

A note on the recent judgement of Punjab & Haryana High Court, on disallowance under section 14A of the I.T. Act, 1961

Recently, the Punjab and Haryana High Court has rendered a very significant judgement in the case of *CIT Vs Hero Cycles Ltd.*[2009] 31 DTR 301 (P&H)

It was held in this case that where it is found that for earning exempted income no expenditure has been incurred, disallowance under section 14A cannot stand. In view of the finding of the Tribunal, it is clear that the expenditure on interest was set-off against the income from interest and the investment in the share and funds was out of the dividend proceeds. In view of this finding of fact, disallowance under section 14A was not sustainable.

For the sake of ready reference, the Head Note and the Conclusion of the aforesaid judgement, on page 302 of the Report, are reproduced as follows :

*Held : Contention that even where the assessee claimed that no expenditure had been incurred, the correctness of such claim could be gone into by the AO and in the present case, the claim of the assessee that no expenditure was incurred was found to be not acceptable by the AO and thus disallowance was justified is not sustainable. In view of finding of the Tribunal, it is clear that the expenditure on interest was set off against the income from interest and the investments in the share and funds were out of the dividend proceeds. In view of this finding of fact, disallowance under s.14A was not sustainable. Whether, in a given situation, any expenditure was incurred which was to be disallowed, is a question of fact. The contention of the Revenue that directly or indirectly some expenditure is always incurred which must be disallowed under s.14A and the impact of expenditure so incurred cannot be allowed to be set off against the business income which may nullify the mandate of s.14A, cannot be accepted. Disallowance under s.14A requires finding of incurring of expenditure; where it is found that for earning exempted income no expenditure has been incurred, disallowance under s. 14A cannot stand. In the present case finding on this aspect, against the Revenue , is not shown to be perverse. Consequently, disallowance is not permissible. – CIT vs.Winsome Textile Industries Ltd. (IT Appeal No. 504 of 2008, dt. 25th August., 2009) **followed***

Conclusion : *Disallowance under s.14A requires finding of incurring of expenditure; where it is found that for earning exempted income no expenditure has been incurred, disallowance under s.14A cannot stand.*

In addition, para (3) of the aforesaid judgement on pages 303 and 304 of the Report is also relevant, which is reproduced as follows :

3. *Learned counsel for the appellant relies upon s. 14A(2) and r. 8D(1)(b) to submit that even where the assessee claimed that no expenditure had been incurred, the correctness of such claim could be gone into by the AO and in the present case, the claim of the assessee that no expenditure was incurred was found to be not acceptable by the AO and thus disallowance was justified. We are unable to accept the submission.*

From the aforesaid para (3) of the judgement, it may be seen that the Hon. High Court has also taken into consideration the provisions of section 14A(2) and rule 8D of the I.T. Rules,1962, while delivering the aforesaid judgement.

Place : Pune

(S.K. Tyagi)

Date : 15.2.2010

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