

(2016) 01 RAJ CK 0208

In the Rajasthan High Court

Case No : DB Income Tax Appeal No. 42 of 2008

Commissioner of Income Tax

APPELLANT

Vs

M/s. Garment Crafts

RESPONDENT

Date of Decision : 12-01-2016

Acts Referred:

Income Tax Act, 1961 — Section 80HHC(3), 80IB

Citation : (2016) 3 WLC 417

Hon'ble Judges : Mr. Ajay Rastogi and Mr. J.K. Ranka, JJ.

Bench : Division Bench

Advocate : Mr. R.B. Mathur, Mr. Anuroop Singhi, Mr. Nikhil Similote and Ms. Meenal Ghiya, Advocates, for the Appellant; Mr. Mahendra Gargieya, Mr. Sanjay Jhanwar and Mr. Gunjan Pathak, Advocate, for the Respondent

Final Decision : Disposed Off

Judgement

Mr. J.K. Ranka, J.—This batch of Income Tax Appeals is directed against order of the Income Tax Appellate Tribunal, Jaipur (for short, "Tribunal") and since the controversy raised and the substantial question of law admitted by this Court is same, for the sake of convenience and as agreed by counsel for the parties, the bunch of appeals are being decided by this common judgment.

2. The brief facts are being taken from DB Income Tax Appeal No. 42/2008 (Commissioner of Income Tax v. M/s. Garment Crafts). This appeal was admitted on the following substantial questions of law:-

"(i) Whether in the facts and circumstances of the case, the ITAT has not acted illegally and perversely in reversing the order passed by the CIT(A) as well as Assessing officer for rejection of books of accounts and estimating the GP rate despite the fact that no quantitative details for verification was by the assessee.

(ii) Whether in the facts and circumstances of the case the ITAT has not acted perversely and illegally in directing to calculate the deduction of both 80-IB on total income".

3. The respondent-assessee in this appeal derives income from export of readymade garments and primarily is an exporter of such goods. The assessee furnished its return of income declaring an income of Rs. 44,71,080/- and thereafter a revised return was filed showing total income at Rs. 31,42,390/- in which deduction u/Sec. 80-IB of the Income Tax Act was claimed by the assessee. The assessee, as aforesaid, claimed deduction u/Sec. 80-IB of the Act @30% at Rs. 66,43,472/- on the total business income of Rs. 2,21,44,906/-. The assessee had claimed deduction in respect of entire profits of business which included export incentives to the tune of Rs. 1,02,02,570/- and it was claimed by the assessee that firstly the income of the entire business has to be computed under the head "Income from business and profession" and then 30% of such income is allowable as deduction u/Sec. 80-IB and accordingly the same was claimed as a deduction @30% as it derived such benefit from an industrial undertaking. The Assessing Officer (for short, "AO"), however, was of the view that in so far as the export incentives received to the tune of Rs. 1,02,02,570/- is concerned, since it does not constitute profit and gain derived from the assessee's industrial undertaking, there being no nexus with the profit of business/business income, therefore, the AO excluded the same for consideration and out of purview of Section 80-IB. He while disallowing relied upon judgments of Hon'ble Apex Court in the case of CIT v. N.C. Budhiraja & Company : (1993) 204 ITR 412 (SC); Cambay Electric Supply Industrial Company Limited v. CIT: (1978) 113 ITR 84 (SC), and CIT v. Sterling Foods : (1999) 237 ITR 579 (SC) and held that it is income earned on sale of import entitlements of duty draw back and excluded the same and reduced it from total business income of Rs. 2,21,44,906/- and accordingly held that deduction u/Sec. 80-IB is available on the actual business income/profit derived on Rs. 1,19,42,336/- and on the basis whereof deduction u/Sec. 80-IB of Rs. 35,82,700/- is allowable as against claimed by the assessee at Rs. 66,43,472/-.

4. The matter was carried in appeal by the respondent before the Commissioner of Income Tax (Appeals) (for short,"CIT(A)") who upheld the findings of the AO and rejected claim of the assessee.

5. Both, the Revenue as well as assessee filed cross appeals before the Tribunal. The Tribunal, in so far as the assessee's appeal is concerned, partly allowed the same and rejected the appeal of the Revenue. In so far as the issue relating to deduction u/Sec 80-IB, is concerned, the Tribunal accepted contention of the assessee and held that duty draw back is integral part of the pricing of the goods, part of the cost of the production of the industrial undertaking and therefore, the duty draw back has to be treated as derived from industrial undertaking and allowed the claim.

6. Ld. counsel for the Revenue jointly contended that by no stretch of imagination, the amount, being in the nature of duty draw back, can be said to be derived as profit of business. Though it may be part of the profit and loss account but it is received from the Government of India as export incentive to

help an exporter. He further contended that though duty draw back is income attributable to the business being carried out by the respondent but definitely not derived from the export business of the industrial undertaking. He relied upon a direct judgment of the Hon"ble Apex Court rendered in the case of Liberty India v. CIT : (2009) 317 ITR 0218 (SC) and in the case of CIT v. Sterling Foods : (1999) 237 ITR 0579 (SC) and contended that the Hon"ble Apex Court has held that the export incentives are not derived from the export business of the industrial undertaking and thus the issue is squarely covered in favour of the Revenue.

7. Per-contra, Id. counsel for the respondents jointly contended that the amount received as export incentive is integral part of the pricing of the goods, the exporter exports the goods taking into consideration the import entitlements/DEPB license/duty draw back and there is direct nexus between the cost of the manufactured goods and the said receipts and DEPB license is to be compensated against the excise/custom duty paid or inputs used in manufacturing and contended that it is also derived from the export business and thus the deduction is allowable.

8. They also contended that this Court in the case of Saraf Seasoning Udyog v. ITO : 2009 317 ITR 0202 (Raj.) has taken into consideration the newly introduced Clause (iiid) u/Sec. 28 of the Act and contended that the judgment of this Court on the same issue is required to be taken into consideration in which even the judgment of the Hon"ble Apex Court in the case of CIT v. Sterling Foods (supra) has been distinguished. They contended that the judgments of Gujarat High Court in the case of CIT v. India Gelatine and Chemicals Ltd. (2005) 275 ITR 0284 (Guj.) and Delhi High Court in the case of CIT v. Eltek SGS P. Ltd.: (2008) 300 ITR 0006 (Del.) also support contention of the assessee. They also relied upon the judgment of this Court in the case of CIT v. Chokshi Contacts (P) Ltd. : (2001) 251 ITR 0587; judgment of Hon"ble Apex Court in the case of Topman Exports v. CIT : (2012) 342 ITR 49 (SC) and contended that the judgments support claim of the assessee, therefore, deduction deserves to be allowed to the assessee.

9. Counsels in some of the cases also contended that in few of the appeals preferred by the Revenue, the tax effect is less than Rs. 20 lac and therefore, in the light of the latest circular of the Central Board of Direct Taxes bearing No. 21/2005 dated 10/12/2015, the board has instructed that the Circular be applied to appeals to be filed and also to pending in High Court and such appeals either are required to be withdrawn/not pressed by the Revenue and therefore, such of the appeals where the tax effect being below 20 lac, deserve to be dismissed in view of the Circular which is binding on the revenue.

10. We have heard counsel for the parties and carefully gone through the material available on record and judgments.

11. Section 80-IB of the Income Tax Act provides for deduction at a specified

percentage in respect of profits and gains derived from the eligible industrial undertakings and other infrastructure development undertaking on fulfilment of specified conditions for a period of 10 or 12 consecutive assessment years from initial assessment year, as the case may be.

12. On perusal of Section 80-IB, in our view, it postulates that the deduction u/ Sec. 80-IB is available to the eligible industrial undertaking where the gross total income of the eligible assessee includes any "profits and gains derived from any eligible business" referred to in the section (emphasis supplied). What has to be seen is "derived from" and not "attributable to". The expression "derived from" is restrictive as against "attributable to", which is wider. There should be immediate nexus and not distant nexus. In our view DEPB/duty draw back benefits do not form part of net profit of undertaking as they are not derived from the eligible business but are incentives under a particular scheme.

13. The Hon''ble Apex Court in the case of CIT v. Sterling Foods (supra), where the controversy was relating to deduction u/Sec. 80-HH of the Act, had an occasion to consider about the profits from sale of import entitlements, its nature and observed ad-infra:-

"We do not think that the source of the import entitlements can be said to be the industrial undertaking of the assessee. The source of the import entitlements can, in the circumstances, only be said to be the Export Promotion Scheme of the Central Government where under the export entitlements become available. There must be, for the application of the words "derived from", a direct nexus between the profits and gains and only industrial undertaking. In the instant case, the nexus is not direct and only incidental. The industrial undertaking exports processed sea food. By reason of such export, the Export Promotion Scheme applies. Thereunder, the assessee is entitled to import entitlements, which it can sell. The sale consideration therefrom cannot, in our view, be held to constitute a profit and gain derived from the assessee's industrial undertaking."

14. Thus, the Hon''ble Apex Court in the identical circumstances relating to import entitlements clearly held that it does not constitute profit and gains derived from the assessee's industrial undertaking.

15. The judgment of the Hon''ble Apex Court in the case of Liberty India v. CIT (supra) , in our view, is also directly on the issue as in the instant case u/Sec. 80-IB of the Act. The Hon''ble Apex Court, in para 14 has observed:

"Analysing Chapter VI-A, we find that section 80IB/80-IA are a code by themselves as they contain both substantive as well as procedural provisions. Therefore, we need to examine what these provisions prescribe for "computation of profits of the eligible business". It is evident that section 80-IB provides for allowing of deduction in respect of profits and gains derived from the eligible business. The words "derived from" are narrower in connotation as compared to the words "attributable to". In other words, by using the expression "derived from", Parliament intended to cover sources not beyond the first degree. In the

present batch of cases, the controversy which arises for determination is : whether the DEPB credit/duty drawback receipt comes within the first degree sources ? According to the assessee(s), DEPB credit/duty drawback receipt reduces the value of purchases (cost neutralization), hence, it comes within first degree source as it increases the net profit proportionately. On the other hand, according to the Department, DEPB credit/duty drawback receipts do not come within first degree source as the said incentives flow from the incentive schemes enacted by the Government of India or from section 75 of the Customs Act, 1962. Hence, according to the Department, in the present cases, the first degree source is the incentive scheme/provisions of the Customs Act. In this connection, the Department places heavy reliance on the judgment of this court in *Sterling Foods* 1999 237 ITR 579. Therefore, in the present cases, in which we are required to examine the eligible business of an industrial undertaking, we need to trace the source of the profits to manufacture. (see *CIT v. Kirloskar Oil Engines Ltd.* reported in 1986 157 ITR 762.)"

The Hon'ble Court analysed Duty Exemption Remission Scheme and held DEPB as an incentive. It held in para 18 as under :

"Analysing the concept of remission of duty drawback and DEPB, we are satisfied that the remission of duty is on account of the statutory/policy provisions in the Customs Act/Scheme(s) framed by the Government of India. In the circumstances, we hold that profits derived by way of such incentives do not fall within the expression "profits derived from industrial undertaking" in section 80-IB."

It held in para 24 as under :

"In the circumstances, we hold that duty drawback receipt/DEPB benefits do not form part of the net profits of eligible industrial undertaking for the purposes of section 80-I/80-IA/80-IB of the 1961 Act."

16. Thus, in our view, the judgment is directly and squarely on the issue and the issue is no more *res integra*. It may also be relevant to observe that the judgments rendered by this Court in the case of *Saraf Seasoning Udyog* (supra) and *CIT v. Chokshi Contacts (P) Ltd.* (supra) are judgments prior to the judgment of the Hon'ble Apex Court in the case of *Liberty India v. CIT* (supra) and thus are *per incuriam*. The judgments in the case of *Topman Exports v. CIT* (supra) and *Vikas Kalra v. CIT* : (2012) 247 CTR 0382, in our view, are in context of section 80HHC read with explanation (baa) of the Income Tax Act, and accordingly are distinguishable. The other judgments, relied upon by counsel for the assessees, are also distinguishable in view of what we have noticed here in above and the arguments of the counsel for the assessees find no force and are hereby rejected.

17. We may also deal with the issue raised by learned counsel for the assessees that in some of the appeals the tax effect being below Rs. 20 lac such appeals deserve to be dismissed in view of the Circular of the Central Board of Direct

Taxes No. 21/2015 dated 10.12.2015. We have gone through the Circular which states (para 3) that where the monetary limit is below Rs. 20 lac insofar as the High Courts are concerned, and that it applies to all pending appeals (para 10) below the specified tax limits, which may be withdrawn/not pressed. However, in view of Article 141 of the Constitution, we are bound by the judgment of the Hon''ble Apex Court and bound to follow such an issue/question which is squarely and directly covered on the issue being law of the land, and the Circular may not be applicable at-least in such matters and even otherwise the Circular of CBDT is not binding on this Court. Thus, we hold that when an issue/question is directly covered by a binding judgment of the Hon''ble Apex Court or of this Court, the Circular supra insofar as such an issue/question is concerned, is not binding on this court and in our opinion if an issue/question is directly or squarely covered as aforesaid by a judgment and is no more res integra, the Circular (supra) would be inapplicable.

18. In view of what we have observed herein above, the question relating to deduction u/Sec. 80-IB in all the appeals is answered in favour of the Revenue and against the assessee and the order of the Tribunal insofar as this issue is concerned, is reversed and appeals of the Revenue allowed.

19. In some of the appeals, in addition to the aforesaid substantial question, other substantial question of law has been framed, we now deal the same hereunder:-

20. DB I.T. Appeal No. 42/2008 (CIT v. M/s. Garment Crafts India Ltd.:

"Whether in the facts and circumstances of the case, the ITAT has not acted illegally and perversely in reversing the order passed by the CIT(A) as well as Assessing Officer for rejection of books of accounts and estimating the GP rate despite the fact that no quantitative details for verification was by the assessee?"

21. It relates to the Assessment Year 2001-02 and the question is that the AO found that the assessee has not maintained books of accounts from which true profit can be deduced, that the books are not reliable, the quantitative details does not match with the stock register maintained vis-a-vis the production/consumption of the raw material, and there are several cuttings and overwriting in the so-called stock register/records and thus applied provisions of Section 145(3) and made a trading addition of Rs. 22,95,317/- and on an appeal by the assessee, the CIT(A) partially allowed the appeal of the assessee and sustained the addition of Rs. 12,42,965/-. On a further appeal by the assessee, the Tribunal, after analysing the past history, came to the conclusion that the total turnover has increased sharply and found that the assessee was able to prove with material and evidence that exports to a concern "Her Style" is less profitable than sales made to other concern and approximately 50% of the turnover is to "Her Style" whereas in the past years, the sale relating to the said company was lower and finding such a fact, the Tribunal deleted the entire trading addition.

22. Ld. counsel for the appellant-Revenue contended that the Tribunal was

unjustified in deleting the trading addition which was rightly made by the AO as once the provisions of Section 145(3) are invoked and the assessee is not able to prove by acceptable evidence the defects noticed and the true profits are not deducible from such accounts and estimation is required to be made and since the assessee itself declared a gross profit rate of 45.76% in past years, therefore, the AO was well justified in applying the said GP Rate and thus supported the order of the Ao.

23. Per-contra, Id. counsel for the assessee contended that the Tribunal has taken into consideration over all results and no just and proper basis was given by the AO in invoking provisions of Section 145(3) and contended that GP Rate cannot be static or increasing over the years and supported order of the Tribunal.

24. We have taken into consideration the facts and in our view, the order of the Tribunal is just and proper and is not required to be interfered with, insofar as the trading addition is concerned, as the Tribunal has found on facts that the assessee had exported approximately 50% of the turnover to a firm "Her Style" whereas the margin of profit was lower in comparison to others and also that in the past only 30% of the total sales was to the firm "Her Style" whereas the same during the current year was almost 50%.

25. Taking into consideration the above facts, in our view, the order of the Tribunal cannot be said to be unjust. The order of the Tribunal is just and proper and we are not inclined to agree with the contention raised by the Revenue. Accordingly, the said question is answered against the Revenue and in favour of the assessee.

26. DB Income Tax Appeal No. 647/2008 (CIT v. M/s. ABC Exports); DB Income Tax Appeal No. 658/2008 (CIT v. M/s. ABC Exports) & DB Income Tax Appeal No. 710/2008 (CIT v. M/s. ABC Exports):

"Whether in the facts and circumstances of the case and in view of the fact that the interest income of the assessee has been included in the "profit of the business" the ITAT was justified in directing to exclude the interest turn over from the total turn over of the business for the purpose of computing the deduction under section 80HHC(3) adopting the formula of "profit of the business" export turn over/total turn over ?"

27. The assessee claimed that the interest received by the assessee from the FDR (Fixed Deposit Receipts) and also from other persons, was in the nature of business income on which the assessee was entitled to deduction u/Sec. 80-HHC of the Income Tax Act. However, the AO was of the view that interest received has no concern or connection over the export turnover/income, and rather it is in the nature of income from other sources and thus rejected claim of the assessee. The CIT(A) also rejected contention of the assessee. However, on a further appeal before the Tribunal, the Tribunal allowed the claim holding that it is income from business.

28. Id. counsel for the Revenue at the outset relied upon the judgment rendered by Larger Bench of this Court in the case of Reliance Trading Corporation v. ITO : (2015) 376 ITR 53 (FB-Raj.) and Division Bench of this Court in the case of CIT and ors. v. Vimal Chand Surana and ors., DB Income Tax Reference No. 4/2003 and other connected cases, decided on 11/09/2015, which has taken into consideration identical question.

29. Per-contra, Id. counsel for the assessee contended that the order of the Tribunal is just and proper and the interest was shown as part of profits and was in the nature of business income, formed part of business income and there was common books of accounts and there was direct nexus of the said amounts having been received on exports. Thus, the Tribunal was correct and justified.

30. We have considered the arguments advanced by counsel for the parties and in our view, the judgment rendered by Larger Bench of this Court in the case of Reliance Trading Corporation v. ITO : (2015) 376 ITR 53 (FB-Raj.) and Division Bench of this Court in the case of CIT and ors. v. Vimal Chand Surana and ors., DB Income Tax Reference No. 4/2003 and other connected cases, decided on 11/09/2015, is squarely applicable on the facts of the instant case and we quote the relevant observations :

"The Larger Bench of this court has taken into consideration the judgment of CIT v. Shri Ram Honda Power Equip (supra) which by and large has touched the controversy in hand and the said judgment of Delhi High Court has taken into consideration the fact about deduction under Section 80HHC of allowing a claim similar to the present controversy, and after examining the controversy has come to the conclusion that the issue has been considered taking into note the judgments rendered by the Hon"ble Apex Court in the case of Tuticorin Alkali Chemicals and Fertilizers Ltd. v. CIT (1997) 227 ITR 172, Cambay Electric Supply Industrial Co. Ltd. v. CIT (1978) 113 ITR 84, CIT v. Sterling Foods (1999) 237 ITR 579, Pandian Chemicals Ltd. v. CIT (2003) 262 ITR 278, and has come to the conclusion that deduction under Section 80HHC is not allowable, and in our view, the judgment of Shri Ram Honda Power Equip (supra), so also Rajasthan Land Development Corporation (Supra), Murli Investment Company (supra) and Avon Apparels (Supra), apply to the facts of the instant case with full force and we, after analysing the facts in the instant reference/appeals so also judgment of Larger Bench hold that interest received/earned does not enure for deduction under Section 80HHC."

31. Taking into consideration the above, in our view, it is income from other sources and when the assessee has not been able to prove nexus of the said receipt vis-a-vis export income, in the light of the judgments of this Court, the question is answered in favour of the Revenue and against the assessee.

32. DB Income Tax Appeal No. 410/2008 (Commissioner of Income Tax v. M/s. Gulshan Fashions Pvt. Ltd.):

"(i)Whether in the facts and circumstances of the case the ITAT has not acted

perversely and illegally in deleting the addition of amount of GP rate taken as 20% by Assessing Officer after considering comparable cases?

(ii) Whether in the facts and circumstances of the case, the ITAT was justified in law and has not acted perversely in holding the duty drawback consultancy charges as revenue expenditure instead of capital expenditure in spite of the fact that the benefit arising out of this expenses was of enduring nature?"

33. The said two questions raised in addition to Section 80-IB, are that the Tribunal erred in deleting the addition on account of gross profit rate taken as 20% by the AO and the duty draw back consultancy charges. While the claim of the assessee was that no estimation of trading account can be made and consultancy charges paid is revenue expenditure. The claim of the revenue was on the contrary that books are required to be rejected as true profits cannot be deduced and consultancy charges are capital in nature and thus capital expenditure.

34. Insofar as the trading addition is concerned, in our view, the AO applied a certain percentage while making trading addition rejecting books of accounts u/ Sec. 145(3) and applied the GP Rate of 20% on the total turnover as disclosed by the assessee. The CIT(A) on a further appeal by the assessee applied a GP Rate of 15%. However, the Tribunal, taking into consideration the judgment rendered by this Court in the case of CIT v. Gotan Lime Khaniz Udyog : (2002) 256 ITR 243, has held that the books of accounts have been maintained in proper manner and deleted the addition and in our view, we find no perversity in the order of the Tribunal in deleting the trading addition as even otherwise it is a finding of fact based on the material on record and there can be no hard and fast rule of increasing the GP Rate over the years.

35. In so far as the disallowance of duty draw back consultancy charges at Rs. 1,09,978/- is concerned, while the AO held that it is capital expenditure in nature and it has enduring effect, however, both i.e. the CIT(A) as well as the Tribunal came to the conclusion that it is revenue in nature. In our view, the finding of the Tribunal that it is not in the nature of enduring effect, is just and proper, the finding of fact recorded by both the appellate authorities is that the consultancy charges have to be paid on account of duty draw back received by the assessee which is to the extent of 1% or 1.5% and this has been paid on year to year basis. When this is a finding of fact recorded by the appellate authorities that these are the consultancy charges on account of receipt of duty draw back and is being paid on annual basis, in our view, it is certainly not in the nature of capital expenditure and has rightly been held to be expenditure, revenue in nature and thus allowable. Thus, both the questions are answered against the revenue and in favour of the assessee.

36. In ultimate analysis, we may summarise the substantial questions of law as under:

(i) The question relating to deduction u/Sec. 80-IB in all the aforesaid appeals is

answered in favour of the Revenue and against the assessee;

(ii) As regards DB Income Tax Appeal No. 42/2008, while the substantial question relating to Section 80-IB is answered against the assessee and in favour of the Revenue, the question relating to trading addition is answered in favour of the assessee and against the Revenue;

(iii) As regards DB Income Tax Appeal No. 647/2008, 658/2008 and 710/2008, while the substantial question relating to Section 80-IB is answered against the assessee and in favour of the Revenue, the other question relating to deduction u/Sec. 80-HHC on interest received is also answered against the assessee and in favour of the Revenue.

(iv) As regards DB Income Tax Appeal No. 410/2008, while the substantial question relating to Section 80-IB is answered against the assessee and in favour of the Revenue, the other question relating to trading addition and the amount of duty draw back consultancy charges is answered in favour of the assessee and against the Revenue.

37. The batch of appeals stands disposed of in the terms as indicated above. No costs.

38. Appeal disposed of above, conclusion summarised in para 36.