

**IN THE INCOME TAX APPELLATE TRIBUNAL
DIVISION BENCH 'A', CHANDIGARH**

BEFORE SHRI SANJAY GARG, JUDICIAL MEMBER
AND MS. ANNAPURNA GUPTA, ACCOUNTANT MEMBER

ITA No.1184/Chd/2016
(Assessment Year : 2013-14)

&

ITA No.734/Chd/2017
(Assessment Year : 2014-15)

Innova Captab,
Plot No.81B, EPIP,
Phase 1, Jhamajri

Vs.

The D.C.I.T.,
Circle Parwanoo.

PAN: AAFV6014N
(Appellant)

(Respondent)

Appellant by : Shri Tej Mohan Singh, Adv.

Respondent by : Shri Gulshan Raj, CIT DR

Date of hearing :19.04.2018

Date of Pronouncement :04.05.2018

ORDER

PER ANNAPURNA GUPTA, A.M. :

Both the above appeals have been preferred by the assessee against separate orders of Ld. Commissioner of Income Tax (Appeals), Shimla (hereinafter referred to as ('Ld.CIT(Appeals)') dated 15.9.2016 and 23.2.2017 relating to assessment years 2013-14 and 2014-15 respectively.

2. It was common ground that the issues involved in both the appeals were identical, therefore they were heard together and are being disposed off by this common order. For the sake of convenience, we shall be dealing with the facts in ITA No.1184/Chd/2016 relating to assessment year 2013-14.

ITA No.1184/Chd/2016:

3. Ground No.1 raised by the assessee reads as under:

“1. That the order passed by the Learned CIT (Appeals) Shimla has erred on Law and on the facts of the case and is not justified in upholding the disallowance of the deduction claimed by the appellant at 100% u/s 80IC and allowing only 25% and thus rejecting the claim of the firm that it is eligible for 100% deduction after making the substantial expansion on 26-03-2010.”

4. The above ground challenges the restriction of deduction claimed by the assessee u/s 80IC of the Income Tax Act 1961 (in short ‘the Act’), at 100% of the eligible profits on account of substantial expansion undertaken by it, to 25% of the eligible profits .

5. Briefly stated, the assessee firm is engaged in the manufacturing of Pharmaceuticals items such as Capsules, Tablets, Ointment etc and is eligible to claim deduction u/s 80IC of the Act. As per the information given in Form No. 10CCB filed for the year under assessment, the assessee started its business activity/operation on 16/10/2006 and initial assessment year for claim of deduction u/s 80IC of the Act was mentioned as assessment year 2007-08. The Assessing Officer noticed that the assessee had also claimed to have undertaken substantial expansion during the financial year 2009-10 and on the basis of said substantial expansion, it has claimed 100% deduction u/s 80IC by claiming assessment year 2010-11 to be the initial assessment year. The Assessing Officer held that in view of the provisions of section 80IC of the Income Tax Act, 1961, the assessee firm had already claimed deduction u/s 80IC of the Act at the rate of 100% for five years from assessment years 2007-08 to 2011-12 i.e. from the date of setting up of the industrial undertaking and in view of the

same, it would be eligible for claim of deduction @ 25% of its eligible business profits for the remaining five years. The AO therefore denied the claim of 100% deduction on the basis of the substantial expansion as claimed by the assessee and restricted the same to 25% of eligible profits for the assessment year under consideration.

6. The Ld.CIT(Appeals) upheld the order of the Assessing Officer on this ground following the decision of the ITAT Chandigarh Bench in the case of Hycron Electronics Vs ITO in ITA No. 798/CHD/2012 dated 27.5.2015.

7. During the course of hearing before us, the Ld.Counsel for the assessee pointed out that the decision of the I.T.A.T. in the case of Hycron Electronics (supra), following which the assessee's claim of deduction u/s 80IC had been restricted to 25% of the eligible profits, had been reversed by the Hon'ble Jurisdictional High Court in a bunch of cases including Hycron Electronics (supra), with the lead case being Stovekraft India vs CIT ITA No.20/2015 dt.28th November 2017.. The Ld. counsel for assessee pointed out that the Hon'ble High Court in the said case had categorically held that even new undertakings, established after the provisions of section 80IC came on the Statute w.e.f. 1.4.2004, were entitled to claim deduction @100% of the profits, on account of substantial expansion undertaken thereafter, as per the definition of the same in the said section and further pointed out that it was categorically held by the Hon'ble

High Court that the deduction @ 100% need not be restricted up to a period of five years only as interpreted by the I.T.A.T. in the case of Hycron Electronics (supra) and can be claimed for the entire period of 10 years eligible for deduction. The Ld. counsel for assessee drew our attention to the relevant findings of the Hon'ble High Court in this regard at para 55 of its order as under:

Thus, in view of the above discussion, these appeals are allowed and orders passed by the Assessment Officer as well as the Appellate Authority and the Tribunal, in the case of each one of the assessees, are quashed and set aside, holding as under:

(a) Such of those undertakings or enterprises which were established, became operational and functional prior to 7.1.2003 and have undertaken substantial expansion between 7.1.2003 upto 1.4.2012, should be entitled to benefit of Section 80-IC of the Act, for the period for which they were not entitled to the benefit of deduction under Section 80-IB.

(b) Such of those units which have commenced production after 7.1.2003 and carried out substantial expansion prior to 1.4.2012, would also be entitled to benefit of would also be entitled to benefit of deduction at different rates of percentage stipulated under Section 80-IC.

(c) Substantial expansion cannot be confined to one expansion. As long as requirement of Section 80-IC(8)(ix) is met, there can be number of multiple substantial expansions.

(d) Correspondingly, there can be more than one initial Assessment Years.

(e) Within the window period of 7.1.20013 upto 1.4.2012, an undertaking or an enterprise can be entitled to deduction @ 100% for a period of more than five years.

(f) All this, of course, is subject to a cap of ten years. [Section 80-IC(6)].

(g) Units claiming deduction under Section 80-IC shall not be entitled to deduction under any other Section, contained in Chapter VI-A or Section 10A or 10B of the Act [Section 80- IB(5)].

8. The Ld. DR fairly conceded that the issue stands decided in favour of the assessee in view of the decision of the Hon'ble Jurisdiction High Court i.e. Himachal Pradesh High Court in favour of the assessee.

In view of the above, since the issue of claim of deduction u/s 80IC on account of substantial expansion undertaken having been decided in favour of the assessee by the jurisdictional High Court, holding the eligibility of the said claim at the rate of 100% of the profits, and the facts in the present case undisputedly being that the assessee is eligible for deduction u/s 80IC of the Act, and had carried out substantial expansion of its undertaking in F Y 2009-10 ,relevant to A.Y 2010-11, respectfully following the decision of the Hon'ble High Court, we hold that the A.Y 2010-11 is to be treated as initial assessment year making the assessee eligible to deduction @100% of its profits thereafter upto the prescribed period which includes admittedly the impugned assessment year also i.e A.Y 2013-14 .

Ground of appeal No.1 raised by the assessee, therefore, stands allowed.

9. Ground of appeal No.2 raised by the assessee reads as under:

"2. That the order passed by the Learned CIT (Appeals) Shimla has erred on Law and on the facts of the case and is not justified in upholding the disallowance of Rs.6,36,887/- as business profit on account of Interest on FDR's pledged with bank as margin money for making Letter of Credit (LC) for making the purchases and income from Drug License Fee and thus disallowing the deduction u/s 80IC on the same."

10. Brief facts relevant to the issue are that on perusal of the Profit & Loss Account, the Assessing Officer noticed that the assessee had credited an amount of Rs.3,41,987/- under the head 'Interest accrued on FDR and Others' and Rs.2,94,900/- under the head 'Drug License Fee' and had also claimed deduction u/s 80IC of the Act on these receipts. When confronted, the assessee submitted that the said income was consequential to its business and hence, deduction u/s 80IC of the Act was rightly claimed on the same. The contention of the assessee was not found to be acceptable by the Assessing Officer in the absence of first degree nexus of the said incomes with the business of the assessee and in view of the judgement of the Hon'ble Supreme Court in the case of M/s Liberty India Ltd. Vs. CIT (317 ITR 218) and Pandian Chemicals Ltd. vs. CIT (SC)262 ITR 278 in this regard. The Assessing Officer accordingly held the amount of 6,36,887/- as ineligible for the claim of deduction u/s 80IC.

11. The Ld.CIT(Appeals) upheld the order of the Assessing Officer following the decision of the ITAT Chandigarh Bench in the case of Hycron Electronics (supra). The relevant findings of the Ld.CIT(Appeals) at para 5.3.2 are as under:

“5.3.2 During appellate proceedings, assessee submitted that the interest has been earned on FDR for letter of credit and bank guarantees with is part and parcel of income of industrial undertaking having direct nexus. Assessee's contention that these FDRs are essential for business, thus, interest on these FDRs should be treated as income of the industrial undertaking is not acceptable as the income on these FDRs does not have a first degree nexus to manufacturing activity to make it eligible for deduction u/s 80IC. The term business has different meaning than manufacturing. Moreover as per specific

provisions u/s 56 of Income Tax Act, the Interest earned on securities shall be chargeable as 'income from other source'. The moot question is whether the income referred supra is derived from manufacturing activity or not. The appellant has failed to establish the first degree nexus with the manufacturing activity. The assessee failed to discharge the primary onus with sufficient evidence.

Further the ITAT Chandigarh while deciding similar issue of deduction u/s 80IC in the case of Hycron Electronics and other group of cases, in ITA 374/Chd/2014- A.Y.2010-11 considered inter alia the following ground of appeal:

3. Under the facts and circumstances of the case and in law, *id. CIT(Appeals), Shimla* has erred in affirming the order of Ld. ITO, Baddi in restricting the appellant's claim of Other Income of Rs.19,75,825/-being eligible for deduction U/s 80IC of the IT Act, 1961.

The ITAT while deciding this ground of appeal held as under:

54. Ground No.3 : After hearing both the parties we find that during assessment proceedings the Assessing Officer noticed that assessee has shown other income; amounting to Rs. 19,75,825/- as per the following details:-

Particulars	Amount(Rs.)
Interest received on Margin	2,85,876/-
Interest received on	70,3287-
Foreign Exchange	75,46,066/-
Miscellaneous Income	73,542/-
Sundry Credit balances written	13/-
Total	79,75,825/-

On this income the assessee has claimed deduction u/s 80IC.It was observed by Assessing Officer that this income has not been derived from the Industrial Undertaking and does not have first degree nexus with the manufacturing activity. Therefore, assessee was asked to justify the claim u/s 80IC of the Act against this income. In response it was stated that income was eligible for deduction u/s 80IC of the Act. The Assessing Officer referred to the decision of Hon'ble Supreme Court in the case of *Pandian Chemicals Ltd Vs. CIT 262 ITR 278 (SC)* and *Liberty India Ltd v CIT 317 ITR 218* and disallowed the claim of deduction against other income. The action of the Assessing Officer was confirmed by Ld. CIT(A)

.....

58. After considering the rival submissions carefully we find that Hon'ble Supreme Court in the case of *Pandian Chemicals Ltd Vs. CIT (supra)* was concerned with the issue of deduction u/s 80HH on interest income received on electricity deposit made by the

assesses. On this issue, the following observations were made:-

The words "derived from" in section 80HH of the Income-tax Act, 1961, must be understood as something which has a direct or immediate nexus with the assessee's industrial undertaking. Although electricity may be required for the purposes of the industrial undertaking, the deposit required for its supply is a step removed from the business of the industrial undertaking.

59. After the above observation, it was held as under:-

"Held accordingly, that interest derived by the industrial undertaking of the assessee on deposits made with the Electricity Board for the supply of electricity for running the industrial undertaking could not be said to flow directly from the industrial undertaking itself and was not profits or gains derived by the undertaking for the purpose of the special deduction under section 80HH."

60. Same view was taken later on in the case of *Liberty India Ltd v CIT (supra)*. It may be noted that that expression 'derived from' has been used in section 80IC also, therefore, as far as interest received on margin money and Interest received on other amounting to Rs.2,85,876/- and Rs.70,328/- are not entitled for deduction u/s 80IC and accordingly we confirm the action of the Assessing Officer and CIT(A) in this respect. (Emphasis added).

5.1.4 *Respectfully following the decision of the jurisdictional ITAT in the matter and placing reliance on the decision of the Apex Court in the case of Liberty India and others referred supra, the action of the AO is upheld with regards to the interest income referred supra. Similar analogy holds true for the Drug Licence fee received . The amount received on account of Drug Licence has no nexus with manufacturing activity. Accordingly, this ground of appeal of the appellant is dismissed."*

12. Before us, the Ld. counsel for assessee reiterated the contentions made before the lower authorities that the interest was earned on FDRs for letter of credit and bank guarantee and the drug licence fee received was on account of sale of the same and both had direct nexus with activity undertaken by the assessee.

13. The Ld. DR, on the other hand, relied upon the order of the Ld.CIT(Appeals) pointing out therefrom that in the

absence of any first degree nexus between the said incomes and the manufacturing activity of the assessee, the same were not eligible for deduction u/s 80IC as held by the Hon'ble Apex Court in the case of Pandian Chemicals Ltd. Vs. CIT 262 ITR 278 (SC) and M/s Liberty India Ltd. Vs. CIT 317 ITR 218 (SC).

14. We have heard rival contentions. We find no merit in the present ground raised by the assessee. There is no infirmity in the order of the Ld.CIT(Appeals) in this regard. The issue being claim of deduction u/s 80IC of the Act on interest earned on FDRs and drug licence fee sold, it is settled law that the deduction under the said section is available only on incomes which have direct nexus/ first degree nexus with the manufacturing activity of the assessee. The interest earned on FDRs is on account of investments of funds made in FDRs and so also the income earned from sale of drug licence is directly attributable to the drugs licence owned by the assessee. There is clearly no nexus of both the said incomes with the manufacturing activities of the assessee. Neither has the Ld. counsel for assessee been able to demonstrate the same either before the lower authorities or even before us. In view of the same, we hold that the Ld.CIT(Appeals) has rightly denied the claim of deduction on the said two incomes following the decision of the Hon'ble Apex Court in the case of Pandian Chemicals Ltd. (supra) and M/s Liberty India Ltd. (supra). In view of the above, ground No.2 raised by the assessee is dismissed.

15. Ground of appeal No.3 raised by the assessee reads as under:

“3. *That the order passed by the Learned CIT (Appeals) Shimla has erred on Law and on the facts of the case and is not justified in upholding the disallowance of Rs.1,67,933/- interest u/s 36(1)(iii) of the Income Tax Act, 1961 being the assumptive interest on the advances given by the appellant as business profit on account of Interest on FDR's pledged with bank as margin money for making Letter of Credit (LC) for making the purchases and income from Drug License Fee and thus disallowing the deduction u/s 80IC on the same.*”

16. The above ground relates to disallowance of interest made u/s 36(1)(iii) of the Act.

17. Brief facts relevant to the issue are that during the assessment proceedings, the Assessing Officer noticed that assessee firm had advanced a sum of Rs.1,12,32,790/- as interest free loans to relatives/friends of directors. The amount advanced for varying periods as detailed in the assessment order was advanced to M/s. Asian Packages (Rs.10,00,000), M/s Vision Airtech (Rs.2,32,790/-) and Rohit Lohriwala (Rs.1,00,00,000/-) with whom no business connection had been established. Simultaneously, the assessee had claimed a deduction of Rs.97,02,299/- as financial charges including interest paid to banks and others. The assessee was asked to justify the interest free advances/loans given without any business expediency whereas the assessee was paying interest on the borrowed capital. The explanation given by the assessee was considered by the Assessing Officer and thereafter, relying

on the judgment of Hon'ble Punjab and Haryana High Court in the case of M/s Abhishek Industries Vs. CIT, 286 ITR 1, he disallowed proportionate interest on the impugned interest free loans advanced. Accordingly, interest on the above amounts was computed at Rs.1,67,933/- and added to the total income of the assessee.

18. The Ld.CIT(Appeals) upheld the disallowance so made but at the same time, directed the Assessing Officer to allow deduction u/s 80IC of the Act on the corresponding increased business income on account of the said disallowance.

19. The Ld. DR during the course of hearing before us pointed out that the assessee in any case has been allowed deduction u/s 80IC on the said disallowance made and, therefore, no prejudice was caused to the assessee. The Ld. counsel for assessee agreed to the same but at the same time relied on the contentions made before the AO for allowability of the claim of interest expenditure.

20. Considering the above and considering our findings on ground No.1 raised by the assessee before us, allowing the assessee 100% deduction on the profits for the year, we dismiss the present ground raised by the assessee since in any case it is eligible to 100% deduction on the increased profits on account of the impugned disallowance, resulting in no tax impact on the assessee on account of the said disallowance. The adjudication on the merits of the case therefore remains a mere academic exercise.

In view of the above, ground No.3 raised by the assessee is dismissed.

21. The appeal of the assessee in 1184/Chd/2016 is, therefore, partly allowed.

ITA No.734/Chd/2017 (A.Y.2014-15)

22. It was the common ground between the parties that the issue involved in this appeal is similar to that involved in ITA No.1184/Chd/2016 and the findings rendered in ITA No.1184/Chd/2016 shall apply mutatis mutandis to this appeal also.

The appeal of the assessee in ITA No.734/Chd/2017 is partly allowed.

23. In the result, both the appeals of the assessee are partly allowed.

Order pronounced in the Open Court.

Sd/-

**(SANJAY GARG)
JUDICIAL MEMBER**

Dated : 04.05.2018

Rati

Copy to:

1. The Appellant
2. The Respondent
3. The CIT(A)
4. The CIT
5. The DR

Sd/-

**(ANNAPURNA GUPTA)
ACCOUNTANT MEMBER**

Assistant Registrar,
ITAT, Chandigarh