(1990) 03 CAL CK 0007

In the Calcutta High Court

Case No : IT Reference No. 20 of 1981

Bhansali and Co. APPELLANT

Vs

Commissioner of Income Tax RESPONDENT

Date of Decision : 01-03-1990

Acts Referred:

Companies (Profits) Surtax Act, 1964 — Section 18
Income Tax Act, 1961 — Section 256(1), 35B, 35B(1), 35B(1)(b), 35B(1)(b)(iii)

Citation : (1995) 78 TAXMAN 501

Hon'ble Judges : Suhas Chandra Sen, J;Bhagabati Prasad Banerjee, J

Bench : Division Bench

Advocate : Sukumar Bhattacharjee and R.N. Saha, for the Appellant; A.N. Bhattacharjee, for the Respondent

Judgement

Suhas Chandra Sen, J.—The Tribunal had made a consolidated statement of case to this Court u/s 256(1) of the income tax Act, 1961, read with section 18 of the Companies (Profits) Surtax Act, 1964. The assessment years involved are in 1974-75 and 1975-76. The questions arise out of the consolidated order of the Tribunal in income tax Appeal Nos. 1321, 1322, 1551 and 1552 (Cal.) of 1979 for which the corresponding R.A. Nos. were 849 to 852 (Cal.) of 1980. The following questions of law have been referred to this Court: " R.A. Nos. 849 and 850 (Cal.) of 1980

1. Whether, on the facts and in the circumstances of the case and on a correct interpretation of section 35B(1)(b)(viii) of the income tax Act, 1961, the Tribunal was justified in holding that the expenditure of Rs. 16,14,215 and Rs. 22,83,134 for the respective assessment years incurred in India on the carriage of goods to their destination outside India did not qualify for the weighted deduction permissible under the said provisions?

2. Whether, on the facts and in the circumstances of the case and on a correct interpretation of section 35B(1)(b)(iii) of the Act, the Tribunal was justified in holding that Rs. 1,47,192 and Rs. 70,251 for the respective assessment years

incurred in India on the transportation of goods from the assessee''s warehouses to ports for the purpose of export did not qualify for the weighted deduction permissible under the said provisions?

R.A. Nos. 851 and 852 (Cal) of 1980

Whether, on the facts and in the circumstances of the case and on a correct interpretation of section 35B(1)(b)(iii) of the income tax Act, 1961, the Tribunal was justified in holding that the weighted deduction for export market development allowance was not admissible in respect of the following items of the expenditure incurred by the assessee-firm :

1. Interest paid to banks on Packing Credit Loans obtained for export business.

2. Bank charges paid in India in connection with negotiation of invoices for export business.

3. Duty of shipping charges paid to the Port Commissioners for export of goods.

4. Goods forwarding charges incurred for export business."

The facts in connection with these two questions as stated by the Tribunal are as under :

The assessee is an exporter of tea and the relevant assessment years are 1974-75 and 1975-76. The assessee claimed Rs. 16,14,215 and Rs. 22,83,134 as freight charges for the respective years to carry goods to destination outside India. Again, in the respective assessments sums of Rs. 1,47,192 and Rs. 70,251 being transport charges for carrying goods to docks for export outside India were claimed. The ITOs refused to allow export market development allowance u/s 35B of the Act in respect of the aforesaid two items of expenditure in both the assessments. The Commissioner (Appeals) referred to certain order of the Tribunal in paragraph 9 of his order, and particularly following the Full Bench decision of the Bombay Tribunal for the assessment year 1973-74 in J.H. & Co. v. Second ITO [IT Appeal Nos. 3255 and 3330 of 1976-77] held that the aforesaid items would not fall for consideration u/s 35B.

2. It has been contended on behalf of the assessee that the claim for weighted deduction u/s 35B in respect of these expenses were not allowed by the ITO, the Commissioner (Appeals) and the Tribunal u/s 35B(1)(b)(iii). But the case of the assessee is that such expenses should be allowed u/s 35B(1)(b)(iii). It has been contended that in the case of Commissioner of Income Tax Vs. Bata India Ltd., , it was held by this Court that expenditures on the carriage of goods to their destination outside India or on the insurance of such goods while in transit were entitled to weighted deduction wherever expenditures might have been incurred. It has been claimed that, in view of the principles laid down in that judgment, the assessee was entitled to claim weighted deduction u/s 35B in the instant case.

Section 35B is as under :

" Export market development allowance. -(1)(a) Where an assessee, being a domestic company or a person (other than a company) who is resident in India, has incurred after the 29th day of February, 1968 whether directly or in association with any other person, any expenditure (not being in the nature of capital expenditure or personal expenses of the assessee) referred to in clause (b), he shall, subject to the provisions of this section, be allowed a deduction of a sum equal to one and one-third times the amount of such expenditure incurred during the previous year:

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(b) The expenditure referred to in clause (a) is that incurred wholly and exclusively on-

(i) Advertisement on publicity outside India in respect of the goods, services or facilities which the assessee deals in or provides in the course of his business;

(ii) obtaining information regarding markets outside India for such goods, services or facilities;

(iii) distribution, supply of provision outside India of such goods, services or facilities, not being expenditure incurred in India in connection therewith or expenditure (wherever incurred) on the carriage of such goods to their destination outside India or on the insurance of such goods while in transit;

(iv) maintenance outside India of a branch, office or agency for the promotion of the sale outside India of such goods, services or facilities;

(v) preparation and submission of tenders for the supply or provision outside India of such goods, services, or facilities, and activities incidental thereto;

(vi) furnishing to a person outside India samples or technical information for the promotion of the sale of such goods, services or facilities;

(vii) travelling outside India for the promotion of the sale outside India of such goods, services or facilities, including travelling outward from, and return to, India;

(viii) performance of services outside India in connection with, or incidental to, the execution of any contract for the supply outside India of such goods, services or facilities;

(ix) such other activities for the promotion of the sale outside India of such goods, services or facilities as may be prescribed.

Explanation 1 - In this section, ''domestic company'' shall have the meaning assigned to it in clause (2) of section 80B.

Explanation 2 - For the purposes of sub-clause (iii) and sub-clause (viii) of clause (b), expenditure incurred by an assessee engaged in the business of-

(i) operation of any ship or other vessel, aircraft or vehicle, or

(ii) carriage of, or making arrangements for carriage of, passengers, livestock, mail or goods, on or in relation to such operation or carriage or arrangements for carriage (including in each case expenditure incurred on the provision of any benefit, amenity or facility to the crew, passengers or livestock) shall not be regarded an expenditure incurred by the assessee on the supply outside India for services or facilities."

Under section 35B, the assessee is allowed a deduction of more than what he has actually spent. This is to encourage development of export trade. In order to claim this deduction the assessee must establish that all the conditions for claiming the deduction have been fulfilled. When the assessee claims a deduction of the nature mentioned in section 35B, he must strictly bring himself within the specific conditions laid down in the section for getting weighted deduction. The first part of section 35B which is sub-section (1)(a) merely declares that the assessee, who fulfills the conditions laid down in section 35B, will be allowed a deduction of a sum equal to one and one-third times of the amount of expenditures incurred during the previous year if the expenditures were of the nature referred to in clause (b). Clause (b) of section 35B(1) lays down that the expenditures must be incurred wholly and exclusively on the activities mentioned in sub-clauses (i) to (ix). Sub-clause (iii) has specifically laid down that expenditure (wherever incurred) on the carriage of such goods to their destination outside India or on the insurance of such goods while in transit will not qualify for weighted deduction. The question that has been referred is confined to section 35B(1)(b)(iii). Therefore, the claim of the assessee will have to be examined under the specific provision of the statute. In view of the limited scope of the question, it is not open to the assessee at this stage to contend that the claim is otherwise allowable u/s 35B(1)(b)(viii).

Even if this question is allowed to be argued, I fail to see how the expenditure incurred on transportation of exportable goods to their destination outside India can come within the provision of performance of services outside India in connection with, or incidental to, the execution of any contract for the supply outside India of such goods, services or facilities. Under sub-clause (viii), the expenditure incurred on the supply of goods outside India is not allowable as such. What is allowable is expenditures wholly and exclusively incurred for "performance of services outside India in connection with, or incidental to, the execution of any contract" for the supply of such goods. The expenditures incurred for the execution of any contract for supply of goods outside India can only be done by sending such goods outside India. But the weighted deduction is provided not for the expenditure wholly and exclusively incurred for execution of the contract for supply of goods, but for performance of services outside India in connection with or incidental to the execution of the contract. Therefore, even under sub-clause (viii) expenditure incurred in India for the purpose of carriage of goods to their destination outside India will not qualify for weighted deduction.

3. Moreover, what is specifically forbidden to be allowed as weighted deduction under sub-clause (ii) cannot be allowed under sub-clause (viii) by giving an extended meaning to the general words employed in that sub-clause. The various sub-clauses under clause (b) of section 35B(1) have tried to enumerate the various categories of expenditure which will qualify for weighted deduction. If a particular category has been specifically mentioned as not allowable in any of the sub-clauses, then that specifically excluded expenditure cannot be allowed as a weighted deduction under any other sub-clause.

4. The construction suggested on behalf of the assessee will lead to absurdity and must be avoided. The Legislature has specifically forbidden allowance of weighted deduction of expenditure on the insurance of such goods while in transit in sub-clause (iii) which deals with distribution, supply or provision of goods meant for export. The manifest intention of the Legislature cannot be defeated by giving an extended meaning to the provision of sub-clause (viii) so as to allow weighted deduction on expenditure on the carriage of goods to their destination or on the insurance of such goods while in transit. It is difficult to comprehend why the Legislature should forbid specifically and in clear words deduction of expenditure incurred on the carriage of goods to their destination outside India or on the insurance of such goods while in transit but at the same time allow these very expenditures as deduction under sub-clause (viii) by implication. The clear language of sub-clause (viii) does not warrant such a construction.

5. An argument was also advanced on the strength of the decision of the Court in the case of Bata India Ltd. (supra) that this Court has held that all the activities mentioned in sub-clauses (i) to (viii) are activities for promotion of sale outside India and, therefore, if it can be established that the expenditure was for promotion of sale outside India, then such expenditure will qualify for weighted deduction.

6. This contention is entirely without any basis. In the case of Bata India Ltd. (supra), it was contended on behalf of the Revenue that since the expenditure was for an activity for promotion of sale outside India of goods, then the assessee in order to succeed must be able to bring its case within sub-clause (ix) of section 35B(1)(b). Since no rules have been framed under sub-clause (ix), the expenditure being of a nature for the promotion of sale outside India could not qualify for weighted deduction. This argument was rejected by pointing out that all the purposes mentioned in sub-clauses (i) to (viii) were activities for the promotion of sale outside India. It was observed that "the activities mentioned in sub-clauses (i) to (viii) do not cease to be activities for the promotion of the sale outside India of such goods, services or facilities, because the expression ''activities''" for the ''promotion of sales outside India'' has not been specifically used in any of these sub-clauses. Advertisement or publicity outside India in respect of goods, services or facilities, obtaining information regarding markets outside India for such goods, services or facilities, distribution, supply of

provision outside India of such goods, services or facilities, maintenance outside India of a branch office or agency for the promotion of the sale outside India of such goods, services or facilities or for the carriage of goods to their destination outside India or insurance of goods in transit, maintenance of a branch office or agency for export, promotion, preparation of and submission of tenders for supply and provision outside India of such goods, services or facilities, furnishing samples or technical information outside India for promotion of export sale, foreign travel for promotion of sale outside India, actual performance of service outside India in connection with the execution of any contract for supply outside India of goods, services or facilities are all instances of ''activities for the promotion outside India'' of goods, services or facilities.

7. It does not, however, follow the above quoted observation that every expenditure incurred on an activity connected with promotion of sale of goods outside India will qualify for weighted deduction. The assessee may carry on many activities for promotion of sale of goods outside India but weighted deduction will be given only in the specific cases mentioned in sub-clauses (i) to (ix). In order to claim weighted deduction, the assessee must be able to establish that the expenditure has been incurred wholly and exclusively on the specific activities enumerated in sub-clauses (i) to (ix) of section 35B(1)(b).

8. The question No. 1 is, therefore, answered in the affirmative and in favour of the Revenue.

From what has been stated hereinabove the question No. 2 is also to be answered in the affirmative and in favour of the revenue.

9. The facts found by the Tribunal in respect of the question arising out of the Tribunal''s decision in R.A. Nos. 851 and 852 (Cal.) of 1980 are as under:

The assessee is an exporter of tea and the relevant assessment years are 1974-75 and 1975-76. The assessee claimed Rs. 16,14,215 and Rs. 22,83,134 as freight charges for the respective years to carry goods to destination outside India. Again in the respective assessments sums of Rs. 1,47,192 and Rs. 70,251, being transport charges for carrying goods to docks for export outside India, were claimed. The ITO refused to allow export market development allowance u/s 35B in respect of the aforesaid two items of expenditure in both the assessments. The Commissioner (Appeals) referred to certain order of the Tribunal in para 9 of his order, and particularly following the Full Bench decision of the Bombay Tribunal for the assessment year 1973-74 in J.H. & Co.''s case (supra) held that the aforesaid items would not fall for consideration u/s 35B.

10. The ITO completed the assessments denying the assessee''s claim for weighted deduction u/s 35B in respect of certain items but the Commissioner (Appeals) allowed export market development allowance under the said section. The items of expenditure are as under :

Items of Expenditure

Assessment year

1974-75

1975-76

Rs.

Rs.

1. Interest paid on packing credit to banks on export business

2,93,495

4,01,228

2. charges paid in India on foreign invoices

47,098

40,821

3. Duty and shipping charges paid to the Port Commissioner

82,286

63,297

4. Goods forwarding charges

22,68,119

19,76,873

11. Being aggrieved, the revenue preferred appeals to the Tribunal whose attention was drawn to para 36 of the Bombay Tribunal''s order in J.H. & Co.''s case (supra) referred to above in respect of first two items. For items No. 3 and 4 the revenue relied upon paragraphs 34 and 35 of the said order of the Bombay Bench of the Tribunal and also the decision in Commissioner of Income Tax Vs. Kasturi Palayacat Co., , particularly the observations appearing at page 316 thereof. The Tribunal''s attention was also drawn to Explanation 2 to section 35B(1) brought in by the Finance Act, 1970 with retrospective effect from 1-4-1968. On the other hand, the learned counsel on behalf of the assessee supported the first appellate order. In regard to the bank interest it was submitted that the said expenditure was incurred not after the export of goods but before the export thereof. In this connection it was stated that the bankers generally allowed special lending facilities to the exporter of merchandise in connection with their export business and in the banking business such lending facilities were termed as packing credit loan. It was further stated that such loans were generally given against standing export contracts. The assessee claimed weighted deduction on the strength of section 35B(1)(b)(viii). The Tribunal set aside the order passed by the Commissioner (Appeals) on the issue and held against the assessee with the following observations :

"11. We are unable to appreciate the stand taken by the learned counsel appearing on behalf of the assessee. Interest paid to bank to facilitate export business does not in our opinion come within the provisions of section 35B. Shri Bhattacharjee has stretched the said provision too long to cover the expenditure within the ambit of section 35B. If it is to be held that the said expenditure was incurred wholly and exclusively on the performance of services outside India in connection with or incidental to the execution of any contract for the supply outside India of such goods, services or facilities, then customs duty paid and packing charges for the purpose of export of goods should also fall within the category contemplated by section 35B(1)(b). Therefore, we hold that the Commissioner (Appeals) was wrong in granting weighted deduction with reference to bank interest.

12. Bank charges were admittedly paid on account of the discounting facilities enjoyed by the assessee for discounting the foreign invoices on their presentation to the bankers after the goods are shipped. These facilities are being enjoyed by the exporters to realise their foreign invoices quickly. Therefore, Shri Bhattacharjee claims it to fall as in the first case. In para 36 of the Special Bench order bank charges were held to be not falling u/s 35B. Hence we are unable to uphold the Commissioner''s decision in the matter. Moreover, our reasonings in respect of the first items would also apply in respect of the bank charges."

In regard to other two items also the Tribunal set aside the order passed by the Commissioner (Appeals) and held against the assessee with the following observations :

"14. In regard to the last two items, Shri Bhattacharjee submits that the same would fall u/s 35B(1)(b)(viii) of the Act. He submits that the Port Authorities charged duty whenever any goods are shipped from any port in India and without payment thereof it is not possible to make any export.

15. In regard to the other item he has led us through the details. Such expenditure were incurred for packing, lining, labour charges for making the goods ready for shipment, packing materials, transportation of goods to port, Entomologist''s fees, Agmark labels, storage, plant and pathologist''s inspection charges, fumigation expenses, stevedoring charges, survey analysis, ward and watch expenditure and issue of certificate of origin. The Special Bench, Bombay held the issues against the assessees in paragraphs 34 and 35 of its order. We cannot find any difference between the customs duty paid to the Port Commissioner and such duty paid to the Government on exports. Moreover, the Madras High Court held that the custom duty paid and the packing charges incurred did not fall within the category contemplated by section 35B(1)(b). Therefore, the order of the Commissioner (Appeals) in regard to the item Nos. 4 and 5 is set aside and that of the income tax Officer is restored."

Interest paid on packing credit to banks on export business and bank charges paid in India.

12. These questions have been gone into and decided by this Court in the case of Brooke Bond India Ltd. v. CIT [IT Ref. No. 14 of 1983, dated 17-2-1989] as also in the case of Brooke Bond India Ltd. v. CIT [IT Ref. No. 13 of 1983, dated 3-8-1989] where it was, inter alia, held that the claim for weighted deduction in respect of interest paid on packing credit was not admissible under the provisions of section 35B.

13. On behalf of the assessee, strong reliance was placed on a decision in the case of Commissioner of Income Tax Vs. Vippy Solvex Product Private Limited, . In that case the assessee, which manufactured and exported deoiled cakes claimed that a sum of Rs. 4,72,960 incurred by it as expenditure was eligible for weighted deduction u/s 35B. The break-up of the expenditure was as follows : (1) Interest paid to bank on export packing credit account - Rs. 3,65,875; (2) Commission and brokerage for export - Rs. 81,500; (3) Postage, telephone and telegram expenses - Rs. 8,460 and (4) Bank commission on export packing credit account - Rs. 17,125. The ITO allowed the claim of the assessee to the extent of one-third of the expenditure, viz., Rs. 1,57,653. The Commissioner found that the order of the ITO was erroneous and prejudicial to the interest of the revenue and, hence, directed the ITO to withdraw the allowance. The Tribunal found that the assessee had paid commission and brokerage amounting to Rs. 81,476 to various parties at different places, namely, Poland, Germany, London, etc., in connection with the export of its products and it was on account of this fact that the assessee was able to make export sales to the extent of Rs. 1,12,54,223 out of the total sales of Rs. 1,72,19,702, that the assessee had also paid interest of Rs. 3,65,875 in the export packing credit account of the bank and this expenditure was also incurred for promoting export sales, that the assessee had furnished a certificate from the bank stating that the assessee had maintained with it an export packing credit loan account and advances from this account were given only for the purchase of raw materials for manufacturing goods to be exported out of India and these advances were made available only when the parties submitted a copy of the export contract entered into with the foreign party, that this account was quite different from the normal cash credit account as the rate of interest on this account was 11 per cent per annum, whereas the interest on normal cash credit account was 17 per cent per annum and that the loan given in the export packing credit loan account was at the rate of 100 per cent of the cost of raw materials, unlike 65 per cent in the case of normal hypothecation/cash credit account.

The Madhya Pradesh High Court held that the findings of fact arrived at by the Tribunal on the basis of the certificate issued by the bank clearly showed that the credits in the account were given for purchase of the materials and the credit was only given when the contract for supply of goods to the foreign parties was shown and, therefore, the findings clearly indicated that the expenditure was incurred in connection with the execution of a contract for supply of goods outside India. Therefore, the assessee was entitled to weighted deduction on Rs. 3,65,875 paid to the bank u/s 35B(1)(b)(viii).

The Madhya Pradesh High Court has pointed out that sub-clause (viii) to clause (b) of section 35B(1) speaks of performance of services outside India in connection with or incidental to the execution of any contract for the supply outside India of such goods, services or facilities. This, therefore, contemplates that the expenditure incurred in connection with the services rendered outside India or expenditure incurred in connection with or incidental to the execution of any contract for the supply outside India of such goods will be covered by this section. The High Court also relied on the findings of fact arrived at by the Tribunal that all the credits in the account in question were given for purchase of raw materials and this credit was only given when the contract for supply of goods to the foreign parties was shown and, therefore, these findings of fact clearly indicated that this expenditure was incurred in connection with the execution of any contract for supply outside India. But it does not appear that in that case the other limb of section 35B(1)(b)(viii) was at all considered. It is not sufficient for the purpose of sub-clause (viii) to clause (b) of section 35B(1) that all the credits in the account would be utilised for the purchase of raw materials for the purpose of executing a contract for sale and supply of goods outside India. The expenditure must be for the limited purpose of performance of services outside India in connection with or incidental to the execution of any contract for sale and supply of goods outside India. The fact that the expenditure was incurred for the purchase of raw materials in India for the purpose of manufacturing goods to be sold pursuant to the contract entered into with the foreign party, which was to be executed outside India will not make the expenditure laid out on purchase of raw materials entitled to weighted deduction. This deduction can be claimed only for rendering services outside India. We respectfully differ with the views expressed by the Madhya Pradesh High Court on this point.

14. The Madras High Court in the case of V.D. Swami and Co. Pvt. Ltd. Vs. Commissioner of Income Tax, Tamil Nadu-I, held in a case u/s 35B(1)(b)(iii) that weighted deduction would not be available in respect of expenses incurred in India, even if such expenses were incurred for the purpose of distribution of goods outside India. It was observed by the Madras High Court in that case:

"... As earlier mentioned, sub-clause (iii) of section 35B(1)(b) expressly excludes ''expenditure not being expenditure incurred in India in connection therewith.'' To maintain that weighted deduction is available even where expenditure is incurred inside India would go against teeth of this specific exclusionary provision. A look at the other sub-clauses of section 35B(1)(b), such for instance as sub-clauses (i), (iv), (vi), (vii), (viii) and (ix), also shows the insistence of Parliament that the weighted deduction cannot be exigible unless the expenditure under the different heads are incurred ''outside India'', a phrase which occurs again and again in the various sub-clauses. To accept learned counsel''s argument that the Indian situs of the export expenditure is no disqualification for eligibility for weighted deduction would be to bring in under one broad indiscriminate sweep, all expenses in an exporter''s business. If that were the position, Parliament need not have troubled to enact so many clauses in section 35B...." (p. 428)

We respectfully agree with the view expressed by the Madras High Court.

Port duty and shipping charges

15. There is no doubt that these are essential expenditures that the assessee has to incur. It is not possible to use the port facilities without paying port charges which are payable in India. But by payment of these port charges, the assessee has not performed any services outside India in connection with export sales. Therefore, these charges are clearly inadmissible as deduction u/s 35B.

16. In the case of Bharat General and Textile Industries Ltd. Vs. Commissioner of Income Tax, , a Division Bench of this Court in construing the provisions of section 35B(1)(b)(iii) held that the expenditures on items like clearing and forwarding charges paid by an assessee in Indian ports on goods exported to foreign countries and expenditures on the carriage of goods to the destination outside India or on the insurance of such goods while in transit were not entitled to weighted deduction.

Goods forwarding charges incurred for export business

17. The finding of fact by the Tribunal is that such expenditures were incurred for packing, linings, labour charges for making the goods ready for shipment, packing materials, transportation of goods to port, Entomologist''s fees, Agmark labels, storage, fumigating expenses, pathologist''s inspection charges, stevedoring charges, survey analysis, watch and ward expenditure and also certificate of origin. All these activities took place in India and the charges were paid in India. These expenditures were incurred on performance of service in India in connection with export sales. The expenditures were not incurred on performance of any service outside India in connection with the execution of the contract for export sales.

18. In that view of the matter, question Nos. 1 and 2 in R.A. Nos. 849 and 850 (Cal.) of 1980 are answered in the affirmative and in favour of the revenue.

19. The question raised in R.A. Nos. 851 and 852 (Cal.) of 1980 is also answered in the affirmative and in favour of the revenue. There will be no order as to costs.

Bhagabati Prasad Banerjee, J.

I agree.

