

IN THE HIGH COURT OF GUJARAT AT AHMEDABAD**R/TAX APPEAL NO. 144 of 2016****FOR APPROVAL AND SIGNATURE:**

HONOURABLE MR. JUSTICE BHARGAV D. KARIA
and
HONOURABLE MR. JUSTICE NIRZAR S. DESAI

Approved for Reporting	Yes	No
		No

THE PRINCIPAL COMMISSIONER OF INCOME TAX-1
 Versus
 ADANI INFRASTRUCTURE SERVICES PVT.LTD.

Appearance:

MS MAITHILI D. MEHTA for the Appellant(s) No. 1
 MR B S SOPARKAR(6851) for the Opponent(s) No. 1

CORAM: HONOURABLE MR. JUSTICE BHARGAV D. KARIA
and
HONOURABLE MR. JUSTICE NIRZAR S. DESAI

Date : 24/09/2026**JUDGMENT****(PER : HONOURABLE MR. JUSTICE BHARGAV D. KARIA)**

1. Heard learned Senior Standing Counsel
 Ms.Maithili D. Mehta for the appellant and
 learned advocate Mr.B.S.Soparkar for the
 respondent.

2. This appeal was admitted vide order
 dated 15th June, 2016 for consideration of
 the following substantial question of law,

arising out of the order dated 17th July, 2015 passed by the Income Tax Appellate Tribunal (for short 'the Tribunal'), Ahmedabad "A" Bench, Ahmedabad in ITA No.1943/Ahd/2012 for Assessment Year 2009-10:

"Whether on the facts and in the circumstances of case and in law, the tribunal was right in upholding the decision of CIT (A) in deleting the addition of Rs.23,77,67,259/- made u/s 14A(2) r.w. Rule 8D (2) (ii)?"

3. The brief facts of the case are as under :

3.1. During the course of assessment proceedings, the Assessing Officer noticed that the assessee earned the dividend

income of Rs.79,20,56,505/-, received profit from partnership firm amounting to Rs.18,38,067/- and received interest amounting to Rs.26,08,28,104/-. Out of these three items, so far as dividend income and partnership profits are concerned, the same were not included in income liable to be taxed in view of the provisions of Section 10(36) and Section 10[2A] of the Income Tax Act, 1961 (for short 'the Act'). So far as interest receipts are concerned, it was noticed by the Assessing Officer that the assessee had set off the same against the interest expenses of Rs.25,77,86,144/-. The Assessing Officer also noted that the investment in the shares of Mundra Port & Special Economic Zone Limited had gone up

from 576.12 Crores to 933.27 Crores whereas, the assessee ceased to hold shares in Adani Enterprises Limited, which were valued at Rs.701.12 Crores in the beginning of the year.

3.2. Considering such facts, the Assessing Officer proceeded on the basis that entire business activity of the assessee was earning tax exempt income from dividend and share of profits from the partnership firm. It was also noted by the Assessing Officer that the assessee incurred interest expenses of Rs.25,77,86,144/-, Rs.6,93,000/- for salaries, Rs.1,98,000/- for professional charges, etc. The Assessing Officer therefore, computed the disallowance under Section 14A of the Act read with Rule 8D of

the Income Tax Rules, 1962 (for short 'the Rules') which included the disallowance of Rs.23,77,67,259/- in respect of the proportionate interest under Rule 8D(2)(ii) of the Rules.

3.3. Being aggrieved, the assessee preferred an Appeal before the CIT(Appeal), who deleted the disallowance considering the contention raised on behalf of the assessee that there was a net interest income and therefore, interest expenses cannot be considered for application of Section 14A of the Act. It was also contended by the assessee that there was a back to back transaction of loan, advanced to the another concern, for which the interest was earned which was in excess of the interest paid for loan, borrowed for

such purpose.

3.4. Being aggrieved, the appellant-Revenue preferred an Appeal before the Tribunal.

3.5. The Tribunal, after considering the submissions made by both the sides, upheld the order passed by the CIT(Appeals) by observing as under:

"9. In the light of the above analysis, the interest expenditure will have to be excluded from the expenses to be allocated under rule 8D(2)(ii) for the reason that the interest expenditure is no way relatable to exempt income. The entire borrowing by the assessee, as we have seen on the facts of this case, has been - passed on the AIDL and entire interest on this borrowing has been received from the

AIDL. It is completely a back to back transaction and the material on record clearly demonstrates that Just because it is routed through the same bank account, it cannot be presumed that the money is out of the common funds. Such a presumption, as has been strenuously argued before us by the learned Departmental Representative, will be contrary to the clearly established facts on record. For this reason also, and in the light of the coordinate bench decision in the case of Champion Commercial Co Ltd (supra), the relief granted by the CIT(A) was quite justified."

4.1. Learned Senior Standing Counsel Ms.Maithili Mehta for the appellant-Revenue submitted that, after considering the fact that the assessee has only the exempt income from the dividend and the profit

from share of the partnership firms, the expenditure incurred on interest of Rs.25,77,86,144/- was rightly considered by the Assessing Officer, for the purpose of application of Section 14A of the Act read with Rule 8D(2)(ii) of the Rules.

4.2. It was submitted that the Assessing Officer has arrived at such finding on the basis that no separate accounts were maintained by the assessee for availing the loan as well as the advancement of such amount to the other concern, on which the interest was earned and therefore, the Assessing Officer was justified in not permitting the assessee to set off the interest expenses against the interest income earned by the assessee.

4.3. It was therefore submitted that both the CIT(Appeals) and the Tribunal have erred in law in considering the netting of the interest income, by permitting the assessee to set off the interest expenses, for deletion of the addition made by the Assessing Officer under Section 14A of the Act read with Rule 8D(2)(ii) of the Rules. It was therefore submitted that the Appeal may be allowed, by answering the question in favour of the Revenue and against the assessee.

5. On the other hand, learned advocate Mr.B.S.Soparkar for the respondent-assessee submitted that there are concurrent findings of fact arrived at by both the CIT(Appeals) and the Tribunal and even otherwise, in assessee's own case for the

Assessment Year 2011-12, similar issue had arisen and the Tax Appeal has already been dismissed by this Court, being Tax Appeal No.1 of 2021, vide order dated 8th January, 2021. It was further submitted that the issue of netting of the interest income is no more res-integra in view of the decision of this Court in case of ***Principal Commissioner of Income Tax Versus Nirma Credit & Capital (P.) Ltd.*** reported in **2017 85 taxmann.com 72 (Gujarat)**. It was also submitted that so far as the aspect of mixed fund raised by the Assessing Officer is concerned, the issue is also covered in favour of the assessee by the decision of this Court in case of ***Principal Commissioner of Income-tax-2, Vadodara v. Shreno Ltd.*** reported in **[2019] 102**

taxmann.com 129. It was therefore submitted that the Appeal may be dismissed by answering the question in favour of the assessee and against the Revenue.

6. Having heard the learned advocates for the parties and considering the facts of the case, it appears that both the CIT(Appeals) and the Tribunal have arrived at concurrent findings of facts. The CIT(Appeals), while deleting the additions made by the Assessing Officer under Section 14A of the Act read with Rule 8D(2)(ii) of the Rules, has held as under:

"3.3 I have considered the facts of the case; assessment order and appellant's written submission. Assessing officer disallowed interest and other expenses under section 14A read with rule 8D since

appellant earned exempt income. The decisions relied upon by the appellant are prior to assessment year 2008-09 when the rule 8D was not applicable. Accordingly, these decisions are not applicable to this assessment year when the disallowance is to be made as per the formula given in rule 8D. Since appellant did not make any disallowance on account of 13 expenses relating to exempt income, provisions of sub-section 14A(3) is applicable as per which disallowance is to be made as per formula given in rule 8D. There is no discretion left after applicability of this provision and therefore these decisions are not relevant now. It is not in dispute that in the appellant's case of rule 8D read with section 14A is applicable since appellant earned substantial exempt income and did not disallow any expense. Accordingly the

judicial decisions relied upon by both the sides are not discussed here.

The disallowances made were in respect of interest Rs.23,77,67,259 and other expenses RS 7,26,15,653. Subsequently assessing officer passed order under section 154 and reduced the disallowance out of other expenses to RS 20,15,150. Therefore appellant's main grievance in this appeal is against disallowance of interest of Rs. 23,77,67,259 computed by the AO under rule 8D(2)(ii). Against this disallowance, appellant submitted that it had earned interest of Rs.25.77,88,144 by advancing money to Adani Infrastructure Developers P Ltd. (AIDPL) from loan taken from IDFC Ltd. on which interest of Rs.25,77,88,144 is paid. Hence there is one to one nexus between loan taken from IDFC and loan given to AIDPL, so no

disallowance of interest expense u/s 14A read with rule 8D(2)(ii) can be made. The facts relating to borrowings from IDFC and lending to AID were completely disclosed during assessment proceedings to the assessing officer which were also mentioned in the assessment order. Therefore it is not in dispute that borrowings from IDFC Ltd were made to lend to AIDPL. It is also clear from the earning of interest income from AIDPL and payment of interest to IDFC which are of identical amount of RS 25,77,88,144. This clearly shows that interest income from AIDPL is directly attributable to interest payment to IDFC Ltd. In the light of these facts, it would be relevant to mention the relevant provisions from IT rules-

"8D (2)- The expenditure in relation to income which does not form part of the

total income shall be the aggregate of the following amounts, namely-

(i)-----

(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-----

From the above it is clear that the disallowance of interest under rule 8D (2) (i) is to be made in respect of any interest which is not directly attributable to any particular income or receipt. In the case of appellant interest payment to IDFC Ltd is directly attributable to interest income/receipt from AIDPL. From the figures of interest receipt and payment and also from the

details of borrowing and lending, it is clear that interest expenditure is directly attributable to the interest income and therefore no disallowance of interest under rule 8D (2) (15) can be made. Since there is no interest payment other than the interest payment to IDFC Ltd (which is directly attributable to the earning of interest income of identical amount), the computation of disallowance of interest under rule 8D(2)(ii) will be nil. Considering these facts, the interest disallowance made by the assessing officer by ignoring the express provisions of section 14A read with rule 8D(2)(ii) cannot be sustained. Accordingly the disallowance of interest made by the AO is deleted. As regards disallowance of other expenses, assessing officer already rectified the assessment order and restricted the disallowance under rule

8D(2) (iii) to the expenses claimed by the appellant. In view of this, appellant did not press ground number 3 which is without prejudice to this ground. Since disallowance under section 14 A read with rule 8D is to be made as discussed earlier, the disallowance of other expenses amounting to Rs. 20,15,150 is confirmed."

7. The aforesaid findings arrived at by the CIT(Appeals) are upheld by the Tribunal, after considering the facts of the case, as reproduced herein above.

8. In case of **Nirma Credit & Capital (P.) Ltd (Supra)**, this Court in similar facts, has held as under :

"11. It is in this context that the computation of factor 'A' in the said formula assumes significance. In plain

terms, 'A' represents the amount of expenditure by way of interest ignoring the interest expenditure already included in clause(i). The expression used by the legislature is "amount of expenditure by way of interest". When the legislature has therefore, used this expression "amount of expenditure", the said term shall have to be interpreted in the manner that will bring about the correct legislative intent and equitable application thereof. As in case on hand, when the assessee pays interest on borrowings as also earns taxable interest on investments made by him during a particular year, his interest expenditure has to be considered as one which is the net of interest paid minus interest earned. Any other view would give the unintended computation of factor 'A' provided in clause(ii) of sub-rule(2) of Rule 8D which will in turn distort the

computation of disallowable expenditure under the said clause. It is true that the legislature has not given any further indication as to how such amount of expenditure would be ascertained. We would therefore have to apply the reasonable test and interpret the provision as is most likely to give effect to legislative intent for disallowance of expenditure by an assessee for earning income which is not accountable to tax. It is true that investment made by the assessee out of such borrowed funds will continue to be factored in denominator in the formula provided in clause(ii) of sub to average of total assets of assessee as on the first and the last day of the previous year. However, ignoring taxable interest earned by the assessee for the purpose of ascertaining the amount of expenditure incurred by the assessee by way of

interest, would amount to distorting the factor 'A' provided by the legislature in clause(ii) of sub rule(2) of Rule 8D. It may be possible for variety of reasons that in a given financial year the assessee might have earned interest income which is higher than the interest paid on the borrowed funds. This may be because assessee's investments may have earned interest at rates higher than the interest rate paid by the assessee on the borrowings or may also be because assessee's investment in earning interest may be higher in value than the assessee's borrowings, inviting interest. In such a situation, essentially, the assessee would have earned more interest than the interest paid. If we accept the interpretation suggested by the Revenue and apply the formula by computing factor 'A' by taking into account interest paid

ignoring the interest earned, there would be disallowance under this formula even if in the net result, the assessee may have not paid any interest on borrowings."

9. In case of **Shreno Ltd. (Supra)**, this Court has held as under :

"16. The primary question which the Supreme Court considered in case of Maxopp Investment Ltd., (supra) was whether disallowance of expenditure under Section 14A of the Act would be applicable in a case where shares or stocks of a company were purchased for the purpose of gaining control over the said company and incidentally tax free dividend income was generated. The assessee had contended that the dominant intention for purchasing the shares was not for earning the dividend but to gain control over the business in

the company in which the shares were purchased. The Supreme Court held that the purpose for which the shares were purchased was inconsequential. As long as such investment generated tax free income, disallowance of expenditure for making such investment would be justified. This issue does not arise in the present case. However, it is true that while disposing of bunch of appeals by the said judgment the Supreme Court also considered the correctness of the view of the Punjab & Haryana High Court in case of Avon Cycles Ltd. v. CIT [2015] 53 taxmann.com 297/228 Taxman 368 (Mag.). It was the case in which the Assessing Officer had invoked Section 14A read with Rule 8D and apportion the expenditure between investments made for earning tax free income and the rest. The CIT (Appeals) had deleted the entire disallowance upon which

in the appeal filed by the Revenue the Tribunal restored portion of the disallowance observing that the funds utilized by the assessee being mixed funds, the disallowance is confirmed in view of the provisions under Rule 8D(2) of the Rules. This decision of the Tribunal was challenged before the High Court. The Court held that the funds utilized by the assessee were mixed funds and the interest paid by the assessee is also an interest on the investments made, was the finding of fact and therefore, no substantial question of law arises. This judgment was carried in appeal by the assessee. The Supreme Court dismissed the appeal confirming the decision of the High Court."

10. In view of the above dictum of law, it is not in dispute that there was no

interest expenditure incurred by the assessee in excess of the interest income earned after setting off the expenditure against the income as admittedly, the interest income is more than the interest expenses incurred by the assessee. Therefore, in view of the decision of this Court in case of **Nirma Credit & Capital (P.) Ltd. (Supra)**, there is no question of invoking Section 14A of the Act.

11. Similarly, the contention raised on behalf of the Revenue regarding the mixed fund employed by the assessee, in absence of the separate accounts maintained for the funds borrowed and the funds advanced by the assessee, the decision of this Court in case of **Shreno Ltd. (Supra)** would be

squarely applicable and the Assessing Officer could not have invoked the provisions of Section 14A of the Act. Moreover, in the facts of the case, there are concurrent findings of fact arrived at by the CIT(Appeals) and the Tribunal that the funds, which were borrowed by the assessee, were given as an advance to Adani Enterprises Limited and therefore, there was back to back transaction for the advancement of the funds, which were borrowed and in such circumstances, there is no interest expenditure incurred by the assessee for earning the exempt income.

12. In view of the foregoing reasons, we are of the opinion that the Tribunal has not committed any error in upholding the decision of the CIT(Appeals) in deleting

the addition of Rs.23,77,67,259/- made under Section 14A(2) of the Act read with Rule 8D(2)(ii) of the Rules. The question of law therefore, is answered in favour of the assessee and against the Revenue.

13. The Appeal is accordingly, dismissed.

(BHARGAV D. KARIA, J)

(NIRZAR S. DESAI, J)

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