

CBDT Notification amending Rule 8D(2) with regard to disallowance of expenditure on exempt income

➤ ***CBDT Notification***

- The CBDT has issued Notification No. 43/2016 dated 2 June 2016, wherein it has amended the computation methodology of Rule 8D(2) of the Income tax Rules, 1962 (“the Rules”), with regard to disallowance of expenditure under section 14A of the Income tax Act, 1961 (“the Act”) relating to exempt income
- As per the CBDT Circular, the expenditure in relation to income which does not form part of the total income shall be the aggregate of following amounts, namely:—
 - i. *the amount of expenditure directly relating to income which does not form part of total income; and*
 - ii. *an amount equal to one per cent of the annual average of the monthly average of the opening and closing balances of the value of investment, income from which does not or shall not form part of total income*
- It further provides that, the amount referred to in clause (i) and clause (ii) shall not exceed the total expenditure claimed by the assessee.

➤ ***Our Comments***

- The limit of 0.5 percent has been increased to 1 percent. In addition to the same, the rate of 1 percent will apply on the annual average of the monthly averages of the opening and closing balances of the value of investments, income from which does not or shall not form part of total income. Disallowance of interest expenditure has been omitted entirely;
- The amendment provides that the amount of disallowance shall not exceed the total expenditure claimed by the assessee. However no clarification is provided about the phrase “total expenditure claimed”. The question whether the disallowance can exceed the exempt income and whether 1 percent is to be applied only to investments which have generated exempt income during the previous year has not been clarified and hence litigation on those points will continue to arise.
- For further detailed discussions on the above Circular please contact:
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