Hindustan Lever Ltd. Vs Commissioner of Income Tax

Civil Appeals Nos. 1911-11-A Of 1981 With Nos. 1912, 1913-13-A Of 1981 And 738 Of 1982

Court: Supreme Court of India

Date of Decision: Sept. 2, 1997

Acts Referred:
Finance (No. 2) Act, 1962 â€" Section 2(5)#Income-tax Act, 1961 â€" Section 28, 43C

Citation: (1999) 156 CTR 506 : (1999) 239 ITR 297 : (1998) 9 SCC 540 : (2000) 108 TAXMAN 181

Hon'ble Judges: S. Saghir Ahmad, J; S. C. Sen, J

Bench: Division Bench

Final Decision: Dismissed

Judgement

1. The assessment years involved in these matters are 1962-63 and 1963-64. The assessee is a manufacturing company. In the relevant years of

account, it made large profits. The assessee had also exported groundnut oil which resulted in an apparent loss of Rs. 3,44 lakhs. However, for the

exports made at a loss, the assessee was rewarded with import entitlements. It utilised the import entitlements in purchasing palm oil from foreign

countries. The imported palm oil was consumed internally by the assesses for manufacturing other products. The particulars of the products

manufactured by the assessee utilising palm oil have not been given in the order of the Tribunal. The contention of the assessee is that the oil which

was purchased by the assessee from foreign countries on the strength of the import entitlement was at a rate much lower than the rate obtaining in

the Indian market for similar products. Since the assessee paid a lower price for the imported palm oil the assessee made a larger profit than what

it would have made had it purchased palm oil locally at a higher rate. The assessee, therefore, would be entitled to benefit of Section 2(5)(i) of the

Finance (No. 2) Act, 1962, in respect of the amount of profit it made in excess of what it would have otherwise made if it had to buy palm oil

locally.

2. (5)(i) An assessee being an Indian company or any other company which has made the prescribed arrangements for the declaration and

payment of dividends within India or an assessee other than a company, whose total income includes any profits and gains derived from the export

of any goods or merchandise out of India, shall be entitled to a deduction, from the amount of income tax and super-tax with which he is

chargeable for the assessment year commencing on the 1st day of April, 1962, of an amount equal to the income tax and super tax calculated

respectively at one-tenth of the average rate of income tax and of the average rate of super tax on the amount of such profits and gains included in

the total income.

2. The entire profit derived from the sale of goods made by the assessee arises out of sale of goods in India. No part of the assessee''s income has

been derived from any export of its products. Section 2(5)(i) of the Finance (No. 2) Act is attracted only when the assessee''s total income

includes any profits or gains derived from export of any goods or merchandise out of India. The assessee has simply consumed some imported

palm oil in manufacturing the products which were ultimately sold in the local market. On behalf of the assessee, it has been pointed out that had

the assessee sold the import entitlement its income would have been profit from export. That may or may not be the position in law. We do not

have to decide this point in the instant case. Here, the assessee has not sold anything which he has imported. He has imported palm oil which he

has utilised in manufacturing other products. It may be that at a particular point of time, palm oil was selling in a foreign country at a rate much

lower than the rate obtaining in the local market. But purchasing something at a rate cheaper than the local market rate does not result in any profit.

Profit arises from sale of goods. The question in this case is whether the assessee''s total income includes ""any profits and gains derived from

export of any goods or merchandise out of India"". The total income has to be computed in accordance with the provisions of the income tax Act.

The 1 assessee''s business income has to be computed in accordance with the pro visions of Section 28 to Section 43C of the income tax Act. It

cannot be said that the total income of the assessee as computed by the income tax Officer comprised any item which was profits and gains

derived from export. The assessee''s contention is that profits and gains made by sale of goods by the assessee were manufactured out of some

imported raw material. It is incomprehensible how by mere utilisation of imported goods the assessee can be said to have derived profits and gains

from the export of any goods or merchandise out of India.

3. The assessee in this case wants not to go to the genesis of the import of palm oil. The contention is that unless the assessee exported goods, it

would not have obtained the import entitlements. The import entitlements were used to import palm oil. If cheap palm oil was not used, the

assessee could not have made the quantum of profit that it did. There is an element of absurdity in this argument. If it is taken to its logical

conclusion it may be said that the goods which were originally exported by the assessee were manufactured in India. Therefore, profits made on

export or even the import entitlements were derived from the manufacturing activity in India. This argument has to be rejected straightaway.

4. On behalf of the assessee strong reliance has been placed on Section 28(iiia), (iiib) and (iiic) of the income tax Act. We fail to see how any of

these three clauses comes to the aid of the assessee in any manner. Clause (iiia) speaks of profits on sale of a licence granted under the Imports

(Control) Order ; Clause (iiib) speaks of cash assistance received or receivable by any person against exports ; and Clause (iiic) speaks of duty of

customs which is not the case here. This argument can be described in the language of Lord Greene, M. R., in the case of Henriksen v. Grafton

Hotel Ltd. [1942] 24 TC 453 (CA) at page 460 as an attempt to rescue the case from shipwreck. Unfortunately, as in that case before Lord

Greene M. R., the attempt has been futile.

5. We were referred to a large number of cases. We shall refer to some of them.

6. In the case of CIT v. Wheel and Rim Company of India Limited , the Madras High Court had to deal with the case of an assessee exporting

goods abroad. The assessee obtained cash subsidy from the Engineering Export Promotion Council. It also obtained import entitlement licences

which were sold by it. The Madras High Court held that these profits and gains arose out of the export sales and specially in view of the rules

framed under the Act, the assessee was entitled to get relief.

7. The Madras view was dissented from by the Kerala High Court in the case of Cochin Company v. CIT . That was again a case of sale of

import entitlements. The Kerala High Court was of the view that sale of import entitlements was not the same thing as export of goods. The Kerala

High Court was of the view that the price received from sale of import entitlements could riot be regarded as profits and gains derived from the

export of goods.

8. None of these two cases really is of any relevance in this case. The case before us is not a case of sale of import entitlement but a case of

utilisation of import entitlement. Because of the exports made by the assessee, the assessee was rewarded with the import entitlements. The

assessee utilised all the import entitlements for import of palm oil which was consumed by the assessee in manufacturing of its own products. The

products were sold for profit. The profit in this case arose out of sale of goods. That is the proximate cause of making of the profit.

9. At this juncture, we can refer to the decision of the Privy Council in the case of CIT v. Raja Bahadur Kamakhaya Narayan Singh [1948] 16

ITR 325> In that case it was pointed out that the word ""derived"" is not a term of art. Its use in the definition demanded an inquiry into the

genealogy of the product. But the Privy Council cautioned that the inquiry should stop as soon as the effective source is discovered. The question

in that case was whether interest in respect of arrears of rent payable for land which was used for agricultural purposes would also be agricultural.

The claim on behalf of the assessee was that since the rent was payable for agricultural land, the interest on delayed payment of such rent was also

of agricultural character and was not taxable. It was explained by the Privy Council at page 328 :

Those who put it in this way say that such interest, when received, has its origin in the tenancy, because, if there had been no tenancy, there would

have been no arrears of rent, and if there had been no arrears of rent, there would have been no statutory interest. Following this sequence of

causes, they say that it is obvious that interest in circumstances such as these must be classified as ''revenue derived from land.

The interest clearly is not rent. Rent is a technical conception, its leading characteristic being that it is a payment in money or in kind by one person

to another in respect of the grant of a right to use land. Interest payable by statute on rent in arrears is not such a payment. It is not part of the rent,

nor is it an accretion to it, though it is received in respect of it.

Equally clearly the interest on rent is revenue, but in their Lordships'' opinion it is not revenue derived from land. It is no doubt true that without the

obligation to pay rent-and rent is obviously derived from land-there could be no arrears of rent and without arrears of rent there would be no

interest. But the affirmative proposition that interest is derived from land does not emerge from this series of facts. All that emerges is that as

regards the interest, land rent and non-payment of rent stand together as cause sine quibus non. The source from which the interest is derived has

not thereby been ascertained.

The word ''derived'' is not a term of art. Its use in the definition indeed demands an enquiry into the genealogy of the product. But the enquiry

should stop as soon as the effective source is discovered. In the genealogical tree of the interest land indeed appears in the second degree, but the

immediate and effective source is rent, which has suffered the accident of non-payment.

10. In the instant case, the immediate source of the profit is sale of goods. The export of other goods is not even the second degree but it has to be

traced to an even more remote degree. The import was of palm oil. The import was possible because of earlier export of goods at a loss. In the

chain of sequence the earlier export would be four degrees away.

11. The decision of the Privy Council in the case of Kamakhaya Naraydn Singh [1948] 16 ITR 325 was cited with approval in the case of Bacha

F. Guzdar (Mrs.) v. CIT) . It was held in that case by this court, after referring to Kamakhaya Narayan Singh"s case [1948] 16 ITR 325 that

where a company deriving income from agriculture declared dividend, the dividend did not arise from any agricultural source and could not be

claimed to be income derived from agricultural activity.

12. There is no necessity for multiplying authorities.

13. We are of the view that the High Court was clearly right in holding that the assessee"s profit from sale of its goods in India cannot be said to

have been derived from export sales. The appeals are, therefore, dismissed. These are four sets of appeals. The assessee in each set must pay Rs.

5,000 as costs.