
(2013) 06 KAR CK 0144
In the Karnataka High Court
Case No : Income Tax A. No. 251 of 2007

Commissioner of Income Tax and Another	APPELLANT
Vs	
Novell Software Development (I) Pvt. Ltd.	RESPONDENT

Date of Decision : 10-06-2013

Acts Referred:

Income Tax Act, 1961 — Section 260A, 80HHC, 80HHE

Citation : (2013) 260 CTR 372 : (2013) 355 ITR 339

Hon'ble Judges : D.V. Shylendra Kumar, J;B.S. Indrakala, J

Bench : Division Bench

Advocate : K.V. Aravind, for the Appellant; T. Suryanarayana for M/s. King and Partridge, for the Respondent

Judgement

D.V. Shylendra Kumar, J.—The appeal by the Revenue u/s 260A of the income tax Act, 1961, directed against the order dated August 11, 2006, passed by the income tax Appellate Tribunal, Bangalore Bench, in I.T.A. No. 2250/Bang/04. In this appeal the Revenue has raised following two substantial questions of law as arising for consideration as both questions and the findings recorded by the Tribunal is erroneous and warrants interference.

Whether the appellate authorities were correct in directing the Assessing Officer not to exclude 90 per cent. of the gains on foreign exchange fluctuations from the business profits for quantification of deduction admissible u/s 80HHE of the Act?

Whether the Tribunal was correct in allowing the cross-objections filed by the assessee that the business profits should not be reduced by unabsorbed depreciation and unabsorbed loss before computing deduction u/s 80HHE of the Act?

2. Under the impugned order, the Tribunal had dismissed the appeal preferred by the Revenue contending that the Commissioner of income tax (Appeals) had committed an error in directing the Assessing Officer not to exclude 90 per cent.

of the gains on foreign exchange fluctuations from the business profits while determining the relief u/s 80HHC of the income tax Act.

3. In the appeal before the Tribunal by the Revenue, the assessee filed a cross-objection against the very order of the Commissioner raising the following issues :

Learned Commissioner of income tax (Appeals) has erred in holding that the deduction u/s 80HHE of the Act has to be determined on the basis of business profits as reduced by brought forward losses. He ought to have appreciated that section 80HHE is a code by itself and, hence, the deduction ought to be allowed without considering the provisions of section 80AB of the Act.

In any event, he should have allowed the deduction by setting off of brought forward losses first against other income.

4. The Tribunal had dismissed the appeal of the Revenue and had allowed the cross-objection of the assessee and, therefore, the present appeal raises the two questions that were decided against the Revenue.

5. The assessee is a company engaged in the business of development of software which it exports in its entirety. The assessment year is 1996-97. The assessee had claimed in its return of income its export profits for the benefit of deduction u/s 80HHC and the export turnover included the amount received due to export and the difference the assessee got due to fluctuation in the foreign exchange rate as exports were invoiced in terms of foreign currency. The assessee had also computed the business profits, without adjusting the brought forward unabsorbed depreciation of the earlier years and carried forward losses of the earlier years and also in the computation of the profits attributable to exports.

6. The Assessing Officer held that the difference attributable to the fluctuation in the exchange rate and the amount received is not any part of the value of the exported software but because of the fortuitous circumstances and, therefore, cannot be added to the export turnover. In so far as the deductions are concerned, the Assessing Officer, therefore, directed that 90 per cent. of the income has to be reduced in arriving at the profits of the business.

7. It so happened that the assessee had only export profit and no other business profit and, therefore, this aspect did not make any difference in characterising as business profit or profit from export business, both being the same in the assessee's case.

8. The assessee appealed against this order to the Commissioner of income tax (Appeals). The Commissioner of income tax (Appeals) allowed the appeal of the assessee in so far as it related to the deduction of gains from the fluctuation in the foreign currency and the consequent gains from foreign exchange from the export profit or export turnover from the profits of the business, but rejected the other contention of the assessee, affirmed the assessment order in question in

the matter of providing for adjustment of carried forward unabsorbed depreciation and carried forward losses of the earlier years. When the Revenue had preferred the appeal on the question of the gains attributable to fluctuation of foreign exchange, the assessee preferred the cross-appeal as already noticed.

9. The Tribunal opined that the difference amount attributable to and termed as gains due to exchange rate fluctuation is very much part of export profit as it is mainly due to the export activity and on the question of deduction of the adjustments to be made of the carried forward unabsorbed depreciation and losses of the earlier years, it opined that first the benefit of deduction u/s 80HHC should be given and, thereafter, such adjustments can be made.

10. Appearing on behalf of the Revenue, the submission of Sri Aravind, learned standing counsel, is that with reference to section 80HHC(i) now read as section 80HHC(iv), the assessee is entitled for the benefit of section 80HHE deduction from the gains that is derived by the assessee from the business of export activity; that the gains attributable to fluctuation in foreign exchange rate is not precisely derived from the export business but because of the fortuitous circumstance of the exchange rate being not the same throughout and the word "derived" having come in for interpretation and noticed by the Supreme Court in the case of *Liberty India Vs. Commissioner of Income Tax*, and following its earlier view taken in *Commissioner of Income Tax, Karnataka Vs. Sterling Foods, Mangalore*, and having held that the profit should be directly attributable to the export activity and, in the instant case, it having been attributed directly to the fluctuation in the exchange rate, the assessee could not have got the benefit and the Tribunal is in error in answering this issue against the Revenue and in favour of the assessee.

11. The distinction made between the words "derived from" and "attributable to" is emphasised to submit derived from is a narrow word and, therefore, ought to be strictly construed as such.

12. On the second question he submits that the issue is now covered in favour of the Revenue and against the assessee in view of the judgment of this court in the case of *J.K. Industries Ltd. Vs. Assistant Commissioner of Income Tax*, where the words "total income" had been understood as total income as arrived at after providing for unabsorbed depreciation and unabsorbed losses of the earlier years and, therefore, after arriving at the total income, allowing the deduction to be made therefrom out of the total income is erroneous.

13. On the other hand, appearing on behalf of the respondent-assessee, Mr. Surayanarayana, learned counsel submits that the second question is no doubt covered against the assessee but not by this judgment but the later judgment of this court in the case of *M/s. J.K. Industries Ltd. Vs. The Joint Commissioner of Income Tax*, and though it was a case rendered in the context of the benefits to be claimed u/s 80HHC, the ratio is equally applicable to the deduction that can be claimed u/s 80HHE of the Act and in terms of the answer to a similar question

posed for determination, the question had been answered in favour of the Revenue and, therefore, the question may be answered in favour of the Revenue.

14. However, with regard to the first question regarding the amount attributable to the fluctuation in the foreign exchange rate, Mr. Suryanarayana would submit that this amount is not the amount which can be said to be derived from the second degree source as pointed out in the very judgment of the Supreme Court in the case of *Liberty India Vs. Commissioner of Income Tax*, in particular paragraph 14, which is also relied upon by the learned counsel for the Revenue that as far as the present appeal is concerned, the only activity of the assessee is to produce software and export and the assessee has no other business activity or profits and the fluctuation in exchange rate is an incidental aspect but it is the entire amount that is received inclusive of difference attributable to the fluctuation in the foreign exchange rate that is treated as the value of the exports and, therefore, no distinction can be made as between the actual value of the export of the goods and the amount attributable to the gains from fluctuation of the foreign exchange rates, etc.

15. In view of the submissions at the Bar, we have examined the questions. The amount which is sought to be attributed as gain from fluctuation of foreign exchange no doubt might have been due to some fluctuation but as these are amounts received in Indian currency as the total amount that an exporter receives ultimately for the export of the goods, it should be taken together with the value of the goods itself in which event, in our opinion, even the amount said to be attributable to the fluctuation in the foreign exchange rate forms part of the value of the export goods and cannot be distinguished therefrom. In fact the converse of this, viz., if the fluctuation in foreign exchange brought down the value, an assessee cannot claim that this amount should be excluded and the export value maintained at a higher figure.

16. Though it may be an aspect beyond the control of the assessee or the Revenue, it does affect the actual value of the exported goods either way. We are of the opinion that the Tribunal has not committed any error on this aspect. Therefore, there is no occasion to exclude 90 per cent. of the amount attributable to export gains from the foreign exchange rate fluctuation and, accordingly, we answer the first question against the Revenue and in favour of the assessee.

17. The second question whether the Tribunal was correct in allowing the cross-objection of the assessee and that the business profits should not be reduced by unabsorbed depreciation and unabsorbed losses is answered in the negative against the assessee and in favour of the Revenue, as this question is answered and covered by the view of the decision in the case of *J.K. Industries Ltd. Vs. Assistant Commissioner of Income Tax*, In the result, this appeal is allowed in part and the judgment of the Tribunal in so far as it relates to the decision on cross-objection by the assessee in the main appeal of the Revenue is set aside and the judgment of the Tribunal rendered in the main appeal of the Revenue in

I.T.A. No. 2250 of 2004 is affirmed and the appeal in so far as this aspect is concerned is dismissed.