

# Supreme Court dismisses revenue's appeal in a batch of over 80 cases, holding that Rule 8D is prospective in operation

February 6, 2018

## In brief

In a recent decision,<sup>1</sup> the Supreme Court (SC) has dismissed the Revenue's appeal against the Bombay High Court (HC) decision, wherein it was held by HC that the applicability of Rule 8D of the Income-tax Rules, 1962 (the Rules) is prospective in operation, and hence, applicable for assessment year (AY) 2008-09 and onwards only.

## In detail

### Facts

- The taxpayer had filed its return of income for AY 2003-04 declaring a loss. During the said year, the taxpayer was in receipt of both taxable income and non-taxable income, i.e., dividend income, which was claimed as exempt under the provisions of the Income-tax Act, 1961 (the Act).
- The Tax Officer (TO) disallowed the proportionate interest under section 14A of Act relating to investment from which dividend income was earned.
- The taxpayer aggrieved by the above order filed an appeal before the Commissioner of Income-

tax (Appeal) wherein only partial relief was granted.

- Being further aggrieved, the taxpayer filed an appeal before the Income-tax Appellate Tribunal (Tribunal), wherein the Tribunal ruled in favour of the taxpayer by placing reliance on the order of the Bombay HC<sup>2</sup> and held that Rule 8D was inserted on 24 March, 2008 and would apply prospectively.
- Following its earlier decision<sup>2</sup>, the HC dismissed the appeal of the Revenue and hence, Revenue appealed before the SC.

### Issue for consideration

Whether Rule 8D of the Rules is prospective in operation as held by the HC or it is retrospective in operation.

### Revenue's contentions

- The provisions of section 14A are clarificatory in nature and Rule 8D is a procedural provision, which provides only a machinery for implementation of sub-sections (2) and (3) of section 14A, and hence, Rule 8D is retrospective in nature.
- The Revenue contended that machinery provisions by which the charging section is to be implemented or workable are to be given retrospective effect, which is co terminus with the period of operation of main charging section i.e., with effect from 01 April 2001. The charging section, i.e., being section 14A, admittedly being retrospective, the machinery provisions, i.e.,

<sup>1</sup> Civil Appeal No. 2165 of 2012 (SC)

<sup>2</sup> [2010] 328 ITR 81 (Bombay)

Rule 8D also has to be retrospective in operation.

### **Supreme Court decision**

- The SC analysed the explanatory memorandum issued with the Finance Bill, 2006 and the CBDT circular dated 28 December 2006 in which it was clearly mentioned that the provisions of section 14A(2) and section 14A(3) were effective from AY 2007-08. Thereafter, the SC observed that the provisions of Rule 8D have been introduced to implement the provisions of section 14(2) and section 14(3) which has also been enacted to be effective from 24 March 2008.
- The SC observed that section 14A was inserted by the Finance Act, 2001 and the provisions were fully workable without their being any mechanism provided for computing the expenditure. Hence, the contention of the Revenue that the provisions of section 14A were not workable without the mechanism provided in Rule 8D was

brushed aside.

- The SC held that there could not be any dispute regarding the proposition that machinery provision of taxing statute had to be given effect to its manifest purposes. However, the applicability of the machinery provision whether it was prospective or retrospective depended on the content and nature of the statutory scheme.
- The SC analysed the principles of statutory interpretation, as decided by the SC in many cases, wherein it was held that every statute is *prima facie* prospective unless it is expressly mentioned or by necessary implication made to have retrospective operations.
- Hence, the SC confirmed the decision passed by the Bombay HC<sup>2</sup> and held that Rule 8D is prospective in operation and would not be retrospective.
- In arriving at the above conclusion, the SC further observed that Rule 8D was further amended with effect from 02 June 2016 providing a

new methodology of computing expenditure and earlier method bought in force from 24 March 2008 was put to rest. By interpreting Rule 8D retrospectively, there would be conflict in applicability of old and new rule, which clearly indicates that the Rule 8D has prospective operation.

### **The takeaways**

- The SC reinforces the principle laid down by its earlier decisions that every statute is *prima facie* prospective unless its expressly mentioned and a retrospective operation should not be given to a statute when it takes away or impairs an existing right or creates a new obligation or imposes a new liability.
- The provisions of Rule 8D shall apply prospectively with effect from AY 2008-09 only.

### **Let's talk**

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