

IN THE HIGH COURT OF JUDICATURE AT MADRAS
DATED : 25.10.2018
CORAM
THE HON'BLE MR.JUSTICE T.S.SIVAGNANAM
&
THE HON'BLE MRS.JUSTICE V.BHAVANI SUBBAROYAN

T.C.(A)Nos.1115 & 1116 of 2008

Commissioner of Income Tax
Chennai

... Appellant / Appellant

Vs.

M/s.TTK LIG Ltd.,
6, Cathedral Road,
Chennai - 600086

... Respondent / Respondent

Tax Case Appeals have been filed under Section 260A of the Income Tax Act, 1961, against the order of the Income Tax Appellate Tribunal Madras 'C' Bench, Dated 30.11.2007 in ITA.No.1448/Mds/2006 & ITA No.1611/2006.

For Appellant : Mr.M.Swaminathan &
Mrs.V.Pushpa
For Respondent : Mr.R.Vijayaraghavan
Assisted by
Mr.V.Vikram

COMMON JUDGMENT

T.S.SIVAGNANAM, J.

These Appeals filed by the Revenue under Section 260A of the Income Tax Act (Act), is directed against the common order passed by the Income Tax Appellate Tribunal Bench 'C', Chennai (Tribunal) in ITA.No. 1448/Mds/2006 & 1611/Mds/2006, pertaining to the assessment years 2001-02 & 2000-01 respectively.

2. The Tax case Appeals have been admitted on the following substantial questions of law:-

(i) Whether in the facts and circumstances of the case, the Tribunal was right in holding that Exchange fluctuation, provision written back, should be treated as income derived out of business for computation of deduction under Section 80HHC, especially when these were not treated as part of the total turnover?

(ii) Whether in the facts and circumstances of the case, the Tribunal was right in holding not 90% of Exchange Fluctuation, provision written back, should not be deducted from the business profits under explanation (baa)?

3. The appeals before the Tribunal were by the Revenue questioning the correctness of the order passed by the Commissioner of Income Tax (Appeals), [CIT(A)], dated 03.02.2006 & 06.03.2006 respectively. The appeals before the CIT(A), were filed by the assessee challenging the assessment orders passed under Section 143(3) of the Act, dated 25.03.2004, for the assessment year 2001-02 and the assessment order dated 31.01.2004 under Section 143(3) r/w Section 147 of the Act for the assessment years 2000-01.

4. The assessee is engaged in the manufacture of rubber contraceptives and for the assessment years under question namely, 2001-02 & 2000-01 respectively, the assessee claimed deduction under Section 80HHC of the Act. The return of income was processed under Section 143(1) of the Act and subsequently, a notice under Section 143(2), dated 17.10.2002 was issued and the case was assigned to a different Commissioner and notice under Section 142(1), dated 11.11.2003, was issued along with the questionnaire. In response, the assessee appeared before the Assessing Officer and filed the details, which were called for and after taking into consideration the details, the assessment was completed under Section 143(3) of the Act. The assessment pertaining to the assessment year 2000-01, is the subject matter of T.C.A.No.1115 of 2008.

5. For the assessment year 2000-01, the assessee filed return of income on 27.11.2000, the return was processed under Section 143(1) of the Act. Subsequently, notice under Section 148 was issued and the assessee was called upon to file documents. The assessee filed reply dated 14.11.2003, after which the assessment was completed under Section 143(3) r/w Section 147 of the Act, by order dated 31.01.2004. This assessment is subject matter of appeal in T.C.A.No.1116 of 2008.

6. For both the assessment years, the Assessing Officer reducing the quantum of deduction, made the following variations namely, (i) 90% of exchange fluctuation; (ii) provision written back; (iii) sales tax refund and these were excluded from the business profit. The assessee filed appeals before the CIT(A), which were allowed by orders dated 03.02.2006, and 06.03.2006, respectively. The Revenue preferred appeals before the Tribunal which were dismissed by order dated 30.11.2007. The Tribunal, while dismissing the appeals filed by the Revenue, rendered the following findings on the above three variations.

6(i) with regard to foreign exchange fluctuations, the Tribunal concurred with the CIT(A) following decision of the Delhi Bench of the Tribunal in the case of Smt.Sujata Grover vs. DCIT, (2002) 74 TTJ (Del) page 347 held that exclusion of 90% of receipts from foreign exchange fluctuations is not justified.

6(ii) With regard to the provision written back, the Tribunal concurred with a view taken by the CIT(A), holding that the provision written back relates to items of expenditure which are integral to the undertaking and excess being established and it cannot be treated as 'other income' so as to attract Explanation (baa) to Section 80HHC. It further held that the decision of the High Court of Bombay in CIT vs. Bangalore Clothing Company (2003) 260 ITR 371 (Bombay) holds the field.

6(iii) With regard to sales tax refund, the Tribunal held that the refund is akin to trading receipt arising to the assessee in the course of its business activities and the sales tax refund forms part of profits of business and they are not subject to Explanation (baa) to Section 80HHC. Further it held that the refund of sales tax has nexus with that of business of the assessee and the same is considered as forming part of the profits of business of the assessee and accordingly, agreed with the findings of the CIT (A) that sales tax refund receivable, cannot be excluded from the profit of the business for the purpose of calculating eligible deduction under Section 80HHC and Explanation (baa) is not applicable.

7. Mr.M.Swaminathan, learned counsel appearing for the Revenue contended that the Tribunal erred in holding that exchange fluctuations, provision written back, sales tax are in the nature of business income and hence, 90% should not be deducted in terms of Explanation (baa) to Section 80HHC. Further, it is submitted that the Tribunal failed to appreciate that the above said incomes does not arise out of the business/export activity of the assessee and the benefit under Section 80HHC is available only for the income derived out of export activity, which is absent in the assessee's case. In support of his contention, the learned counsel placed reliance on the decision of the High Court of Bombay in the case of Commissioner of Income Tax vs. Dresser Rand India (P) Ltd., [2010] 191 Taxman 339 (Bombay); the decision of the High Court of Delhi in the case of Rollatainers Ltd., vs. Commissioner of Income Tax in ITA.No.166 of 2004, dated 16.02.2017, the decision in the case of Commissioner of Income Tax vs. TVS Motors Ltd., [2014] 364 ITR 1(Mad); the decision of the Division Bench of this Court in the case of M/s.K.H.Shoes Limited vs. Assistant Commissioner of Income Tax in TCA.No.731 of 2004, dated 21.04.2017 and the decision of the Hon'ble Supreme Court in the case of Commissioner of Income Tax vs. K.Ravindranathan Nair [2007] 295 ITR 228 (SC).

8. Mr.R.Vijayaraghavan, learned counsel assisted by Mr.V.Vikram, learned counsel appearing for the assessee sought to sustain order passed by the Tribunal by contending that the variations done by the Assessing Officer cannot be excluded and referred to Section 80HHC (3)(a) of the Act and in particular Explanation (baa). It is argued that the proper procedure would be to first take profits and gains of business including domestic sales and from that the brokerage etc., and others of similar nature should be removed. By referring to the decision of the Hon'ble Supreme Court in the case of K.Ravindranathan Nair, (supra), it is submitted that in the said decision, it was held that these are independent income and connected with the regular activity of the assessee and in the facts of the case, the Hon'ble Supreme Court dealt with receipts during the year which was interpreted as 'independent income'. However, the Hon'ble Supreme Court did not deal with the case like the respondent/assessee, wherein this was allowed as a deduction in the previous year, which was claimed by the assessee in the

subsequent year. Therefore, it is submitted K.Ravindranathan Nair, (supra), did not deal with the facts and circumstances akin to the case of the assessee. Further, it is submitted that gratuity is for not any independent activity, but that of the assessee. With regard to the sales tax paid, which was allowed as a deduction under Section 80HHC and it is applied when the refund is given, in other words it is trading receipt arising in the course of business activity. Thus, it is submitted that the nature of every receipt has to be considered and as pointed out by the Hon'ble Supreme Court, there are four variables which are to be taken into consideration. In support of his contentions, the learned counsel relied on the decision of the High Court of Himachal Pradesh in Commissioner of Income Tax vs. Purewal & Associates Ltd., [2016] 243 Taxman 0392 (HP); decision of the High Court of Bombay in the case of Alfa Laval India Ltd., vs. Deputy Commissioner of Income Tax (2003) 133 Taxman 0740; and the decision of the Hon'ble Supreme Court in the case of Commissioner of Income Tax vs. Alfa Laval (India) Ltd., (2007) 295 ITR 0451, by which the appeal filed by the Revenue against the decision of the High Court of Bombay was dismissed. Reliance was also placed on the decision of the High Court of Calcutta in the case of Commissioner of Income Tax vs. Sinclair Murray & Co., Pvt Ltd., (1969) 75 ITR 0494, and the decision of the Hon'ble Supreme Court in the case of Commissioner of Income Tax-VII vs. Punjab Stainless Industries, (2014) 364 ITR 0144 (SC).

9. Heard the learned counsels appearing for the parties and perused the materials placed on record.

10. The assessee's case, on the three variations done by the Assessing Officer are that the gain on account of the foreign exchange resulted from variation in rates and was directly related to the imports/exports transaction of goods and therefore, it formed a part of the sales price; that the goods, which were booked at a particular sale price and the realisation made against the same, were at times more because of improved rate of exchange as on the date of realisation, therefore, the same qualifies to be included as profit of business.

11. The revenue pitches its case relying on the decision of the Hon'ble Supreme Court in K.Ravindranathan Nair, (supra).

12. Before we examine the applicability of the said decision, we may note as to what was said in the said decision by the Hon'ble Supreme Court.

13. The facts in the said case was that the assessee therein carried out processing of cashew nuts at its factory, which were then exported. The assessee also processed cashew nuts for export on job work basis, which were returned after processing. The assessee earned processing charges, and consequently, the assessee was both a job worker and an exporter. The assessee claimed export incentives under Section 80HHC(3) of the Act, but did not include the receipts received as processing charges in his total turnover. The business proceeds included receipts towards processing charges. These receipts were not included by the assessee in the total turnover. The issue which arose before the Supreme Court was whether, the Revenue was correct in including the processing charges in the total turnover, while arriving at export profits under Section 80HHC(3), as it stood at the relevant time. The Supreme Court held the expression derived from in sub-section (3) in section 80HHC, is narrower than the

words attributable to and consequently, it is only profits derived from exports, which become the basis for working out the formula provided in sub-section (3). The Supreme Court further held that if the processing charges were part of the gross total income, being profits from business, then they had to be included in the total turnover in the formula provided under sub-section (3). Further, it was pointed out that the expression included in such profits indicated that the processing charges formed a part of a gross total income being business profits. The contention of the assessee that processing charges were liable to be excluded from the total turnover was rejected by the Supreme Court. The question whether processing charges constitute independent income like rent, commission, brokerage and whether liable to be excluded to the extent of 90% from the gross total income while arriving at business profits was considered and it was held that processing charges, which was part of gross total income was an independent income like rent, commission, brokerage, etc, and therefore, 90% of the said sum has to be reduced from the gross total income to arrive at the business profits and since the said processing charges was an important component of business profits, it also had to be included in the total turnover in the said formula to arrive at business profits in terms of clause (baa) in Explanation to Section 80HHC of the Act. It was emphasised that Explanation (baa) requires that receipts constituting independent income having no nexus with exports was required to be reduced from business profits under clause (baa). Consequently, in the said case, it was held that processing charges, constituted independent income, similar to rent, commission, etc, which formed part of gross total income, and the same had to be reduced by 90% as contemplated in clause (baa) to arrive at business profits. Therefore, the said processing charges were includable in the total turnover in the formula under Section 80HHC(3) of the Act.

14. Mr.M.Swaminathan, after referring to the decision in the case of K.Ravindranathan Nair, (supra), argued that exchange fluctuations, provision written back, and sales tax refund, which do not have any nexus with export are to be treated as independent income and to be excluded to the extent of 90% as stipulated in the Explanation. To support his stand, reliance was placed on the decision in the Dresser Rand pvt. Ltd., (supra), wherein the Court was considering the submission made on behalf of the assessee as to whether processing charges formed part of business profits and if so, if 90% of such receipts are liable to be excluded under Explanation (baa) did not fall for determination before the Supreme Court in K.Ravindranathan Nair, (supra). It is submitted that in Dresser Rand India (P) Ltd., (supra), this contention advanced by the assessee was rejected and it was held that the Hon'ble Supreme Court while construing the provision of Section 80HHC, held that there are four variables, which are required to be considered namely, business profits, export turnover, total turnover and 90% of the sums referred to in Explanation (baa). Therefore, it was held that ambit of controversy, which was raised in K.Ravindranathan Nair, (supra), did as a matter of fact require determination of the nature of receipts of a similar nature, which are liable to be excluded under Explanation (baa), though they constitute a part of business profits and held that the principles laid down in K.Ravindranathan Nair, (supra), constitute the ratio of the judgment which would bind the High Courts.

15. Mr.M.Swaminathan, contended that in Dresser Rand India (P) Ltd., (supra), one of the issues was sales tax refund, which was required to be reduced in terms of the Explanation and the stand taken by the Revenue was accepted by the Court. We have gone through the decision in Dresser Rand India (P) Ltd., (supra). The substantial question of law, which was framed for consideration was whether the Tribunal was justified in law in holding that 90% of recovery of freight, insurance and packing receipts, sales tax refund and service income are not to be excluded from profits of business within the meaning of clause (baa) of Explanation to Section 80HHC of the Act for the purpose of computation of reduction under Section 80HHC of the Act. We find from paragraph 17 of the judgment, that the counsel for the assessee conceded before the Court that the ratio laid down in K.Ravindranathan Nair, (supra), while dealing with processing charges would apply to the case of the assessee with regard to recovery of freight and insurance and packing receipts, sales tax refund and service income. Therefore, we find that the said question was answered in favour of the revenue partly on account of the concession recorded by the counsel for the assessee. However, we find in paragraphs 11 to 15, there were discussion as regards the effect of the decision in the case of K.Ravindranathan Nair, (supra), since the assessee therein argued that the issue raised before the Court was not an issue before the Supreme Court in K.Ravindranathan Nair, (supra). In any event, we find that the decision with regard to sales tax appears to have been rendered based on the concession recorded by the assessee. Therefore, we do not propose to dwell further on the said decision.

16. What is important to note in the instant case is the facts and manner in which the assessee was assessed for the relevant assessment years. More or less, an identical case was dealt with by the High Court of Bombay in the case of Alfa Laval India Ltd.,. One of the substantial questions of law which was framed for consideration was whether the Tribunal was right in law in holding that interest from customers, sales tax set off and other refunds, claims etc, do not form part of business profits for calculating deduction under Section 80HHC. It was contended on behalf of the assessee that for computation of deduction under Section 80HHC, what is relevant is profits of business as computed under head profits and gains of business or profession and in the said case, the sales tax set off, claims, refund etc, under the caption other income have been assessed under the head profits and gains of business or profession. It was argued that once these incomes are treated as part of business income and computed under the head profit and gains of business or profession, the same cannot be excluded from business profits, while computing deduction under Section 80HHC of the Act.

17. The assessee therein relied on the decision of the Bombay in the case of Bangalore Clothing Company (supra) and it was submitted that amounts in question being part of operational income, the same could not be excluded for the purpose of deduction under Section 80HHC of the Act. Revenue contended that the income shown under the caption other income has no nexus with the business of the assessee and the amounts in question were not part of operational income and hence not includable for computing deduction under Section 80HHC of the Act. The submission made on behalf of the assessee was accepted by the Court and it was pointed out that the Assessing Officer has computed the income by way of sales tax set off,

claims, refunds etc., under the head profits and gains of business or profession and in other words, the Assessing Officer has not assessed these under the head income from other sources or under any other head and having assessed the income under the head profits and gains of business or profession, it is not open to the Assessing Officer to treat these income as if assessed under the head 'income from other sources', so as to exclude the same from business profits while computing deduction under Section 80HHC of the Act. Thus, it was held that the sales tax set off etc., have been computed and assessed under the head profits and gains of business or profession as part of operational income and not under the head income from other sources and could not be deducted from business profits while computing deduction under Section 80HHC of the Act. Ultimately, it was held that the Assessing Officer having accepted that the said income as part of the business profit and the same could not be excluded from business profit while calculating deduction under Section 80HHC of the Act, answered the said substantial question of law in favour of the assessee.

18. The decision in the case of Alfa Laval India Ltd.,(supra), was challenged by the Revenue before the Hon'ble Supreme Court which was dismissed leaving the question open.

19. It was argued by Mr.R.Vijayaraghavan that in this appeal no substantial question of law arises for consideration and the entire matter revolves on facts, which have been concurrently held in favour of the assessee. Reliance was placed on the decision in the case of Sinclair Murray and Co., (supra). In the said case, the question was whether money was trading receipt or not, is a pure question of fact or a mixed question of fact and law. The Court accepted the submission that if a pure question of fact has to be decided, the matter requires to be remanded to the Tribunal, if in the opinion of the High Court, there was an error. However, in the said case, since it was a mixed question of fact, the Court proceeded to decide the matter and found it not desirable to send back the matter to the Tribunal after a lapse of 15 years of the assessment.

20. In Punjab Stainless Industries, (supra), the assessee was a manufacturer and exporter of stainless steel utensils and in the process of manufacturing some portion of the steel, which could not be used or reused for manufacturing utensils, remains unused, was treated as scrap, which the assessee disposed of in the local market and income arising from sale was also reflected in the profit and loss account. The assessee for the purpose of availing deduction under Section 80HHC, income from sale proceeds of scrap was not included in the total turnover, but was shown separately in profit and loss account. The Revenue submitted that the sale proceeds from scrap should have been included in total turnover as the assessee was also selling scrap and that was also part of sale proceeds. The High Court held that the proceeds generated from the sale of scrap would not be included in 'total turnover'. The Hon'ble Supreme Court pointed out that to ascertain whether turnover would also include sale proceeds from scrap, one has to know the meaning of the term turnover, as turnover has neither been defined in the Act nor has been explained by any of the CBDT circulars and one has to look at the meaning of term 'turnover' in ordinary accounting or commercial parlance. It was held that in simple word turnover, would mean only amount of sale proceeds received in respect of goods, in which an assessee is dealing and sale proceeds from scrap may either be shown

separately in profit and loss account or may be deducted from the amounts spent by manufacturing unit on raw material, which was steel in the case of the said assessee. Further, it was held that raw material which was not capable of being used for manufacturing utensils would have to be either sold as scrap or might have to be re-cycled if manufacturing unit is also having a re-rolling plant. If the assessee does not have a re-rolling plant, the manufacturer would dispose of the scrap of steel to some one, who wants to recycle it and when such scrap is sold, sale proceeds of scrap cannot be included in the term turnover, since the assessee's unit was engaged primarily in manufacturing and selling of steels utensils and not scrap of steel and the proceeds of such scrap would not be included in sales in profit and loss account of the assessee and since, the assessee was not primarily dealing in scrap, but was a manufacturer of stainless steel utensils, only sale proceeds from sale of utensils would be treated as his turnover. Thus, it was held that the sale proceeds from scrap of steel is not to be included in the total turnover for computation of deduction under Section 80HHC, where the unit is engaged primarily in manufacturing and selling of steel utensils and not scrap of steels.

21. When we examined the facts of the case, the assessee had explained to the Assessing Officer that the difference in value was due to exchange fluctuation, which has been accounted separately in profit & loss account and the value adopted by it is based on actual realisation of foreign exchange.

22. With regard to sale of scrap, the assessee contended that the scrap, which was sold forms an integral part of the revenue generated from the industrial undertaking, since the same is derived from operational activity of the undertaking. After examining the factual position, the CIT(A) accepted the case of the assessee and duly supported its finding by referring to the decisions on the point.

23. Thus, in the facts and circumstances of the case, we are of the considered view that no substantial question of law arises for consideration in these appeals and the decision in the case of Alfa Laval India Ltd.,(supra) would squarely apply to the facts and circumstances of this case.

24. At this juncture, it would be relevant to take note of the decision of the High Court of Himachala Pradesh in Purewal & Associate Ltd., (supra), wherein the Court considered the object of Section 80HHC which was to grant an incentive to earners of foreign exchange and therefore, held that it has to be essentially considered with reference to that object. In paragraph 22 of the judgment, the Court noticed Section 41(1) and pointed out that it creates a legal fiction and can be extended for the purpose allowing from profits of business as referred to in Section 80HHC of the Act. The relevant portion of the judgment reads as follows:-

22.It would also be noticed that Section 41(1) creates a legal fiction and can be extended for the purpose of allowing deduction from profits of the business, as referred to in Section 80HHC of the Act. The income chargeable to tax under Section 41(1) of the Act is from reversal of any loss, expenditure or trading liability which had extinguished or ceased to exist. The legal fiction can only be extended to the extent that the provisions of Section 80HHC have to be understood excluding the legal fiction created by deeming provisions contained in Section

41(1) of the Act as the source of income which is chargeable cannot be related to export of goods or merchandise because if any other meaning is assigned to the aforesaid fiction created with respect to Section 41(1), it would be against the basic purpose and object of Section 80 HHC of the Act. If that be so, then the exclusion of 90% of the deemed income under Section 41(1) of the Act is not in accordance with the correct interpretation of Explanation (baa) to Section 80HHC of the Act and, therefore, the ITAT, in such circumstances, has rightly allowed the appeal of the assessee.

25. In our view, the above decision would also come to the assistance of the case of the assessee. Thus, for the above reasons, we hold that there is no substantial questions of law arising for consideration in these appeals and the decision purely revolves around the factual matrix and it is not a case of decision on mixed questions of fact and law. Thus, we are not inclined to interfere with the order passed by the Tribunal confirming the order passed by the CIT(A).

In the result, the appeals filed by the Revenue are dismissed and we hold that in the facts and circumstances of this case, no substantial questions of law arises for consideration. No costs.

(T.S.S.J) (V.B.S.J)
25.10.2018

pbn
Internet : yes/no
Speaking Order/Non-Speaking Order

To

The Deputy Commissioner of Income-tax,
Company Circle IV (3),
Chennai - 600 006.
T.S.SIVAGNANAM.J.,
and
V.BHAVANI SUBBAROYAN.J.,

pbn

Pre-delivery Judgment in
T.C.(A)Nos.1115 & 1116 of 2008

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