IN THE INCOME-TAX APPELLATE TRIBUNAL, SURAT BENCH, SURAT
BEFORE SHRI PAWAN SINGH, JUDICIAL MEMBER AND
SHRI BIJAYANANDA PRUSETH, ACCOUNTANT MEMBER

आयकर अपील सं./ITA No.556/SRT/2024

(Assessment Year: 2018-19)

(Hybrid Hearing)

Meril Life Sciences Private Limited, M1-M2, Meril Park, No.135/139, Muktanand Marg, Chala, Vapi, Vapi – 396191	**Vs.**	The PCIT, Valsad
स्थायीलेखासं./जीआइआरसं./PAN/GIR No.: **AAFCM1444G**		
(Appellant)		**(Respondent)**

Appellant by	Shri A. Gopalkrishnan Aiyer, CA
Respondent by	Shri Ritesh Mishra, CIT-DR
Date of Hearing	10/10/2024
Date of Pronouncement	13/11/2024

आदेश / O R D E R

PER BIJAYANANDA PRUSETH, AM:

This appeal by the assessee emanates from the order passed under section 263 of the Income-tax Act, 1961 (in short, 'the Act') by the Learned Principal Commissioner of Income Tax, Valsad [in short, 'Ld. PCIT'], dated 16.03.2024 for assessment year (AY) 2018-19.

2. Grounds of appeal raised by the assessee are as under:

1. The order passed u/s 263 passed by the Learned PCIT is contrary to the facts of the case and law and prejudicial to the Appellant.

2. On appreciation of the facts and circumstances of the case and interpretation of law the learned PCIT has erred in holding that the order of the learned assessing officer passed u/s 143(3) r.w.s. 144B dated 24/04/2021 is erroneous and prejudicial to the interest of revenue in respect of Net Foreign Exchange Gain not added to taxable income to the tune of Rs.2,63,509/-. The

order of the learned PCIT U/s. 263 of the Act is contrary to facts of the case and law and deserves to be deleted in toto.

3. On appreciation of the facts and circumstances of the case and interpretation of law the learned PCIT has erred in holding that the order of the learned assessing officer U/s 143(3) r.w.s. 144B dated 24/04/2021 is erroneous and prejudicial to the interest of revenue in respect of disallowance U/s. 14A of the Act to the tune of Rs. 98,88,137/-. The order of the learned PCIT U/s. 263 of the Act is contrary to facts of the case and law and deserves to be deleted in toto.

4. On appreciation of the facts and circumstances of the case and interpretation of law the learned PCIT has erred in setting aside the order of the Learned Assessing Officer u/s 143(3) r.w.s. 144B dated 24/04/2021 and in directing the learned Assessing Officer to frame the assessment order afresh. The order of the Learned PCIT U/s. 263 of the Act is contrary to facts of the case and law and deserves to be deleted in toto.

5. The appellant craves leave to add, alter, amend, modify or alter the above grounds of appeal at any stage of appellate proceedings."

3. The additional ground raised by the assessee are as follows:

"On the facts and in the circumstances of the case the learned Principal Commissioner of Income-tax has erred in invoking jurisdiction u/s 263 of the Act by holding that the order of the Learned Assessing Officer u/s 143(3) r.w.s. 144B of the Act dated 21.04.2021 is erroneous and prejudicial to the interest of revenue. The notice u/s 263 dated 29.02.2024 issued is not in accordance with the provisions of the Act and deserves to be quashed in toto."

4. Let us first decide as to whether the additional ground raised by the appellant could be admitted by us. The Rule regarding grounds of appeal to be considered by ITAT is Rule 11 of Income Tax (Appellate Tribunal) Rules, 1963. The same reads as under:

***"Grounds which may be taken in appeal**. –*
11. The appellant shall not, except by leave of the Tribunal, urge or be heard in support of any ground not set forth in the memorandum of appeal, but the Tribunal, in deciding the appeal, shall not be confined to the grounds set forth in the memorandum of appeal or taken by leave of the Tribunal under this rule:
***Provided** that the Tribunal shall not rest its decision on any other ground unless the party who may be affected thereby has had a sufficient opportunity of being heard on that ground."*

4.1 The Learned Commissioner of Income-tax– Departmental Representative (Ld. CIT-DR) has not raised any objection to admission of the additional ground raised by the assessee.

4.2 It is seen that the additional ground raised by the appellant is purely legal in nature and no additional facts are necessary to adjudicate the same. It emerges from the facts available on record before the lower authorities. It also goes to the root of the matter. The Hon'ble Supreme Court in case of National Thermal Power Co. Ltd. vs. CIT, 229 ITR 283 (SC) held that the power of the Tribunal in dealing with appeals is expressed in the widest possible terms. The Hon'ble Court did not find any reason as to why the assessee should be prevented from raising a question before the Tribunal for the first time so long as the relevant facts are on record in respect of that item. It further observed that the power of the Appellate Assistant Commissioner in permitting assessee to raise an additional ground in accordance with law, as held in case of Jute Corporation of India Ltd. vs. CIT, 187 ITR 688 (SC), is also available to ITAT in respect of appeals pending before it. Since the additional ground raised purely is a legal issue arising out of the facts as obtained in the orders of lower authorities, the same is admitted.

5. Facts of the case in brief are that the assessee company filed its return of income of AY.2018-19 on 30.11.2018, declaring income of Rs.39,24,06,630/-. The case was selected for complete scrutiny under CASS and after issuing

notices u/s 143(2) and 142(1), the assessment order u/s 143(3) r.w.s. 144B of the Act was passed on 21.04.2021 accepting the returned income.

5.1 Subsequently, the PCIT, Valsad verified the record and noticed various issues based on which he issued notice u/s 263 of the Act on 29.02.2024 and asked assessee as to why the assessment order dated 21.04.2021 should not be revised u/s 263 of the Act in respect of the following issues: (i) net foreign exchange gain not added to total income – Rs.2,63,509/-, (ii) depreciation on addition to intangible assets – Rs.96,87,432/- and (iii) disallowance u/s 14A of the Act – Rs.98,88,137/-. The assessee submitted replies vide letters dated 08.03.2024, 09.03.2024 and 15.03.2024. The PCIT accepted the explanation of assessee on the issue of depreciation. However, on the other two issues, the explanation of assessee was not accepted and the PCIT treated the assessment order dated 21.04.2024 as erroneous and prejudicial to the interests of revenue u/s 263 of the Act. He set aside the said assessment order u/s 263 with a direction to the AO to frame fresh assessment order as per the discussion in the 263 order after hearing the assessee. He also directed the AO to make proper and meaningful enquiry on the issues.

6. Since jurisdictional issue is involved, we shall first take up the additional ground raised by the Ld. AR. In the additional ground, the appellant has submitted that the PCIT erred in invoking jurisdiction u/s 263 of the Act by holding that order of AO u/s 143(3) r.w.s 144B of the Act is erroneous and prejudicial to the interests of revenue. The notice u/s 263 is not in accordance

with the provisions of the Act. Before deciding the ground, it would be proper to reproduce section 263 of the Act to appreciate scope and admit of the said section:

> *"**263**. (1) The [Principal Chief Commissioner or Chief Commissioner or Principal Commissioner] or] Commissioner may call for and examine the record of any proceeding under this Act, and if he considers that any order passed therein by the [Assessing] Officer [or the Transfer Pricing Officer, as the case may be,] is erroneous in so far as it is prejudicial to the interest of the revenue, he may, after giving the assessee an opportunity of being heard and after making or causing to be made such inquiry as he deems necessary, pass such order thereon as the circumstances of the case justify, [including,-*
>
> *(i) An order enhancing or modifying the assessment or cancelling the assessment and directing a fresh assessment; or*
> *(ii) An order modifying the order under section 92CA; or*
> *(iii) An order cancelling the order under section 92CA and directing a fresh order under the said section].*
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> ***********
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> *Explanation 2.—For the purposes of this section, it is hereby declared that an order passed by the Assessing Officer [or the Transfer Pricing Officer, as the case may be,] shall be deemed to be erroneous in so far as it is prejudicial to the interests of the revenue, if, in the opinion of the Principal [Chief Commissioner or Chief Commissioner or Principal] Commissioner or Commissioner,—*
>
> *(a) the order is passed without making inquiries or verification which should have been made;*
> *(b) the order is passed allowing any relief without inquiring into the claim;*
> *(c) the order has not been made in accordance with any order, direction or instruction issued by the Board under section 119; or*
> *(d) the order has not been passed in accordance with any decision which is prejudicial to the assessee, rendered by the jurisdictional High Court or Supreme Court in the case of the assessee or any other person."*

6.1 It is clear from a plain reading of section 263 of the Act that the PCIT or the CIT may call for and examine the records of any proceedings under the Act. If he considers that any order passed by the AO or the TPO is erroneous in so far as it is prejudicial to the interests of revenue, he is required to give assessee

an opportunity of being heard and after making or causing to be made such enquiry as he deems necessary, he may pass such order thereon as the circumstances of the case justify including enhancing or modifying the assessment order, cancelling the assessment and directing a fresh assessment. Explanation 2 was inserted below sub-section (1) with effect from 01.06.2015 to declare as to what shall be deemed to be "erroneous in so far as it is prejudicial to the interest of revenue". The instances which would fall in the above category are: (i) the order is passed without making inquiries and verification which should have been made; (ii) the order is passed allowing the relief without inquiring into the claim; (iii) the order has not been made in accordance with any order, direction, or instruction issued by the Board u/s 119 of the Act; or (iv) the order has not been passed in accordance with any decision which is prejudicial to the assessees, rendered by the jurisdictional High Court or the Supreme Court in the case of the assessee or any other person.

6.2 Let us examine the assessment order in the background of the statutory provisions discussed above. The impugned assessment order was passed u/s 143(3) r.w.s. 144B of the Act on 21.04.2021 for AY.2018-19. As mentioned by the AO, the case was selected for complete scrutiny. Therefore, the AO was not precluded from making any inquiry and verification; which is the case in limited scrutiny assessment. It is also seen that the return of income of the assessee was quite high at Rs.39,24,06,630/-. It is common knowledge that the number

of scrutiny assessments in the present regime is rather very small, i.e., less than 0.5% of the total returns filed by the assessees during the year. Out of the cases selected for scrutiny, the number of cases under limited scrutiny is far more as compared to the cases under complete scrutiny. Therefore, only a very small number of cases are picked up for complete scrutiny. Hence, the AO was duty bound to carry out proper inquiry, investigation and verification in respect of various issues emanating from the return of income and other details filed by the assessee. However, it is seen that the AO has passed a cryptic order in a perfunctory manner without discussing anything on any issue. It is not at all a reasoned and speaking order. For proper appreciation, the assessment order may be reproduced for ready reference and clarity:

> *"1. The assessee-company filed its return of income for AY.2018-19 on 30.11.2018 admitting income of Rs.39,24,06,630/-. The case was selected for scrutiny under CASS and notice u/s 143(2) was issued on 22.09.2019. Notice u/s 142(1) was issued on 08.12.2020 asking for information and explanation with regard to various issues appearing in the record. The assessee filed replied on various darted. After considering the assessee's replies, the assessment is completed as under:*
>
> *Returned Income - Rs.39,24,06,630/-*
> *Assessed Income - Rs.39,24,06,630/-"*

6.3 It is, therefore, clear that the AO has made the assessment order without making proper inquiries or verifications which should have been made. From the paper book, it is clear that the assessee had submitted only one written submission dated 18.12.2020 before AO, which is at pages 28 to 37 of the paper book. This has been referred to by the PCIT at different places in his 263 order. We find that at point nos. 39 and 40 in respect of addition and deletion of

assets, copies of invoices were attached on "random basis" and assessee submitted that it would submit all documents, if the AO need the same. Similarly, at point no.41, for addition of intangible assets, assessee requested to grant some more time to submit the details. Further, at point nos. 49 & 50, assessee requested AO to provide some details for reconciliation with the books of assessee and further submission before AO. However, it is clear from the facts on record that the AO passed the order without obtaining the details, which the assessee in its reply had assured to submit in future. Therefore, the AO has passed the assessment order in haste without making inquiries or verification which should have been made. Therefore, it is a clear case of lack of inquiry or verification which should have been made, as provided in clause (a) of Explanation (2) below sub-section (1) of section 263 of the Act. The above Explanation was inserted in section 263(1) by the Finance Act, 2015 w.e.f. 01.06.2015. Since the subject assessment year is 2018-19, it is covered by the above Explanation. At this juncture, we make it clear that additions to returned income is not mandatory in all cases under complete scrutiny; but, lack of inquiry and verification and inadequate inquiry would certainly make the assessment order incomplete and not in consonance within the scope of "complete scrutiny". Hence, in view of the facts discussed above and clear statutory provisions, the PCIT was perfectly within his right to invoke provisions of section 263 of the Act. Accordingly, the additional ground of the assessee is dismissed.

7. Ground No.2 is against the order of PCIT holding that the order of AO was erroneous and prejudicial to the interests of revenue for not adding Rs.2,63,509/- in respect of net foreign exchange gain. The PCIT has discussed this issue at para 2 of his order as well as para 3 of show cause notice. He has worked out the disallowance in a tabular form which is as under:

Sr. No.	*Particulars*	*Amount*
1.	*Exchange Gain (Capital)*	*Rs.13,88,588/-*
2.	*Less: (i) exchange gain (loss)(capital)* *(ii) exchange loss (capital)*	*Rs.7,16,061/-* *Rs.4,09,018/-*
3.	*Balance exchange Capital Gain*	*Rs.2,63,509/-*

7.1 According to the PCIT, the AO was required to add Rs.2,63,509/- to the total income, which he failed to do. In the computation of income, the assessee has reduced exchange gain (capital) of Rs.13,88,588/- and added exchange loss (capital) of Rs.4,09,018/- to the total income for the subject year. Under Clause 18 of the tax audit report, the assessee has made an adjustment to block of asset with respect to exchange loss of *Rs.*7,16,061/- and at Clause 21(a) of the tax audit report, foreign exchange loss on capital asset of Rs.4,09,018/- has been reported. In view of the above, details of balance foreign exchange gain of Rs.2,63,509/- is not available on record. This was required to be added but AO has not asked any question about it. Hence, the order is erroneous and prejudicial to the interests of revenue u/s 263 of the Act.

7.2 The assessee had made detailed submission before PCIT during 263 proceedings. It submitted that during the year under consideration, the assessee had net foreign exchange gain of Rs.9,79,570/- on capital assets

imported from outside India. Summary of the same along with treatment to taxable income was given as below:

Particulars	*Amount (in Rs.)*	*Treatement to taxable income*
Exchange Gain on Capital Assets	*13,88,588*	*Reduced from taxable income*
Exchange loss on Capital Assets	*(4,09,018)*	*Added to taxable income*
Balance Exchange gain	*9,79,570*	*Net amount reduced from taxable income*

7.3 The assessee submitted that Section 43A of the Act provides that exchange gain (loss) on capital assets acquired from outside India is to be adjusted from actual cost of the asset as defined in clause (1) to section 43(1) of the Act. Accordingly, in compliance with the provisions of section 43A of the Act, the net exchange gain of Rs. 9,79,570/- was reduced from the actual cost of capital assets. The net exchange gain of Rs. 9,79,570/- relates to (i) capital assets forming part of block of assets, and (ii) capital assets charged to capital work in progress (CWIP), the break-up of which was as under:

Capital Asset	*Net Exchange Gain (in Rs.)*	*Treatment to Actual Cost of Capital Asset*
Forming part of Block of Assets	*7,16,061*	*Reduced from Block of Asset Refer Schedule 18 to Tax Audit (Under additions - Row No. 3)*
Forming part of CWIP	*2,63,509*	*Adjusted from CWIP for Income tax purpose.*
Total	*9,79,570*	

7.4 As the net foreign exchange gain on capital assets imported was adjusted from the cost of asset in accordance with section 43A of the Act, consequential

adjustment for the same is made while computing the taxable income as per provisions of the Act. The assessee further submitted that the AO has conducted complete scrutiny for AY.2018-19. The details of addition / deletion of assets, including the depreciation claim of the assessee were called for by AO, which were duly submitted to his satisfaction. The disallowance of foreign exchange loss on capital asset is duly reported in tax audit report under clause 21 (a). The net gain on capital assets forming part of the block of assets is also duly reported in tax audit report under clause 18. These details regarding all the above aspects of foreign exchange gain have been duly disclosed and reflected by the assessee company in its annual accounts and tax audit Audit report filed along with the return of income and were available on record. After considering the same, AO has assessed the total income of the assessee. Accordingly, the assessment order passed by AO is correct and the assessee requested PCIT not to consider the assessment order as erroneous or prejudicial to the interests of revenue.

8. However, the PCIT has not accepted the contention of the assessee and held that the order of AO is erroneous and prejudicial to the interests of revenue. The finding is at para 6 of the above u/s 263 of the Act. The same table given at para 7 above was reproduced and the PCIT held that assessee has not explained balance exchange capital gain of Rs.2,63,509/-. This should have been added to total income, the failure of which made the assessment order erroneous and prejudicial to the interests of revenue.

8.1 The Ld. AR of the assessee has relied on the submission made by assessee before PCIT and submitted that details of working of balance exchange capital gain of Rs.2,63,509/- had been given to PCIT which is at page nos. 47 to 50 of paper book. As per ICDS, the exchange gain has to be reduced from block of assets or capital work in progress, as the case may be. This cannot be treated as income as per ICDS and IND AS-21. The extracts were enclosed at page nos. 116 to 132 of the paper book.

8.2 On the other hand, Ld. CIT-DR relied on order of PCIT and submitted that the balance exchange capital gain of Rs.2,63,509/- should have been added to the income of the assessee.

8.3 We have heard both the parties and perused the materials available on record. We have also gone through the relevant portion of the Income Computation and Disclosure Standards – VI (ICDS) and Indian Accounting Standards (Ind AS) 21. There are two issues in this ground. The first is as to whether PCIT rightly invoked jurisdiction u/s 263 in respect of net foreign exchange gain of Rs.2,63,509/- not added to total income by AO and the second issue is regarding the merit of addition. After perusing the questionnaire issued by AO and reply of assessee to AO during assessment proceedings, we find that such issue was neither raised by AO nor replied to by assessee. What the AO called for and the assessee furnished was copies of invoices for addition and deletion to assets at point 39 and 40 of the Annexure to notice u/s 142(1) of the Act. No question regarding addition of foreign exchange capital gain to total

income was asked by AO or explained by assessee during assessment proceedings. Hence, this case clearly falls under clause (a) of Explanation 2 below sub-section (1) of section 263 of the Act. Hence, the PCIT has rightly invoked jurisdiction u/s 263 of the Act.

8.4 As regards merit of addition, we find that the assessee has properly explained the issue. Submission of assessee has already been discussed above. As per ICDS-VI, relating to effect of changes in foreign exchange rates and provisions of section 43A of the Act, the exchange gain on account of purchase of capital assets shall be reduced from block of assets or capital worked-in-progress, as the case may be. The same cannot be considered as income of assessee. The assessee has reduced Rs.7,16,061/- from block of assets and Rs.2,63,509/- from CWIP. This fact has not been rebutted by the PCIT or the Ld. CIT-DR. Hence, the PCIT should have accepted the impugned issue, like the issue regarding depreciation on intangible assets, while giving his finding instead of directing AO to frame fresh assessment order. The appellant succeeds on this ground.

8.5 In the result, this ground is allowed.

9. The next ground pertains to disallowance of Rs.98,88,137/- under Rule 8D r.w.s. 14A of the Act. The issue was dealt with by PCIT at para 4 of his order u/s 263 of the Act. He observed that assessee had made investment in shares of subsidiary companies but did not disallow any expenditure under Rule 8D r.w.s 14A of the Act. The assessee submitted that it had not earned any exempt

income and hence no disallowance u/s 14A could be made. The PCIT also observed that value of opening and closing stock do not match with the audited figures. The PCIT also stated that no income can be earned in vacuum and the assessee company must have made certain expenditure in connection with investments in its subsidiary companies. Hence, the PCIT held that AO failed to make appropriate disallowance u/s 14A r.w.r. 8D. The amount of disallowance as per Rule 8D worked out to Rs.98,88,137/- (being 1% of Rs.98,88,13,788/-).

9.1 In response to the show cause notice of PCIT, the assessee submitted that the AO had raised specific query vide Q. No.46 of notice u/s 142(1), dated 08.12.2020. The assessee had provided all details vide point no. 46 in its reply dated 18.12.2020. The assessee had invested in its subsidiaries in foreign countries as well as in India. The assessee had provided details of investment in subsidiaries and submitted that no exempt income was earned in AY.2018-19. Hence, there could be no disallowance. In any case, income for foreign subsidiaries are taxable in India and hence section 14A cannot be applied on their income. As there was no foreign investment in the Indian subsidiary, the assessee has not incurred any expanse. The assessee had also sufficient own funds of Rs.251.81 Crore, against which investment in Indian subsidiaries, i.e., M/s Meril Life Sciences India Pvt. Ltd. as on 31.03.2018 was only Rs.12.13 Crore. It was also submitted that amendment to section 14A is prospective and applicable for AY.2022-23 onwards and not for AY.2018-19.

9.2 However, the PCIT in para 6.2.1, 6.2.2 and 6.3 held that while finalizing the assessment order, the AO should have disallowed expenditure u/s 14A to the total income. No application of mind in this regard have been made by AO in course of the assessment proceedings, therefore, the order is erroneous in so far as it is prejudicial to the interests of revenue. At para 11.1, the PCIT stated that the Department has lost lawful tax of Rs.35,10,626/- on income of Rs.1,01,51,646/-, being (i) Rs.2,63,509/- on account of exchange capital gain and (ii) Rs.98,88,137/- on account of disallowance u/s 14A of the Act. Accordingly, assessment order u/s 143(3) and 144B of the Act passed by the AO was set aside within the meaning of section 263 of the Act, with the direction to AO to frame fresh assessment as per the discussion in the 263 order.

9.3 Before us, the Ld. AR has filed paper book including the submissions made before the AO and PCIT on the above issue. It was submitted that the AO had issued specific question in the notice u/s 142(1), dated 08.12.2020 regarding expenses for earning on exempt income and computation as per Rule 8D r.w.s. 14A of the Act. In reply thereto, assessee had filed comprehensive reply vide letter dated 18.12.2020 and the answer is at para 46 of the reply. Since the AO was satisfied about the reply of assessee on the issue of Rule 8D r.w.s. 14A of the Act, he did not make any disallowance. Further, it was submitted that the PCIT has wrongly concluded that expenditure incurred shall be disallowed even in absence of income in view of amendment brought in section 14A of the Act by Finance Act, 2022, which is applicable prospectively

from AY.2022-23 onwards. The Ld. AR relied on the decisions in the following cases for the above proposition: (i) Keti Construction Ltd., (2024) 162 taxmann.com 278 (Madhya Pradesh), (ii) Era Infrastructure (India) Ltd., (2022) 141 taxmann.com 289 (Delhi), (iii) Avantha Realty Ltd., (2024) 164 taxmann.com 376 (Calcutta), (iv) CLP India Pvt. Ltd., ITA No.290/Ahd/2020 and (v) Bajaj Capital Ventures (Ahd – Trib.) (P.) Ltd., (2022) 140 taxmann.com 1 (Mumbai – Trib).

9.4 The Ld. CIT-DR, on the other hand, relied on the decision of the PCIT. He submitted that the PCIT has rightly applied provisions of section 14A as amended by Finance Act, 2022. He submitted that disallowance u/s 14A would be attracted even if exempt income is not earned during the year.

9.5 We have heard rival submissions of both the parties and perused the materials available on record. We have also deliberated the case laws relied upon by both parties. The issue in the instant ground is whether the AO was wrong in not making addition u/s 14A r.w. Rule 8D of the Act. The Ld. AR submitted that the AO had issued a specific query on the above issue which was duly replied to by the assessee. Therefore, AO has not made any addition after considering reply of the assessee and after application of his mind to the impugned issue. In order to decide the issue, we have gone through the query raised by AO during assessment proceedings. The AO had issued notice u/s 142(1) on 08.12.2020 and enclosed Annexure containing 52 questions. The said

notice and the Annexure are at pages 13 to 27 of the paper book. The relevant part of the query is reproduced below for ready reference:

> *"46. It is seen from records that you have incurred expenses for earning exempt income.*
>
> *1) Kindly provide following details with respect to the investments during the year under consideration:-*
>
> *a) Nature of investment*
> *b) Amount of investment*
> *c) Source of investment*
> *d) Interest paid on the fund utilized*
>
> *2) Kindly provide monthly opening and closing balance during the year with respect to investments.*
> *3) Kindly provide details of exempt income earned during the year under consideration.*
> *4) Provide following details for the expenses incurred for earning exempt income:*
>
> *a) Direct expenses*
> *b) Indirect expenses*
> *c) Interest paid on borrowed funds utilized for the investment*
>
> *5) Computation as per Rule 8D read with section 14A of the Income Tax Act."*

9.6 The assessee filed reply to the above query which is attached at page 28 to 37 of the paper book. The answer to Question No.46 is as under:

> *"46. We have not incurred any expenses for earning exempt income.*
>
> *1. During the year the company has made investments in its subsidiary companies which are also in the same line of business activities. The details of investments made during the year in prescribed format is attached in Annexure 44.*
> *2. The monthly opening and closing balance during the year with respect to investment is attached In Annexure 44.*
> *3. We have not earned any exempted income during the year under consideration.*
> *4. We have not earned any exempted income during the year and hence there is,*
>
> *a) no direct expenses incurred for earning such exempt income and*
> *b) no Indirect expenses incurred for earning such exempt income.*

c) Interest expense on borrowed funds have been incurred for business activities only. No funds are deployed in earning exempt income from investments during the year.

5. Computation as per rule 8D rw 14A:-
During the year the company has not earned any exempt income under section 10. The company has not specifically incurred any expense for earning any such income. Accordingly, no expense has been disallowed under section 14A.

Further we would like to inform your goodself that,
Interest expenses have been incurred for business activities. No funds are deployed in exempt investments during the year. Also73u71ng~trTe year the Company has not earned any exempted income u/s 10. The company has not specifically incurred any expenses for earning any such Income accordingly no expenses has been disallowed under section 14A. Further we would like to inform you that:

Our company is in the field of medical business and company has Invested in unlisted shares of its subsidiary companies both overseas and Indian which are in the same line of activity for growing the business of the company. Income whether dividend or capital gain from overseas subsidiary is always taxable in India.

The Company has not earned any exempt income during the year and income exempt u/s 10 in a particular assessment, may not have been exempt earlier and can become taxable in future years. Further, income earned in a subsequent year may or may not be taxable depending upon the nature of transaction entered in to the subsequent assessment year. So the expected dividend income from Indian subsidiary company which during the financial year 2017-18 is exempt u/s 10 of the Act and become taxable In the present situation whereas dividend income from overseas subsidiary is taxable.

The company has Invested in the unlisted shares of the subsidiary companies. So the sale of shares would also attracts capital gain tax.

We have not earned any dividend income during the year which was exempt and did not form part of the total Income. Therefore, in the absence of any clear findings or nexus between expenses incurred and exempt income, no ad hoc disallowance could be made.

Our aforesaid pleadings have been accepted by higher judicial authorities in the following decisions:

1) Commissioner of Income Tax V. Holcim India (P.) Ltd. (High Court of Delhi)
2) Commissioner of Income Tax V. Shivam Motors (P.) Ltd (High Court of Allahabad)

3) Commissioner of Income-tax-1 V. Corrtech Energy Pvt. Ltd. (High Court Gujarat)

In view of the above and also in the absence of any tax exempt income during the year, we request your goodself not to disallow any expenditure u/s section 14A r.w.s Rule 8D.

47. The company has not acquired new foreign financial interest during the year. However, the company has made investment in its existing foreign subsidiaries. The details of such foreign financial interest in the nature of financial Interest acquired during the year under consideration as per prescribed format along with the copy of relevant bank statement showing such investment is attached in Annexure 44. The company has made investment in its overseas operating subsidiaries. Such investments have been made from internal accruals and borrowings."

9.7 Against the above factual background, let us see whether the order of the AO is erroneous and prejudicial within the meaning of section 263 of the Act. A bare reading of the section reveals that the PCIT can call for and examine the record of any proceedings under the Act and if he considers that any order passed by the AO is erroneous in so far as it is prejudicial to the interests of the revenue, he may after giving opportunity of hearing and after making or causing to be made such inquiry as he deems necessary, pass such order as the circumstances of the case justify. The Hon'ble Supreme Court in the case of Malabar Industries Ltd. vs. CIT, 243 ITR 83 (SC) held that every loss of revenue as a consequence of an order of the AO cannot be treated as prejudicial to the interests of revenue. When an AO adopts one of the courses permissible in law and it results in loss of revenue or when two view are possible and the AO has taken one view with which the Commissioner does not agree, it cannot be treated as erroneous order prejudicial to the interests of revenue unless the view taken by the officer is unsustainable in law. In the subsequent decisions,

the same principles have been affirmed by the Hon'ble Supreme Court. The Hon'ble Court in case of CIT vs. Greenworld Corporation, 314 ITR 81 (SC) held that the jurisdiction u/s 263 can be exercised only when both the following conditions are satisfied *i.e.*, (i) the order of the Assessing Officer should be erroneous and (ii) it should be prejudicial to the interests of revenue. These conditions are conjunctive. An order of assessment passed by the Assessing Officer should not be interfered with only because another view is possible. The Hon'ble Apex Court in case of Max India Ltd. vs. CIT 295 ITR 282 (SC) held that the Commissioner has to be satisfied of the twin conditions as stated above. If one of them is absent, recourse cannot be had to Section 263 of the Act. We find that the impugned issue of "disallowance of expenditure incurred in relation to income not includible in total income" u/s 14A of the Act was duly considered by the AO at the time of assessment proceedings. He has certainly examined the above issue by calling for the details from the assessee and after examination, he accepted the explanation given by the assessee. This is evident from the notice u/s 142(1) and reply of assessee reproduced above. Thus, the AO has duly considered the issue, applied his mind and taken a considered view.

9.8 In the instant case, as stated above, the AO had called for the explanation on the impugned issue from the assessee and assessee had furnished its explanation, which clearly shows that the AO had undertaken the exercise of examining as to whether any expenditure is liable to be disallowed

under Rule 8D r.w.s. 14A of the Act. It is clear that the AO was satisfied with the assessee's explanation and therefore he accepted same. The grievance of the PCIT is that the AO should have made further inquiry in respect of the impugned issue in the light of provisions of section 14A of the Act and Rule 8D, rather than accepting the assessee's explanation. Therefore, it could not be said that it was the case of "*lack of inquiry*". There is a distinction between "*lack of inquiry*" and "*inadequate inquiry*". If there was any inquiry, even inadequate, that could not, by itself, give occasion to the PCIT to pass order u/s 263 of the Act merely because he has different opinion in the matter. It is only in cases of lack of inquiry that such a course of action could be opened. In the present case, the AO has duly examined the facts and formed an opinion that no addition is necessary in view of the reply of the assessee on the subject-issue. Therefore, the decision of PCIT that the order passed by AO was erroneous and prejudicial to the interest of revenue is not correct.

9.9 We find that the PCIT has referred to and relied upon the Explanation below section 14A which was inserted by Finance Act, 2022, w.e.f. 01.04.2022. It was inserted to clarify that notwithstanding anything to the contrary contained in the Act, the provisions of section 14A shall apply and shall be deemed to have always applied in a case where exempt income has not accrued or arisen or has not been received during the previous year relevant to assessment year and the expenditure has been incurred during the said previous year in relation to such exempt income. We find that this amendment

was inserted by Finance Act, 2022, w.e.f. 01.04.2022. Hence, it would apply from AY.2022-23 onwards. The decisions relied upon by the Ld. AR in the cases of (i) Keti Construction Ltd. (supra), (ii) Era Infrastructure (India) Ltd. (supra), (iii) Avantha Realty Ltd. (supra), (iv) CLP India Pvt. Ltd. (supra) and (v) Bajaj Capital Ventures (P.) Ltd. (supra) are directly on the issue and are in favour of the assessee. In case of Keti Construction Pvt. Ltd. (supra), it was held that amendment made by Finance Act, 2022 in section 14A is applicable prospectively from AY.2022-23. In case of Era Infrastructure (India) Ltd. (supra), it was held that amendment made by Finance Act, 2022 to section 14A by inserting a non-obstante clause and Explanation will take effect from 01.04.2022 and cannot be presumed to have retrospective effects. Similar view was taken by the Hon'ble Calcutta High Court in case of Avantha Realty Ltd. (supra). The ITAT, Ahmedabad in case of CLP India Pvt. Ltd. (supra), after referring to the decision in case of Era Infrastructure Ltd. (supra) held that the insertion of Explanation to section 14A by Finance Act, 2022 is operative from AY.2022-23 onwards and not applicable for earlier assessment years. In case of the appellant, the assessment year is AY.2018-19 and hence respectfully following the decisions cited supra, it is held that the Explanation of section 263 of the Act invoked by the PCIT cannot be applied to the facts of the present case. In view of the above discussions and the decisions cited supra, we set aside the order passed u/s 263 of the Act by the PCIT.

10. In the result, the grounds of appeal of the assessee is allowed.

11. In the combined result, the appeals raised by the assessee is allowed.

Order is pronounced on 13/11/2024 in the open court.

Sd/-	**Sd/-**
(PAWAN SINGH)	**(BIJAYANANDA PRUSETH)**
JUDICIAL MEMBER	**ACCOUNTANT MEMBER**

Surat

दिनांक/ Date: 13/11/2024

SAMANTA

Copy of the Order forwarded to:

1. The Assessee
2. The Respondent
3. The CIT(A) / PCIT
4. CIT
5. DR/AR, ITAT, Surat
6. Guard File

By Order

// TRUE COPY //

Assistant Registrar/Sr. PS/PS
ITAT, Surat