that before proceeding to compute the disallowance under Section

14A as per Rule 8D, the Assessing Officer should consider the working of expenses made by the assessee and when he is not satisfied with the said working and terms it as incorrect, based on objective criteria and for cogent reasons, he can then proceed to work out the disallowance under Section 14A as per Rule 8D of the Rules.

21. We cannot find any fault with this conclusion of the First Appellate Authority based as it is on the language of sub-section (2) of Section 14A of the Act, reproduced above. The Commissioner was aware that the assessee is acting as an Asset Management Company of Reliance Mutual Fund. Its principal business is of managing the mutual fund schemes of Reliance Mutual Fund. As Investment Manager, the assessee has earned management and advisory fees. The assessee has invested its own surplus fund in various investments and earned income thereon which included exempt dividend income and exempt capital gains. Once the main activity is of Investment Manager and the expenses are primarily in relation to this activity, the assessee invested the surplus funds into various securities which

has given them exempt income. The Tribunal has found that the total investments made are of Rs.70.62 crores as on 1-4-2007 and which has come down to 68.26 crores as on 31-3-2008. The investment is mainly made by the assessee in various schemes of Reliance Mutual Fund and its subsidiaries. There should not be any dispute that the investments made in the various schemes of Reliance Mutual Fund and also in the group concerns are on account of business policy. The assessee received dividend from 27 transactions, out of which 8 receipts were by way of direct credit to its Bank account and 19 receipts were in the form of reinvestment of dividend, namely, the dividend amount was reinvested and it did not physically receive the sum. The transactions relating to earning of dividend income as well as long term capital gains are limited. Even the Investment Schedule of the Balance Sheet was perused by the Tribunal and it found that all the transactions are mainly restricted within the group companies/schemes.

22. Therefore, these transactions were analysed and in the backdrop of the business of the assessee, the Tribunal

concluded that there was no necessity to apply the formula prescribed in Rule 8D(2)(iii) of the Rules. We are, therefore, not in agreement with Mr. Suresh Kumar that Rule 8D(2)(iii) has been overlooked or ignored by the Tribunal completely. In the peculiar facts and circumstances of the assessee's case and the nature of its investments made, the Tribunal concluded that the disallowance worked out by the assessee should have been accepted. However, it did not accept the figure of disallowance worked out by the assessee. That although the Tribunal, in one line or sentence in para 8, says that the disallowance to be made under Rule 8D is determined at Rs.3,50,000/-, we are not in agreement with Mr. Suresh Kumar that the Tribunal has accepted the applicability of this Rule/sub-rule/clause. This one sentence or one line cannot be read in isolation and out of context. Once the formula prescribed in Rule 8D(2)(iii) of the Rules could not have been applied is the essential conclusion, then, merely because the Tribunal did not accept the working of disallowance by the assessee in its entirety, does not mean that the appeal raises a substantial question of law. We do not think

that the Tribunal's exercise can be termed as totally erroneous or illegal. It is neither perverse. The Tribunal's order cannot be said to be vitiated by an error of law apparent on the face of the record. We do not think that the working by the Tribunal or the determination of the disallowance at Rs.3,50,000/- does not meet the ends of justice. It is restricted bearing in mind the facts and peculiar to the assessee's case. Partly the assessee's arguments have been accepted and the appeal allowed by setting aside the order of the Assessing Officer and that of the Commissioner of Income Tax (Appeals). We do not think that the question proposed by Mr. Suresh Kumar is a substantial question of law.

23. As a result of the above discussion, we do not find any merit in this appeal of the Revenue. It is dismissed. No costs.

(PRAKASH D. NAIK, J.) (S.C. DHARMADHIKARI, J.)