

IN THE INCOME TAX APPELLATE TRIBUNAL
“A” BENCH : BANGALORE

BEFORE SHRI N.V. VASUDEVAN, JUDICIAL MEMBER AND
SHRI JASON P. BOAZ , ACCOUNTANT MEMBER

ITA Nos.1093/Bang/2009, 1266/Bang/2010 & 1057/Bang/2012
Assessment years : 2006-07, 2007-08 & 2008-09

M/s. K. Mohan & Company (Exports) Pvt. Ltd., B1, 62-5, Begur Road, Bommanahalli, Bangalore – 560 068. PAN: AAACL 9811H	Vs.	The Assistant Commissioner of Income Tax, Circle 11(5), Bangalore.
APPELLANT		RESPONDENT

ITA No.1103/Bang/2012
Assessment year : 2008-09

The Assistant Commissioner of Income Tax, Circle 11(5), Bangalore.	Vs.	M/s. K. Mohan & Company (Exports) Pvt. Ltd., Bangalore – 560 068. PAN: AAACL 9811H
APPELLANT		RESPONDENT

Assessee by	:	Shri V. Srinivasan, C.A.
Revenue by	:	Shri P. Dhivahar, Jt. CIT(DR)

Date of hearing	:	09.04.2015
Date of Pronouncement	:	24.04.2015

ORDER

Per BENCH:

ITA 1093/B/2009

This appeal by the assessee is against the order dated 4.9.2009 of CIT(Appeals)-I, Bangalore relating to assessment year 2006-07.

2. Grounds No.1 to 8 are general in nature and calls for no specific adjudication.

3. Ground Nos. 2, 3, 4 & 7 raised by the assessee read as follows:-

“2. The CIT(Appeals) ought to have appreciated that the receipts from forward contracts had direct nexus with the undertaking of the Appellant to be considered as having been derived from export business and therefore the Appellant’s computation of deduction under Section 10B did not require interference and ought to have deleted the disallowance made by the assessing officer.

3. Without prejudice, the CIT(Appeals) ought to have appreciated that forward contracts could not be booked unless and otherwise export contracts or export bills were submitted to the bankers and could be settled only by way of delivering export proceeds.

4. Without prejudice, the CIT(Appeals) ought to have appreciated that the requirement of Section 10B was not the income derived from export of goods or merchandise as concluded by the assessing officer and the same being contrary to the requirement of Section 10B, ought to have sustained the disallowance as made by the assessing officer.

7. Without prejudice, the CIT(Appeals) ought to have appreciated that for the assessment year 2005-06, the Tribunal in the Appellant’s own case had not at all distinguished the order of the Mumbai Bench in the case of D.KishoreKumar & Co vs.

DCIT reported in (2005) 2 SOT 769 and therefore the CIT(Appeals) ought to have followed the said order of the Mumbai Bench.”

4. The issue that arises for consideration is as to whether receipts from forward contracts can be considered as profits derived from the business for the purpose of computing deduction u/s. 10B of the Income Tax Act, 1961 (Act)? The material facts that are relevant in this regard are as follows. The assessee is a company engaged in the business of manufacture and export of readymade garments. The assessee has two Export Oriented Units (EOUs), EOU-I & EOU-II, besides domestic unit (DTA)

5. On perusal of the profit and loss account of the assessee, the AO noticed that the Assessee had earned profit on account of forward contract of Rs. 1,10,97,116/-. The profit so earned was reduced from the finance expenses paid and the net finance expenses had been debited to the profit and loss account. The above income have been considered in the DTA, EOU-I and EOU-II as under:

Unit	Amount
DTA	4,99,370
EOU-I	61,58,900
EOU-II	44,38,846
Total	1,10,97,116

6. According to the AO deduction U/S.10B of the Act provides for a deduction of such profits and gains as are derived by a 100% Export Oriented Undertaking from the export of articles or things. Therefore, section 10B shall apply only to profits that are “**derived from**” export of article or things. The AO was also of the view that u/s.10B(3) the sale proceeds of articles or things are to be received in convertible foreign exchange. In the light of the aforesaid provisions, the AO was of the View that the assessee had indulged in hedging foreign currency risk and at best, the said transaction can be termed as ‘financial transaction’. It is also pertinent to mention that assessee has already booked fluctuation of foreign exchange in the accounts and the same is being treated as part of Total turnover. According to the AO by no stretch of imagination, hedging of foreign currency, although pertaining to assessee’s own exports, can be treated as “income derived from export of goods and merchandise”. It may be mentioned that only the “income derived from export of goods and merchandise” is eligible to exemption u/s 10B. Consequently, the income earned by way of profit on forward contracts was not included in export turnover while arriving at deduction u/s 10B.

7. Before CITA the Assessee submitted that it is engaged in the business of exports only. The Assessee enters into a contract with the bankers in order to hedge export sales against any foreign exchange fluctuation. These contracts booked by the banks strictly in accordance with RBI guidelines which are reproduced below:-

- a) Only entities which export to other countries can book forward contracts.
- b) These contracts can be booked based on actual orders on hand or based on orders in pipeline or based on past performance
- c) These contracts will have to be delivered only by delivering export documents or export proceeds lying in EEFC accounts
- d) On the delivery date, if the exporter is unable to deliver export documents or dollars from its EEFC account, the banker will cancel the contract and whatever is the difference between the contract rate and prevailing rate on the date of cancellation will be either paid to or received from the exporter from the exporter as the case maybe.
- e) Cancellation of a contract due to non delivery of the contracted amount on the due date may result in profit or loss as per the spot rate on due date.

8. The Assessee pointed out that during the previous year it had booked forward Contracts only for a part of the export turnover which clearly indicated that the Assessee did not over book forward contracts in order to speculate. Whatever contracts booked were based on business requirements substantiated by actual exports performed. The Assessee placed reliance on the decision of the Hon'ble ITAT, Mumbai bench in the case of *D Kishorekumar and Co. V DCIT (ITA No.3883/Mum/1997 dated 31.03.2005)* wherein it was held that income from cancellation of forward contract was part and parcel of income eligible for deduction u/s 80 HHC. The Assessee argued that since it had entered into forward contracts to cover losses arising on account of devaluation in foreign currency, the profit on forward contract is nothing but sale proceeds of goods exported out of India and are part and parcel of the business profits of the Unit.

9. The CIT(A) however found that similar issue had come up for consideration in Assessee's case for AY 05-06 and the Tribunal in I.T.A.No.113/Bang/09 (A.Y.2005-06) dated 07-08-2009, after distinguishing the facts of the Assessee's case from the case cited by the Assessee, i.e. *D. Kishore Kumar & Co. Vs. DCIT (supra)*, arrived at a conclusion that hedging in foreign exchange through forward contracts tantamounts to speculation business which is different from and has no relation with the business of the assessee i.e., garments export and hence, found the action of A.O. justified. Following the said decision, the CIT(A) upheld the order of the AO.

10. Aggrieved by the order of the CITA, the assessee has raised the aforesaid grounds before the Tribunal. The Id. counsel for the assessee submitted before us that the decision rendered by the Tribunal in assessee's own case for the earlier assessment years has not been challenged by the assessee before the Hon'ble High Court of Karnataka. Nevertheless, it was submitted by him, that the decision rendered by the Tribunal for A.Y. 2005-06 requires reconsideration. In this regard, the Id. counsel drew our attention to the provisions of section 43(5), which read as follows:-

43. In sections 28 to 41 and in this section, unless the context otherwise requires —

.....

.....

(5) "speculative transaction" means a transaction in which a contract for the purchase or sale of any commodity, including stocks and shares, is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scrips:

Provided that for the purposes of this clause—

(a) a contract in respect of raw materials or merchandise entered into by a person in the course of his manufacturing or merchanting business to guard against loss through future price fluctuations in respect of his contracts for actual delivery of goods manufactured by him or merchandise sold by him; or

(b) to (d).....

shall not be deemed to be a speculative transaction.

11. It was first pointed out by the Id. counsel for the assessee that speculative transaction means a transaction in which a contract for the purchase or sale of any commodity is ultimately settled otherwise by actual delivery. According to him, the expression "commodity" used in section 43(5) of the Act does not include foreign exchange, which was subject matter of the forward contract in the present case. In this regard, our attention was drawn to the decision rendered by the ITAT Ahmedabad Bench in *Adani Enterprises Ltd. v. ACIT [2015] 55 taxman.com 375 (Ahd-Trib)*. In the aforesaid case, the assessee was engaged in export, import and domestic trading of various commodities. The assessee borrowed money for the purpose of its business i.e., global trading various commodities. As per terms of borrowing of foreign currency working capital loan, the assessee had to enter into a currency swap arrangement. The

assessee entered into currency swap transaction in respect of outstanding foreign currency loans as per the prevailing RBI guidelines. The currency swap transaction on settlement resulted in a loss of Rs.6.05 crores. The question before the Tribunal was whether the aforesaid loss can be said to be speculative loss. The Tribunal accepted the argument of the assessee that the word "commodity" in section 43(5) of the Act cannot cover currency which is only a medium of exchange with which goods and services can be bought. The relevant observations of the Tribunal are contained in para 4.10 of the order of the Tribunal.

12. According to the Id. counsel for the assessee, foreign currency swap transaction which was the transaction in the case of *Adani Enterprises (supra)* is akin to the foreign exchange forward contract entered into by the assessee in the present case and applying the decision of Ahmedabad Bench of the Tribunal, it has to be held that the gain received by the assessee on settlement of foreign exchange forward contract has to be considered as profits of the business of the assessee on which deduction u/s. 10B should be allowed.

13. The Id. counsel for the assessee further placed reliance on the decision of ITAT Bangalore Bench in the case of *Star Exports & Imports v. ACIT, ITA No.997/Bang/2012, A.Y. 2009-10*, wherein this Tribunal considered the decision rendered by the Tribunal in assessee's own case (K. Mohan & Co. Exports Pvt. Ltd.) and by its order dated 6.2.2005, held

that the decision rendered by the Tribunal referred to above need not be followed as it was contrary to the decision rendered by the Hon'ble Gujarat High Court in the case of *CIT v. Friends & Friends Shipping Co. [2013] 217 taxman 267 (Guj)*. In the case of *Star Imports & Exports (supra)*, the question before the Tribunal was as to whether loss on account of foreign exchange contracts to hedge against foreign exchange fluctuation was a speculative loss u/s. 43(5) or a normal business loss? The Tribunal after considering the decision of the Hon'ble Gujarat High Court in the case of *Friends & Friends Shipping Company (supra)*, wherein it was held that forward contracts entered into with the banks in respect of foreign exchange are not to be regarded as speculative transactions. The Hon'ble Court observed that the assessee was not a dealer in foreign exchange and forward exchange contract was incidental to the assessee's regular course of business. Following the aforesaid decision, the Tribunal held as follows:-

“In view of the above decision of the Hon'ble Gujarat High Court we are of the opinion that the decisions relied on by the revenue which are of various Tribunal Benches pale into insignificance. Judicial discipline requires us to follow judgment of High Court unless and until a contrary judgment of jurisdictional High Court is shown by the parties to the litigation. Even if there is a conflict of opinion between various High Courts, unless and until, there is a jurisdictional High Court decision, one way or the other, an assessee can rightly submit that the one in its favour should be followed. We are therefore, of the opinion that the assessee has to succeed in this appeal.”

14. The Revenue had, before the Tribunal, placed reliance on the decision of Tribunal rendered in the case of *K.M. Mohan & Co. Export Pvt. Ltd. (supra)* for A.Y. 2005-06.

15. Besides the above, the Id. counsel for the assessee also placed reliance on the decision of the ITAT Mumbai Bench in the case of *S. Vinodkumar Diamonds Pvt. Ltd. v. DCIT (supra)*.

16. The Id. DR, on the other hand, placed strong reliance on the decision rendered by the Tribunal in assessee's own case and submitted judicial discipline requires that the same should be followed. He drew our attention to the provisions of section 10B(4) of the Act and highlighted the fact that deduction is allowed only on profits derived from export of articles or things. According to him, gain on foreign exchange forward contracts cannot be said to be derived from the business of export of articles or things. He also placed reliance on the decision of the Hon'ble Supreme Court in the case of *Liberty India, 317 ITR 218* wherein the concept of the words "derived from" was explained by the Supreme Court as immediate or direct nexus with the business of the assessee. It was also submitted by him that the transaction of foreign exchange forward contract entered into by the assessee was not a hedging transaction as it did not fall within the ambit of clause (a) of section 43(5) of the Act. In this regard, he submitted that only contracts in respect of raw materials or merchandise are covered under clause (a) and not foreign exchange forward contracts.

He also highlighted the fact that foreign exchange contract itself was done by the assessee in a systematic manner for a period of time and there is every reason to believe that it was a separate business which itself contradicts the provisions of section 28 of the Act.

17. The Id. DR relied on the following decisions in support of the revenue's case that the income derived from foreign exchange forward contracts cannot be regarded as income from business:-

(a) Shankara Infrastructure Materials Ltd. v. ACIT (2015) 53 taxmann.com 429, (Bang. Trib.)

(b) Araska Diamond (P.) Ltd. v. ACIT, 52 taxmann.com (Mumbai-Trib.)

18. Besides the above, the Id. DR also submitted that it will not be correct to say that foreign currency is not a commodity. According to him, foreign currency is used as a medium of exchange or valid legal tender. It could be regarded as a commodity. In this regard, our attention was drawn to the definition of 'commodity' as given in website www.investopedia.com, wherein it has been explained that some traditional examples of commodities would be grains, gold, beef, oil and natural gas. More recently, definition was extended to include financial products such as foreign currencies and indexes. The definition in website www.investorwords.com giving identical meaning was also placed before us.

19. It was also submitted by him that in all the cases cited by the Id. counsel for the assessee, there was nexus established between foreign exchange forward contracts and the export orders of the concerned assessee. According to him, in the present case, the assessee has not filed any documentary evidence to show nexus between exports made by it and foreign exchange forward contract.

20. The Id. AR, in his rejoinder, submitted that in the order of assessment, the AO has clearly recorded the fact that foreign currency forward contracts, although pertaining to assessee's own exports, cannot be treated as income derived from export of goods and merchandise. According to him, this finding of the AO is itself enough evidence that he had not disputed the fact that foreign exchange forward contracts was in relation to the exports made by the assessee. It was also pointed out by him that the expression "profits of the business" u/s. 10B means profits of the business of the undertaking which has a broader connotation.

21. We have given a very careful consideration to the rival submissions. The Assessee is engaged in the business of readymade garments. The Assessee realizes the export proceeds in foreign exchange. As a result of variation in the rates of foreign exchange, the Assessee might receive more or less than the contracted value in Indian rupee at the time of realization of export proceeds. In order to safeguard against such uncertainties, the Assessee enters into a forward contract in foreign exchange. The RBI

guidelines in regard to forward exchange contract provides that only entitles which export to other countries can book forward contracts. The contracts have to be based on actual orders on hand or based on orders in pipeline or based on past performance. The forward contract can be performed only by delivering export documents or export proceeds lying in EEFC accounts. On the delivery date, if the exporter is unable to deliver export documents or dollars from its EEFC account, the banker will cancel the contract and whatever is the difference between the contract rate and prevailing rate on the date of cancellation will be either paid to or received from the exporter from the exporter as the case may be. Cancellation of a contract due to non- delivery of the contracted amount on the due date may result in profit or loss as per the spot rate on due date. It is not in dispute that the forward contracts which resulted in gain to the Assessee were entered into in relation to export orders which the Assessee had procured.

22. In AY 06-07, on identical facts and circumstances, this Tribunal held that the gain or loss on forward contract in foreign exchange was "Speculative" in character and cannot be regarded as income derived from export business on which deduction u/s.10B of the Act can be allowed.

23. The CIT(A) in AY 06-07 had allowed the claim of the Assessee by placing reliance on *D. Kishore Kumar & Co. Vs. DCIT (2005) 2 SOT 769 (Mum.)* the decision of the ITAT Mumbai Bench in the case of wherein the question before the Hon'ble Tribunal was as to whether the profit on

cancellation of forward contract in foreign exchange was to be regarded as profits of the business on which deduction u/s.80HHC of the Act can be allowed. The Tribunal held that the imports in connection with which assessee had entered into forward contracts, actually took place, profit on cancellation of said contracts effectively only reduced costs of purchases in respect of these imports and could not be, by any logic, construed as transactions independent of Assessee's business. The Tribunal also held that even though the transactions had been settled without delivery, the conditions of Section 43(5) of the Act describing speculative transaction, were clearly fulfilled, but the requirement of Expln.-2 to Sec.28 was not fulfilled in as much as it could not be concluded that the transactions were of such a nature as to constitute a business by itself. The Tribunal explained that profit on cancellation of forward contracts is generally revenue neutral because the question of profit on cancellation of forward contracts can only arise in a situation when the value of foreign currency is increasing vis-à-vis domestic currency, and when the foreign exchange value is so increasing, the ultimate payment made in foreign currency was not to go up, there would not have been gains on cancellation of contracts but then the actual costs, in terms of domestic currency that the assessee pays when he has to pay for imports in foreign currency does not also go up.

24. The revenue challenged the order of CIT(A) for AY 06-07 and the same was considered by the ITAT Bangalore in ITA No.113/Bang/09 for AY

05-06 by order dated 7.8.2009. The Tribunal did not agree with the decision rendered by the Mumbai Bench in the case of *D.Kishore Kumar & Co. (supra)* on which the CIT(A) had placed reliance in allowing the claim of the Assessee. The Tribunal held :-

- (i) The forward contract was not settled by actually delivery and was therefore speculative transaction within the meaning of Sec.43(5) of the Act.
- (ii) Clause (a) to Sec.43(5) of the Act exempting hedging transactions from the purview of Sec.43(5) of the Act was not applicable to the case of the Assessee as it applied only when the contract is for actual delivery of goods manufactured or merchandise sold by an Assessee and “foreign Exchange is not goods manufactured or merchandise sold.
- (iii) In the decision rendered by the Mumbai Bench in the case of *D.Kishore Kumar & Co. (supra)*, the effect of Expln.-2 to Sec.28 of the Act was not considered.
- (iv) The tribunal in para 20 of its order further held that in the case of the Assessee there are a number of transactions and the forward contracts have been taken in respect of 46% of the export turnover. Thus, it is not an isolated transaction. Hence, in view of Expln.-2 to

Sec.28, the profit from the forward contract will have to be assessed as profit from speculation business.

- (v) In para 21 of its order the Tribunal held that deduction u/s.10B of the Act is to be allowed only on the profits of the business of the undertaking. "profit of the business of the undertaking" according to the Tribunal would be only profit from manufacture and export of readymade garments and not from gain on forward contract which has to be assessed as profits of "Speculation Business" separately.

25. The CIT(A) in the present assessment year to which this appeal relates to, followed the order of the ITAT and upheld the action of the AO in excluding the gain on forward foreign exchange contracts from the profits of the business on which deduction u/s.10B of the Act has to be allowed. Though the Tribunal in the order for AY 06-07 gave several reasons why deduction u/s.10B of the Act should not be allowed on gain on foreign exchange forward contract, the only basis given by the AO in the present AY 07-08 to which this appeal pertains, is that the gain on foreign exchange forward contract is not derived from the business of export of readymade garments. The AO has not assessed the said gain as "Speculative Income" but as regular "Business Income".

26. From the arguments advanced before us on the basis of several judicial pronouncements of various benches of ITAT, it becomes clear that there is an apparent conflict of judicial opinion on the question as to

whether the gain on forward foreign exchange contracts is to be regarded as Income from speculative business. None of the decisions rendered are in the context of the question as to whether such gain can be said to be profits derived from the business of export on which deduction u/s.10B of the Act has to be allowed.

27. The decisions where it was held that gain on forward foreign exchange contracts is to be regarded as Income from business, which were cited on behalf of the Assessee are as follows:

(i) *ITA No.1320/Bang/2012 for AY 09-10 M/S.Hanuman Weaving Factory Vs. ACIT order dated 23.8.2013.* In this decision the Tribunal distinguished the case of *K.Mohan & Co. (Assessee's case for AY 06-07* by observing that the issue therein was as to whether gain on forward foreign exchange contracts is to be regarded as Income derived from the business of export eligible for deduction u/s.10B of the Act. The Tribunal ultimately held that the gain in question was to be regarded as "Income from Business".

(ii) *London Star Diamond Company (I) Pvt.Ltd. Vs. DCIT (2013) 54(II)ITCL 254 (Mum"D"-Trib)*. In this decision also the ruling was that gain on forward foreign exchange contracts is to be regarded as Income from business and not income from speculative business u/s.43(5) of the Act.

(iii) *Star Exports & Imports Vs. ACIT ITA No.997/Bang/2012 (AY 09-10) order dated 6.2.2015.* In this decision the decision of the Hon'ble Gujarat High Court in the case of *Friends and Friends Shipping Pvt. Ltd. (2013) 217 Taxmann 267* was followed. In the aforesaid decision the revenue treated loss in forward contract in foreign exchange as speculative loss and did not allow set off of such loss against income from business. The Tribunal held that the loss was not speculative loss and the set off claimed by the Assessee had to be allowed. The Hon'ble High Court upheld the order of the Tribunal. This decision was referred to by the Tribunal in the order in the case of *Star Exports & Imports (supra)* and it was further observed that decision rendered by the Tribunal in the case of Assessee *K. Mohan & Co. for AY 06-07* pale into insignificance as the decision of the Hon'ble High Court has to be followed. The claim of the Assessee was accordingly upheld.

(iv) *Adani Enterprises Ltd. Vs. ACIT (2015) 55 Taxmann.com 375 (Ahd.-Trib):* In this case it was held that Sec.43(5) of the Act do not apply to currencies and therefore loss incurred by Assessee in currency swap contract cannot be denied to be set off against other heads of income taking it as speculative loss.

28. As can be seen from the above decisions referred to by the learned counsel for the Assessee, none of the decisions rendered are in the context of the question as to whether such gain can be said to be profits derived

from the business of export on which deduction u/s.10B of the Act has to be allowed. We are therefore of the view that the decision rendered in Assessee's own case in AY 06-07 is applicable, wherein the Tribunal took the view that deduction u/s.10B of the Act is to be allowed only on the profits of the business of the undertaking. "Profit of the business of the undertaking", according to the Tribunal, would be only profit from manufacture and export of readymade garments and not from gain on forward contract, has to be followed in the present AY also. As we have already observed, the AO has assessed the said gain as "Business Income" and therefore the decisions referred to above relied upon by the learned counsel for the Assessee are not relevant and helpful to the plea of the Assessee before us. In view of the above conclusions, we do not deem it necessary to elaborate on the arguments advanced by the learned counsel for the Assessee before us.

29. For the reasons given above, we dismiss ground No. 2 to 4 and ground No.7 raised by the Assessee before us.

30. Ground Nos. 5 & 6 raised by the assessee reads as follows:-

“5. The CIT(Appeals) ought not to have upheld the inclusion of inter unit job work charges for arriving at the total turnover of the EOU.

6. The CIT(Appeals) failed to appreciate that the inter unit job work charges represented job works carried out by one EOU by utilizing the facility available with it to the other EOU.”

31. As we have already seen the assessee is engaged in the manufacture of readymade garments for exports. The Assessee has two Export Oriented Units (EOUs) and other units which fall under Domestic Tariff Area (DTA). The manufacturing activity involves several processes which results in one EOU undertaking certain manufacturing process for the other EOU and such Inter Unit transactions, are permitted under the EOU regulations. Profits from both the EOUs are eligible for deduction u/s 10B. The assessee company has shown a break-up of the Turnover of all the units as under :-

	DTA	EOU I	EOU II	Total
Sales – Export (RMG & Samples)	15,16,20,901	193,69,48,059	139,87,61,923	348,73,30,383
Sales - Domestic	57,98,871	30,25,398	10,46,001	98,70,270
Labour Charges	6,75,188	-	-	6,75,188
Sale of Misc. items	1,22,54,744	21,01,187	8,03,684	1,51,59,615
Inter Unit Transfers (Tailoring/ Washing/EMB)	15,87,54,791	34,63,195	6,81,34,730	1,51,59,615
Total	32,91,04,495	194,55,37,839	146,87,338	351,30,35,956

32. The Assessee while computing deduction u/s.10B of the Act took the total turnover of EOU-I and EOU-11, at Rs. 194,20,74,644 and Rs. 140,06,11,608 respectively. The inter unit transfers were excluded from the total turnover. According to the AO the inter unit transfers were also to be regarded as part of the total turnover for the purpose of computing

deduction u/s.10B of the Act. The AO accordingly adopted total turnover of EOU-I and EOU-II is Rs. 194,55,37,839 and Rs. 146,87,46,338 respectively for the purpose of computing deduction u/s.10B of the Act.

33. The Assessee's stand was that the Inter Unit charges do not form part of the turnover and entries relating to these transactions have been made only with a view to arrive at the correct profits of the undertakings: These charges cannot be viewed separately and only the end result which is to be looked into, namely, the readymade garments which are exported which alone need to be reckoned for the purpose of arriving at Total Turnover figure. The Inter Unit charges are credited in one EOU and they are debited in another EOU. These charges are not recovered from any outsider. They do not affect the overall profit of the EOUs which remain the same. They are shown as two different EOUs as they are under different licenses. There will be no effect on the deduction as both the Units are claiming deduction under section 10B.

34. The AO, however, did not agree with the submissions of the Assessee. In this regard the AO referred to the provisions of Section 10B which reads as follows:-

“10B. (1) Subject to the provisions of this section, a deduction of such profits and gains as are derived by a hundred per cent export-oriented undertaking from the export of articles or things or computer, software for a period of ten consecutive assessment years beginning with the assessment year relevant to the pervious year in which the undertaking begins to manufacture or produce

articles or things or computer, software, as the case may be, shall be allowed from the total income of the assessee:

.....

.....

(4) For the purposes of sub-section (1), the profits derived from export of articles or things or computer software shall be the amount which bears to the profits of the business of the undertaking, the same proportion as the export turnover in respect of such articles or things or computer software bears to the total turnover of the business carried on by the undertaking.

Explanation 2 (iii) “export turnover” means the consideration in respect of export by the undertaking of articles or things or computer software received in, or brought into India by the assessee in convertible foreign exchange in accordance with sub-section (3), but does not include freight, telecommunication charges or insurance attributable to the delivery of the articles or things or computer software outside India or expenses, if any, incurred in foreign exchange in providing the technical services outside India.”

(emphasis supplied)

35. According to the AO, from a plain reading of Section 10B it was clear that the said provision provides deduction qua undertaking and not qua company. Hence, while arriving at the deduction for an undertaking, the profits of the undertaking have to be arrived at by considering the unit as the only existing business of the assessee. The same is done in most cases by maintaining separate books of accounts. This fiction of separate entity requires that every transaction done with an external entity, be it another unit of the same company or another company, be considered as external transaction and be included in the accounts of the unit accordingly.

It is precisely for this reason that the assessee has also maintained separate books for the Units and has indicated the inter-unit transfer of each unit. The expense incurred for doing the job work forms part of the expenditure booked in the accounts of the unit and hence exclusion of the inter-unit charges will provide for incorrect computation of the profits and also of the deduction u/s 10B.

36. According to the AO, the very fact that the section itself provides for the "Total turnover" (in sub-section (4)) and "Export Turnover (in sub-section (4) and in Explanation quoted supra) to be calculated for the undertaking, implies that the Act requires that they be calculated for the undertaking alone and not for the total business. The assessee's contention regarding commercial sense of "Turnover" is not relevant when specific definitions and manner of computation has been provided in the section.

37. The AO also took support for his conclusion from Form 56G which is required to be filed by the assessee, wherein the following particulars are required to be given:-

1. Name of the assessee:
2. Assessment year:
3. Name of the undertaking
4. Location and address of the undertaking
5. Nature of business of the undertaking
6. Date of initial registration in FTZ /EPZ / SEZ
7. Date of commencement of manufacture or production
8. Number of the consecutive year for which the deduction is claimed

9. Total turnover of the business
10. Total turnover of the undertaking
11. Total profits derived by the business
12. Total profits derived by the undertaking
13. Total export turnover

38. According to the AO, the Act envisages different Turnover for the business and the undertaking, and different profits for the business and the undertaking. The inter-units transfers will not be a part of the "Total Turnover" for the Assessee as a whole, but will definitely form a part of the Total Turnover for the undertaking. On considering business of the Unit/Undertaking independent of the Assessee, the inter-unit transfer acquires the character of sale. Hence, the same is includible as part of total turnover of the unit. The AO accordingly computed deduction u/s.10B of the Act by including inter-unit transfer as part of total turnover of the concerned unit which provided service to the other unit.

39. On appeal before the CIT(A), the assessee submitted that the word "turnover" is a commercial term and should be construed in the commercial sense and in accordance with the normal rules of accountancy. Accordingly, "turnover" means gross in-flow of cash receivables and other considerations arising in the course of ordinary activities of an enterprise from the sale of goods or from rendering of services to the buyer or client. In the assessee's case, inter-unit job work charges relate to the assessee only and there is no buyer. The Assessee relied on the guide to company

audit issued by the Institute of Chartered Accountants which states as follows:-

“Total turnover, that is, the aggregate amount for which sales are effected by the company, giving the amount of sales in respect of each class of goods dealt with by the Company and indicating the quantities of such sales for each class separately.

Note (i) The term “Turnover” would mean the total sales after deducting therefrom goods returned, price adjustments, trade discount and cancellation of bills for the period of audit, if any, adjustments which do not relate to turnover should not be made e.g. writing off bad debts, royalty, etc.”

40. The CIT(A) did not agree with the submissions of the assessee and he held as follows:-

”12. I see no merit in the above arguments of the A.R. The legislature was aware of such a predicament when this Section was drafted. Therefore, it made the Section a self-contained code. It specifically spoke as to computation of business profit of an undertaking and spoke of total turnover as well as export turnover of the undertaking. It is now well settled that total turnover is equal to export turnover plus domestic turnover.

This definition is now adopted by the ITAT Special Bench, Chennai, in the case of ITO Vs. Sak Soft Ltd. (2009) reported in 313 ITR 353. While deciding that case, the Learned ITAT followed the decision of the Hon’ble Supreme Court in the case of CIT Vs. Lakshmi Machine Works (2007) 290 ITR 667 (SC) wherein the Hon’ble Court held that since the term ‘turnover’ is in relation to ‘business profits’ only, it must include the receipts which only involves elements of profit. Based on such interpretation, it was held that reimbursement of expenditure has no element of profit and hence reimbursement of sales tax and Excise Duty do not form part of the total turnover. On the same ratio, the Hon’ble Supreme Court in the case of CIT Vs. Ravindranathan Nair (2007) 295 JTR 228 (SC) held that

processing charges received by the assessee EOU is includible in the total turnover as it included element of profit. Similar is the case here.

13. The receipt for doing job work from another EOU is nothing but its domestic turnover because the element of profit therefrom is not denied and only set off of job charges done for each other is claimed against each other. The A.R. probably treats "Sales" as a synonym of "turnover" and therefore pleads that none of EOUs can be considered as seller or buyer. Section 44AB of I.T.Act puts a coma in between the word "Sales" and "Turnover" to distinguish that both terms are distinct and have different connotations. Sales does not include goods returned, price discount etc., Turnover has a wider connotation. The word "or" interspersed between the words "turnover" and "gross receipts" in S-44AB of IT Act evinces that both can be used interchangeably and are synonymous. It includes all receipts even having no element of profit. Such is the interpretation of the term "Gross Receipts" by the Guidance Note issued by ICAAI reproduced below:-

The term 'gross receipts' is also not defined in the Act. It will include all receipts whether in cash or in kind arising from carrying on of the business which will normally be assessable as business income under the Act. Broadly speaking, the following items of income and/or receipts would be covered by the term gross receipts in business"

- (i) profits on sale of a licence granted under the Imports (Control) Order, 1955 made under the Imports & Exports (Control) Act, 1947;
- (ii) Cash assistance (by whatever name called) received or receivable by any person against exports under any scheme of the Government of India;
- (iii) Any duty of customs or excise re-paid or repayable as drawback to any person against exports under the Customs & Central Excise Duties Drawback Rules, 1995;
- (iv) The aggregate of gross income by way of interest received by the money lender;

- (v) Commission, brokerage, service and other incidental charges received in the business of chit funds;
- (vi) Reimbursement of expenses incurred (e.g. packing, forwarding, freight, insurance, traveling, etc.) and if the same is credited to a separate account in the books, only the net surplus on this account should be added to the turnover for the purpose of Section 44AB;
- (vii) The net exchange rate difference on export sales during the year on the basis of the guiding principle explained in (vi) above will have to be added;
- (viii) Hire charges of cold storage;
- (ix) Liquidated damages;
- (x) Insurance claims — except for fixed assets;
- (xi) Sale proceeds of scrap, wastage, etc. unless treated as part of sale or turnover, whether or not credited to miscellaneous income account;
- (xii) Gross receipts including lease rent in the business of operating lease;
- (xiii) Lease rent or interest on financing in the business of finance lease; and
- (xiv) Hire charges received in the case of hire purchase business and installments received in the case of installment sale. “

(underlined for emphasis)

Here even if it is acknowledged for arguments sake that the receipt for job work does not involve an element of profit, still it cannot be denied that the same is not receipt and therefore not includible in “total turnover”. The basic misunderstanding; I visualize, has crept in because the EOUs have been considered as two units of the same business and hence the claim of set off. The law is very clear on that issue. Each 100% EOU is notified separately by the competent authority and their profit / exemption

/ loss need to be computed separately. Each is independent and separate from the other for all purposes and therefore the job work done by each of them has to be included in the total turnover of that concern only for computation of exemption u/s. 10B of IT Act. I hold them includible in the turnover of respective EOUs even if both are owned by the same assessee. I hold that set-off is not liable to be given as per the provisions of Act because relief is to be computed qua undertaking and not company (vide supra).”

41. Aggrieved by the order of CIT(Appeals), the assessee has preferred the present appeal before the Tribunal.

42. The Id. counsel for the assessee drew our attention to the decision of Hon'ble Supreme Court in *CIT v. Punjab Stainless Steel Industries, 364 ITR 144 (SC)*. In the aforesaid decision, the question whether the sale of scrap should form part of the total turnover while computing deduction u/s. 80HHC of the Act came up for consideration. The assessee in that case was a manufacturer and exporter of stainless steel utensils. In the process of manufacturing of stainless steel utensils, some part of the steel which cannot be used or reused for manufacturing utensils remains unused, which is treated as scrap. The assessee sells the scrap in the local market. The income arising from sale of scrap is reflected in the profit & loss account of the assessee. While computing deduction u/s. 80HHC, the assessee did not include the sale proceeds of the scrap in the total turnover and was showing the same separately in the profit & loss account. According to the revenue, sale of scrap was also part of the turnover and

should be included in the total turnover. The Hon'ble Supreme Court on the above issue observed as follows:-

“Normally, the term “turnover” would show the sales effected by a business unit. In the course of business, in addition to the normal sales, the business unit may also sell some other things. In ordinary accounting parlance, as approved by all accountants and auditors, the term “sales”, when reflected in the profit and loss account, would indicate sale proceeds from sale of the articles or things in which the business unit is dealing. When other things like old furniture or a capital asset, in which the business unit is not dealing are sold, the sale proceeds therefrom would not be included in “sales” but would be shown separately. Sale proceeds from scrap may either be shown separately in the profit and loss account or may be deducted from the amount spent by the manufacturing unit on the raw material from which goods are manufactured. The raw material, which is not capable of being used for manufacturing the goods will have to be either sold as scrap or might have to be re-cycled or disposed of to someone who would re-cycle the scrap. When such scrap is sold, the sale proceeds of the scrap cannot be included in the term ‘turnover’. Therefore, the proceeds of such scrap would not be included in ‘sales’ in the profit and loss account of the assessee.

The situation would be different in the case of the buyer, who purchases scrap from the assessee and sells it to someone else. The sale proceeds for such a buyer would be treated as “turnover” for the simple reason that the buyer of the scrap is a person who is primarily dealing in scrap.

When a recognised body of accountants, such as the Institute of Chartered Accountants of India, after due deliberation and consideration publishes certain material one can rely upon it. The meaning given by the institute clearly denotes that in normal accounting parlance the word “turnover” would mean “total sales”. The sales would definitely not include scrap which is either to be deducted from the cost of raw material or is to be shown separately under a different head. There is no reason not to accept the meaning of the term “turnover” given by a body of Accountants, having a statutory recognition.

If all accountants, auditors, businessmen, manufacturers etc. are normally interpreting the term 'turnover' as sale proceeds of the commodity in which the business unit is dealing, there is no reason to take a different view."

43. According to the Id. counsel for the assessee, the inter-unit transfer between Unit-I & II in the present case would also be akin to sale of scrap. According to the Id. counsel for the assessee, the inter-unit transfers will only ultimately go to reduce the cost of sales of the assessee and need not be regarded as turnover of the unit providing inter-unit services. The Id. counsel for the assessee further drew our attention to the decision of the Special Bench ITAT in the case of *ITO v. Sak Soft Ltd., 313 ITR (AT) 353 (Chn.)*. In the aforesaid decision, the question for consideration before the Special Bench was, as to the meaning of total turnover and export turnover for the purpose of computing deduction u/s. 10B of the Act. The Special Bench observed as follows:-

“ To say that in the absence of any definition of “total turnover” for the purpose of “total turnover” for the purpose of section 10B, there is no authority to exclude anything from the expression as understood in general parlance would be wrong, as there has to be an element of turnover in the receipt if it has to be included in the total turnover. That element is missing in the case of freight, telecom charges or insurance attributable to delivery of the goods outside India and expenses incurred in foreign exchange in connection with the provision of technical services outside India. These receipts can only be received by the assessee as reimbursement of such expenses incurred by him. Mere reimbursement of expenses cannot have an element of turnover. It is only in recognition of this position that in the definition of “export turnover” in section 10B the aforesaid two

items have been directed to be excluded. Secondly, the definition of export turnover contemplates that the amount received by the assessee in convertible foreign exchange should represent “consideration” in respect of the export. Any reimbursement of the two items of expenses mentioned in the definition can under no circumstances be considered to represent “consideration” for the export of the computer software or articles or things. Thus the expression “total turnover” which is not defined in section 10B should also be interpreted in the same manner. Thus the two items of expenses referred to in the definition of “export turnover” cannot form part of the total turnover since the receipt by way of recovery of such expenses cannot be said to represent consideration for the goods exported since total turnover is nothing but the aggregate of the domestic turnover and the export turnover. In the formula prescribed by section 10B(4) the figure of export turnover has to be the same both in the numerator and in the denominator of the formula. It follows that the total turnover cannot include the two items of expenses recovered by the assessee and referred to in the definition of “export turnover”.

44. The Id. counsel for the assessee laid emphasis on the observations of the Special Bench wherein they have emphasized that mere reimbursement of expenses cannot have an element of turnover. He also emphasized that for a receipt to be called as turnover, there should be an element of income embedded in such receipt. When a receipt does not have an element of income embedded, then it cannot be called as turnover. According to him, the aforesaid decisions clearly lay down the proposition that inter-unit expenses incurred by one unit on behalf of the other unit cannot be considered as total turnover of the unit incurring the expenses in getting it reimbursed by the other unit. It was also pointed out by him that the unit providing services recognizes the expenses in the debit side of the

profit & loss account and also recognizes the receipt on the credit side of the profit & loss account, thereby having NIL effect on the profits as per the profit & loss account. The unit receiving the services claims the expenses incurred by the other unit as expenses and thereby profits of the unit receiving the benefit of services provided by the other unit gets reduced to that extent. It was his submission that there is no attempt on the part of the assessee in either of the units to either decrease the total turnover or increase the profits of the business, thereby discharging the claim for deduction u/s. 10B of the Act.

45. The Id. counsel for the assessee also made an alternate submission that when there are inter-unit transfers between the same assessee, then there cannot be any element of profit in such transfers and therefore the profit element of the unit captively consuming the services of other unit, its profit should be excluded while computing deduction u/s. 80HH of the Act. For the above proposition, Id .counsel for the assessee relied on the decision of the Hon'ble Madras High Court in *CIT v. Metal Powder Co. Ltd., (2012) 75 DTR 233 (Mad)*.

46. The Id. DR submitted that section 10B(7) of the Act provides that provisions of section 80IA(8) & (10) shall apply to the undertaking referred to in section 10B also. Section 80IA(8) of the Act provides for a situation where any goods or services held for the purpose of eligible business are transferred to any other business carried on by the assessee. In such

circumstances, it is provided therein that the cost as recorded in the books of account of eligible business should correspond to the market value of goods or services. According to him, therefore, the inter-unit services and the cost thereof should correspond to the market value. It is for this reason that the inter-unit services and the cost received by the unit rendering services should be taken as part of turnover of the unit rendering the services. In all respects, he placed reliance on the order of CIT(Appeals).

47. We have carefully considered the submissions of the learned counsel for the Assessee and the learned DR before us. As far as Grounds No.5 and 6 are concerned, they relate to the manner of computation of total turnover. The learned counsel for the Assessee placed strong reliance on the decision of the Hon'ble ITAT Special Bench in the case of *ITO Vs. Sak Soft Ltd. 313 ITR (AT) 353 (Chennai) (SB)*. The assessee in that case was engaged in the export of computer software entitled to deduction u/s.10B of the Act. While claiming deduction under s. 10B, the assessee has declared export turnover of Rs. 8,33,64,528. The details furnished by the assessee showed that it had incurred the following expenditure in foreign currency :-

(Rs.)	
1. Employer's NIC contribution	2,19,672
2. Salary at London office	20,92,763
3. Lodging expenses at London	6,263
4. Travelling expenditure	5,62,896
5. Professional charges at London office	25,462
Total	29,07,056

48. According to the AO, the aforesaid expenditure was to be excluded from the export turnover in terms of cl. (iii) of Explan. 2 below the section and accordingly he excluded the same from the export turnover and arrived at the export turnover at Rs. 8,04,57,472 (i.e., Rs. 8,33,64,528 minus Rs. 29,07,056). He further reduced the export turnover by Rs. 8,25,125 but that was for the reason that the inward remittances were not proved. He thus arrived at the export turnover at Rs. 7,96,32,347. The AO thereafter computed the deduction under s. 10B by applying the following formula prescribed by s. 10B(4) :-

$$\text{Deduction under s. 10B} = \frac{\text{Profits of the business} \times \text{Export turnover}}{\text{Total turnover}}$$

49. The profits of the business as computed by him came to Rs. 3,39,85,047. The figure of export turnover, as already seen, was taken at Rs. 7,96,32,347. The figure of total turnover was taken at Rs. 9,26,23,216.

The deduction was accordingly calculated at Rs. 2,92,18,474. The question before the Special Bench was as to whether the AO should have taken the figure of total turnover which is the denominator in the above formula at Rs. 8,97,16,160 i.e., after deducting the expenditure of Rs. 29,07,056 from the total turnover of Rs. 9,26,23,216.

50. The Special Bench held that as per cl. (iii) of Expln. 2 to s. 10B, freight, telecom charges and insurance attributable to delivery of goods outside India and expenses incurred in foreign exchange in providing technical services outside India have to be excluded from export turnover. On the basis of parity principle, same have to be excluded also from the total turnover though that expression has not been defined in the section. The Special Bench held that element of turnover is missing in these receipts and receipts are received by the assessee only as reimbursement of expenses incurred by it. Secondly, the definition of export turnover contemplates that the amount received by the assessee in convertible foreign exchange should represent "consideration" in respect of the export. Any reimbursement of the items of expenses mentioned in the definition can under no circumstances be considered to represent "consideration" for the export. Thus, the expression 'total turnover' should also be interpreted in the same manner and the said items of expenses cannot form part of total turnover. Expression 'total turnover' as defined in ss. 80HHE and 80HHF excludes freight, telecom charges, etc and expenses incurred in foreign exchange in providing technical services outside India. Statutorily

parity is maintained between export turnover and total turnover in these sections. Hence, there is no reason why such parity cannot be maintained between export turnover and total turnover in s. 10B. Words 'total turnover' appearing in various provisions of the Act should be construed in the same manner unless it leads to contextual inconsistencies or repugnancy. Therefore, for the purpose of applying the formula under sub-s. (4) of s. 10B, the freight, telecom charges or insurance attributable to the delivery of articles or things or computer software outside India or the expenses, if any, incurred in foreign exchange in providing the technical services outside India are to be excluded both from the export turnover and from the total turnover, which are the numerator and the denominator respectively in the formula.

51. In the case of *CIT Vs. Punjab Stainless Steel Industries 364 ITR 144 (SC)*, the Hon'ble Supreme Court had to answer a question as to whether scrap sale should be considered as part of the total turnover for the purpose of allowing deduction u/s.80HHC of the Act. The Assessee in the case before the Hon'ble Supreme Court was a manufacturer and exporter of stainless steel utensils. In process of manufacturing, some portion of steel, which could not be used or reused for manufacturing utensils, was treated as scrap. Assessee disposed of said scrap in local market and income arising from sale was also reflected in P&L account. For purpose of availing deduction u/s 80HHC, income from sale proceeds

of scrap was not included in total turnover but was shown separately in P&L account. Revenue submitted that sale proceeds from scrap should have been included in 'total turnover' as assessee was also selling scrap and that was also part of sale proceeds. High Court held that proceeds generated from the sale of scrap would not be included in 'total turnover'. On further appeal, the Hon'ble Supreme Court held to ascertain whether turnover would also include sale proceeds from scrap, one has to know the meaning of the term 'turnover'. The term 'turnover' has neither been defined in income tax Act nor has been explained by any of CBDT circulars. One has to look at meaning of term 'turnover' in ordinary accounting or commercial parlance. In simple words, word "turnover" would mean only amount of sale proceeds received in respect of the goods in which an assessee is dealing in. Sale proceeds from scrap may either be shown separately in P&L Account or may be deducted from amount spent by manufacturing unit on raw material, which was steel in case of assessee. Raw material, which was not capable of being used for manufacturing utensils would have to be either sold as scrap or might have to be re-cycled in form of sheets of stainless steel, if manufacturing unit is also having its re-rolling plant. If it is not having such a plant, the manufacturer would dispose of scrap of steel to someone who would re-cycle said scrap into steel so that said steel can be re-used. When such scrap is sold sale proceeds of scrap cannot be included in term 'turnover', since assessee unit was engaged primarily in manufacturing and selling of

steel utensils and not scrap of steel. Proceeds of such scrap would not be included in 'sales' in P&L Account of assessee. Since assessee was not primarily dealing in scrap but was a manufacturer of stainless steel utensils, only sale proceeds from sale of utensils would be treated as his "turnover". Meaning given by ICAI also clearly denotes that in normal accounting parlance the word "turnover" would mean "total sales" and said sales would definitely not include scrap material. Further intention behind enactment of s 80HHC was to encourage export so as to earn more foreign exchange. Legislature would surely like to give more benefit to persons who were making an effort to help nation in process of bringing more foreign exchange. View expressed by High Court was in conformity with normal accounting practice followed by traders. Proceeds generated from sale of scrap would not be included in 'total turnover'.

52. In the present case, the Assessee has two EOU's EOU-I and EOU II. Both the EOUs are manufacturing and exporting readymade garments. Let us assume that the process of manufacture of readymade garments involves 4 different activities say, washing cloth, cutting cloth, stitching and packing. Depending on work load some activity will be undertaken by one EOU on behalf of the other EOU. Say EOU-I will undertake the job of washing for EOU-II. The charges attributable to the said activity are debited in EOU-I Profit and Loss account and the receipt from EOU-II by way of reimbursements are recorded in the credit side of the profit and loss account. Thus as far as EOU-I is concerned, there the effect is neutral. As

far as EOU-II is concerned, the expenditure incurred by EOU-I for washing is recognised in the Profit and Loss account. Thus the profits of EOU-II are not inflated. Therefore by the process adopted by the Assessee there is no effect on the true profits from the business of both the EOUs for the purpose of allowing deduction u/s.10B of the Act. The question is should EOU-I recognise the services rendered by it to EOU-II as its 'turnover'. The Assessee is a manufacturer of readymade garments and does not do the activity of washing. As explained by the Hon'ble Supreme Court in the case of *Punjab Stainless Steel Industries (supra)* the term 'turnover' has neither been defined in the Act nor has been explained by any of the CBDT circulars. One has to look at the meaning of the term 'turnover' in ordinary accounting or commercial parlance. In ordinary accounting parlance, as approved by all accountants and auditors, the term 'sales', when reflected in the Profit and Loss Account, would indicate sale proceeds from sale of the articles or things in which the business unit is dealing. When some other things like old furniture or a capital asset, in which the business unit is not dealing are sold, the sale proceeds therefrom would not be included in 'sales' but it would be shown separately. The reasoning adopted by the CIT(A) in the present case is that "Sales" and "Turnover" are not synonymous. According to him the word "Sale" and "Turnover" as used in Sec.44AB of the Act reveals the intention of the legislature in this regard. According to him the term "Turnover" would include have a wider connotation and would also include inter-unit sales. According to him there

would have been an element of profit in the inter unit services to the unit providing service to the other unit. Factually it has not been demonstrated so. The CIT(A) has also proceeded to hold that even assuming that there was no profit element, yet such receipts have to be considered as includible in "total turnover". We do not think that the above reasoning can be adopted in the context of the provisions of Sec.10B of the Act. In any event, the approach of the Hon'ble Supreme Court in the case of *Punjab Stainless Steel Industries (supra)*, clearly suggests that the "total turnover" should be only in relation to the business of the Assessee which in this case is manufacture and sale of garments. Had garments been sold locally by either of the units than they were to be included in the "Total Turnover". Keeping in mind the facts and circumstances of the present case and the precedents on which the learned counsel for the Assessee has placed reliance, we are of the view that the inter unit transfer should not be treated as part of the "Total Turnover" while computing deduction u/s.10B of the Act. We hold accordingly and allow the relevant ground of appeal of the Assessee.

53. In the result, the appeal by the assessee is partly allowed.

ITA 1266/B/2010

54. This appeal by the assessee is against the order dated 9.9.2010 of the CIT(Appeals)-I, Bangalore, relating to A.Y. 2007-08.

55. The assessee has filed concise grounds of appeal, of which ground No.2 is with regard to the inclusion of inter-unit job work in the total turnover of the assessee while computing deduction u/s. 10B of the Act. This issue is identical to grounds 5 & 6 raised by the assessee in ITA No.1093/Bang/2009. For the reasons stated therein, we allow the claim of the Assessee in this regard.

56. Ground No.3 of the concise grounds is with regard to action of the CIT(Appeals) in upholding the disallowance of employees contribution to ESI payments by invoking the provisions of section 43B of the Act. The AO was of the view that the assessee company has belatedly paid the employees' contribution for ESI and therefore an amount of Rs.8,46,458 was added u/s. 2(24)(x) r.w.s. 36(1)(va) of the Act.

57. The assessee raised a specific ground of appeal challenging the addition made by the AO as aforesaid viz., ground No.7 before the CIT(A). The CIT(A) has, however, not addressed the issue in the impugned order. At the time of hearing, it was brought to our notice that the issue in the aforesaid ground of appeal is squarely covered by the decision of the Hon'ble High Court of Karnataka in *Spectrum Consultants (India) Pvt.Ltd. Vs. CIT, (2013) 34 Taxman.com 20* wherein it was held that if the employees contribution to ESI is paid on or before the due date for filing return of income u/s. 139(1), then the same cannot be disallowed. The AO is therefore directed to verify if the employees contribution to ESI has been

paid by the assessee within the time limit as laid down in the aforesaid decision of the Hon'ble High Court of Karnataka and allow the claim of the assessee, if it is found to be in accordance with the said decision.

58. The Id. counsel for the assessee also made a prayer for adjudication of ground No.12 (1) & 12(2) as raised by the assessee in the original grounds of appeal which are with regard to the action of the revenue authorities in treating the gain on foreign exchange contracts as income not derived from the export business and therefore not eligible for deduction u/s. 10B of the Act. We may also mention that the assessee did not specifically raise a ground of appeal before the CIT(A) on the above issue. According to the Id. DR, the issue therefore should not be considered for adjudication. We are, however, of the view that the powers of the Tribunal to entertain a ground arising out of the assessment proceedings cannot be curtailed. We therefore entertain for adjudication ground Nos.12(1) & 12(2) of the original grounds of appeal. This issue is identical to ground Nos.2, 3, 4 & 7 raised by the assessee in ITA No.1093/Bang/2009. For the reasons stated therein, the action of the revenue authorities is upheld and the relevant grounds are dismissed.

59. In the result, the appeal by the assessee is partly allowed.

ITA No.1057 & 1103/Bang/2012

60. ITA 1057/12 is an appeal by the assessee, while ITA 1103/12 is an appeal by the Revenue. Both these appeals are directed against the order dated 19.6.2012 of the CIT(Appeals)-I, Bangalore, relating to A.Y. 2008-09.

ITA 1057/12

61. We shall first take up for consideration appeal by the assessee. Ground No.2 is identical to ground Nos.2, 3, 4 & 7 raised by the assessee in ITA No.1093/Bang/2009. For the reasons stated therein, the action of the revenue authorities is dismissed.

62. Ground No.3 raised by the assessee reads as follows:-

“3. The learned CIT(A) is not justified in upholding the taxation of long term capital gains at the rate of @0% instead of 10% under the facts and in the circumstances of the appellant’s case.”

63. The assessee during the previous year had sold units of mutual fund and derived long term capital gain of Rs.43,73,000. The assessee had claimed long term capital gain as exemption u/s. 10(38) of the Act. Since the assessee had not paid Securities Transaction Tax (STT) on sale of units of mutual funds, the claim for exemption us. 10(38) of the Act was not available to the assessee. The said sum was accordingly brought to tax @ 20% by the AO. Before the CIT(Appeals), the assessee submitted

that it had not claimed indexation benefits under the second proviso to section 48 of the Act and therefore rate of tax on long term capital gain should be 10% and not 20% as levied by the AO. The CIT(A) did not discuss this issue, nevertheless, he upheld the order of the AO. Aggrieved by the order of CIT(A), the assessee has raised ground No.3 before the Tribunal.

64. We have heard the submissions of the Id. counsel for the assessee and the Id. DR. Section 112(1) reads as follows:-

Tax on long-term capital gains.

112. (1) Where the total income of an assessee includes any income, arising from the transfer of a long-term capital asset, which is chargeable under the head "Capital gains", the tax payable by the assessee on the total income shall be the aggregate of,—

(a) in the case of an individual or a Hindu undivided family, [being a resident,]—

(i) the amount of income-tax payable on the total income as reduced by the amount of such long-term capital gains, had the total income as so reduced been his total income ; and

(ii) the amount of income-tax calculated on such long-term capital gains at the rate of twenty per cent :

Provided that where the total income as reduced by such long-term capital gains is below the maximum amount which is not chargeable to income-tax, then, such long-term capital gains shall be reduced by the amount by which the total income as so reduced falls short of the maximum amount which is not chargeable to income-tax and the tax on the balance of such long-term capital gains shall be computed at the rate of twenty per cent;

(b) in the case of a [domestic] company,—

(i) the amount of income-tax payable on the total income as reduced by the amount of such long-term capital gains, had the total income as so reduced been its total income ; and

(ii) the amount of income-tax calculated on such long-term capital gains at the rate of [twenty] per cent :

65. It can be seen from the aforesaid proviso that if the benefit of indexation is not claimed under second proviso of section 48, then the rate of tax on long term capital gain will only be @ 10%. In the present case, neither the AO nor the CIT(A) has examined the question as to whether the benefit of indexation was claimed by the assessee or not. We therefore set aside the order of the AO for fresh consideration in the light of the provisions of law referred to above, after affording opportunity of being heard to the assessee.

66. In the result, the appeal by the assessee is accordingly partly allowed.

ITA 1103/12

67. The only issue that arises for consideration in the revenue's appeal is as to whether the CIT(Appeals) was justified in directing the AO to compute deduction u/s. 10B on the profits of EOU Unit-II without adjusting the losses of EOU Unit-I from the "profits and gains of business /

profession” before computing such deduction, without appreciating the facts and circumstances of the case.

68. The assessee has two 100 EOUs. The AO found that the EOU-I and SEZ units suffered losses. The assessee claimed relief u/s 10B in respect of the income earned by its profit-making EOU i.e. Unit-II without aggregating the income and losses of all its units. Quoting section 2(45) of the Act for determining the total income of the assessee and the decision of the Hon'ble High Court of Karnataka in the case of *CIT v. Himmatsingike Seide Ltd (286 ITR 255)*, the AO held that the aggregate of the income and losses of all the units of the assessee had to be taken into account for calculating the deduction u/s 10B of the Act. Besides, the AO found from the assessee's submissions during the assessment proceedings that the long-term capital gains of Rs.43,73,000/- in respect of which exemption u/s 10(38) had been claimed actually related to debt funds in respect of which no STT had been made. Taking into consideration all these factors, the AO held that the assessee was not entitled to exemption u/s 10B in respect of the profit of EOU-II and has also assessed long-term capital gains of Rs.43,73,000/- arising from the sale of debt funds and brought the same to tax.

69. Aggrieved, the assessee preferred appeal before the first appellate authority on the following relevant grounds of appeal:-

“2(A) The learned A.O. has erred in denying the deduction u/s 10B of the Act to which the appellant is legitimately entitled to while computing the assessment of the appellant.

2(B) The denial of deduction is on the erroneous appreciation of the position of law .and on misplacing reliance on the ratio of the decision of the Karnataka High Court reported in 286 ITR 255 which is inapplicable to the facts of the case.

3. Without prejudice to the above, apart from the denial, the learned A.O. ought to have granted a greater deduction u/s 10B of the Act, although not specifically claimed for by considering the profits appertaining to the income from the cancellation (of) forward contracts of 100% EOU units.

4. The learned A.O. has erred in subjecting the long term capital gains at 20% instead of 10% in accordance with law.”

70. The assessee made the following submissions in the Statement of Facts accompanying the appeal memo on this issue before the CIT(Appeals):-

“4 It is the submission of the appellant that the profits from the export unit, which are entitled to deduction u/s 10B of the Act, while computing the deduction as ascribed to such unit should be considered on standalone basis in terms of the provision of section 10B of the Act. The learned A.O. relied on the decision of the Karnataka High court in the case of CIT V. Himatasingike Seide Limited reported in 286 ITR 255, which is altogether on different fact, situation and for different legal proposition. It is not the case of the appellant at all while computing the gross total. income, the income or loss from all the units including EOU units, in respect of which deduction is claimed should not be included. Even if the income from all the EOU units including the unit in respect of which deduction u/s 10B of the Act, is claimed there is still gross total income and so long there is a positive gross total income deduction u/s 10B of the Act, in respect of the unit has to be given. In the instant case of the appellant there is positive gross total income after

considering all the losses and the deduction claimed u/s 10B of the Act is far less than the gross total income and it is calculated in accordance with the provisions of the Act in fact by committing an error in favour of the revenue, as the appellant committed a mistake while calculating the deduction in excluding the income from forward contracts relating to the export unit as not export income and consequently, not eligible to deduction u/s 10B of the Act. However, such income has been taxed under the head business itself and not under the head other sources or not as appertaining to or dehors to that EOU unit. The learned A.O. after having accepted as business income of the export unit ought to have given greater deduction in accordance with law by not restricting to the amount as claimed by the appellant and granted greater deduction whereas, even the restricted deduction claimed he denied it unreasonably.”

71. The Id. CIT(Appeals) on a consideration of the submissions of the assessee held that the issue under consideration was covered in favour of the assessee by the decision of the Hon'ble High Court of Karnataka in the case of *CIT & Another v. Yokogawa India Ltd.* 341 ITR 385. Therefore, he directed the AO to follow the decision and recompute the deduction u/s 10B accordingly. Aggrieved by the order of the CIT(A), the revenue has filed the present appeal before the Tribunal.

72. At the time of hearing of this appeal, the Id. counsel for the assessee filed before us the decision of the Bangalore Bench of the Tribunal in *Mindtech India Ltd. v. ITO*, ITA No.1054/Bang/2013, order dated 4.7.2014, wherein the issue was whether section 10B is an exemption provision under Chapter III or a deduction under Chapter VIA of the Act was considered and this Tribunal took the view that the provisions

are exemption provisions and therefore loss of EOU or other units will not enter the computation of total income at all. In fact, the CIT(A) has followed the decision of the Hon'ble High Court of Karnataka in *CIT v. Yokogawa India Ltd., 341 ITR 385*, wherein it was held that section 10A and 10B are exemption provisions and therefore income of such units have to be excluded at source itself before arriving at GTI and since income is not to be included in the income of the assessee at all, there is no occasion to set off losses of the assessee in respect of its other business against profits of the exempt unit. Following the aforesaid decision of the Hon'ble High Court of Karnataka, we uphold the order of the CIT(Appeals) and dismiss the appeal by the Revenue.

73. In the result, ITA 1057/B/12 is partly allowed and ITA 1103/B/12 is dismissed.

74. To sum up, the appeals by the Assessee are partly allowed and the appeal by the Revenue is dismissed.

Pronounced in the open court on this 24th day of April, 2015.

Sd/-
(JASON P. BOAZ)
Accountant Member

Sd/-
(N.V. VASUDEVAN)
Judicial Member

Bangalore,
Dated, the 24th April, 2015.

/D S/

Copy to:

1. Assessee
2. Revenue
3. CIT
4. CIT(A)
5. DR, ITAT, Bangalore.
6. Guard file

By order

Assistant Registrar/
Senior Private Secretary
ITAT, Bangalore.