

IN THE HIGH COURT OF GUJARAT AT AHMEDABAD**TAX APPEAL NO. 188 of 2011****FOR APPROVAL AND SIGNATURE:****HONOURABLE MR.JUSTICE AKIL KURESHI****and****HONOURABLE MR.JUSTICE A.J. SHASTRI**

1	Whether Reporters of Local Papers may be allowed to see the judgment ?	
2	To be referred to the Reporter or not ?	
3	Whether their Lordships wish to see the fair copy of the judgment ?	
4	Whether this case involves a substantial question of law as to the interpretation of the Constitution of India or any order made thereunder ?	

BANPAL OILCHEM PVT LTD....Appellant(s)

Versus

ASSISTANT COMMISSIONER OF INCOME TAX....Opponent(s)

Appearance:

MR TUSHAR P HEMANI, ADVOCATE for the Appellant(s) No. 1

MR NITIN K MEHTA, ADVOCATE for the Opponent(s) No. 1

CORAM: HONOURABLE MR.JUSTICE AKIL KURESHI**and****HONOURABLE MR.JUSTICE A.J. SHASTRI****Date : 05,07/07/2016**

ORAL JUDGMENT**(PER : HONOURABLE MR.JUSTICE AKIL KURESHI)**

1. The assessee is in the appeal against the judgement of the Income Tax Appellate Tribunal dated 17.9.2010. At the time of admission, following substantial question of law was framed :

"Whether the Tribunal below committed substantial error of law in holding that the assessee was not entitled to deduction under Section 80IB of the Income Tax Act, 1961 in respect of DEPB and DEPB premium, without appreciating that there was no element of income embedded in such receipts."

2. This question arises in the following background. The assessee is engaged in processing and exporting Castor-oil and other similar products. For the assessment year 2002-2003, the assessee filed return of income in which the assessee had raised claim of deduction under section 80-IB of the Income Tax Act,1961 ("the Act" for short). While processing such claim, the Assessing Officer noticed that the claim included income of Duty Entitlement Pass Book ("DEPB for short) of Rs.17.72 lacs (rounded off) and DEPB premium income of Rs.2.96 lacs. Along with other sundry receipts, the Assessing Officer disallowed the deduction qua these incomes holding that the same cannot be stated to be derived from the eligible business of the industrial

undertaking.

3. The assessee carried the matter in appeal. CIT(Appeals) reversed the view of the Assessing Officer and directed him to allow deduction under section 80-IB of the Act on the DEPB and DEPB premium income on the ground that same was part of the business profit of the assessee.
4. The issue was carried in appeal by the Revenue before the Tribunal. The Tribunal applied the decision of Supreme Court in case of **Liberty India v. Commissioner of Income tax** reported in (2009) 317 ITR 218 and held that the issue was squarely covered in favour of the Revenue. The decision of the CIT(Appeals) on this point was reversed. It is this judgement the assessee has challenged in the present appeal.
5. Learned counsel for the appellant contended that though the Supreme Court in case of **Liberty India** (supra), held and declared that the income from DEPB cannot be stated to have been derived from the export business of the assessee, had no occasion to consider the question as to what would form the income from DEPB. He submitted that it is not the whole face value of the DEPB which can be stated to be the income of the assessee but only the premium, if any, received by the assessee which can be stated to be income arising out of DEPB. This aspect has been amply clarified by the Supreme Court in case of **Topman Exports v. Commissioner of Income Tax, Mumbai** reported in (2012) 342 ITR 49. The Supreme Court had no occasion to examine this issue in case of

Liberty India (supra) and the ratio of the decision of the Supreme Court in case of **Liberty India** (supra) therefore, should be confined to what was the issue before the Court and what was actually decided. Counsel submitted that while eliminating any sum from the deduction under section 80-IB of the Act, it is the net of the receipt and not the gross receipt which should be excluded. This principle has been laid down by the Supreme Court in case of **ACG Associated Capsules Pvt. Ltd. v. Commissioner of Income tax** reported in (2012) 343 ITR 89(SC) in context of deduction under section 80HHC of the Act. This Court in case of **Commissioner of Income-tax v. Nirma Ltd.** reported in (2014) 367 ITR 12 (Guj.) applied such principle in context of provisions contained in section 80-I, 80-IA, etc. Relying on such decisions counsel submitted that the Tribunal committed an error in providing for exclusion of the entire value of the DEPB and not just the premium received thereon by the assessee.

6. On the other hand, learned counsel Shri Nitin Mehta for the department opposed the appeal contending that scheme of deduction under section 80HHC and 80-I, 80-IA, 80-IB etc. are vastly different. Observations of the Supreme Court in case of **Topman Exports** (supra), were made in context of provisions contained in section 80HHC of the Act which provides for a formula for computing the deduction in case of an assessee who is engaged in export business alongside other businesses. He submitted that the decision in case of **Liberty India** (supra) was rendered in the background of deduction under section 80-IB of the Act. Such decision holds the field. The ratio laid down would

squarely apply in facts of the present case and was therefore, rightly applied by the Tribunal.

7. In order to resolve this controversy we may notice that section 80-IB of the Act pertains to deduction in respect of profits and gains from certain industrial undertakings other than infrastructure development undertakings. Sub-section(1) of section 80-IB provides that where the gross total income of an assessee includes any profits and gains derived from any business referred to in sub-sections (3) to (11C), 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. Sub-section(2) of section 80-IB lays down the conditions for an industrial undertaking to claim deduction under the said section. Sub-section (3) to sub-section (11C) specifies the different businesses to which such deductions would apply.
8. In context of such deductions under section 80-IB of the Act, question that arose before the Supreme Court in case of **Liberty India** (supra) was whether the increased profit of an industrial undertaking on account of DEPB would qualify for deduction under section 80-IB of the Act. In the said case, the assessee had claimed such deduction on sum of Rs.22.70 lacs on the increased profit on account of DEPB and duty drawbacks. The Assessing Officer had denied deduction on the ground that such benefit

constituted export incentives and does not represent profit derived from industrial undertaking. This issue ultimately reached the Supreme Court in which it was held that the deduction under section 80-IB of the Act was profit linked deduction. Each of the eligible businesses in sub-section(3) onwards of section 80-IB constitutes a stand-alone item in the matter of computation of profits and sections 80-IB/80-IA are the Code by themselves as they contain both substantive as well as procedural provisions. It was further observed that the words "derived from" are narrower in connotation as compared to the words "attributable to". The Parliament while using the expression "derived from" intended to cover sources not beyond the first degree. In this background, it was held as under :

"16. DEPB is an incentive. It is given under Duty Exemption Remission Scheme. Essentially, it is an export incentive. No doubt, the object behind DEPB is to neutralize the incidence of customs duty payment on the import content of export product. This neutralization is provided for by credit to customs duty against export product. Under DEPB, an exporter may apply for credit as percentage of FOB value of exports made in freely convertible currency. Credit is available only against the export product and at rates specified by DGFT for import of raw materials, components etc.. DEPB credit under the Scheme has to be calculated by taking into account the deemed import content of the export product as per basic customs duty and special additional duty payable on such deemed imports. Therefore, in our view, DEPB/Duty Drawback are incentives which flow from the Schemes framed by Central Government or from Section 75 of the Customs Act, 1962, hence, incentives profits are not profits derived from the eligible business under Section 80-IB. They belong to the category of ancillary profits of such

Undertakings.

17. The next question is - what is duty drawback? Section 75 of the Customs Act, 1962 and Section 37 of the Central Excise Act, 1944 empower Government of India to provide for repayment of customs and excise duty paid by an assessee. The refund is of the average amount of duty paid on materials of any particular class or description of goods used in the manufacture of export goods of specified class. The Rules do not envisage a refund of an amount arithmetically equal to customs duty or central excise duty actually paid by an individual importer-cum-manufacturer. Sub-section (2) of Section 75 the Customs Act requires the amount of drawback to be determined on a consideration of all the circumstances prevalent in a particular trade and also based on the facts situation relevant in respect of each of various classes of goods imported. Basically, the source of duty drawback receipt lies in Section 75 of the Customs Act and Section 37 of the Central Excise Act.

18. Analysing the concept of remission of duty drawback and DEPB, we are satisfied that the remission of duty is on account of the statutory/policy provisions in the Customs Act/ Scheme(s) framed by the Government of India. In the circumstances, we hold that profits derived by way of such incentives do not fall within the expression "profits derived from industrial undertaking" in Section 80-IB"

The Supreme Court thus went on to examine accounting treatment that these incentives would receive and observed as under :

"22. The cost of purchase includes duties and taxes (other than those subsequently recoverable by the enterprise from taxing authorities), freight inwards and other expenditure directly attributable to the acquisition. Hence trade discounts, rebate, duty drawback, and such similar items are deducted in determining the costs of purchase.

Therefore, duty drawback, rebate etc. should not be treated as adjustment (credited) to cost of purchase or manufacture of goods. They should be treated as separate items of revenue or income and accounted for accordingly (see: page 44 of Indian Accounting Standards & GAAP by Dolphy D'souza). Therefore, for the purposes of 23 AS-2, Cenvat credits should not be included in the cost of purchase of inventories. Even Institute of Chartered Accountants of India (ICAI) has issued Guidance Note on Accounting Treatment for Cenvat/Modvat under which the inputs consumed and the inventory of inputs should be valued on the basis of purchase cost net of specified duty on inputs (i.e. duty recoverable from the Department at later stage) arising on account of rebates, duty drawback, DEPB benefit etc. Profit generation could be on account of cost cutting, cost rationalization, business restructuring, tax planning on sundry balances being written back, liquidation of current assets etc. Therefore, we are of the view that duty drawback, DEPB benefits, rebates etc. cannot be credited against the cost of manufacture of goods debited in the Profit & Loss account for purposes of [Sections 80-IA/80-IB](#) as such remissions (credits) would constitute independent source of income beyond the first degree nexus between profits and the industrial undertaking.

23. We are of the view that Department has correctly applied AS-2 as could be seen from the following illustration:

Expenditures	Amount (Rs.)	Income	Amount (Rs.)
Opening Stock	100	Sales	1,000
Purchases (including customs duty paid)	500	Duty Drawback received	100
Manufacturing overheads	300	Closing stock	200

Administrative, Selling and Distribution Exp.	200		
Net profit	200		

Note: In above example, Department is allowing deduction on profit of Rs. 100 under [Section 80-IB](#) of the 1961 Act.

24. In the circumstances, we hold that Duty drawback receipt/DEPB benefits do not form part of the net profits of eligible industrial undertaking for the purposes of [Sections 80I/80-IA/80-IB](#) of the 1961 Act.”

9. Section 80-IB, we may recall provides deduction in respect of profits and gains from certain industrial undertakings other than infrastructure development undertakings. The industrial undertaking eligible for such deductions have been specified in sub-section (3) to sub-section (11C) of the said sub-section and provides incentives for variety of industries. For example, under sub-section(4) of section 80-IB in case of an industrial undertaking in an industrially backward State specified in the Eight Schedule, deduction of 100% of the profits and gains derived from such industrial undertaking is provided for five assessment years beginning with the initial assessment year and thereafter, at the rate of 25%, upto a maximum of 10 consecutive assessment years. Like-wise, under sub-section(10) of section 80-IB, deduction is provided in case of an undertaking developing and building housing projects. These deductions thus relate either to the nature of industry or its location in a specified area or a backward

area. Essentially, these deductions are granted not on account of the exports made by the industry of its goods so manufactured by an industry covered under any of the sub-sections of section 80-IB of the Act. It can be seen that a manufacturer of goods who sales his product in India would receive no benefit of DEPB while another manufacturer of the same product and exports such product, would receive export incentive in the nature of DEPB scrips at a specified percentage of the FOB value of the export. This value of DEPB with premium if so sold at a premium, would go on to enhance the profit of the assessee. It was therefore, that the Supreme Court in case of **Liberty India** (supra) dissociated the DEPB benefit received by an undertaking which was otherwise eligible for deduction under section 80-IB of the Act since the deduction was for the industry, covered under any of the sub-sections of section 80-IB and not for exports. DEPB was seen as an export incentive and the profit derived on account of such export incentive made available by the Government of India was considered as not having been derived from the activity carried on by the eligible industry.

10. Section 80HHC of the Act on the other hand pertains to deduction in respect of profits retained for export business. Under sub-section(1) of section 80HHC where an assessee, being an Indian company or a person resident in India, is engaged in the business of export out of India of any of the goods or merchandise to which the section applies, there would be in computing of the total income-of the assessee, a deduction to the extent of profits referred to in sub-section (1B), derived by the assessee from the export of

such goods or merchandise. Sub-section (1B) of section 80HHC specifies the extent of deduction on the profit as provided in sub-section(1). Sub-section(3) of section 80HHC provides a formula to ascertain an assessee's profit relatable to its export business. For example, under clause(a) of sub-section(1) where the export out of India is of goods or merchandise manufactured or processed by the assessee, the profits derived from such export shall be the amount which bears to the profit of the business, the same proportion as the export turnover in respect of such goods bears to the total turnover of the business carried on by the assessee. This provision in mathematical terms is expressed as under :

$$\text{Profits derived from exports} = \frac{\text{profits of the business} \times \text{export turnover}}{\text{Total Turn over}}$$

11. Section 80HHC contains an explanation clause defining various terms such as export turnover in clause(b) of the explanation, total turnover in clause(ba) and profits of the business in clause(baa). Term 'profits of the business' has been defined in clause (baa) as under :

“profits of the business” means the profits of the business as computed under the head “Profits and gains of business or profession” as reduced by—

(1) ninety per cent of any sum referred to in clauses (iiia), (iiib) (iiic), (iiid) and (iiie) of section 28 or of any receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in such profits; and

(2) the profits of any branch, office, warehouse or any other

establishment of the assessee situate outside India;”

12. It is as per this definition of profits of the business that the question of eliminating 90% of the DEPB or duty draw back from the numerator of the said formula arises.
13. In essence, this formula enables us to ascertain the assessee's profit relatable to its export business by ascertaining its proportion to the profits of the business. It was in context of this deduction under section 80HHC of the Act and the formula provided under sub-section(3) thereof and definition of profits of the business that the Supreme Court in case of **Topman Exports** (supra) examined the nature of DEPB benefits. Before the Supreme Court therefore, the context was deduction under section 80HHC of the Act and the requirement of eliminating 90% of the DEPB benefits from the numerator of the formula. This section, as noted, provides for deduction in respect of profits retained for export business. It was in background of this specific statutory provision that the Supreme Court in case of **Topman Exports** (supra) came to the conclusion that when DEPB is transferred by a person, the entire sum received by him on such transfer does not become his profits. It is only the amount that he receives in excess of the DEPB which represents his profits on transfer of the DEPB. The Supreme Court also referred to section 28(iid) which provides that any profit on the transfer of the DEPB, being the Duty Remission scheme under the export and import policy, would be chargeable to tax under the head “profits and gains of business or profession”.

14. For variety of reasons, we cannot accept the contention of the counsel for the assessee that by virtue of judgement of the Supreme Court in case of **Topman Exports** (supra), the method of computing deduction under section 80-IB of the Act in relation to DEPB benefits should also be changed. First and foremost, as noted, the decision in case of **Liberty India** (supra) and **Topman Exports** (supra), were rendered in the background of entirely different statutory provisions. Section 80-IB of the Act grants deductions to eligible industries and has nothing to do with the export of a product. If therefore, an industry eligible for deduction under section 80-IB also exports the product, the DEPB benefits are seen in addition to and not as having been derived by the industry out of its eligible business. On the other hand, section 80HHC of the Act has direct co-relation to the export business of an assessee and essentially aims to grant deduction at specified percentage on the assessee's export profit to be ascertained through a complex formula provided in sub-section(3) of the section by further applying the definition of term "profits of the business" contained in clause (baa) of the explanation. Secondly, in case of **Liberty India** (supra), the Supreme Court had quoted a hypothetical example in which the assessee had opening stock of Rs.100, had incurred expenditure of Rs.1000 and on the credit side it had shown sales of Rs.1000, duty draw back of Rs.100 and closing stock of Rs.200 and that is how claimed net profit of Rs.200. The department however, recognised deduction under section 80-IB of the Act on the profit of Rs.100, ignoring the duty drawback of Rs.100 received by the assessee. This formula was specifically approved by the

Supreme Court in background of its conclusion that the benefits of DEPB cannot be stated to have been derived from the industrial undertaking of the assessee which was eligible for deduction under section 80-IB. Accepting the contention of Shri Hemani would amount to rewriting the judgement in case of **Liberty India** (supra). Further, it was not and could not have been argued that the decision in case of **Liberty India** (supra) should be seen to have been impliedly overruled by the later judgement in case of **Topman Exports** (supra). We may record that the decision in case of **Liberty India** (supra) was rendered by two Judge Bench of the Supreme Court whereas **Topman Exports** (supra) was rendered by three Judge Bench. However, in **Topman Exports** (supra), the Supreme Court was not oblivious of its decision in case of **Liberty India** (supra). Judgement was noticed, referred to and discussed. The judgement was neither disapproved nor overruled. Having noticed the earlier judgement, there is no scope for us to understand the ratio in case of **Topman Exports** (supra), having impliedly overruled the decision in case of **Liberty India** (supra).

15. In view of such conclusions, reliance of the counsel for the appellant on the judgements in case of **ACG Associated Capsules Pvt. Ltd.** (supra) and of this Court in case of **Nirma Ltd.** (supra) would be of no consequence. Principle of netting while excluding certain sum from the claim of assessee for deduction under section 80-IB of the Act is neither new nor unfamiliar. Such principle however, cannot be applied in the present case since this very issue of exclusion of the entire amount of DEPB from the profit

eligible for deduction under section 80-IB of the Act is well entrenched since long by virtue of judgement of the Supreme Court in case of **Liberty India** (supra).

16. In the result, the question is answered against the assessee and in favour of the department. Tax appeal is dismissed.

(AKIL KURESHI, J.)

(A.J. SHASTRI, J.)

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