
(2011) 10 KAR CK 0034

In the Karnataka High Court

Case No : ITA No. 489 of 2010 C/W 1359 of 2006 and 732 of 2007

Anil Kumar

APPELLANT

Vs

Income Tax Officer

RESPONDENT

Date of Decision : 21-10-2011

Acts Referred:

Customs Act, 1962 — Section 2 (18), 50, 50 (1), 50 (2)

Income Tax Act, 1961 — Section 256 (1), 256 (2), 35 B, 80 HHC, 80 HHC (1)

Citation : (2012) 204 TAXMAN 162

Hon'ble Judges : Ravi Malimath, J;N. Kumar, J

Bench : Division Bench

Advocate : A. Shankar and M. Lava, for the Appellant; M. Thirumalesh, for the Respondent

Final Decision : Allowed

Judgement

N. Kumar, J.—These appeals are preferred by the assessee challenging the order passed by the Tribunal which has held, to be eligible for the benefit u/s 80HHC of the Income Tax Act, 1961, the foreign exchange is to be earned by exporting goods from India, otherwise, the assessee is not entitled to the benefit. As common questions of law is involved in all these appeals, they are taken up together and disposed of by this common order. The assessee is the proprietor of M/s Maharaja Metal Industries Ltd. Bangalore engaged in purchase and sale of non-ferrous metals, scraps, skimming ashes and drosses chemicals and other commodities. The purchases are made from one country and exported to another country at a margin of profit by arranging direct shipment from the purchasing country to the selling country. The bills are settled through Bank of Baroda in India. The proceeds are received through convertible foreign currency and payments are also made in convertible foreign currency. The assessee is also maintaining the Exchange Earners Foreign Currency Account (EEFC) account. The assessee claims that the entire business is covered by Foreign Exchange Management, 1999. The bills are raised in the name of M/s. Maharaja Metal Industries, Bangalore, and the sale bills are raised by M/s Maharaja Metal

Industries.

2. For the assessment year 2001-02, the assessee on a total turn over of Rs. 2,74,02,676, he has shown net profit of Rs. 51,85,088, which the assessee claimed as deduction u/s 80HHC. While examining the books of account of the assessee, it was noticed that the assessee was engaged in purchasing the goods from one country and selling it to another country. He had claimed 100% deduction on export profit as against 80% allowable from the assessment year 2001-02. The assessee accepted the said mistake, filed a revised return and paid taxes on 20% of the income at Rs. 11,25,020. He also claims certain other benefits about which we are not concerned in these appeals.

3. The assessing authority found that there was no export of any goods or merchandise out of India since the assessee was engaged in purchase of goods from one country and selling to another country. The assessee imported the materials from foreign country like Kenya and made payments in foreign exchange. The suppliers raised their invoices and the materials were taken for delivery by the assessee in various ports as per the terms of the trade. As per the Sale of Goods Act, the ownership of the materials contained in the invoices pass on to the buyer on the materials reaching the destination, as per the terms of the agreement along with the invoice. The properties in the invoice pass on to the buyer on receipt of the materials at the designated port. The assessee sold the above materials to his customers at South Africa, Bahrain etc. He directed the materials to be delivered at different destinations as per the terms of the sale invoice raised by him. The assessee's ownership of the materials exported comes to an end on the goods being delivered at the port of the destination as agreed with the customers. The assessee being a resident Indian becomes the owner of the imported materials in India and the same is sold to foreign buyers, which become export in his hands. The assessee has received the entire sale consideration in foreign exchange in accordance with the Reserve Bank of India's Rules.

4. After referring to the various judgments relied on behalf of the assessee, his contention was rejected on the ground that the transaction in this case is not in conformity with section 80HHC of the Income Tax Act.

5. According to the assessing authority, the word export as per the Law Lexicon, page 684, refers to taking out of goods which had become part and parcel of the mass of the property of the local area, and will not apply to goods in transit that is brought into the area for purposes of being transported out of it. Relying on the judgment of the Apex Court in *The Central India Spinning and Weaving and Manufacturing Company, Limited, The Empress Mills, Nagpur Vs. The Municipal Committee, Wardha*, it was held, when the goods of the assessee have not reached the Indian territory, it cannot be classified as export out of India. Therefore, according to the assessing officer, the word export means of take out of the territories administered by any local government to sea or to any foreign territories administered by another local government. The decisions on which

reliance is placed by the assessee have totally ignored the expression in the section "export out of India of any goods or merchandise and the necessity of customs clearance". Therefore, he was of the view, as the assessee has not exported out of India any goods or merchandise, since the goods did not pass through the customs stationed in India and since the goods have not moved from Indian Territory, it cannot be said that there is export of goods or merchandise out of India. Section 2(18) of the Customs Act, 1962 defines "export" as taking out of India to a place out side India. Therefore, he was denied the benefit of exemption from payment of taxes on profits earned out of export. Aggrieved by the said order, the assessee preferred an appeal before the Commissioner of income tax (Appeals-II), Bangalore. The appellate authority held that the assessing officer has done a very thorough, comprehensive and good job by framing the assessment order in a very logical and speaking manner. He has very well brought out a case to establish that the meaning and requirement as meant for the term export out of India is distinct and different from any other definition for the term export, including those used for the purpose of RBI regulation or for purposes of Sales Tax Act, or any other Act. As far as section 80HHC of the income tax Act is concerned, the term export out of India makes it necessary that the goods exported requires customs clearance in India. There cannot be any other situation to give any other interpretation to this requirement and therefore he declined to interfere with the said order and dismissed the appeal. Aggrieved by the said order the assessee preferred an appeal to the Tribunal. The Tribunal held that the word export has not been defined under the Act. The assessing officer at page 5 of his order has mentioned that the export means to take out of the territory administered by any local government. The Tribunal was not prepared to act upon the Hindi terminology which goes against the aforesaid definition. Therefore, it held that if the Hindi version is given effect to, the purpose of the Act will be frustrated. The provisions of section 80HHC was enacted with a view to give some incentive to the customers for exporting goods from India so that the export business will increase and in turn, the foreign exchange reserves would increase. If the goods are not exported from India, the provisions of section 80HHC are not applicable. The assessee has purchased the goods from South Korea and sold it to South Africa. The goods were not brought to India for the purpose of export out of India. Therefore, the basic requirement that the export must be out of India was not satisfied and therefore, they declined to interfere with the orders passed by the lower authorities and dismissed the appeal. Aggrieved by the said order, the assessee have preferred these appeals.

6. The substantial questions of law that arises for consideration are as follows :

- (1) Whether in the facts and circumstances of the case, the Tribunal was justified in law in holding that the appellant is not entitled to benefit of deduction u/s 80HHC of the Act?
- (2) Whether the Tribunal was justified in law in holding that levy of interest u/s 234B is valid in law under the facts and circumstances of the appellant case?

7. Shri Shankar, learned counsel appearing for the assessee contended that the whole object of enacting the said section 80HHC is to earn precious foreign exchange for the country. As on the date, this provision was enacted, the country was actually in need of foreign exchange. Whether the goods are exported from India or from any country outside India to another country, the criteria is that the assessee should earn profit, and the said profit is to be brought into the country by way of foreign exchange. If the intention of the Parliament was that the goods or merchandise has to be exported from India instead of out of India, they would have used the words from India. The very object of using this expression export out of India is to avoid such a situation, because the object is to earn foreign exchange whether it is from a trade which involves export of goods from India or from one country outside India into another country. The interpretation placed by the authorities is contrary to the object with which the aforesaid provision was introduced and is also contrary to the express words used in the statute, and therefore he submits that the orders are to be set aside and the assessee is to be granted the benefit of deduction. In support of his contention, he has relied on several judgments of the High Court as well as the Supreme Court.

8. Per contra, learned counsel Shri Thirumalesh appearing for the revenue contended that the expression export out of India has a definite connotation in law. The word export which is used is a verb. The dictionary meaning of the word export makes it clear that the goods have to move from one country to another country. He also points out in this connection that the court has to bear in mind the meaning given to the export out of India in Explanation (aa) to section 80HHC. He also relied upon Explanation (ii) to sub-section (2) of section 80HHC, where stock transfers are deemed to be export out of India and submitted that the purpose of enacting this provision is not only to earn foreign exchange, but also to encourage local trade. Therefore, both the conditions have to be satisfied before an assessee is entitled to the said benefit and this is precisely what the authorities on proper understanding of the provisions have held and therefore, no case for interference is made out.

9. Therefore, the substantial question of law No. 1 could be referred as under :

To be eligible for the benefit of section 80HHC, is it necessary that the goods exported out of India, has to be necessary from the Indian Soil after crossing its customs barrier?

10. Section 80HHC(1) reads as under :

(1) where an assessee, being an Indian company or a person (other than a company) resident in India, is engaged in the business of export out of India of any goods or merchandise to which this section applies, 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 to the extent of profit referred to in sub-section (1B), derived by the assessee from the export of such

goods or merchandise:

Provided

(1A)"

(1B)"

(2)"

(3)"

(3A)"

(4)"

(4A)"

(4B)"

Explanation " For the purpose of this section

(a)"

(aa) "export out of India" shall not include any transaction by way of sale or otherwise, in a shop, emporium of any other establishment situate in India, not involving clearance at any custom station as defined in Customs Act, 1962 (52 of 1962)

(b)

(ba)"

(c)".

(d)".

Explanation (2) to sub-section (2) of section 80HHC reads as under :

For the removal of doubts, it is hereby declared that where any goods or merchandise are transferred by an assessee to a branch, office, warehouse or any other establishment of the assessee situate outside India and such goods or merchandise are sold from such branch, office, warehouse or establishment, then, such transfer shall be deemed to be export out of India of such goods and merchandise 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 section 50 of the Customs Act, 1962 (52 of 1962), shall for the purpose of this section, be deemed to be the sale proceeds thereof.

11. Chapter VIA of the Act deals with deductions to be made in computing the total income. Part-C deals with deductions in respect of certain incomes and one such deduction is provided u/s 80HHC. Therefore, it is clear that this Chapter-VIA contains beneficial provisions granting several deductions to an assessee which would be in the nature of an incentive. Section 80HHC is an incentive to an

assessee to carry on export business so that in turn, the country earns foreign exchange. Therefore, the entire profit out of the business is exempted from payment of tax for some years and subsequently, it is scaled down percentage-wise. Therefore, while interpreting this provision, if two views are possible, it is settled law that the view which is favorable to the assessee is to be preferred by the courts.

12. Now section 80HHC provides that an assessee who is engaged in the business of export out of India of any goods or merchandise, to which the said section applies in computing his total income, deduction to the extent of profits referred to in sub-section (1)(b) derived by the assessee from the export of such goods or merchandise is allowed. In the entire provision, there are no express words which provide that the export of such goods is to be from India. Two conditions which require to be satisfied before an assessee claims deduction under this provision are,

(1) the assessee must be engaged in the business of export out of India of any goods or merchandise

(2) sale proceeds of such goods or merchandise exported out of India are receivable by the assessee in convertible foreign exchange.

If these two conditions are fulfilled, the assessee is entitled to the benefit conferred u/s 80HHC.

13. In Explanation (2) to sub-section (2), when a deemed export in India takes place, is explained. Where any goods or merchandise are transferred by an assessee to a branch office, warehouse, or any other establishment of the assessee situated outside India, and such goods or the merchandise are sold from such branch office, warehouse or establishment, then such transfer shall be deemed to be export out of India of such goods and merchandise, 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 section 50 of the Customs Act shall be deemed to be the sale proceeds thereof. This explanation is an explanation to sub-section (2). In sub-section (2)(a), it is made clear that all goods or merchandise other than those specified in clause (b), which are exported out of India, the sale proceeds in convertible foreign exchange is to be received or brought into India within a period of six months from the end of the previous year or within such further period as the competent authority may allow in this behalf. Therefore, the law has prescribed a limit within which the sale proceeds in convertible foreign exchange is to be brought into this country. In the case of stock transfer from India to a place outside India where the assessee has a branch office, warehouse, or other establishment, if that date is taken into consideration as the starting point for six months time to bring back the foreign currency, it would cause injustice to the assessee. Therefore, Explanation (2) makes it clear that only when the assessee sells such goods or merchandise from such branch office, warehouse or establishment, such transfer shall be deemed to be export out of

India and six months period is to be computed from the date of such sale from a territory to an ultimate purchaser.

14. Explanation (aa) makes it clear that in what circumstances it will not be an export out of India. Any transaction by way of sale or otherwise in a shop, emporium or any other establishment situated in India not involving clearance at Customs station though the goods are exported out of India would not fall within the phrase export of India and the assessee is not entitled to the benefit of deduction. In other words, it is only in cases as mentioned in the said explanation, it can be said that it is not export out of India and in all other cases, it amounts to export out of India. In fact this provision was the subject matter of a judgment by the Allahabad High Court in the case of Ram Babu and Sons and Another Vs. Union of India (UOI) and Another, wherein it is held as under :

Section 80HHC was made to give certain benefits to exporters. However, explanation (aa) was inserted by the Finance (No. 2) Act of 1991, with effect from 1-4-1986. An exception was carved out from the main provision of section 80HHC. In our opinion, explanation (aa) was to play a loophole in the Act since there was possibility that the goods after purchase may not be exported at all and yet the benefit may be claimed. In our opinion, explanation (aa) is constitutionally valid as it was made to plug a loophole in section 80HHC. It is settled law that in fiscal statutes greater latitude is given to the legislature and the legislature has an option to pick and choose the item which is to be taxed.

"..Explanation (aa) means is that it will not be an export out of India if two conditions are satisfied : (i) it should be a transaction by way of sale otherwise in a shop, emporium or an establishment situate in India; (ii) it should not involve clearance in the customs as defined in the Customs Act. Both these conditions must be satisfied if the transaction is to be held to be not an export out of India. Hence, if either of these two conditions is not satisfied, it is an export out of India. Hence, if the transaction involves clearance at customs, it will be an export out of India within the meaning of Explanation (aa).

15. This judgment was considered by the Apex Court in the case of Commissioner of Income Tax Vs. Silver and Arts Palace, the Apex Court has held as under :

The Allahabad High Court specifically considered the effect of introduction of Explanation (aa) to section 80HHC(4A) of the Act and had taken the view in Ram Babu and Sons and Another Vs. Union of India (UOI) and Another, that this Explanation means that, for the purpose of this section, there will be no export out of India if two conditions are cumulatively fulfilled. viz., (a) it is a transaction by way of sale or otherwise in a shop, emporium or establishment situate in India, and (b) that it does not involve clearance in any customs station as defined in the Customs Act. This view of the Allahabad High Court had been consistently followed by several other High Courts, including the Rajasthan High Court itself in Income Tax Officer Vs. Vaibhav Textiles, Reliance was placed on a

number of orders of the income tax Tribunal following the view taken in Ram Babus case (supra), consistently and the law laid down therein. If fact, even in the case of the respondent-assessee, for the previous assessment years, the Tribunal had taken the same view. Although the revenue attempted to canvass against the view by seeking references u/s 256(1) and (2) of the Act, the attempt failed. There was no further challenge to the settled consistent judicial view taken on the issue. It was also pointed out that the judgment of the Allahabad High Court in Ram Babus case (supra), had been challenged by the revenue before this court, but the special leave petition, was summarily dismissed. In view of this position, the Tribunal felt that consistency of the judicial decision should be respected and followed.

16. Therefore, it is clear if a transaction in question is by way of sale, in" a shop, emporium or an establishment situated in India and it does not involve clearance at any customs station, then it is not an export out of India. Therefore, the aforesaid explanations read with the main section do not in any way indicate that, to be eligible for the benefit of deduction u/s 80HHC, the goods or merchandise has to emanate from India. Though we do not find any direct decision on the point, this question has been discussed by several High Courts as well as the Supreme Court in different contexts which throw light upon the interpretation of these words. In fact, the circular issued by the Board in Circular No. 621 dated 19-12-1991 reads as under :

Tax concession for export of..

31. Under the existing provisions of section 80HHC of the income tax Act, exporters are allowed, in the computation of their total income, a deduction of the entire profits derived from export of goods or merchandise other than mineral oil, minerals and ore.

31.1. In view of the fact that significant value addition is achieved when a mineral is processed or when a stone is cut and polished, it is desirable to encourage their export. The benefit of deduction u/s 80HHC has, therefore, been extended to exporters of processed or when a stone is cut and polished, it is desirable to encourage their export. The benefit of deduction u/s 80HHC has, therefore, been extended to exporters of processed minerals. The list of processed minerals, in respect of which this concession is being extended, is being provided in a new twelfth Schedule to the income tax Act.

31.2 This amendment taken effect from the 1-4-1991 and will, accordingly, apply, in relation to the assessment year 1991-92 and subsequent years.

17. The Apex Court in the case of J.B. Boda and Co. Pvt. Ltd. Vs. Central Board of Direct Taxes, New Delhi, while interpreting the section 80O of the Act considered. The question whether the commission retained out of the gross premium payable in foreign exchange would be eligible for deduction u/s 80O. In that context, the Apex Court has held as under :

The appellant instead of remitting the entire amount to the foreign" reinsurers and then receiving remittance from the said reinsurers the commission due to it, entered into an agreement with the foreign reinsurers, that while remitting the reinsurance premia, the appellant would retain the fee due to it for the technical services rendered and this arrangement is effected only with the concurrence or the permission of the Reserve Bank of India. The question in the instant case is, whether instead of remitting the amount to the foreign reinsurers first and receiving the commission due to the appellant later, the arrangement by which the appellant remitted the reinsurance premia, after retaining the fee due to it for technical services rendered will satisfy the requirement of section 80O of the income tax Act."

In answering the said question, it held as under :

..the objective was to encourage Indian companies to develop technical know-how and to make it available to foreign companies so as to augment the foreign exchange earnings of this country and establish a reputation of Indian technical know-how for foreign countries. The objective was to secure that the deduction under the section shall be allowed with reference to the income which is received in convertible foreign exchange in India or having been received in convertible foreign exchange outside India, is brought to India by and behalf of taxpayers in accordance with the foreign exchange regulations.

Then it proceeded to hold as under :

..It seems to us that a "two-way-traffic" is unnecessary. To insist on a formal remittance to the foreign reinsurers first and thereafter to receive the commission from the foreign reinsurer, will be an empty formality and a meaningless ritual, on the facts of this case.

We are of the view that the income is received in India in convertible foreign exchange, in a lawful and permissible manner through the premier institution concerned with the subject-matter the Reserve Bank of India. In this view, we hold that the proceedings of the Central Board of Direct Taxes dated 11-3-1986, declining to approve the agreements of the appellant with Sedgwick Offshore Resources Ltd. London, for the purposes of section 80O of the income tax Act, are improper and illegal.

18. The Apex Court in COMMISSIONER OF INCOME TAX Vs. BOMBAY BURMAH TRADING CORPORATION, while interpreting the provisions of section 35B of the Act, the deductions in respect of the execution of any contract for the supply outside India of such goods, services or facilities, held that the Tribunals reading of the section that the export should be ex-India is not supported by the language of the provision or any authority. The High Court has, therefore, rightly concluded that to avail of the benefit of deduction, the provision does not require that the export should be ex-India" is not supported by any of the provision or any authority. The High Court has therefore, rightly concluded that to avail the benefit of deduction the provision does not claim that the export should be ex-

India.

19. The Apex Court in the case of Commr. of Income Tax-IV, Tamil Nadu Vs. B. Suresh, dealing with section 80HHC has held as under :

The basic requirement of section 80HHC is earning in foreign exchange and retention of profits for export business. Profits are embedded in the "income" earned. Earning of income depends on sale of goods and services. Today the difference between the two is getting blurred with globalization and cross-examination border transaction. Today with technological advancement one has to change our thinking regarding concepts like goods, merchandise and articles.

20. In fact, the Bombay Bench of the income tax Tribunal in S.M. Synergy v. Dy. CIT (..) 109 ITR 34 (Bom), dealt with the very question which arises for consideration in this case. After carefully scrutinising the provision of law, various judgments and after noticing the judgments of the Apex Court, it is held that,

.. The direct shipment of goods to another country without touching base in India should not be an impediment to the assessee from claiming the benefits of section 80HHC, if it was otherwise entitled to do so. When third country trade is a recognized feature of the new import export policy and procedure of the Government of India, there is no reason to deny deduction u/s 80HHC solely on the ground that the exports were not made ex-India. It is undisputed that the assessee had earned foreign exchange for the country. The focus and emphasis of foreign polity is to increase the foreign reserves of the country. So, the word "export" does not mean only sending goods out of ones own country to another. The wordings of section 80HHC do not provide for such an interpretation at all as distinguished from the expression "from India to a place outside India" as appearing in sub-section (1) of section 80HHE. The assessee is entitled for deduction u/s 80HHC on profit of shipment in respect of plant and machinery sold in Bangladesh.

21. In this context, it is necessary to know how the Parliament has chosen to make known its intention in the event the goods have to be exported from India. Section 80HHC deals with deductions in respect of profits from export of computer software etc.

22. There also the words used are "export out of India". But to be eligible for deduction under the aforesaid provision, mere export out of India is not sufficient. What is to be exported out of India should be from India to a place outside India by any means. Such a wording is conspicuously missing in section 80HHC. It stands to reason. Today, India is a leader in the world insofar as software is concerned. If the intention of the Parliament is not only the assessee should earn foreign exchange in the process of exporting out of India, the country also should be benefited by way of encouraging local talent and activity in India. They have chosen to carve out a separate section by way of section 80HHC. The Parliament here wants to achieve dual object. First, they want to earn foreign exchange by export out of India and secondly, what is to be

exported out of India namely, computer software or its transmission should be from India so that the software industry in the country grows. Such an intention is conspicuously missing while drafting section 80HHC. There the stress is only on earning foreign exchange, not the goods and merchandise to be exported out of India, they do not necessarily have to be from India. Therefore, the law does not require the goods to be physically exported out of India. The provision does not require that the export should be from India. There need not be a two-way traffic of bringing the goods from a foreign country into the Indian shores and thereafter exporting that goods from Indian shores to the off-shore, because it is a mere empty formality and meaningless ritual in which the country gains nothing, because, if the goods have to be brought into the country, precious foreign exchange is wasted and when it is sold, though the assessee gets foreign exchange, it is only to compensate what he has already parted in purchasing and what really is the gain is the profit which he has earned. If that profit is brought to this country, the object of earning foreign exchange is achieved and then u/s 80HHC he is entitled to the said benefit.

23. In that view of the matter, we are of the view that the authorities have not properly understood the object and intent of the Parliament in making these provisions and they have misread the section. Therefore, the impugned order passed by the three authorities is vitiated and cannot be sustained in law. The substantial questions of law are answered in favor of the assessee and against the revenue. Hence, we pass the following: ORDER

The appeals are allowed. The impugned orders are set aside. The assessee is entitled to the benefit of section 80HHC in accordance with law. The substantial question of law is answered in favor of the assessee and against the revenue.