* IN THE HIGH COURT OF DELHI AT NEW DELHI

\+ ITA Nos. 804/2007, 820/2007, 238/2008, 237/2008
1076/2008 and 329/2004

% *Reserved on: November 25, 2009*
Pronounced on: November 30, 2009

Commissioner of Income Tax, Delhi - II . . . Appellant

through : Mr. N.P. Sahni with
Mr. P.C. Yadav, Advocates

VERSUS

Maharashtra Seamless Ltd. . . . Respondent

through : Mr. O.P. Sapra with
Mr. Sandeep Sapra, Advocates

CORAM :-
THE HON'BLE MR. JUSTICE A.K. SIKRI
THE HON'BLE MR. JUSTICE SIDDHARTH MRIDUL

1. Whether Reporters of Local newspapers may be allowed to see the Judgment?
2. To be referred to the Reporter or not?
3. Whether the Judgment should be reported in the Digest?

A.K. SIKRI, J.

1. All these appeals are filed by the Commissioner of Income Tax in which the respondent assessee is the same. These appeals pertain to different assessment years and most of the questions raised in these appeals are common. These were taken up for arguments together and are being disposed of by this common judgment. However, for

2. ITA No. 804/2007 (Assessment Year 2000-2001)
ITA No. 233/2008 (Assessment Year 2001-2002)

In these appeals, the following questions of law are sought to be raised, which are identical :-

"ITA No. 804/2007

(a) Whether on the facts of the present case, the ITAT was correct in law in holding that the rental income received by the assessee from Telecommunication department and M/s. Vaibhav Laxmi & Co. was to be assessed as business income?

(b) Consequentially, whether the rental income received as above could be taken into account as "business income" for the purpose of calculation of deduction under Section 80HHC of the Income Tax Act, 1961?

(c) Whether the ITAT was correct in law in holding that the receipts by way of sale of DEPB licences is a part of sale consideration and 90% of the same is not liable to be deducted from the profits of business as per explanation (baa) to Section 80HHC?

(d) Whether the ITAT was justified in law in holding that sale proceeds of scrap and wastage are to be excluded from "total turnover" for calculating deduction under Section 80HHC?

(e) Whether on the facts and circumstances of the present case, receipt from customers for delayed payment was liable to be excluded from the "total turnover" for the purpose of deduction under Section 80HHC of the Act?

(f) Whether the ITAT was right in holding that for the purpose of explanation (baa) of Section 80HHC (3) interest paid having nexus with interest received has to be deducted and only the net interest has to be considered for deduction?

ITA No. 233/2008

(a) Whether on the facts of the present case, the ITAT was correct in law in holding that the rental income received by the assessee from Telecommunication department

for the purpose of calculation of deduction un Section 80HHC of the Income Tax Act, 1961?

(c) Whether the ITAT was correct in law in holding that the receipts by way of sale of DEPB licences is a part of sale consideration and 90% of the same is not liable to be deducted from the profits of business as per explanation (baa) to Section 80HHC?

(d) Whether the ITAT was justified in law in holding that sale proceeds of scrap and wastage are to be excluded from "total turnover" for calculating deduction under Section 80HHC?

(e) Whether on the facts and circumstances of the present case, receipt from customers for delayed payment was liable to be excluded from the "total turnover" for the purpose of deduction under Section 80HHC of the Act?

(f) Whether the ITAT was right in holding that for the purpose of explanation (baa) of Section 80HHC (3) interest paid having nexus with interest received has to be deducted and only the net interest has to be considered for deduction?"

3. Question Nos. (a) and (b)

These questions are taken up together for consideration.

The first aspect which requires to be examined is as to whether the rental income received by the assessee from Telecommunications Department and M/s. Vaibhav Laxmi & Co. and M/s. Jaguar Overseas Ltd. respectively is to be treated as business income. Rental income from the Telecommunications Department was received for operating Post Office from the premises of the assessee and from M/s. Vaibhav Laxmi & Co. and M/s. Jaguar Overseas Ltd. for use of plant and machinery.

4. The claim of the assessee is that it had approached the Post &

smooth running of the business. The motive was not to ear income. As regards the rent from M/s. Vaibhav Laxmi & Co. and M/s. Jaguar Overseas Ltd., the submission of the assessee was that it got some of the goods manufactured on job work basis from third parties and since the company unit was situated in a remote area, it had requested these companies to install a small unit in the adjacent premises to save transportation charges. It was, thus, argued that the rental income received as incidental to business and should be treated as business income.

5. The ITAT has accepted the aforesaid submission of the assessee. It has recorded a finding of fact that the occupation of the property by the aforesaid two tenants was to discharge the function efficiently and smoothly and, therefore, letting out was subservient and incidental to the main business. Holding that such an income would be treated as business income, the Tribunal relied upon the judgment of the jurisdictional High Court in the case of *Commissioner of Income Tax* v. *Modi Industries Ltd.*, 210 ITR 1 as well as that of the Madhya Pradesh High Court in *Commissioner of Income Tax, Bhopal* v. *National Newsprint and Papers Ltd.*, 114 ITR 388. The Supreme Court has taken similar view in *Universal Plast Ltd.* v. *Commissioner of Income Tax*, 237 ITR 454.

6. We, thus, find that to this extent no question of law arises for

account for the purpose of deduction under Section 80HH(Act.

7. Under Section 80HHC of the Act, deduction in respect of profits retained for export business is admissible. Sub-section (1) thereof, *inter alia*, provides that the assessee would be allowed, in computing the total income of the assessee, a deduction to the extent of such goods or merchandise. The expression, thus, used is that only such business income would be taken into consideration for the purpose of calculation of deduction under that provision which is *derived by* the assessee from the export business. Same expression is used in Section 80-IA and 80-IB, etc. which relate to deductions in respect of profits of goods from industrial undertakings or enterprises engaged in infrastructure development or Special Economic Zone (SEZ). Those provisions came up for interpretation before the Supreme Court in *Liberty India* v. *Commissioner of Income Tax*, (2009) 317 ITR 218.

8. In that case, the assessee was engaged in the manufacturing of fabrics out of yarns and also various textile items purchased from the market. It had claimed deduction under Section 80-IB of the Act on the increased profits of Rs.22,70,056/- as profit of the industrial undertaking on account of DEPB and duty drawback credited to the profit and loss account. The question which fell for consideration

business of industrial undertaking. It was in this context Apex Court discussed the meaning of the words *'derived from'*. Even before discussing the implication of the aforesaid words, the Court pointed out that though focus was on the analysis of Section 80-IB, the basic scheme of Section 80-I, 80-IA and 80-IB remains the same. The Court was of the view that the words *'derived from'* are narrower in convocation as compared to the words *'attributable to'*. Thus, by using the expression *'derived from'*, the Parliament intended to cover sources not beyond the first degree. Accordingly, only *such* profits are to be computed as if such eligible business is the only source of income of the assessee. Therefore, the devices adopted to reduce or inflate the profits of the eligible business have got to be rejected in view of the overriding provisions of sub-section (5) of Section 80-IA, which is required to be read into Section 80-IB because of common scheme of incentives in the form of deductions as contained in both the sections, which were linked to profits and not for investments. Giving this interpretation to the aforesaid provision, the Court observed as under :-

> "14....On analysis of Sections 80IA and 80IB it becomes clear that any industrial undertaking, which becomes eligible on satisfying Sub-section (2), would be entitled to deduction under Sub-section (1) only to the extent of profits derived from such industrial undertaking after specified date(s). Hence, apart from eligibility, Sub-section(1) purports to restrict the quantum of deduction to a specified percentage of profits. This is the importance of the words "derived from industrial undertaking" as against "profits attributable to industrial undertaking".

those incomes would constitute independent source of beyond the first degree nexus between profits of the industrial undertaking and, therefore, were not to be treated as profits *derived from* the business of industrial undertaking eligible for deduction under Section 80-IB of the Act.

10. When we apply this principle to the facts of this case, the irresistible conclusion would be that such rental income is not directly attributed to the export business. It is clearly not *derived from* any export activity. Thus, even if question No.(a) is answered in favour of the assessee, the assessee shall still not be entitled to take into consideration the rental income treated as business income for the purpose of calculation of deduction under Section 80HHC of the Act. Thus, question (b) is decided in favour of the Revenue and against the Assessee.

11. Question Nos. (c) and (d)

Again, these questions are interrelated to each other and hence taken up together for consideration.

12. Income was generated by the assessee by way of sale of DEPB licences. The AO had deducted 90% of such receipts from the profits of business as per explanation (baa) to Section 80HHC. The case of the assessee was that it was only a supporting manufacturer and not

house. The AO as well as the CIT(A) held that DEPB licenc export incentives received by the assessee, which were covered under clause (iii) of Section 28 of the Act and, therefore, reduction thereof by 90% of the same from the business profits while computing deduction under Section 80HHC was justified. Reversing this decision of the CIT(A), the Tribunal has held as under :-

> "The assessee is a supporting manufacturer and had received these licenses on declaimer issued by the Export House. Such export incentives are available to exporters only. The exporter had disclaimed incentive in favour of the assessee obviously to give some incentive to the assessee so as to promote its export business and, therefore, such incentive in case of supporting manufacturer has to be considered as part of its sale consideration as it would effectively increase the sale price of the supporting manufacturer. The provisions of Section 80HHC have also been enacted keeping in mind the fact that export incentives are available in case of exporters. This, is clearly from the fact that after deducting 90% of incentives, as per explanation (baa), 90% of the same as allocated in the ratio of export turnover to total turnover, has to be added to the quantum of deduction available to the exporter. But this provision of addition is not available in case of supporting manufacturer. Therefore, in case the sale proceeds from DEPB licenses are considered for deduction under explanation (baa) manufacturer, it will lead to discrimination. An identical situation had been considered by the Tribunal in case of National Mineral Development Corporation (supra) in which it was held that export benefits received by the assessee as a supporting manufacturer by virtue of disclaimer issued by MMTC has to be regarded as part of sale consideration and not of the nature of export benefits falling u/s 28(iiia). Respectfully following the said decision, we hold that the receipts by way of sale consideration will be considered as a part of sale consideration in the case of the assessee and 90% of the same will not be deducted from the profit of business as per explanation (baa)."

13. Explanation (baa) to Section 80HHC of the Act defines "profits of business" in the following manner :-

(1) ninety per cent of any sum referred to in clauses (i (iiib), (iiic), (iiid) and (iiie) of Section 28 or of 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.."

Keeping in view this definition, the aforesaid position in law, as explained by the Tribunal seems to be correct. Accordingly, question No. (c) is answered against the Revenue.

14. Insofar as question No. (d) is concerned, that is clearly covered by the judgment of the Madras High Court in the case of *Commissioner of Income Tax* v. *Madras Motors Ltd./M.M. Forgings Ltd.*, 257 ITR 60, namely, turnover relating to other business of spare parts as well as sale of motorcycles and television, etc. in that case could not be included in the total turnover of the assessee for the purpose of computation of special deduction under Section 80HHC. The Court observed that Section 80HHC of the Act applies only to the goods which are not only exported out of India but the sale proceeds of which are receivable in convertible foreign exchange. The legislature has intended the situation where the business could relate to goods which would fetch foreign exchange but there could also be business in relation to these goods which may not be exported or which may not fetch foreign exchange. The thrust of the opening clause of clause (b) of sub-section (3) of Section 80HHC of the Act, has a stress

have to be read in the colour of the opening clause. The sub has been created only to see the ratio of the income out of the export to the total income out of the business in respect of those goods because of the obvious difficulty of segregating the profits earned out of export alone. The total turnover of the business would contemplate only the business regarding such goods part of which are exported and the others are not so exported. Hence, it is impermissible to apply the section even to goods which are outside the limits of clause (a) of sub-section (2).

Thus, this question is also answered against the Revenue and in favour of the assessee.

15. Question No. (e)

The interest/receipts from customers for delayed payment has direct nexus with the export activity. This issue is discussed elaborately in ITA No. 248/2009 entitled *Commissioner of Income Tax, Delhi – I* v. *Advance Detergents Ltd.*, which judgment has also been pronounced in today's date. In such a case, receipt in the form of interest, etc. on delayed payment is treated as part of sale price and would be directly relatable to the business of the assessee. Even the judgment of the Madras High Court in *Madras Motors Ltd.* (supra) also answers this question in favour of the assessee on the interpretation of Section 80HHC.

16. Question No. (f)

This question is answered by this Court in *Commissioner of Income Tax* v. *Shri Ram Honda Power Equip*, 289 ITR 475. The Court held that clause (baa) of the explanation to Section 80HHC envisages a two step process in computing profits derived from exports. First, the Assessing Officer is required to apply Sections 28 to 44 in order to compute the profits and gains of business or profession. In doing so, the Assessing Officer may find that certain incomes, which have no nexus to the export business of the assessee, are not allowable and, therefore, ought to be treated as income from other sources. Once the Assessing Officer computes what is business income then he proceeds to the next step of deducting 90 per cent of the receipts referred in clause (baa) of the explanation to Section 80HHC in order to arrive at the profits derived from profits.

17. It was further opined that at that stage the following questions will have to be determined, namely :-

(i) Does the expression "interest" in explanation (baa) connote net interest, i.e. the gross interest income less the expenditure incurred by the assessee for earning such income, or does it connote gross interest?

(ii) If the expression "interest" implies net interest, then should netting not be allowed where the interest income is computed to be business income?

in Section 80HHC is indicative to *'net interest'*, i.e. gross inte

the expenditure incurred by the assessee in earning such interest.

In view thereof, this question also stands decided in favour of the assessee and against the Revenue.

18. ITA No. 820/2007 (Assessment Year 2000-2001)
ITA No. 237/2008 (Assessment Year 2001-2002)

The following question, as it appears in ITA No. 820/2007, which is identical in these appeals is raised by the Revenue :-

> "Whether on the facts of the present case, the ITAT was correct in law in holding that the interest income received by the assessee at Rs.1.49 crores would be "business income" for the purpose of deduction under Section 80-IB of the Income Tax Act, 1961?"

In view of the judgment of the Supreme Court in *Liberty India* (supra) and our judgment in ITA No. 248/2009 pronounced today, we hold that interest received on delayed payment from the customers would be business income for the purpose of deduction under Section 80-IB of the Act, but interest which is received on the FDRs, etc. would not be included in the business income as that is not *derived from* the business contemplated under Section 80-IB of the Act.

19. ITA No. 329/2004

The question of law on which this appeal was admitted reads as under :-

Facts succinctly stated are that the assessee had deduction of Rs.2,25,68,314/- under Section 80-IA. It included following interest incomes :-

a) Rs.3,01,04,374/- from customers on delayed payment.

b) Rs.4,76,739/- on account of interest on margin money deposits.

c) Rs.5,58,568/- on account of interest on deposits with MSEB.

The AO held that the assessee would be entitled to aforesaid deductions under Section 80-IA of the Act, except deduction with reference to interest earned on deposits out of surplus. The Commissioner of Income Tax, on examination of records, was of the view that the assessee was not entitled to deduction under Section 80-IA with reference to interest to customers on late payment, interest on margin money deposits and interests from MSEB etc. After issuing show-cause notice, he passed orders under Section 263 of the Act for fresh assessment. This order was challenged by the assessee before the Tribunal. The Tribunal has set aside the order passed under Section 263 of the Act holding that the view taken by the AO was one of the possible views and, therefore, the Commissioner could not assume jurisdiction under Section 263 of the Act.

20. We find from the order of the Commissioner of Income Tax passed

income which can, in some manner, be attributable to the t

There must be a direct link between the income earned and the industrial undertaking in the sense that the industrial undertaking must be the immediate source of income. The Commissioner had referred to so many judgments in holding this view. On this premise, he was of the opinion that the view of the AO was wrong. It was purely a legal question and the interpretation to Section 80-IA, as given by the Commissioner, was correct. On that basis, if he came to the conclusion that the interest earned under some categories were not derived from *derived from the business*, we are of the opinion that this formed a justified ground for revising the order under Section 263 of the Act. It is more so when the view of the Commissioner stands vindicative and the aforesaid interpretation is now accepted by the Supreme Court in its judgment in *Liberty India* (supra).

21. We, therefore, decide the issue in the negative, i.e. in favour of the Revenue and against the assessee insofar as the validity of order under Section 263 of the Act is concerned. At the same time, we are of the opinion that the matter need not be referred back to the AO for fresh consideration as all these aspects stand determined.

22. Insofar as interest income from customers on delayed payment is concerned, that is derived from the business and would qualify for

and interest on other deposits (which is already excluded by himself) will not be treated as *derived from* the business of industrial undertaking for the purpose of Section 80-IA of the Act.

The question is answered in the aforesaid manner.

23. ITA No. 1076/2008

Since the order under Section 263 of the Act passed by the Commissioner in respect of assessment year 1998-99 was set aside by the Tribunal, following the order which was subject matter of ITA No. 329/2004, this issue also stands determined in the same manner in favour of the Revenue and against the assessee thereby upholding the order passed under Section 263 of the Act by the Commissioner.

Insofar as various deductions are concerned, which were identical in nature, as in the other year, they would also be treated in the same manner as decided in ITA No. 329/2004, i.e. the interest income received by the assessee from customers for delayed payment would be eligible for deduction under Section 80-IA of the Act, whereas interest on margin money and interest from MSEB would not qualify for such deduction.

24. All these appeals stand disposed of.

(A.K. SIKRI)
JUDGE