(2016) 07 GUJ CK 0039

GUJARAT HIGH COURT

Case No: Tax Appeal No. 1085 of 2008 with Tax Appeal No. 676 of 2008 with Tax Appeal No. 1086 of 2008 with Tax Appeal No. 1812 of 2008

Commissioner of Income-Tax	APPELLANT
Vs	
Metrochem Industries Ltd.	RESPONDENT

Date of Decision: July 19, 2016

Acts Referred:

- Income Tax Act, 1961 - Section 37(1), Section 80HHC

Citation: (2016) 389 ITR 181

Hon'ble Judges: Mr. K.S. Jhaveri and Mr. G.R. Udhwani, JJ.

Bench: Division Bench

Advocate: Mrs. Mauna M. Bhatt, Advocate, for the Appellant No. 1; Mr. Hardik V. Vora, Advocate, for the Opponent No. 1

Final Decision: Disposed Off

Judgement

Mr. K.S. Jhaveri, J. (Oral)—All these appeals are preferred against different judgments. Tax Appeal No. 1085 of 2008 is preferred against the order dated 30.3.2007 of the Income Tax Appellate Tribunal, Ahmedabad Bench "A", Ahmedabad (for short, "the Tribunal") in ITA No. 1373/Ahd/2000 for the Assessment Year 1996-1997. Tax Appeal No. 676 of 2008 is preferred against the order dated 30.3.2007 of the Tribunal in ITA No. 1484/Ahd/2000 for the Assessment Year 1997-1998. Tax Appeal No.1086 of 2008 is preferred against the order dated 30.3.2007 of the Tribunal in ITA No. 1524/Ahd/2000 for the Assessment Year 1996-1997, while Tax Appeal No. 1812 of 2008 is preferred against the order dated 30.3.2007 of the Tribunal in ITA No. 1483/Ahd/2000 for the Assessment Year 1994-1995. By way of the impugned orders, the Tribunal held in favour of the assessee by confirming the order of CIT (A).

2. At the time of admitting present appeals, following questions of law were framed for our consideration:-

Tax Appeal No.1085 of 2008

"A. Whether the Appellate Tribunal is right in law and on facts in holding that foreign exchange fluctuation and duty drawback is an income derived from industrial undertaking, eligible for deduction under section 80I and 80IA of the Act and thereby directing the Assessing Officer to consider the claim of the assessee upon necessary material to be placed on record by the assessee?

B. Whether the Appellate Tribunal ought not to have appreciated that foreign exchange fluctuation and duty drawback cannot be stated to be derived from industrial undertaking and, therefore, not eligible for deduction u/S.80I and 80IA of the Act?

C. Whether the Appellate Tribunal is right in law and on facts in reversing the order of the CIT(A) and holding that discount/kasar can be stated to be derived from industrial undertaking, therefore, eligible for deduction under section 80I and 80IA of the Act?

D. Whether the Appellate Tribunal is right in law and on facts in holding that only the net interest is required to be excluded while calculating deduction under section 80I and 80IA of the Act?

E. Whether the Appellate Tribunal is right in law and on facts in holding that laboratory sample testing charges and sales tax set-off income form part of eligible profit for the purpose of computation of deduction under section 80HHC of the Act?"

Tax Appeal No. 676 of 2008

"A. Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the CIT(A) in allowing the deduction under section 80I in respect of (i) interest (ii) vatav, kasar and incidental charges (iii) advances written off, and (iv) managerial remuneration?

B. Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the CIT(A) in allowing the depreciation of Rs.1,82,071/- on building at Baroda and depreciation of Rs.5,82,091/- on Baroda unit?

C. Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the CIT(A) in deleting the disallowance of deferred revenue expenses towards CEPT of Rs.51,20,508/- and payment to different agencies of Rs.34,15,460/-, in connection with the effluent treatment plant?

D. Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the CIT(A) allowing deduction under section 80HHC of the Act on (a) laboratory sample testing receipts, (b) foreign exchange fluctuations, (c) discount, kasar and incidental charges, (d) sales tax set off, (e) insurance premium, (f) sundry balances written off?"

Tax Appeal No. 1086 of 2008

"A. Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the CIT(A) deleting the disallowance of Rs.97,23,550/- made in respect of amount paid to farmers on account of damage/penalty in view of the decision of this Hon''ble Court in pollution matters?

B. Whether the Appellate Tribunal ought not have appreciated that the amount of Rs.97,23,550/- paid to the farmers was on account of penalty for infringement of law and, therefore, not allowable under section 37 of the Act?

C. Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the CIT(A) deleting the disallowance of Rs.91,46,637/- made in respect of contribution for effluent treatment plant?

D. Whether the Appellate Tribunal ought not have appreciated that the amount of Rs.91,46,637/- incurred towards contribution for common effluent treatment plant was in the nature of penalty and, therefore, not allowable under section 37 of the Act and, in the alternative, was a capital outlay and, therefore also, not allowable under section 37 of the Act?

E. Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the CIT(A) directing that only the net interest income should be excluded from eligible profit for the purpose of computation of deduction under section 80I and 80IA of the Act?

F. Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the CIT(A) deleting the disallowance of Rs.2,64,051/- being depreciation on new project at Baroda?

G. Whether the Appellate Tribunal is right in law and on facts in not adjudicating the Revenue''s ground relating to the issue of vatav, kasar, laboratory testing fees and sales tax set-off for the purpose of computation of deduction under section 80HHC of the Act?"

Tax Appeal No. 1812 of 2008

"A. Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the CIT(A) directing to allow deduction under section 80I/80IA of the Act on vatav, kasar and discount income and sales tax set off?

B. Whether the Appellate Tribunal is right in law and on facts in holding that only the net interest is to be excluded while working out deduction under section 80I and 80IA of the Act?

C. Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the CIT(A) deleting the disallowance of Rs. 16,27,680/- made out of job work charges?

D. Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the CIT(A) deleting the addition under section 43B of Rs.2,18,08,262/- being the refund of excise duty on the ground that the same was not credited to the profit and loss account?

E. Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the CIT(A) directing the Assessing Officer not to exclude receipt on account of laboratory sample testing, sales tax set off/refund and discount, vatav/kasar, from the profit within the meaning of Explanation (baa) to section 80HHC of the Act?"

3. Since common issues are involved in all these appeals, they are taken up for hearing together and are being disposed of by this common order.

4. So far as issue with regard to Vatav, kasar, discount and sales tax set-off under Section 80-I is concerned, learned counsel for the appellant submitted that the CIT (A) had held that this income cannot be said to be derived from industrial undertaking. However, the Appellate Tribunal has reversed the findings of CIT (A) and allowed the claim of the assessee. He further submitted that so far as the issue with regard to netting of interest is concerned, the same will be now governed by the decision of the Apex Court in the case of **ACG Associated Capsules Pvt. Ltd v. CIT reported in 343 ITR 89 (SC).** So far as issue with regard to rebate on job work charges is concerned, it is submitted that since the concerned company could not carry out the Job work of the desired quality, the assessee claimed discount/rebate as there was no liability of payment on the assessee. So far as refund of excise duty is concerned, it is submitted that allowance of excise duty is subject to the provisions of Section 43B of the Act and the Appellate Tribunal has not given any finding in respect of the provisions of Section 43B of the Act. He further submitted that so far as issue regarding refund of excise duty is concerned, the same is wrongly allowed in favour of the assessee. It is also submitted that so far as laboratory sample testing charges and discount, vatav, kasar etc. and sales tax set off is concerned, the same is wrongly framed and the same is covered by the earlier decision reported in **Commissioner of Income tax v. Meghalaya Steels Ltd. reported in (2016) 383 ITR 217** and **ADCI Dye Chem P. Ltd. v. Deputy Commissioner of Income-tax reported in (2015) 370 ITR 408 (Guj)**.

5. Learned counsel for the respondent supported the impugned orders and submitted that the Tribunal has not committed any error while passing the impugned order. He prayed to dismiss present appeals.

6. Heard learned advocates for both the sides. We have also gone through the impugned order, judgments cited before us and the material on record. So far as issue with regard to Vatav, kasar, incidental charges and advances written off are concerned, the same is covered by the decision in the case of **Commissioner of Income-Tax v. Nirma Ltd. reported in (2014) 367 ITR 12 (Guj)**, wherein it is

observed as under :-

"Insofar as question Nos. 1, 4, 8, 10 and 11 are concerned, they have a common element, namely, whenever certain income is to be excluded for the purpose of deduction under section 80-I, 80-IA and 80HH, etc. gross income is to be excluded or only the net thereof is the question. In a separate order passed by us today in Tax Appeal No.810 of 2013, we have rejected the Revenues appeal making following observations:

The question is when certain income of the assessee is excluded from the claim of deduction under section 80I or 80HH of the Act, should the gross income be excluded or should it be only net, that is, total receipt minus the expenditure incurred by the assessee for earning such income which should be so excluded.

Such a question in the context of deduction under section 80HHC came up for consideration before the Supreme Court in the case of **ACG Associated Capsules Pvt. Ltd v. CIT, 343 ITR 89 (SC)**. The Supreme Court held that for the purpose section 80HHC of the Act, it is not the entire amount received by the assessee on sale of DEPB credit, but the sale value of less the face value of the DEPB that will represent profit on transfer of DEPB credit by the assessee. Heavy reliance was placed in the case of **Topman Exports v. CIT, 342 ITR 49 (SC)**. Extending such logic, it was further held that even other amounts, such as, interest or rent when are to be excluded for the purpose of explanation (baa) to section 80HHC of the Act. Ninety per cent of not the gross rent or gross interest, but the net thereof shall have be excluded. It was observed as under:

If we now apply Explanation (baa) as interpreted by us in this judgment to the facts of the case before us, if the rent or interest is a receipt chargeable as profits and gains of business and chargeable to tax under section 28 of the Act, and if any quantum of the rent or interest of the assessee is allowable as expense in accordance with sections 30 to 44D of the Act and is not to be included in the profits of the business of the assessee as computed under the head Profits and gains of business or profession, ninety per cent of such quantum of the receipt of rent or interest will not be deducted under clause (1) of Explanation (baa) to section 80HHC. In other words, ninety per cent of not the gross rent or gross interest but only the net interest or net rent, which has been included in the profits of business of the assessee as computed under the head Profits and gains of business or profession, is to be deducted under clause (1) of Explanation (baa) to section 80HHC for determining the profits of the business.

In view of such decision, question No.3 raised by the Revenue gets automatically answered since the amounts referred to in the said question are to be excluded for the purpose of deduction under section 80HHC of the Act.

Learned counsel for the Revenue vehemently contended that the ratio of the decision in the case of ACG Associated Capsules Pvt. Ltd (supra) cannot be applied to

a situation where the exclusion from the claim of deduction relates to section 80HH or section 80-I of the Act. He strenuously urged that the language used in both the sets of provisions are different. Section 80HHC is also vitally different and that therefore the concept of netting may not be automatically applied to deduction under section 80HH and 80-I of the Act. He submitted that number of tax appeals have been admitted by this Court on this issue and this appeal may also be likewise admitted. He drew our attention to the order dated 6.5.2013 passed by this Court in the case of Bloom Decor Ltd. in Tax Appeal No. 447 of 2013 where at the instance of the assessee, similar question was not considered.

On the other hand, learned counsel Shri Soparkar for the assessee, in addition to relying on the decision in the case of ACT Associated Capsules Pvt. Ltd. (supra), also placed heavy reliance on an order dated 30.11.2013 in Tax Appeal No. 213 of 2006 in the case of Rajoo Engineers Ltd. in which the Revenues appeal raising such a question came to be dismissed relying on the decision in the case of ACG Associated Capsules Pvt. Ltd. (supra). The counsel also relied on a decision of the Delhi High Court in the case of Essel Shyam Communication Ltd. v. Commissioner of Income tax, (2012) 28 taxmann.com 243 (Delhi), in which in detailed consideration, relying on the decision of the Supreme Court in the case of ACG Associated Capsules Pvt. Ltd. (supra), exclusion was approved for deduction under section 80-IA of the Act.

Having heard the learned counsel for the parties, we see no reason to entertain this tax appeal. The Supreme Court in the case of ACG Associated Capsules Pvt. Ltd. (supra) has already laid down the foundation for the logic for excluding the net profit and not the gross profit from the claim of deduction when it is found that the source of income does not quality for such deduction under section 80HHC of the Act. It is true that section 80HHC represents vastly different scheme of deduction and also provides for complex formula for deriving for the eligible profit for deduction under different situations depending on whether the exporter is also engaged in the local business or not.

However, this distinction would not be material insofar as central question of exclusion of certain profit from the activity which is not eligible for deduction under section 80HH and 80-I are concerned. The logic being when the profit is being excluded form the claim of deduction, not the gross profit but the net thereof, that is the gross profit minus the expenditure incurred for earning such profit should be excluded. That is precisely how this Court in the case of Rajoo Engineers (supra) viewed the situation. That is how the Delhi High Court in the case of Essel Shyam Communication (supra) held referring to the decision in the case of ACG Associated Capsules Pvt. Ltd. (supra).

It is true that in the case of Bloom Decor Ltd., a question was suggested by the assessee which may have some bearing on the controversy on hand. However, the entire focus of the order of the Court was regarding applicability of the decision of the Supreme Court in the case of Topman Exports (supra) and not on the question

of netting. In any case, therein, the decision in the case of ACG Associated Capsules Pvt. Ltd was not noticed.

Insofar as question Nos. 2, 5, 7 and 12 are concerned, it is an undisputed position that the issues are covered by a decision of this Court in the case of **Dy. C.I.T. v. Harjivandas Juthabhai Zaveri, 258 ITR 785** in which the Court upheld the decision of the Tribunal granting benefit of deduction under section 80I of the Act on various incomes, such as, job work receipt, sale of empty soda ash bardan, sale of empty barrels and plastic waste. Such questions are, therefore not required to be considered.

So far as question Nos.3, 6, 9 and 15 are concerned, the same are stated to be covered by the decision of this Court in the case of **Nirma Industries Ltd. v. Deputy CIT, 283 ITR 402 (Guj.)** in which the Court upheld the assessees claim for deduction under section 80I of the Act on the interest received on late payment of sale consideration as amount derived from eligible business. These questions are, therefore, not required to be considered.

Coming to question No.14, we notice that the issue pertains to the assessees claim for deduction under section 35AB of the Act. The Tribunal has in the impugned judgment remanded the matter back to the Assessing Officer for full verification of such claim. It is clarified that the issues are kept open and shall be examined by the Assessing Officer, afresh.

The sole surviving question No.13, pertains to disallowance of soda ash project interest expenses of Rs.3.33 crores (rounded off) and lab project interest of Rs.12.27 crores (rounded off). The Assessing Officer, questioned the assessee on these expenses and deleted the same on two grounds, firstly that the interest was paid by way pre-operative expenditure and secondly the assessee had capitalized such expenditure. The assessee carried the matter in appeal. CIT (Appeals) relying on a decision of this Court in the case of **CIT v. Alembic Glass Industries Ltd., 103 ITR 715 (Guj)** held in favour of the assessee. In addition to coming to the conclusion that there was commonality of business it was further held that the expenditure was in connection with the expansion of the existing business. On such ground, the expenditure was held allowable.

It is this order of the CIT (Appeal) which the Tribunal upheld in the impugned judgment.

Having heard the learned counsel for the parties and having perused the documents on record, we notice that CIT (Appeals) and the Tribunal concurrently came to the conclusion that there was inter-connection, inter-lacing and inter-dependence of the management, financial and administrative control of various units of Nirma Limited. It was on this ground, the Tribunal held that the business in question is continuation of the existing business and not a new business. In this context, the decision relied on by the authorities below of this Court

in the case of Alembic Glass Industries Ltd. (supra) laid down tests for ascertaining whether a business was part of existing business or the assessee was starting a new unit. It was held that merely because the unit was coming to a distant point by itself would not mean that it was a new business.

If the facts as recorded by the CIT (Appeals) and the Tribunal can be said to have achieved finality, it would emerge that the assessee through its existing administrative mechanism started a new facility for production of soda ash and had also set up facility for production of a material called lab for its captive consumption for the purpose of existing of existing manufacture in business. It is no doubt that the assessee is engaged in the business of manufacture of soap and the soda ash and lab so produced is used by way of captive consumption. When such facts viewed in light of the findings of the CIT (Appeals) and the Tribunal, we have no reason to interfere with the ultimate conclusion. Had it been a case of entirely a new project undertaken by the assessee as canvassed by the counsel for the Revenue, a serious question of claiming pre-operative expenditure of interest by way of revenue expenditure would arise. However, when the authorities below found that it was an expansion of the existing business, applying the tests laid down by this Court in the case of Alembic Glass Industries Ltd. (supra), in view of the decision of the Supreme Court in the case of **Deputy CIT v. Core Health Care Ltd., 298 ITR 194 (SC)**, the fact whether the borrowing is capital or revenue expenditure would be of no consequence."

7. So far as issued with regard to Vatav, kasar, discount and sales tax set-off under Section 80-I is concerned, the same is covered by the decision in the case of **Commissioner of Income tax v. Meghalaya Steels Ltd. reported in (2016) 383 ITR 217**, wherein it is observed as under:-

"24. We do not find it necessary to refer in detail to any of the other judgments that have been placed before us. The judgment in Jai Bhagwan case (supra) is helpful on the nature of a transport subsidy scheme, which is described as under:

"The object of the Transport Subsidy Scheme is not augmentation of revenue, by levy and collection of tax or duty. The object of the Scheme is to improve trade and commerce between the remote parts of the country with other parts, so as to bring about economic development of remote backward regions. This was sought to be achieved by the Scheme, by making it feasible and attractive to industrial entrepreneurs to start and run industries in remote parts, by giving them a level playing field so that they could compete with their counterparts in central (non-remote) areas.

The huge transportation cost for getting the raw materials to the industrial unit and finished goods to the existing market outside the state, was making it unviable for industries in remote parts of the country to compete with industries in central areas. Therefore, industrial units in remote areas were extended the benefit of subsidised

transportation. For industrial units in Assam and other northeastern States, the benefit was given in the form of a subsidy in respect of a percentage of the cost of transportation between a point in central area (Siliguri in West Bengal) and the actual location of the industrial unit in the remote area, so that the industry could become competitive and economically viable." (Paras 14 and 15)

25. The decision in **Sahney Steel and Press Works Ltd. v. Commissioner of Income Tax, A.P. - I, Hyderabad (1997) 7 SCC 764**, dealt with subsidy received from the State Government in the form of refund of sales tax paid on raw materials, machinery, and finished goods; subsidy on power consumed by the industry; and exemption from water rate. It was held that such subsidies were treated as assistance given for the purpose of carrying on the business of the assessee.

26. We do not find it necessary to further encumber this judgment with the judgments which Shri Ganesh cited on the netting principle. We find it unnecessary to further substantiate the reasoning in our judgment based on the said principle.

27. A Delhi High Court judgment was also cited before us being **CIT v. Dharampal Premchand Ltd., 317 ITR 353** from which an SLP preferred in the Supreme Court was dismissed. This judgment also concerned itself with Section 80-IB of the Act, in which it was held that refund of excise duty should not be excluded in arriving at the profit derived from business for the purpose of claiming deduction under Section 80-IB of the Act.

28. It only remains to consider one further argument by Shri Radhakrishnan. He has argued that as the subsidies that are received by the respondent, would be income from other sources referable to Section 56 of the Income Tax Act, any deduction that is to be made, can only be made from income from other sources and not from profits and gains of business, which is a separate and distinct head as recognised by Section 14 of the Income Tax Act. Shri Radhakrishnan is not correct in his submission that assistance by way of subsidies which are reimbursed on the incurring of costs relatable to a business, are under the head "income from other sources", which is a residuary head of income that can be availed only if income does not fall under any of the other four heads of income. Section 28(iii)(b) specifically states that income from cash assistance, by whatever name called, received or receivable by any person against exports under any scheme of the Government of India, will be income chargeable to income tax under the head "profits and gains of business or profession". If cash assistance received or receivable against exports schemes are included as being income under the head "profits and gains of business or profession", it is obvious that subsidies which go to reimbursement of cost in the production of goods of a particular business would also have to be included under the head "profits and gains of business or profession", and not under the head "income from other sources".

7.1 In view of above observations, this issue is answered in favour of the assessee and against the department.

8. So far as the issue with regard to netting of interest is concerned, the same will be now governed by the decision of the Apex Court in the case of **M/s ACG Associated Capsules Pvt. Ltd. v. The Commissioner of Income Tax, Central-IV, Mumbai, reported in 343 ITR 89 (SC)**, wherein it is observed as under:-

"Before we deal with the contentions of learned counsel for the parties, we may extract Explanation (baa) to Section 80HHC of the Act.

"Explanation:- For the purposes of this section,-

(baa) "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".

9. Explanation (baa) extracted above states that "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 the receipts of the nature mentioned in clauses (1) and (2) of the Explanation (baa).

Thus, profits of the business of an assessee will have to be first computed under the head "Profits and Gains of Business or Profession" in accordance with provisions of Section 28 to 44D of the Act. In the computation of such profits of business, all receipts of income which are chargeable as profits and gains of business under Section 28 of the Act will have to be included. Similarly, in computation of such profits of business, different expenses which are allowable under Sections 30 to 44D have to be allowed as expenses. After including such receipts of income and after deducting such expenses, the total of the net receipts are profits of the business of the assessee computed under the head "Profits and Gains of Business or Profession" from which deductions are to made under clauses (1) and (2) of Explanation (baa).

10. Under Clause (1) of Explanation (baa), ninety per cent of any receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in any such profits are to be deducted from the profits of the business as computed under the head "Profits and Gains of Business or Profession". The expression "included any such profits" in clause (1) of the Explanation (baa) would mean only such receipts by way of brokerage, commission, interest, rent, charges or any other receipt which are included in the profits of the business as

computed under the head "Profits and Gains of Business or Profession". Therefore, if any quantum of the receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature is allowed as expenses under Sections 30 to 44D of the Act and is not included in the profits of business as computed under the head "Profits and Gains of Business or Profession", ninety per cent of such quantum of receipts cannot be reduced under Clause (1) of Explanation (baa) from the profits of the business. In other words, only ninety per cent of the net amount of any receipt of the nature mentioned in clause (1) which is actually included in the profits of the assessee is to be deducted from the profits of the assessee for determining "profits of the business" of the assessee under Explanation (baa) to Section 80HHC.

11. For this interpretation of Explanation (baa) to Section 80HHC of the Act, we rely on the judgment of the Constitution Bench of this Court in Distributors (Baroda) P. Ltd. v. Union of India and Others (supra). Section 80M of the Act provided for deduction in respect of certain intercorporate dividends and it provided in sub-section (1) of Section 80M that "where the gross total income of an assessee being a company includes any income by way of dividends received by it from a domestic company, 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 income by way of dividends an amount equal to" a certain percentage of the income mentioned in this Section. The Constitution Bench held that the Court must construe Section 80M on its own language and arrive at its true interpretation according to the plain natural meaning of the words used by the legislature and so construed the words "such income by way of dividends" in sub-section (1) of Section 80M must be referable not only to the category of income included in the gross total income but also to the quantum of the income so included. Similarly, Explanation (baa) has to be construed on its own language and as per the plain natural meaning of the words used in Explanation (baa), the words "receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in such profits" will not only refer to the nature of receipts but also the quantum of receipts included in the profits of the business as computed under the head "Profits and Gains of Business or Profession" referred to in the first part of the Explanation (baa). Accordingly, if any quantum of any receipt of the nature mentioned in clause (1) of Explanation (baa) has not been included in the profits of business of an assessee as computed under the head "Profits and Gains of Business or Profession", ninety per cent of such quantum of the receipt cannot be deducted under Explanation (baa) to Section 80HHC.

12. If we now apply Explanation (baa) as interpreted by us in this judgment to the facts of the case before us, if the rent or interest is a receipt chargeable as profits and gains of business and chargeable to tax under Section 28 of the Act, and if any quantum of the rent or interest of the assessee is allowable as an expense in accordance with Sections 30 to 44D of the Act and is not to be included in the profits

of the business of the assessee as computed under the head "Profits and Gains of Business or Profession", ninety per cent of such quantum of the receipt of rent or interest will not be deducted under clause (1) of Explanation (baa) to Section 80HHC. In other words, ninety per cent of not the gross rent or gross interest but only the net interest or net rent, which has been included in the profits of business of the assessee as computed under the head "Profits and Gains of Business or Profession", is to be deducted under clause (1) of Explanation (baa) to Section 80HHC for determining the profits of the business.

13. The view that we have taken of Explanation (baa) to Section 80HHC is also the view of the Delhi High Court in Commissioner of Income-Tax v. Shri Ram Honda Power Equip (supra) and the Tribunal in the present case has followed the judgment of the Delhi High Court. On appeal being filed by the Revenue against the order of the Tribunal, the High Court has set aside the order of the Tribunal and directed the Assessing Officer to dispose of the issue in accordance with the judgment of the Bombay High Court in Commissioner of Income-Tax v. Asian Star Co. Ltd. (supra). We must, thus, examine whether reasons given by the High Court in its judgment in Commissioner of Income-Tax v. Asian Star Co. Ltd. (supra) were correct in law.

14. On a perusal of the judgment of the High Court in Commissioner of Income-Tax v. Asian Star Co. Ltd. (supra), we find that the reason which weighed with the High Court for taking a different view, is that rent, commission, interest and brokerage do not possess any nexus with export turnover and, therefore, the inclusion of such items in the profits of the business would result in a distortion of the figure of export profits. The High Court has relied on a decision of this Court in **Commissioner of Income-Tax v. K. Ravindranathan Nair [(2007) 295 ITR 228 (SC)]** in which the issue raised before this Court was entirely different from the issue raised in this case. In that case, the assessee owned a factory in which he processed cashew nuts grown in his farm and he exported the cashew nuts as an exporter. At the same time, the assessee processed cashew nuts which were supplied to him by exporters on job work basis and he collected processing charges for the same. He, however, did not include such processing charges collected on job work basis in his total turnover for the purpose of computing the deduction under Section 80HHC (3) of the Act and as a result this turnover of collection charges was left out in the computation of profits and gains of business of the assessee and as a result ninety per cent of the profits of the assessee arising out of the receipt of processing charges was not deducted under clauses (1) of the Explanation (baa) to Section 80HHC. This Court held that the processing charges was included in the gross total income from cashew business and hence in terms of Explanation (baa), ninety per cent of the gross total income arising from processing charges had to be deducted under Explanation (baa) to arrive at the profits of the business. In this case, this Court held that the processing charges received by the assessee were part of the business turnover and accordingly the income arising therefrom should have been included in the profits and gains of business of the assessee and ninety per cent of

this income also would have to be deducted under Explanation (baa) under Section 80HHC of the Act. In this case, this Court was not deciding the issue whether ninety per cent deduction is to be made from the gross or net income of any of the receipts mentioned in clause (1) of the Explanation (baa).

15. The Bombay High Court has also relied on the Memorandum explaining the clauses of the Finance Bill, 1991 contained in the circular dated 19.12.1991 of the Central Board of Direct Taxes to come to the conclusion that the Parliament intended to exclude items which were unrelated to the export turnover from the computation of deduction and while excluding such items which are unrelated to export for the purpose of Section 80HHC, Parliament has taken due note of the fact that the exporter assessee would have incurred such expenditure in earning the profits and to avoid a distorted figure of export profits, ninety per cent of the receipts like brokerage, commission, interest, rent, charges are sought to be excluded from the profits of the business. In our considered opinion, it was not necessary to refer to the explanatory Memorandum when the language of Explanation (baa) to Section 80HHC was clear that only ninety per cent of receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in such profits computed under the head profits and gains of business of an assessee could be deducted under clause (1) of Explanation (baa) and not ninety per cent of the quantum of any of the aforesaid receipts which are allowed as expenses and therefore not included in the profits of business of the assessee.

16. In the result, we allow the appeal and set aside the impugned order of the High Court and remand the matter to the Assessing Officer to work out the deductions from rent and interest in accordance with this judgment. No costs.

Civil Appeal No. 4534 of 2008

This is an appeal against the order dated 19.01.2007 of the Delhi High Court in I.T.A. No. 541 of 2006.

2. The facts of this case very briefly are that Bharat Rasayan Limited (for short ''the assessee'') filed a return of income tax claiming a deduction of Rs.72,76,405/- under Section 80HHC of the Act. In the assessment order, the Assessing Officer held that ninety per cent of the gross interest has to be excluded from the profits of the business of the assessee under Explanation (baa) to Section 80HHC of the Act and deducted ninety per cent of the gross interest of Rs.50,26,284/- from the profits of the business of the assessee. The assessee preferred an appeal contending that only ninety per cent of the net interest should have been deducted from the profits of the business of the assessee under Explanation (baa) to Section 80HHC, but the Commissioner of Income Tax (Appeals) rejected this contention of the assessee. Aggrieved, the assessee filed an appeal before the Income Tax Appellate Tribunal (for short ''the Tribunal'') and the Tribunal allowed the appeal of the assessee and

held that the assessee was entitled to deduct the expenses from the interest received and only ninety per cent of the net amount of interest could be excluded under Explanation (baa) to Section 80HHC and remitted the matter to the Assessing Officer to examine whether there is factually an excess between the interest paid and interest received and take a fresh decision. The Revenue filed an appeal against the order of the Tribunal before the High Court, but by the impugned order the High Court following its decision in **Commissioner of Income-Tax v. Shri Ram Honda Power Equip** (supra) sustained the order of the Tribunal and dismissed the appeal.

3. We have held in our judgment in the case of M/s ACG Associated Capsules Pvt. Ltd. v. Commissioner of Income Tax that ninety per cent of not the gross interest but only the net interest, which has been included in the profits of the business of the assessee as computed under the heads ''Profits and Gains of Business or Profession'' is to be deducted under clause (1) of Explanation (baa) to Section 80HHC for determining the profits of the business. Since, the view taken by the High Court in the impugned order is consistent with our aforesaid view, we find no merit in this appeal and we accordingly dismiss the same. There shall be no order as to costs."

8.1 Accordingly, this issue is answered in favour of the assessee and against the department.

9. So far as issue with regard to rebate on job work charges is concerned, the amount is paid by the assessee, therefore, the Tribunal is right in law and on facts in confirming the order passed by the CIT(A) deleting the disallowance of job work charges. Accordingly, the issue is answered in favour of the assessee and against the revenue.

10. So far as issue regarding refund of excise duty is concerned, the same is covered in favour of the assessee in view of the decision of the Apex Court in the case of **Laxmi Machine Works v. CIT, reported in 290 ITR 667.** Accordingly, the issue is answered in favour of the assessee and against the revenue.

11. So far as question with regard to common effluent treatment plant is concerned, the same is covered by the decision of this Court in Tax Appeal No.1392 of 2006, wherein it is held as under:-

"The following questions are proposed for admission of this appeal:-

"(A) Whether the Appellate Tribunal is right in law and on facts in holding that sales tax and excise duty are not to be treated as part of turnover for the purpose of computation of deduction under section 80HHC?

(B) Whether the Appellate Tribunal is right in law and on facts in holding that the amount of Rs.51 lakhs paid by the assessee towards contribution to common effluent treatment plant was an allowable revenue deduction.?"

So far as the issue raised in question No.1 is concerned, the same is covered by the decision of the Apex Court in the case of **Laxmi Machine Works v. CIT, 290 IT 667**, in favour of the assessee.

So far as the issue raised in second question is concerned, the same has been considered by this Court and the Tribunal has discussed the issue as under:

"7. As regards the third ground, the Assessing Officer noted that this is a recurring issue and following his order in assessment year 1996-97, he disallowed the claim of the assessee for the contribution of Rs.50,00,000/- to Odhav Common Effluent Treatment Plant and Rs.1 lac to Naroda Environment Project. The CIT (A) allowed the claim of the assessee by observing in paragraph 7.3 of his order as under:-

"3. I have considered the facts of the and the submissions made on behalf of the appellant. It is seen that this issue has already been decided by me in favour of the appellant, while deciding the appeal filed by the appellant for A.Y. 96-97. Following the said appellate order dated 12.7.99 for A.Y.96-97 in the appellant''s own case, it is held that the Assessing Officer was not justified in disallowing Rs.51 lacs paid by the appellant company as per the direction by the Hon''ble Gujarat High Court. Therefore, the disallowance of Rs.51 lacs made by the Assessing Officer is directed to be deleted."

8. The assessee''s contention is that it is compulsorily required to contribute as per the directions of the Gujarat High Court and placing reliance on the decision of the Gujarat High Court in the case of **Navsari Cotton and Silk Mills Ltd. 135 ITR 546**, the expenditure is claimed to be a revenue expenditure. A similar issue has come up before the Gujarat High Court in the case of Alembic Glass Industries Ltd. published in Ahmedabad Chartered Accountants Association unreported judgments wherein it was held that the assessee being member of federation of Gujarat Mills and Industries, contribute a sum of Rs.5000/- for construction of a building and auditorium and the amount was held to be an allowable deduction. In view of the aforesaid decision of the Gujarat High Court, we are of the opinion that the contribution made by the assessee is an allowable deduction and the CIT(A) was justified in allowing the same."

Considering the above facts, we see no merits in the appeal. The appeal stands dismissed at the admission stage."

11.1 In view of above observations, this issue is answered in favour of the assessee and against the department.

12. So far as the issue with regard to Foreign Exchange Fluctuation under Section 80IA is concerned, the same will be now governed by the decision of this Court in the case of **Commissioner of Income-tax v. Priyanka Gems reported in 367 ITR 575**, wherein it is observed as under:-

"25. Under the circumstances, we have no hesitation in upholding the view of the Tribunal. Quite apart, the issue is substantially covered by the decision of the Commissioner of Income-tax v. Amba Impex(supra). Consistent and at times independent trend of the judicial pronouncements of Courts across the country need not be disturbed. Even independently, we are of the view that the foreign exchange gain arising out of the fluctuation in the rate of foreign exchange cannot be divested from the export business of the assessee. As noted, once export is made, due to variety of reasons, the remission of the export sale consideration may not be made immediately. Under the accounting principles, therefore, the assessee, on the basis of accrual, would record sale consideration at the prevailing exchange rate on the quoted price for the exported goods in the foreign currency rates. If during the same year of the export, the remission is also made, the difference in the rate recorded in the accounts of the assessee and that eventually received by way of remission either positive or negative, would be duly adjusted. May be the accounting standards require that the same may be recorded in separate foreign exchange fluctuation account. Nevertheless any deviation either positive or negative must have direct relation to the export actually made. Payment would be due to the assessee on account of the factum of export. Current price of the goods so exported would also be pre-decided in the foreign exchange currency. The exact remittance in Indian rupees would depend on the precise exchange rate at the time when the amount is remitted. This fluctuation and possibility of increase or decrease, in our opinion, can have no bearing on the source of such receipt. Primarily and essentially, the receipt would be on account of the export made. If this is so, any fluctuation thereof also must be said to have arisen out of the export business. Mere period of time and the vagaries of rate fluctuation in international currencies cannot divest the income from the character of the income from assessees export business. In that view of the matter, the Revenues contention that such income cannot be said to have been derived from the export business must fail. If this is the position when the remittance is made during the same year of the export, we fail to see what material change can it bring about if within the time permitted under sub-section(2) of section 80HHC, the remittance is made but in the process accounting year has changed. To our mind mere change in the accounting year can have no real impact on the nature of the receipt. The conclusion of the Assessing Officer that since the year during which such sale proceeds were received by the assessee export was not made, would not in any manner change the situation. The assessee being engaged in the business of export and having made the export, mere fact of the remittance being made after 31st of March of the year when export was made, would not change the situation insofar as, relation of such income to the assessees export business is concerned. Clause (baa) to the Explanation to section 80HHC provides for exclusion of certain incomes for computation of export profit under section 80HHC. Sub-clause (1) of clause (baa) thereof pertains to 90% of the sum referred to in clauses (iiia), (iiib),(iiic),(iiid) and (iiie) of section 28 or any receipts by way of brokerage, commission, interest, rent, charges or any other receipt of similar nature

included in such profits. The term foreign exchange difference is not specified in any of the categories specifically mentioned in the said clause. The Revenue, however, contended that the same must be included by necessary implication as part of other receipts. Legislature, however, has used the term any other receipt of similar nature. This expression similar nature would have considerable bearing on the ultimate conclusion that we arrive in this respect. What is to be excluded under the said sub-clause(1) of clause (baa) is any other receipt of a nature similar to the brokerage, commission, interest, rent or charges. The receipt by way of foreign exchange fluctuation not being similar to any of these receipts mentioned above, application of clause (baa) must be excluded. Sub-rule (1) of rule 115 only provides for adopting the rate of exchange for calculation of value of rupee of any income accruing or arising in case of an assessee and provides that the same shall be telegraphic transfer of buying rate of such currency on the specified date. The term specified date has been defined in Explanation-2 to the said sub-rule (1). Rule 115 of the Income-tax Rules, 1962 thus has application for a specific purpose and has no bearing while judging whether foreign exchange rate fluctuation gain can form part of the deduction under section 80HHC of the Act. In case of **Commissioner of Income-tax and others v. Chowgule and Co. Ltd. reported in (1996) 218 ITR 384**, the Court held that rule 115 does not lay down that all foreign currencies received by the assessee will be converted into Indian rupees only on the last date of the accounting period. Rule only fixed the rate of conversion of foreign currency. If there is no foreign currency to convert on the last date of accounting period, then no question of invoking rule 115 will arise.

26. Reference to Explanation-2 below sub-section (2) of section 80HHC also is of no avail. Such explanation covers the cases where any goods or merchandise are transferred by an assessee to its branch office, warehouse or any other establishment situated outside India and thereafter sold from such branch, office, warehouse or establishment. In such a case, it is provided that transfer shall be deemed to be export out of India and the value of such goods or merchandise declared in the shipping bill or bill of export as referred to in sub-section (1) of 50 of the Customs Act, 1962 shall, for the purpose of section 80HHC, be deemed to be sale proceeds thereof. Two things thus emerge. Firstly, the explanation would have application only if it is a case of transfer of goods or merchandise by an assessee to its branch office, warehouse or establishment situated outside India before the sale of goods to the foreign importer. In none of the cases, it is even contended by the Revenue that such facts arise and that, therefore, the explanation would apply. Second aspect is that even in such a case what is to be adopted for the purpose of value of goods or merchandise is that declared in the shipping bill or bill of export referred to in sub-section(1) of section 50 of the Customs Act. Here the term used is value of goods or merchandise and such value of goods or merchandise can as well be the price agreed to between the parties and indicated in foreign currency terms. Having so adopted the value of goods as indicated in the export documents, what

the assessee may actually receive in terms of Indian currency, would depend on the time of remission and the precise foreign exchange rate of the foreign currency at that point of time.

27. We would now refer to the decision cited by counsel for the Revenue. In case of **Pandian Chemicals Ltd. v. Commissioner of Income-tax reported in (2003) 262 ITR 278**; the question arose whether interest derived by the industrial undertaking from the deposit made with the Electricity Board for supply of electricity for running the industrial undertaking can be said to have been derived from its business. It was in this context held that such income cannot be said to have been derived from the industrial undertaking and would, therefore, not be eligible for deduction under section 80HHC of the Act.

28. In case of **Liberty India v. Commissioner of Income-tax reported in (2009) 317 ITR 218(SC)**, the question examined by the Supreme Court was whether duty draw back receipts and duty exemption pass book benefits form part of the net profit of eligible industrial undertaking for the purpose of deduction under section 80I, 80IA or 80IB of the Act. In this context, it was held that the words derived from has narrower connotation as compared to the words attributable to by using the expression derived from. Parliament intended to cover sources not beyond the first degree.

29. In case of **Commissioner of Income-tax v. Sterling Foods reported in (1999) 237 ITR 579**, the Court held that the facts were that the assessee was engaged in the processing of prawns and sea food and exporting it. In the process the assessee earned import entitlements granted by the Government of India under Export Promotion Scheme. The assessee could use such import entitlements itself or sell the same to others. The assessee sold such entitlements and earned income and included such income for relief under section 80HHC of the Act. The Court held that such income cannot be said to have been derived from assessees industrial undertaking. In the present case, however, we find that the source of the income of the assessee was the export. On the basis of accrual, income was already reflected in the assessees account on the date of the export on the prevailing rate of exchange. Further income was earned merely on account of foreign exchange fluctuation. Such income, therefore, was directly related to the assessees export business and cannot be said to have been removed beyond the first degree.

30. In case of **Commissioner of Income-tax v. Shah Originals reported in (2010) 327 ITR 19(Bom)**, the Bombay High Court considered a case where the assessee, an exporter, was given an option to keep a specified percentage of the receipts on account of the export in its Exchange Earners Foreign Currency (EEFC) Account. The assessee realised the full amount on account of the export but kept the portion thereof in EEFC Account. The assessee received higher amount in Indian rupees on such amount so set apart due to the fluctuation in the foreign exchange rate. Conscious of the fact that the assessee had received the entire proceeds of the

export transaction and thereafter, gained due to the foreign fluctuation on the account kept by the assessee in the EEFC Account, the Court held that such gain cannot be said to have been derived from the assessees export business. Thus the significant and distinguishing feature of this case is that the assessee had received the entire proceeds of the export sale. The foreign exchange fluctuation gain arose subsequent to the assessee receiving the sale consideration. It was in this background, the Court held and observed as under:-

11. The assessee admittedly in the present case received the entire proceeds of the export transaction. The Reserve Bank of India, has granted of facility to certain categories of exporters to maintain a certain proportion of the export proceeds in an EEFC account. The proceeds of the account are to be utilised for bona fide payments by the account holder subject to the limits and the conditions prescribed. An assessee who is an exporter is not under an obligation of law to maintain the export proceeds in the EEFC account but, this is a facility which is made available by the Reserve Bank. The transaction of export is complete in all respects upon the repatriation of the proceeds. It lies within the discretion of the exporter as to whether the export proceeds should be received in a rupee equivalent in entirety or whether a portion should be maintained in convertible foreign exchange in the EEFC account. The exchange fluctuation that arises, it must be emphasized, is after the export transaction is complete and payment has been received by the exporter. Upon the completion of the export transaction, what the seller does with the proceeds, upon repatriation,is a matter of his option. The exchange fluctuation in the EEFC account arises after the completion of the export activity and does not bear a proximate and direct nexus with the export transaction so as to fall within the expression derived by the assessee in sub-section (1) of section 80HHC. Both the Assessing Officer and the Commissioner of Income-tax (Appeals) have made a distinction, which merits emphasis. The exchange fluctuation, as both those authorities noted, arose subsequent to the transaction of export. In other words, the exchange fluctuation was not on account of a delayed realisation of export proceeds. The deposit of the receipts in the EEFC account and the exchange fluctuation which has arisen therefrom cannot be regarded as being part of the profits derived by the assessee from the export of goods or merchandise.

31. In the case of **Universal Radiators v. Commissioner of Income-tax reported in (1993)201 ITR 800**, the assessee was engaged in the business of manufacturing radiators. For such purpose the assessee would import ingots. In transit the goods were seized by Pakistan authorities. The Insurance company settled the claim. On account of devaluation of Indian rupee, the assessee received in Indian currency amount higher than that computed on the date of settlement of claim. The assessee claimed that the difference was not taxable. In this background, the Court held that the assessee was not engaged in the business of buying and selling of ingots and, therefore, compensation paid by the insurer to the assessee was not for any trading or business activity, but a just equivalent in money of the goods lost, nevertheless

such receipt was taxable.

32. Under the circumstances, we find no error in the judgments of the Tribunal.

33. Learned counsel Mr. Nitin Mehta for the Revenue, however, contended that the foreign exchange fluctuation gain may arise under various circumstances, not all of them may be covered under section 80HHC of the Act. Primarily, we do not see any distinction possible on the basis of different situations under which foreign exchange fluctuation may result. We are conscious that law permits hedging of foreign exchange fluctuation risk to an importer or an exporter. The exporter may, therefore, take steps as found commercially prudent to safeguard himself against drastic foreign exchange rate fluctuations and in the process may also limit the possibility of gain in case of favourable currency rate trends. Nevertheless, the resultant gain in foreign exchange rate would still be due to the export made by the assessee. In any case, no such facts are recorded by the Assessing Officer in any of these cases. We would, therefore, not entertain such speculative contention.

34. In the result, the question is answered in favour of the assessees and against the Revenue. All Tax Appeals are dismissed."

12.1 In view of above observations, this issue is answered in favour of the assessee and against the department.

13. So far as the issue with regard to Duty Drawback is concerned, the same will be now governed by the decision of the Apex Court in the case of **Liberty India v. Commissioner of Income Tax reported in 317 ITR 218**, wherein it is observed as under:-

"15. Continuing our analysis of Sections 80-IA/80-IB it may be mentioned that sub-section (13) of Section 80-IB provides for applicability of the provisions of sub-section (5) and sub-sections (7) to (12) of Section 80-IA, so far as may be, applicable to the eligible business under Section 80-IB. Therefore, at the outset, we stated that one needs to read Sections 80-I, 80-IA and 80-IB as having a common Scheme. On perusal of sub-section (5) of Section 80-IA, it is noticed that it provides for manner of computation of profits of an eligible business. Accordingly; 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 eligible business has got to be rejected in view of the overriding provisions of subsection (5) of Section 80-IA, which are also required to be read into Section 80-IB. [See Section 80-IB(13)]. We may reiterate that Sections 80-I, 80-IA and 80-IB have a common scheme and if so read it is clear that the said sections provide for incentives in the form of deductions which are linked to profits and not to investment. On analysis of Sections 80-IA and 80-IB 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 dates. 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".

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 neutralise 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 of 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/Schemes 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.

19. Since reliance was placed on behalf of the assessees on AS-2 we need to analyse the said Standard. 20.

20. AS-2 deals with Valuation of Inventories. Inventories are assets held for sale in the course of business; in the production for such sale or in form of materials or supplies to be consumed in the production.

21. "Inventory" should be valued at the lower of cost and net realizable value (NRV). The cost of "inventory" should comprise all costs of purchase, costs of conversion and other costs including costs incurred in bringing the "inventory" to their present location and condition.

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 and 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 and 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. .....

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 80-I/80-IA/80-IB of the 1961 Act.

25. The appeals are, accordingly, dismissed with no order as to costs."

13.1 In view of above observations, this issue is answered in favour of the assessee and against the department.

14. In **ADCI Dye Chem P. Ltd. v. Deputy Commissioner of Income-Tax reported in (2015) 370 ITR 408 (Guj)**, it is observed as under:-

"7.0. Heard the learned advocates for the respective parties at length. The question which is posed for consideration of this Court is whether the learned Tribunal was right in law in confirming that appellant was not entitled to deduction under Section 80IA of the Income Tax Act, 1961 in respect of Central Excise Duty set off and sales

tax set off ? At the outset, it is required to be noted that the aforesaid issue is squarely covered against the assessee in view of the decision of the Hon''ble Supreme Court in the case of **Liberty India v. CIT reported in 317 IT 218(SC)** as well as in the case of Sterling Foods (supra). It is required to be noted that with respect to export incentive under the scheme of DEPB, it is held by the Hon''ble Supreme Court in the case of Liberty India (supra) that in respect of DEPB and duty drawback the assessee is not entitled to deduction under Section 80IB of the Act. In the facts and circumstances of the case and so observed by the learned Tribunal, the assessee must claim the Central Excise Duty set off to be in the nature of duty drawback linked with export profit while claiming deduction under Section 80HHC of the Act. Therefore, it is rightly observed by the Tribunal that for claiming deduction under Section 80HHC, the assessee itself claimed that Central Excise Duty set off is export incentive by way of duty drawback, the assessee cannot take different stand while claiming deduction under Section 80IA of the Act. Under the circumstances and if that be so applying the decisions of the Hon''ble Supreme Court in the case of Liberty India(supra) and Sterling Food (supra) and the stand taken by the assessee while claiming deduction under Section 80HHC under the Act, the learned Tribunal has rightly held that the assessee shall not be entitled to deduction under Section 80IA of the Act on the Central Excise Duty set off as well as Sales Tax set off. Under the circumstances, question of law raised in the present Tax Appeals in the aforesaid facts and circumstances of the case is held against the assessee and in favour of the revenue. Consequently, all the appeals deserve to be dismissed and are accordingly dismissed."

14.1 Accordingly, this issue is answered in favour of the department and against the assessee.

15. So far as issue with regard to deleting the disallowance of Rs.97,23,550/- made in respect of amount paid to farmers on account of damage/penalty is concerned, we may refer to **Swadeshi Cotton Mills Co. Ltd. v. Commissioner of Income Tax reported in (1998) 233 ITR 199 (SC)**, wherein it is observed as under:-

"3. **In M/s. Prakash Cotton Mills Pvt. Ltd. (1973 AIR SCW 2412)** (supra) this Court has considered the question whether the interest paid for delayed payment of sales tax under the Bombay Sales Tax Act, 1959 and damages paid for delayed payment of contribution under the Employees'' State Insurances Act were permissible deduction under Section 37(1) of the Income-tax Act, 1961 (hereinafter referred to as ''the Act''). This Court has held that whenever any statutory impost paid by an assessee by way of damages or penalty or interest, is claimed as an allowable expenditure under Section 37(1) of the Act, the assessing authority is required to examine the scheme of the provisions of the relevant statute providing for payment of such impost notwithstanding the nomenclature of the impost as given by the statute, to find whether it is compensatory or penal, in nature. The authority has to allow deduction under Section 37(1) of the Act, wherever such examination reveals

the concerned impost to be purely, compensatory in nature. Wherever such impost is found to be of a composite nature, i.e., partly of compensatory nature and partly of penal nature, the authorities are obligated to bifurcate the two components of the impost and give deduction to that component which is (sic) penal in nature. In that case this Court has approved the judgment of the Andhra Pradesh High Court in **Commr. of Income Tax v. Hyderabad Allwyn Metal Works Ltd., 172 ITR 113 : (1988 Tax LR 1486)** where the Court was dealing with the deduction of the amount paid by way of damages under Section 14(B) of the Employees'' Provident Funds and Miscellaneous Provisions Act, 1952. It was held that the said amount comprises both the element of penal levy as well as compensatory payment and that it will be for the authority under the Act to decide with reference to the provisions of the Employees'' Provident Funds Act, 1952 and the reasons given in the order quantifying the damages to determine what proportion should be treated as penal and what proportion as compensatory and that the entire sum can neither be considered as mere penalty nor as mere interest."

16. So far as issue with regard to disallowance being depreciation on new project is concerned, it has been the consistent view of the Tribunal to allow the claim of the assessee and, we do not find any infirmity in such decision. Therefore, this issue is answered in favour of the assessee and against the department.

17. In view of above observations, all these appeals are disposed of.