

(2014) 06 KAR CK 0231

In the Karnataka High Court

Case No : I.T.A. Nos. 472, 1074, 563 and 1029 of 2008

Ge Be P. Ltd

APPELLANT

Vs

Assistant Commissioner of Income Tax

RESPONDENT

Date of Decision : 30-06-2014

Acts Referred:

Income Tax Act, 1961 — Section 10B, 143(3), 260A, 80HH

Citation : (2015) 371 ITR 32

Hon'ble Judges : N. Kumar, J;B. Manohar, J

Bench : Division Bench

Advocate : S. Parthasarathi, Advocates for the Appellant; K.V. Aravind, Advocates for the Respondent

Judgement

N. Kumar, J.—All these appeals are taken up together for consideration since they arise from a common order and the assessee is common. These income-tax appeals are filed under section 260A of the Income-tax Act, 1961 (hereinafter referred to as "the-Act" for short), against the order dated January 18, 2008, passed by the Income-tax Appellate Tribunal, Bangalore "B" Bench (hereinafter referred to as "the Tribunal" for short).

2. The facts of the case in brief are:

The assessee is a 100 per cent, export oriented undertaking ("EQU" for short) engaged in the manufacturing of X-ray tubes, high voltage tanks, CT detectors used in CT scanners and X-ray equipment. By virtue of being 100 per cent, export oriented undertaking, the assessee is entitled to deduction under section 10B of the Act in respect of the profits earned from this unit. The assessee is a part of the GE group of companies having operations all over the world. The assessee filed its" return of income declaring a total income of Rs. 21,12,38,610 on October 28, 2003. The assessee claimed deduction of Rs. 73,12,83,454 under section 10B of the Act. The assessee admitted the turnover from manufacturing activity at Rs. 354.13 crores. The assessee also declared the turnover of 24.33 lakhs on the export of spares/components. The assessee"s case was selected for

scrutiny and an assessment order under section 143(3) of the Act came to be passed on March 27, 2006. The Assessing Officer restricted the deduction under section, 10B of the Act at Rs. 72,68,33,060 on the ground that the turnover on account of export of spares/components was not to be included in the eligible profits to determine the deduction under section 10B of the Act. An amount of Rs. 24.33 lakhs was deducted in order to arrive at the profit of the business for the purpose of section 10B. The assessee claimed for inclusion of Rs. 66,17,795 representing the sale, of scrap in the company's profits for calculating the deduction under section 10B of the Act. The Assessing Officer disallowed the claim of the assessee. Aggrieved by the said order, the assessee preferred an appeal to the Commissioner of Income-tax (Appeals)-I, Bangalore (hereinafter referred to as "the first appellate authority"). The appellate authority did not agree with the contention of the assessee and rejected both the claims of the assessee. Aggrieved by the said order, the assessee preferred an appeal before the Tribunal.

3. The Tribunal held that the primary activity of the assessee is manufacture and sale of X-ray tubes and high voltage tanks for diagnostic imaging equipment. It is incidental that spare parts are imported for this purpose by the associate companies. Only on the income derived from such manufacturing activity, deduction under section 10B can be allowed. There has to be a direct nexus between the manufacturing activity and the receipts in question. Therefore, it held that the income on sale of spare parts is not eligible profit for the purpose of computing deduction under section 10B of the Act.

4. In so far as the sale of scrap is concerned, relying on the order of the Tribunal in the assessee's own case in I.T.A. No. 3624(B) of 2004 for the assessment year 2001-02, the Tribunal has granted relief under section 10B of the Act in respect of sale of scrap. The order of the authorities below was set aside and a direction was issued to include the income derived from sale of scrap for relief under section 10B of the Act. In I.T.A. No. 189 of 2007, the assessee filed a Miscellaneous Application No. 44 of 2008 for clarification. The said application was allowed holding that profit on sale of scrap and spare parts is not to be deducted under section 10B of the Act, but the net profit should be adjusted from the profit of the undertaking and not total sale receipts. Accordingly, the matter was restored to the Assessing Officer for the purpose of netting as discussed above. Aggrieved by these orders, these appeals are filed by the assessee as well as the Revenue.

5. The substantial questions of law that arise for consideration in these appeals are:

"(i) Whether the Tribunal was justified in not considering the profit on export of spare parts while allowing the exemption under section 10B of the Income-tax Act, 1961, when the import of spare parts or purchase of spare parts were exclusively for production of commodities exported and the export profit earned in foreign exchange?

(ii) If the court were to hold that the assessee is not entitled to the benefit of section 10B of the Act for the export of spare parts where the cost of importing or purchase of spare parts were to be excluded while computing the export profit eligible for exemption under section 10B of the Act?

(iii) Whether the Tribunal was correct in holding that incidental income derived by the assessee from, the sale of scrap would be entitled to exemption under section 10B of the Act despite the same having been not derived from the export of articles or things?"

6. Questions Nos. 1 and 2

Learned counsel for the assessee assailing the impugned order contended that having regard to the total turnover of the export business, the turnover in respect of the import and export of spare parts is negligible. However, it forms part of export business of the assessee. It is incidental to the export business and, therefore, the profit derived from the export of spare parts is also eligible for deduction under section 10B of the Act.

Per contra, the learned counsel appearing for the Revenue submitted that for the application of section 10B of the Act, the conditions stipulated in sub-section (2) of section 10B, namely, the article which is exported should have been manufactured or produced must be complied with, apart from other conditions stipulated in the said provisions. In so far as the spare parts which were imported or exported as such are concerned, they did not undergo any manufacturing activity or involved in any production activity and, therefore, the authorities below were justified in excluding that portion of the turnover from the benefit under section 10B of the Act.

7. Section 10B is a special provision in respect of the newly established 100 per cent, export oriented undertakings: Subject to the provisions of section 10B, a deduction of such profits and gains as are derived by a hundred percent, export oriented undertaking from the export of articles or things or computer software for a period of ten consecutive assessment years shall be allowed from the total income of the assessee. To attract this provision, the assessee has to comply with the requirements mentioned in sub-section (2). One of the requirements is that the products so exported should have been manufactured by the assessee or it should be an article or thing produced by the assessee. It is only then, the benefit of section 10B is available. In the instant case, the assessee is importing spare parts. The said spare parts are used in the production of articles for export. Those spare parts which are used for producing articles are extended the benefit of section 10B. There is no dispute on that count. The dispute is that, when the spare parts are imported and without any change or they being used in any production/manufacturing activity, if they are exported, the profits and gains derived from such export is eligible for the benefit under section 10B of the Act having regard to the conditions prescribed under sub-section (2) which is a condition precedent for availing of the benefit under section 10B. Until those

conditions are fulfilled, the assessee is not entitled to the benefit of section 10B. When the assessee imports spare parts and exports them in the same condition, may be along with the articles produced and the spare parts exported are not involved in any manufacturing activity or in production activity, section 10B is not attracted. Therefore, all the three authorities have rightly held that the assessee is not entitled to the benefit of section 10B. In the facts and circumstances, we do not see any infirmity in the said orders. Therefore, the substantial questions of law Nos. 1 and 2 are answered in favour of the Revenue and against the assessee. However, when the income derived from the sale of spare parts is held to be ineligible for the benefit under section 10B, the entire amount representing the value of spare parts is to be excluded and the profits and gains derived from sale of such spare parts alone is liable for tax. That is the exercise to be undertaken by the assessing authority and the said amount is to be excluded.

8. Question No. 3

Learned counsel for the Revenue assailing the aforesaid finding contended that scrap is not derived from producing the articles of export. Having regard to the language in section 10B of the Act only for such profits and gains which are derived by the assessee from the export of articles or things, section 10B is attracted. Admittedly, the scrap is not exported and, therefore, he submits that the Tribunal was not justified in holding that the assessee is entitled to the benefit of section 10B even in respect of the scrap.

Per contra, the learned counsel appearing for the assessee submitted that the profit earned by sale of scrap constitutes profits and gains of the assessee and, therefore, section 10B is attracted and the Tribunal was justified in extending the benefit of section 10B to the assessee.

9. The apex court in the case of the Commissioner of Income Tax, Karnataka Vs. Sterling Foods, Mangalore, , while dealing with the deductions under section 80HH explained the meaning of the word "derived from" held as under:

"The use of the word "derived from" suggests that the original source of the product has to be found. As a matter of plain English, when it is said that one word is derived from another, often in another language, what is meant is that the source of that word is another word, often in another language. As an illustration, the word "democracy" is derived from the Greek word "demos", the people and most dictionaries will so state. That is the ordinary meaning of the word "derived from" and there is no reason to depart from that ordinary meaning here. There must be, for the application of the words "derived from", a direct nexus between the profits and gains and the industrial undertaking."

Keeping in mind the principle laid down by the apex court, no doubt the assessee is not in the business of export of scrap but is in the business of export of X-ray equipment, high voltage tanks and detectors used in CT scanners and after manufacturing these products, they are exported. In the process of manufacturing, the unutilised raw materials forms part of scrap and that scrap

also has value. But it is not exported and, hence, they are eligible for the benefit under section 10B of the Act. The assessee should have earned profits and gains from such export of articles or things. The said articles or things should have been manufactured or produced by the assessee. The section does not require that the profits and gains derived should be from the articles or things which are exported only. It is the profits and gains derived by an 100 per cent, export oriented undertaking from the export of articles. Therefore, when the assessee undertakes manufacturing activity or production activity and in the process it results in any scrap, the said scrap attracts the nexus between the profits and gains derived from the assessee from export business. Therefore, it satisfies the requirements of section 10B and the Tribunal has rightly held that the assessee is entitled to the benefit of section 10B even in respect of the profits earned out of sale of scrap materials within the country. In that view of the matter, we do not see any infirmity in the order passed by the Tribunal. Accordingly, the third substantial question of law is answered in favour of the assessee and against the Revenue.

All the appeals are disposed of accordingly.