(2014) 12 CAL CK 0023

CALCUTTA HIGH COURT

Case No: G.A. No. 1420 of 2014, I.T.A.T. No. 41 of 2014, G.A. No. 1735 of 2014 and I.T.A.T. No. 59 of 2014

Reckitt Benckiser (India) Ltd.		APPELLANT
	Vs	
The Addl. Commissioner of Income Tax		RESPONDENT

Date of Decision: Dec. 23, 2014

Acts Referred:

- Income Tax Act, 1961 - Section 10B, 260A, 80HH, 80-I, 80-IA

Citation: (2015) 1 CALLT 577 : (2015) 231 TAXMAN 585

Hon'ble Judges: Soumitra Pal, J; Arindam Sinha, J.

Bench: Division Bench

Advocate: Nageswar Rao, Advocate and Avra Majumder, for the Appellant; Nizamuddin, for the Respondent

Judgement

1. These two appeals being ITAT No. 41 of 2014 and ITAT No. 59 of 2014 under section 260A of the Income Tax Act, 1961 have been preferred by the assessee and the revenue respectively against order dated 30th December, 2013 passed by the Income Tax Appellate Tribunal ''A'' Bench, Kolkata in ITA No. 701/Kolkata/2011 relating to the assessment year 2007-08. The assessee sought formulation of questions mentioned in paragraph-8 of its stay application, while the revenue wanted formulation of questions as mentioned in paragraph-4 of its stay application.

2. We have heard Mr. Nageswar Rao, learned Advocate on behalf of the assessee as well as Md. Nizamuddin, learned Advocate on behalf of the revenue. By consent of the parties, we admit the appeals on the following questions framed.

3. In the assessee''s appeal, the question for adjudication is as follows:

"Whether on the facts and circumstances of the case and in law, the Tribunal erred in holding that the "interest income" earned by the Appellant/Petitioner cannot be said to be "derived by" the eligible undertaking/units as required for claiming deduction under sub-section (2) of section 80IC of the Act, 1961?

4. In the revenue''s appeal, the question for adjudication is as follows:

"Whether on the facts and circumstances of the case, the Tribunal has erred in allowing deduction of Rs. 87.05 lakhs on account of scraps sale T&M Fee under section 80IC of the I.T. Act, by disregarding the intention of the Parliament in using the expression "derived by" which has narrower connotation in comparison to the phrase "Attributable To" used in the other provision of the Income Tax Act?"

5. The appeals are taken up for hearing and we have heard the submissions made on behalf of the respective parties.

6. With regard to the questions formulated, the issue is interpretation of the word "derived" as used in Section 80IC of the Income Tax Act, 1961.

7. On the question regarding interest income Mr. Rao relied on several decisions, on two of which he laid emphasis. He submitted that this was a question of law which required answer by this Court while it had been decided by two Division Benches respectively of Gauhati High Court and Karnataka High Court. The Gauhati High Court delivered its decision in the case of CIT v. Megkalaya Steels Ltd.:356 ITR 232 and the Karnataka High Court in CIT & Anr. v. Motorola India Electronics (P) Ltd.: 46 Tasmann.Com 167.

8. In Megkalaya Steels case, the Court, inter alia, held as follows:

"Shorn off rhetorical legal arguments, compassionate pleas and emotionally surcharged submissions, what surfaces from beneath the mass of materials placed before this court, by way of pleadings and otherwise, is that there is no dispute, in this set of appeals, that, in order to claim deduction either under section 80-IB or under section 80IC, an assessee has to establish that there is a direct, intrinsic and first degree nexus between a subsidy, on the one hand, and the profits and gains, on the other hand, derived from or derived by, the industrial undertaking concerned. There is also no dispute that if any of the subsidies, in question, goes on to reduce the cost of production of an industrial undertaking, the resultant profits and gains are deductible under the provisions of section 80-IB or 80-IC, as the case may be. Surfacing from beneath this statutory requirement, the legal proposition is that if the subsidy is non-operational in nature, there will be no entitlement of deduction; but the subsidy, if operational, would entitle an assessee to claim deduction."

....

....

"The facts are, therefore, not in dispute on this aspect. The dispute is: Whether the interest subsidy is payable on non-operational or operational subsidy? If the object of the relevant scheme is borne in mind, it clearly shows that interest subsidy, having aimed at reducing the interest payable on working capital by an industrial undertaking, helps directly in reducing the cost of manufacturing or production activities and establish thereby direct and first degree nexus between the industrial activities of the assessee-respondents, on the one hand, and the interest subsidy, on the other, received by the assessee-respondents and, in consequence thereof, since interest subsidy results into profits and gains derived from, or derived by, an industrial undertaking, there is no reason as to why such profits and gains, earned by an industrial undertaking on the strength of such a subsidy, namely, interest subsidy, be not allowed to be deducted from the taxable income of the industrial undertaking concerned"".

9. Mr. Rao, however, submitted a Special Leave Petition preferred against this decision before the Supreme Court had been admitted along with connected matter, to be registered as C.C. No. 20502-2013.

10. The Karnataka High Court in Motorola''s case, inter alia, held in paragraph-8 therein as under:

"In the instant case, the assessee is a 100% EOU, which has exported software and earned the income. A portion of that income is included in EEFC account. Yet another position of the amount is invested within the country by way of fixed deposits, another portion of the amount is invested by way of loan to the sister concern which is deriving interest or the consideration received from sale of the import entitlement, which is permissible in law. Now, the question is whether the interest received and the consideration received by sale of import entitlement is to be construed as income of the business of the undertaking. There is a direct nexus between this income and the income of the business of the undertaking. Though it does not par take the character of a profit and gains from the sale of an article, it is the income which is derived from the consideration realised by export of articles. In view of the definition of Income from Profits and Gains'' incorporated in sub-section (4), the assessee is entitled to the benefit of exemption of the said amount as contemplated under section 10B of the Act. Therefore, the Tribunal was justified in extending the benefit to the aforesaid amounts also. We do not find any merit in these appeals".

11. Mr. Rao went on to submit the answers to the question given by the Gauhati High Court and Karnataka High Court were correct and, in particular, the Gauhati High Court had considered the law declared in several decisions made by the Supreme Court. He further urged the decision in Liberty India Vs. Commissioner of Income Tax, , considered by the Gauhati High Court, was focussed on the analysis of section 80-IB and the basic scheme of sections 80-I, 80-IA and 80-IB. That decision, according to him, could not be relied on for an interpretation of the provisions in

section 80IC of the said Act. He went on to submit section 80-IB(1) and (2) was with regard to the eligibility, while 80-IB(3) was with regard to the quantification. He pointed out that even in the quantification provision under section 80-IB(3) the word "derived" had been used. Therefore, in quantification under the said section, the effect of eligibility was narrow. On the other hand, according to him, section 80IC(1) and (2) was with regard to the eligibility which, on the contrary, made the effect thereof narrow, while the quantification provision being section 80IC(3) did not use the word "derived" making its application in terms of eligibility in relation to quantification, wider. He submitted the absence of use of the word "derived" in section 80IC(3) was a conscious omission by the legislature. As such, once the assessee was found to be an eligible undertaking under the provisions of section 80IC, interest income earned from profit generated by such undertaking was deductible. He also submitted use of the word "business", in the said section would support such interpretation.

12. Mr. Nizamuddin, learned Advocate for the Revenue, on the other hand, submitted the interpretation of the word "derived" had been repeatedly made by the Supreme Court as followed by several High Courts. He relied on Pandian Chemicals Ltd. Vs. Commissioner of Income Tax, , CIT-IV. Globe Organics Ltd. Laws (APHJ-2014-12-I (ITA No. 254 of 2003, decided on 2nd December, 2014), Pine Packaging (P) Ltd. Vs. Commissioner of Income Tax, and Fenner (India) Ltd. Vs. Commissioner of Income Tax (No. 2), .

13. In Pandian Chemicals Ltd. the Hon''ble Supreme Court while interpreting the word ''derived'', had held, inter alia, as under:

5. The High Court rejected the submission of the appellant by relying upon the decision of this Court in Cambay Electric Supply Industrial Co. Ltd. Vs. The Commissioner of Income Tax, Gujarat-II, Ahmedabad, , where this Court had clearly stated that the expression "derived from"'' had a narrower connotation than the expression ''attributable to'':

"...In this connection, it may be pointed out that whenever the Legislature wanted to give a restricted meaning in the manner suggested by the learned Solicitor-General, it has used the expression ''derived from'', as, for instance, in section 80J. In our view, since the expression of wider import, namely ''attributable to'', has been used, the Legislature intended to cover receipts from sources other than the actual conduct of the business of generation and distribution of electricity."

6. "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, hut the immediate and effective source is rent, which has suffered the accident of non-payment. And rent is not land within the meaning of the definition."

14. This definition was approved and reiterated in 1955 by a Constitution Bench of this Court in the decision of Bacha F. Guzdar Vs. Commissioner of Income Tax, Bombay, . It is clear, therefore, that the word ''derived from'' in section 80HH of the Income-tax Act, 1961 must be understood as something which has direct or immediate nexus with the appellant''s industrial undertaking. Although electricity may be required for the purposes of the industrial undertaking, the deposit required for its supply is a step removed from the business of the industrial undertaking. The derivation of profits on the deposit made with Electricity Board cannot be said to flow directly from the industrial undertaking itself."

15. The interpretation of the word ''derived'' as made by the High Courts are as under:

"In Globe Organics Limited the High Court of Andhra Pradesh held:

"The interest paid on intercorporate deposits can by no means is said to be an activity of the industry so established. When the making of intercorporate deposits itself is not part of the manufacturing activity, the question of the income derived therefrom being treated as qualified for deduction under section 80HH of the Act, does not arise. In I.T.T.A. No. 216 of 2003, this Court dealt with the matter and the same factual situation obtains in this case also."

16. In Pine Packaging Private Limited the High Court of Delhi held:

"It is not disputed that for income to qualify for deduction under the said section, the profit/income earned should be derived from business of manufacture or production of article or thing, which is eligible for deduction.

The expression "derived from" in taxation laws means something which has direct or immediate nexus with the specified activity, which in the present case means manufacture or production of article or thing. Manufacture or production of article or thing should be the direct and proximate cause of the said receipt and not the indirect causation and reason for the said income. Mere second/third connection is not sufficient; the manufacture/production should be the causa causaus. The expression "derived from" is a narrower expression than the words "attributable to" which includes direct as well as indirect receipts which may not have immediate or direct nexus with the specified activity. In the present case, in view of words "derived from", we have to look at the immediate source which has generated or resulted in the said receipt/income. The immediate source will be the first degree source and not the second or the third degree source, which is a step removed from the specified activity (see Pandian Chemicals Ltd. Vs. Commissioner of Income Tax, and Liberty India Vs. Commissioner of Income Tax, "

17. In Fenner (India) Ltd. the High Court of Madras, held, inter alia, -

"14. The other part of the question is relatable to the interest earned by the industrial undertaking. This sort of a question arose for consideration in the case of

Commissioner of Income Tax Vs. Pandian Chemicals Ltd., . The question relatable to the interest raised therein figured as question No. 3 and it runs as under:

"Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the interest on deposit with the Tamil Nadu Electricity Board should be treated as income derived from an industrial undertaking for the purpose of relief under s. 80HH?

15. The question so raised had been discussed in paras. 7 to 15 therein by a Division Bench of this Court, which ultimately held that the Tribunal has committed an error of law holding that the interest earned on the deposit with the Tamil Nadu Electricity Board by the assessee should be treated as income derived from industrial undertaking for the purpose of relief under s. 80HH of IT Act.

16. This decision, being that of a Division Bench of this Court, is binding on us and in this view of the matter, there is no other go for us, except to conclude that the interest earned by the industrial undertaking cannot at all be eligible to be included in the gross total income for claiming deduction of an amount equal to twenty per cent in the process of computation of the profits and gains of the said industrial undertaking and this part of the question is, therefore, answered against the assessee."

18. Keeping these interpretations of the word ''derived'' in mind, let us now scan section 80IC in the context of this case. We find the said section postulates gross total income of an assessee shall include any profits and gains derived by an undertaking from any business referred to in sub-section(2)to be entitled to a deduction from such profits and gains as specified in sub-section (3). Sub-section(2) applies to any undertaking which has begun or begins to manufacture or produce any article or thing.

19. To our mind the facts of this case where the assessee has earned income from fixed deposits which deposits were profits and gains of the undertaking, the income obtained as interest on such profits and gains cannot be said to be derived from the business of manufacture or production of any article or thing by the assessee''s undertaking.

20. In consideration of the facts and circumstances of this case, applying the provision in question and the interpretation of the word ''derived'' given in the several decisions discussed above, we answer the question raised in the assessee''s appeal in the negative, in favour of the revenue and against the assessee.

21. On the question raised by the revenue in its appeal, we find a decision thereon by the High Court of Madras in Fenner (India) Ltd. (supra) relied on by the revenue in urging its case regarding the question formulated in the assessee''s appeal. In paragraph 13 of the said decision the High Court of Madras held as follows:--

"13. As already stated, in the industrial undertaking in the manufacture of V-Belts, oil seals, O-Rings and rubber moulded products, certain scrap materials resulted in, which has a saleable value. To say that the scrap materials has no direct link or nexus with the industrial undertaking cannot be at all be expected or commend acceptance, especially, on the facts and in the circumstances of the case. For the sake of emphasis, we may say that the scrap materials come within the manufacturing process of the industrial undertaking in the manufacture of certain products such as V-Belts, oil seals, O-Rings and certain rubber moulded products, etc. In this view of the matter, we are of the view that profits and gains from the sale of scrap materials is eligible to deduction in an amount equal to twenty per cent under S. 80HH, inasmuch as such gains or profits are derived from the industrial undertaking and includible in the gross total income of the assessee and the question relatable to the profit on the sale of scrap is thus answered in favour of the assessee."

22. We are persuaded by the reasoning of the said Court and answer the question accordingly. The question in the revenue''s appeal is answered in the negative, in favour of the assessee and against the revenue. Accordingly, both the applications being GA No. 1420 of 2014 and GA No. 1735 of 2014 are disposed of and the appeals being ITAT No. 41 of 2014 and ITAT No. 59 of 2014 are dismissed.

Urgent certified photocopy of this order, if applied for, be supplied to the parties upon compliance with all requisite formalities.