

* **HIGH COURT OF DELHI : NEW DELHI**

+ **ITA No.643 of 2007**

Judgment reserved on: January 23, 2008

% Judgment delivered on: February 19, 2008

The Commissioner of Income Tax
Delhi-IV
New Delhi.

...Appellant

Through Mrs. P.L. Bansal, Adv.

Versus

Eltek SGS (P) Ltd.
F-225A, Sainik Farms,
New Delhi.

...Respondent

Through Mr.Kaanan Kapur, Adv.

Coram:

HON'BLE MR. JUSTICE MADAN B. LOKUR
HON'BLE MR. JUSTICE V.B. GUPTA

1. Whether the Reporters of local papers may
be allowed to see the judgment? Yes
2. To be referred to Reporter or not? Yes
3. Whether the judgment should be reported
in the Digest? Yes

MADAN B. LOKUR, J.

The Revenue is aggrieved by an order dated 30th June, 2006 passed by the Income Tax Appellate Tribunal, Delhi Bench 'C' in ITA No. 3669/D/2003 relevant for the Assessment Year 2001-2002.

2. The short question that has arisen for consideration in this appeal under Section 260-A of the Income Tax Act, 1961 (for short the Act) is with regard to the claim of deduction by the Assessee on customs duty drawback of Rs.42,92,725/- under Section 80-IB of the Act.

3. The Assessing Officer declined to grant a deduction by relying upon the decision of the Supreme Court in *Commissioner of Income Tax v. Sterling Foods*, [1999] 237 ITR 579. It may at one be pointed out that the decision of the Supreme Court related to import entitlement under the Export Promotion Scheme of the Government of India and on the interpretation of Section 80-HH of the Act.

4. Feeling aggrieved by the assessment order, the Assessee preferred an appeal before the Commissioner of Income Tax (Appeals) [CIT (A)] who set aside the order passed by the Assessing Officer by holding that *Sterling Foods* did not apply to the facts of the case and

the language used in Section 80-HH of the Act was materially different from the language used in Section 80-IB of the Act.

5. The Revenue preferred an appeal before the Tribunal which dismissed the appeal and upheld the view expressed by the CIT (A).

6. In the first instance, it is necessary to appreciate the decision of the Supreme Court in *Sterling Foods*.

7. The Assessee in that case was engaged in processing prawn and other sea foods which it had exported. As a result of an Export Promotion Scheme announced by the Central Government, the Assessee earned certain import entitlements. The Assessee could either use the import entitlement or sell it to others. In that case, the Assessee sold the import entitlements to some third parties and its income, therefore, included the sale proceeds of such import entitlements, for which the Assessee claimed relief under Section 80-HH(1) of the Act, which reads as follows:

“80HH. Deduction in respect of profits and gains from newly established industrial undertakings or hotel business in backward areas. – (1) Where the gross total income of an assessee includes any profits and gains derived from an industrial undertaking, or the business of a hotel, to which this section applies, there shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of the assessee, a deduction from such profits and gains of an

amount equal to twenty per cent thereof.”

It will at once be seen that the language used in Section 80-HH of the Act relates to “profits and gains derived from an industrial undertaking”.

8. In *Cambay Electric Supply Industrial Co. Ltd. v. CIT*, [1978] 113 ITR 84, the Supreme Court drew a distinction between the expression “derived from” and “attributable to”, the latter being wider in import than the expression “derived from”. It was observed that the expression “attributable to” was used when the legislature intended to cover receipts from sources other than the actual conduct of the business.

9. In *Sterling Foods*, the Supreme Court held that on the language of Section 80-HH of the Act, the expression “derived from” is a narrower expression and so the industrial undertaking had to be the source of the profit or gain. In other words, the industrial undertaking had to be the direct source of the profit and not a means to earn the profit. Referring to import entitlements under the Export Promotion Scheme, the Supreme Court concluded that they were entitlements that the Assessee had earned under the scheme of the Central Government which was intended to encourage exports. The source referable to the

profits and gains arose out of the sale proceeds of the import entitlements and was, therefore, referable to the Scheme of the Central Government and not the industrial undertaking of the Assessee. This is what the Supreme Court had to say in the penultimate paragraph of the decision –

“We do not think that the source of the import entitlements can be said to be the industrial undertaking of the assessee. The source of the import entitlements can, in the circumstances, only be said to be the Export Promotion Scheme of the Central Government whereunder the export entitlements become available. There must be, for the application of the words “derived from”, a direct nexus between the profits and gains and the industrial undertaking. In the instant case, the nexus is not direct but only incidental. The industrial undertaking exports processed sea food. By reason of such export, the Export Promotion Scheme applies. Thereunder the assessee is entitled to import entitlements, which it can sell. The sale considerations therefrom cannot, in our view, be held to constitute a profit and gain derived from the assessee’s industrial undertaking.”

10. On the other hand, the entitlement to duty drawback that we are concerned with is referable to Section 75 of the Customs Act, 1962. This Section reads as follows: -

“75. Drawback on imported materials used in the manufacture of goods which are exported. – (1) Where it appears to the Central Government that in respect of goods of any class or description manufactured, processed or on which any operation has been carried out in India, being goods which have been entered for export and in

respect of which an order permitting the clearance and loading thereof for exportation has been made under section 51 by the proper officer, or being goods entered for export by post under section 82 and in respect of which an order permitting clearance for exportation has been made by the proper officer, a drawback should be allowed of duties of customs chargeable under this Act on any imported materials of a class or description used in the manufacture or processing of such goods or carrying out any operation on such goods, the Central Government may, by notification in the Official Gazette, direct that drawback shall be allowed in respect of such goods in accordance with, and subject to, the rules made under subsection (2):

Provided	xxx	xxx
Provided further that	xxx	xxx''

A perusal of the above provision shows that an exporter is entitled to drawback on the duty of customs chargeable under this Act on any imported material if those imported materials have been used in the manufacture or processing of goods for export. Of course, this is subject to a notification issued by the Central Government with respect to the goods of any class or description.

12. In other words, duty drawback is in the nature of reimbursement of the customs duty that an exporter has paid on imported goods, which are subjected to a manufacturing process and then exported. In that sense, the export has a direct nexus with the

industrial undertaking itself.

13. That apart, Section 80-IB of the Act does not use the expression “profits and gains derived from an industrial undertaking” as used in Section 80-HH of the Act but uses the expression “profits and gains derived from any business referred to in sub-section.....”

Section 80-IB (1) of the Act reads as follows: -

“80-IB (1) Where the gross total income of an assessee includes any profits and gains derived from any business referred to in sub-section (3) to (11), (11A) and (11B) such business being hereinafter referred to as the eligible business, there shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of the assessee, a deduction from such profits and gains of an amount equal to such percentage and for such number of assessment years as specified in this section.”

A perusal of the above would show that there is a material difference between the language used in Section 80-HH of the Act and Section 80-IB of the Act. While Section 80-HH requires that the profits and gains should be derived from the industrial undertaking, Section 80-IB of the Act requires that the profits and gains should be derived from any business of the industrial undertaking. In other words, there need not necessarily be a direct nexus between the activity of an industrial undertaking and the profits and gains.

14. This issue, particularly in relation to duty drawback, came up for consideration in *Commissioner of Income Tax v. Indian Gelatine and Chemicals Ltd.*, [2005] 275 ITR 284. While considering the object of the duty drawback scheme, the Gujarat High Court explained it in the following terms –

“The object of the duty drawback scheme is to reimburse exporters for tariffs paid on the imported raw materials and intermediates and Central excise duties paid on domestically produced inputs which enter into export production. Customs duties and excise duties on inputs raise the cost of production in industries and thereby affect the competitiveness of exports. Therefore, exporters need to be assisted for neutralizing the escalation in their costs attributable to such customs and excise duties. Duty drawback is, therefore, intended to reduce the cost of production. Hence, duty drawback is an integral part of the pricing of the goods and, therefore, part of the cost of production of the industrial undertaking and, therefore duty drawback has to be treated as “derived from” the industrial undertaking.”

15. We have no reason to disagree with the interpretation given by the Gujarat High Court to the object of the duty drawback scheme.

16. While dealing with the merits of the case, the Gujarat High Court rejected the contention of the Revenue that benefits under the duty drawback scheme are not derived from the industrial undertaking but merely attributable to it. The Gujarat High Court observed as

follows –

“The object of the duty drawback is to reimburse customs duties and excise duties paid by the assessee. As customs duties and excise duties are admittedly an integral part of the cost of production any receipts by way of reimbursement of such duties are inextricably linked with the cost of production which has to be reflected in the profit and loss account of the assessee and, therefore, the Revenue’s argument cannot be accepted”

17. Learned counsel for the Revenue has relied upon a decision of this Court in *Commissioner of Income Tax v. Ritesh Industries Ltd., [2005] 274 ITR 324*. The question of law that was framed for consideration by this Court was as follows -

“Whether the amount of ‘duty drawback’ can be regarded as income derived from an industrial undertaking so as to entitle the assessee to a deduction under section 80-I of the Income Tax Act, 1961?”

18. While answering the question in favour of the Revenue, in the context of Section 80-I of the Act, this Court held that “merely because under the scheme to encourage exports the duty is refunded subsequently by way of “duty drawback”, it cannot be regarded as the profit and gain “derived” from the industrial undertaking. It may constitute profits or gains of the business by virtue of Section 28 of the Act, but, it cannot be construed as profits or gains “derived” from the

industrial undertaking for, its immediate and proximate source is not the industrial undertaking but the scheme for duty drawback.”

19. We are of the view that the decision in *Ritesh Industries* is distinguishable since it concerns Section 80-I of the Act which again uses the expression “profits and gains derived from an industrial undertaking”.

20. It is crucial to appreciate the difference in language in Section 80-HH, Section 80-I and Section 80-IB of the Act. While the language used in Section 80-HH of the Act and in Section 80-I of the Act is similar, there is a clear departure in the language used in Section 80-IB of the Act and it is this choice of words that makes all the difference that we are concerned with.

21. We are of the opinion that it is not necessary for us to go as far as the Gujarat High Court has done in coming to the conclusion that duty drawback is profit or gain derived from an industrial undertaking. It is sufficient if we stick to the language used in Section 80-IB of the Act and come to the conclusion that duty drawback is profit or gain derived from the business of an industrial undertaking. The language used in Section 80-IB of the Act is not as broad as the expression “attributable to” referred to by the Supreme Court in

Sterling Foods and *Cambay Electric* nor is it as narrow as the expression “derived from”. The expression “derived from the business of an industrial undertaking” is somewhere in between.

22. Consequently, we are of the view that the source of the duty drawback is the business of the industrial undertaking which is to manufacture and export goods out of raw material that is imported and on which customs duty is paid. The entitlement for duty drawback arises from Section 75(1) of the Customs Act, 1962 read with the relevant notification issued by the Central Government in that regard.

23. Learned counsel for the Revenue also drew our attention to *Pandian Chemicals Ltd. v. Commissioner of Income Tax*, [2003] 262 ITR 278. However, on a reading of the judgment we find that that also deals with Section 80-HH of the Act and does not lay down any principle different from *Sterling Foods*. In fact, in *Pandian Chemicals* reliance has been placed on *Cambay Electric Supply Industrial Co. Ltd.* and the decision seems to suggest, as we have held above, that the expression “derived from an industrial undertaking” is a step removed from “the business of the industrial undertaking”.

24. In view of the law laid down and explained by various decisions, in our opinion, no substantial question of law arises for

consideration.

25. The appeal is dismissed. We assess counsel's fee at Rs.10,000/-. The Revenue will deposit this amount by a cheque drawn in favour of the Registrar General of this Court within four weeks from today.

26. List for compliance on 24th March, 2008.

MADAN B. LOKUR, J

FEBRUARY 19, 2008
kapil

V.B. GUPTA, J

Certified that the corrected copy of the judgment has been transmitted in the main Server.