

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

BEFORE SMT. DIVA SINGH, JUDICIAL MEMBER AND  
DR. B.R.R. KUMAR, ACCOUNTANT MEMBER

**ITA No.681/Chd/2007**

Assessment Year: 2002-03

M/s Vardhman Textiles Ltd. (Formerly known as Mahavir Spinning Mills Ltd.) Chandigarh Road, Ludhiana	Vs.	The DCIT Range-I Ludhiana
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PAN/GIR No. AABCM4692E

**ITA No.691/Chd/2007**

Assessment Year: 2002-03

The ACIT Circle-I Ludhiana	Vs.	M/s Vardhman Textiles Ltd. (Formerly known as Mahavir Spinning Mills Ltd.) Chandigarh Road, Ludhiana
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**ITA No.475/Chd/2008**

Assessment Year: 2003-04

M/s Vardhman Textiles Ltd. (Formerly known as Mahavir Spinning Mills Ltd.) Chandigarh Road, Ludhiana	Vs.	The ACIT Circle-I Ludhiana
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**ITA No.530/Chd/2008**

Assessment Year: 2003-04

The ACIT Circle-I Ludhiana	Vs.	M/s Vardhman Textiles Ltd. (Formerly known as Mahavir Spinning Mills Ltd.) Chandigarh Road, Ludhiana
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**ITA No.938/Chd/2008**

Assessment Year: 2004-05

M/s Vardhman Textiles Ltd. (Formerly known as Mahavir Spinning Mills Ltd.) Chandigarh Road, Ludhiana	Vs.	The JCIT Range-I Ludhiana
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**ITA No.981/Chd/2008**

Assessment Year: 2004-05

The ACIT Circle-I	Vs.	M/s Vardhman Textiles Ltd. (Formerly known as Mahavir
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Ludhiana

Spinning Mills Ltd.)  
Chandigarh Road, Ludhiana**ITA No.528/Chd/2009**

Assessment Year: 2005-06

M/s Vardhman Textiles Ltd.  
(Formerly known as Mahavir  
Spinning Mills Ltd.)  
Chandigarh Road, Ludhiana

Vs.

The Addl.CIT  
Range-I  
Ludhiana**ITA No.575/Chd/2009**

Assessment Year: 2005-06

The ACIT  
Circle-I  
Ludhiana

Vs.

M/s Vardhman Textiles Ltd.  
(Formerly known as Mahavir  
Spinning Mills Ltd.)  
Chandigarh Road, LudhianaAssessee By : Shri. Subhash Aggarwal  
Revenue By : Sh. Ashish AbrolDate of hearing : 06/02/2018  
Date of Pronouncement : 04/05/2018**ORDER****PER BENCH:**

All the above appeals have been filed by the Assessee and Cross appeal have been filed by the Revenue.

2. For the sake of convenience we reproduced hereunder year wise grounds of both the appeals:

Assessee has raised the following grounds in ITA No. 681/Chd/2007 for A.Y. 2002-03:

1. *That the impugned order has been passed by CIT(A) without proper application of mind and is bad in law and on facts so far as the following grounds are concerned: -*
2. *That the Ld. CIT(A) has erred in law and on facts while upholding the decision of assessing officer for excluding 90% of Miscellaneous Income of Rs.84.17 lacs from profits of business while calculating deduction under section 80HHC of Income Tax Act.*
3. *The Ld. CIT(A) has erred in law while upholding the decision of assessing officer for reducing 90% of interest-income of Rs.739.65 being interest received from costumers amounting to Rs.735.70 lacs and interest received from suppliers amounting to Rs.3.95 Lacs from profits of business while calculating deduction u/s 80HHC*
4. *That the Ld. CIT(A) has erred in law and on facts while upholding the decision of assessing officer for increasing indirect cost of trading goods to Rs.85,53,579/- instead of Rs.16,14,306/- declared by the appellant while*

calculating profit/ loss on trading goods for deduction under section 80HHC of Income Tax Act.

5. That the Ld. CIT(A) has erred in law and on the facts while confirming the action of assessing officer for excluding export turnover amounting to Rs.81,39,65,243/- in respect of export oriented unit (EOU) from export turnover of the appellant while calculating deduction under section 80HHC of Income Tax Act.

6. That the Ld. CIT(A) has erred in law and on the facts while confirming the decision of assessing officer for decreasing profits exempted under section 10B of the EOU's in as much as:-

(i) Other income of Rs.1,25,83,000/- (i.e. 71,26,000 + 54,57,000) has been excluded from eligible profits of the undertakings of the appellant while calculating exemption under section 10B.

(ii) Head Office Expenses has been allocated to profits/losses earned by the EOU's of the appellant.

7. That the Ld. CIT(A) Was erred in law and on the facts while allocating expenses amounting to Rs.2,00,000/- to exempted dividend income earned by the appellant and disallowing the same under section 14A of Income Tax Aqt. /

8. That the Ld. CIT(A) has erred in law and on the facts while confirming the action of assessing officer for treating the Sales Tax subsidy/Exemption amounting to Rs.4,60,68,415/- as a revenue receipt.

9. That the Ld. CIT(A) has erred in law and on the facts while not allowing deduction under proviso to section 80HHC on export incentives amounting to Rs.79.04 Lacs being DEPB sold instead of 1.72 Lacs being profit on sale of DEPB.

Revenue has raised the following grounds in ITA No. 691/Chd/2007 for A.Y. 2002-03:

1. That the Ld. CIT(A) erred in law and facts in not excluding 90% of following receipts under clause (baa) of Explanation below section 80HHC(4C) of the Act even though these receipts are also of similar nature to the receipts specified in this clause:

- i) Claims received Rs. 59.92 lacs
- ii) Excess provision written back Rs.149.36 lacs
- iii) Previous year income Rs. 4.65 lacs

2. That the Ld. CIT(A) erred in law and facts in directing not to reduce 90% of gains of Rs. 17,20,094/- from exchange fluctuation even though receipts on account of exchange fluctuation are similar to income/receipts specified in clause (baa) of Explanation below section 80HHC(4C) of the Act.

3. That the Ld. CIT(A) erred in law and facts in deleting addition of Rs.22,57,000/-made in respect of expenses apportioned u/s 14A for earning dividend income of Rs. 1,80,58,994/- by estimating only Rs.2 lacs out of personal, administrative and misc. expenses etc. as expenditure incurred for earning the dividend income.

4. That the order of the Ld. CIT(A) be set aside and that of the A.O. be restored.

Assessee has raised the following grounds in ITA No. 475/Chd/2008 for A.Y. 2003-04:

1. That the Ld. CIT (A) has erred in law and on facts while confirming the action of assessing officer for taxing the capital receipt on account of Sales Tax Exemption/Subsidy amounting to Rs.4,89,49,449/- received from Government of Punjab as the revenue receipt of the assessee.

2. The Ld. CIT (A) has erred in law and on facts while treating interest received from banks/ICD etc. amounting Rs. 208.68 Lacs as Income from other sources instead of Income from Business.

3. That the Ld. CIT (A) has erred in law and on the facts while reducing the Deduction u/s 10B :-

(a) That the Ld. CIT (A) has erred in law and on facts while applying method of calculating deduction u/s 1 OB other than that specified u/s 10B and at variance to the method regularly adopted by the assessee in earlier years and accepted by the department.

(b) That the Ld. CIT (A) has erred in law and on facts while affirming the action of the Ld. Assessing officer for calculation of trading profits/loss in the unit claiming deduction u/s 10B at variance to the method given in section 80HHC of the Income Tax Act.

(c) That the Ld. CIT (A) has erred in law and on facts while affirming the notional calculation of trading profits/losses of 10B unit instead of actual trading profit/loss.

(d) That the Ld. CIT (A) has erred in law and on the facts while upholding the decision of assessing officer for increasing the Total Turnover of undertakings for calculating exemption u/s 1 OB of Income Tax Act by the following amounts:

Particulars	Amount ( in Rs.)	
	Name of Undertakings	
	Anant-II	Anant-III
Excise Duty	24,29,868/-	23,16,464/-
Export Turnover of Trading Goods	-	6,75,09,263/-

(e) That the Ld. CIT(A) has erred in law and on the facts while reducing profits of undertakings for calculating deduction u/s 10B by the following amounts: -

Particulars	Amount (in Rs.)	
	Name of undertakings	
	Anant-II	Anant-III
Interest From Banks & Customers	6,133/-	7,827/-
Rent received from employees	99,761/-	83,134/-
Cash discount received from cotton suppliers	4,83,159/-	6,19,048/-
Brokerage recd against export invoices	2,34,587/-	3,00,564/-
Duty Draw Back	22,56,533/-	28,91,184/-
Recd against sale of PPE Quota Cert.	80,000/-	1,02,500/-
Disc recd. From IOC &	1,16,458/-	1,28,682/-

HPCL		
Received against sample sale	22,332/-	28,613/-
Misc.	52,136/-	71,092/-
	33,51,100	42,32,644/-

3A. That the Ld. CIT (A) has erred in law and on facts while confirming the action of the assessing officer for allocating expenses of head office to units claiming deduction under section 10-B and 80-IB.

4. That the Ld. CIT (A) has erred in law and on the facts while reducing deduction u/s 80HHC :-

(a) That the Ld. CIT (A) has erred in law and on the facts in excluding 100% of Export Turnover of export oriented units from Export Turnover of the assessee while calculating the deduction u/s 80HHC of Income Tax Act.

(b) Without prejudice to ground no. 4 (a) above, the Ld. CIT (A) has erred in law and on facts while excluding 100% of export turnover of the export oriented units instead of 90% of export turnover as excluded by Ld. Assessing officer while calculating deduction u/s 80-HHC of the Income Tax Act.

(c) That the Ld. CIT (A) has erred in law and on facts while applying method of calculating cost of trading goods exported for deduction u/s 80HHC other than that specified u/s 80HHC and at variance to the method regularly adopted by the assessee in earlier years.

(d) That the Ld. CIT (A) has erred in law and on the facts while apportioning proportionate Personnel Expenses, Administration Expenses, Financial Expenses and Depreciation not relating to trading activities of the assessee's business for calculating indirect cost of Trading Exports while calculating deduction u/s 80HHC of Income Tax Act.

(e) That the Ld. CIT (A) has erred in law and on the facts while reducing 90% of miscellaneous receipts amounting to Rs. 115.07 Lacs from profits of business eligible for deduction u/s 80HHC.

(f) The Ld. CIT (A) has erred in law and on facts while excluding 90% of interest received from customers amounting to Rs. 41131951 from profits of business eligible for deduction u/s 80HHC for calculating deduction u/s 80HHC of the Income Tax Act.

(g) That the Ld. CIT (A) has erred in law and on facts while excluding 100% of interest income amounting to Rs. 20867862 from profits of business eligible for deduction u/s 80HHC for calculating deduction u/s 80HHC of the Income Tax Act.

(h) That the Ld. CIT (A) has erred in law and on facts while excluding 90% of sale value amounting to Rs. 11778346 on transfer of DEPB instead of 90% of profit on transfer of DEPB amounting to Rs. 433719 from the eligible profits while calculating deduction u/s 80-HHC of the Income Tax Act.

(i) The CIT (A) has erred in law and on facts while not allowing deduction under proviso to section 80HHC (3) on DEPB receipts.

5. That the CIT (A) has erred in law and on the facts while reducing profits of Arisht Spinning Mills, Unit - 1 eligible for deduction u/s 80IB by following amounts: -

Particulars	Amount(in Rs.)
Rent received from employees	89,323/-
DEPB Benefit	72,00,370/-
	98,73,971/-

Revenue has raised the following grounds in ITA No. 530/Chd/2008 for A.Y. 2003-04:

1. That the Ld. CIT(A)-II has erred in law & facts in deleting the addition made by the A.O. on proportionate basis out of personal, administrative, financial and misc. expenses to earning of dividend income.
2. That the Ld. CIT(A) has erred in law & facts in directing the A.O. to allocate the expenses net of income of the Head Office in the proportion of turnover of Head Office, Anand Spinning Mills Unit-II and Anant Spinning Mills Unit-III for calculating exemption u/s 10B.
3. That the Ld. CIT(A) has erred in law & facts in directing the A.O. not to exclude 90% of rental income received, from employee's of company, misc. receipt & discount and sundry balance written off for calculating deduction u/s 80HHC.
4. That the Ld. CIT(A) has erred in law & facts in directing the A.O. to add the loss on export of trading goods for calculating deduction u/s 80HHC
5. That the Ld. CIT(A) has erred in law & facts in allowing/the deduction u/s 80IB amounting to Rs.4,51,31,894/- in the case of Anant Spinning Mills Unit-II however the unit is 100% export unit which is not eligible for deduction u/s 80IB.
6. That the Ld. CIT(A) has erred in law & facts in directing the A.O. to recompute deduction u/s 80IB allowable to Anant Spinning Mills Unit-I by taking head office expenses to the net of the Head Office income in proportion of sales of the unit to the total sales of the business of the assessee company.
7. That the Ld. CIT(A) has erred in law & facts in allowing deduction u/s 80IB on misc. income amounting to Rs.2.23 lacs in respect of Arist Spinning Mills Unit-I as the misc. income is not directly related to income generated from industrial undertaking.

Assessee has raised the following grounds in ITA No. 938/Chd/2008 for A.Y. 2004-05:

1. The Ld. CIT(A) has erred in law and on facts while confirming the action of the assessing officer for treating interest income amounting to Rs. 14159428 Lacs as "Income from other Sources" instead of "Income from Business or Profession", detailed as below:-

PARTICULARS	AMOUNT
Interest received from Bank	55,70,61/-
Other Interest Received	5054404/-
Interest from ICD deposits	8547963/-
Total	14159428/-

2. That the Ld. CIT(A) has erred in law and on facts while taxing the capital receipt amounting to Rs.5,25,05,262/- on account of Sales Tax Exemption/ Subsidy received from Government of Punjab as the revenue receipt of the assessee.
3. Without prejudice to the ground (2) above, the Ld. CIT(A) has erred in law and on facts while taxing the capital receipt amounting to Rs.5,25,05,262/- on account of Sales Tax Exemption/Subsidy received from Government of Punjab as 'Income from other Sources'.

4. That the Ld. CIT(A) has erred in law and on the facts while confirming the action of the assessing officer for reducing profits of units eligible for deduction u/s 10B ( Anant II, Anant III & Arisht EOU ) and 80IB ( Anant II & Arisht EOU ) by the following amounts :-

(Amount in Rs.)			
Particulars	Anant II	Anant III	Arisht EOU
Interest received from others	4,405/-	7,653/-	-
Other Claims received	2,368/-	27,043/-	31,382/-
Rent received from employees	71,956/-	1,09,020/-	1,96,978/-
Miscellaneous Income	1,92,467/-	3,65,170/-	-
Commission	-	-	40,404/-

5. (i)(a) That the Ld. CIT(A) has erred in law and on facts while applying method of calculating deduction u/s 10B other than that specified u/s 10B and at variance to the method regularly adopted by the assessee in earlier years and accepted by the department.

(i)(b) That the Ld. CIT(A) has erred in law and on the facts while not adjusting actual profit / loss on sale of trading goods while calculating profits of units eligible for deduction u/s 10B.

(ii) That the Ld. CIT(A) has erred in law and on the facts while increasing the Total Turnover of units eligible for deduction u/s 10B by the following:-

		Anant II	Anant III	Arisht EOU
a)	Excise Duty	48,83,121/-	14,22,538/-	1,55,68,698/-
b)	Export Turnover of Trading goods	1,01,28,889/-	6,87,98,501/-	24,02,439/-

6. (i) That the Ld. CIT(A) has erred in law and on the facts while not increasing profits of business eligible for deduction u/s 80HHC by 10% of interest received.

(ii) That the Ld. CIT(A) has erred in law and on the facts while reducing profits of business eligible for deduction u/s 80HHC by 90% of interest received from suppliers and customers amounting to Rs.3,61,67,246/-.

(iii) That the Ld. CIT(A) has erred in law and on the facts in excluding Export Turnover of units claiming deduction u/s 10B amounting to Rs.119,61,79,475/- from Export Turnover of the assessee while calculating the deduction u/s 80HHC of Income Tax Act.

(iv) Without prejudice to Ground No. 2 above the Ld. CIT(A) has erred in law and on the facts in excluding Sales Tax Subsidy amounting to Rs.5,25,05,262/- from the eligible profits of the business while calculating deduction u/s 80HHC of the Income Tax Act.

(v)(a) That the Ld. CIT(A) has erred in law and on the facts while not allowing deduction u/s 80HHC (3)(c)(iii) on export incentives amounting to Rs.4,10,03,794/-.

(v)(b) That without prejudice to ground 9 (xi)(a) above the Ld. CIT(A) has erred in law and on the facts while excluding 90% of DEPB receipts by way of DEPB self

consumed as well as DEPB yet to be consumed amounting to Rs.18.01 lacs and 43.74 lacs respectively.

(vi)(a) That the Ld. CIT(A) has erred in law and on facts while applying method of calculating cost of trading goods exported for deduction u/s 80HHC other than that specified u/s 80HHC and at variance to the method regularly adopted by the assessee in earlier years.

(vi)(b) That the Ld. CIT(A) has erred in law and on the facts while apportioning full amount of Personnel, Administrative and Financial Expenses and Depreciation to the indirect cost of Trading Goods while calculating deduction u/s 80HHC of Income Tax Act, ignoring the fact that full amount of these expenses were not related to the trading activities.

7. That the Ld. CIT(A) has erred in law and on the facts while confirming the action of the assessing officer for disallowing 50% of the foreign traveling expenses of Rs.8,71,000/-.

8. That the Ld. CIT(A) has erred in law and on the facts while disallowing foreign traveling expenses of wife of Chairman & Managing Director amounting to Rs.2,95,671/-.

9. That the Ld. CIT(A) has erred in law and on the facts while not allowing line / bay charges amounting to Rs. 58.33 lacs as revenue expenditure.

Revenue has raised the following grounds in ITA No. 981/Chd/2008 for A.Y. 2004-05:

1. That the Ld. CIT(A) has erred in law & facts in directing the A. O. to consider interest income received by the assessee on delayed payment from customers as "business income" instead of "Income of other sources" as considered by the A. O.

2. That the Ld. CIT(A) has erred in law & facts in directing the A. O. to allow the deduction u/s 80IB on the balance profit of its unit after deduction u/s 10B which is not admissible as per section 10B(6) (iii).

3(a) That the Ld. CIT (A) has erred in law & facts in directing the A. O. to treat the gain on forex fluctuation to be the income eligible for deduction u/s 10B.

3(b) That the Ld. CIT (A) has erred in law & facts in directing the A. O. to treat the interest received from customers and suppliers to be the income eligible for deduction u/s 10B.

4. That the CIT(A) has erred in law & facts in directing the A.O. to recomputed deduction u/s 80IB by taking head office expenses to the net of the Head Office income in proportion of sales of the unit to the total sales of the business of the assessee company.

5. That the Ld. CIT(A) has erred in law & facts in directing the A. O. to reduce 90% instead of 100% of interest received from suppliers and customers for the purpose of deduction u/s 80HHC.

6. That the CIT(A) has erred in law & facts in directing the A.O. not to reduce scrap sales from total turnover and profit of the assessee company.

7. That the CIT(A) has erred in law & facts in directing the A.O. not to exclude 90% of rental income received from employees of the company, Misc. receipts and foreign exchange fluctuation for calculating deduction u/s 80HHC.

8. That the CIT(A) has erred in law & facts in deleting the addition u/s 14A made by the A.O. on proportionate basis out of personal and administrative and financial expenses to earning of dividend income.

9. That the order of the Ld. CIT(A) be set aside and that of the A.O. be restored.

Assessee has raised the following grounds in ITA No. 528/Chd/2009 for A.Y. 2005-06:

1. The Ld. CIT (A) has erred in law and on facts while confirming the action of the Assessing officer for treating interest income amounting to Rs. 70,41,07.6/- as "Income from other Sources" instead of "Income from Business or Profession".

2. That the Ld. CIT(A) has erred in law and on the facts while confirming the action of the Assessing officer for reducing profits of units eligible for deduction u/s 10B and/or 80IB by the following amounts :-

Particulars	(Amount in Rs. )		
	Anant III	VSGM(EOU)	Auro-W-II
Interest received from others	78,274	-	-
Other Claims received	3,098	-	-
Rent	4,35,231/-	2,49,469/-	80,621/-
Misc. Income	14,67,478/-	37,624/-	34,680/-
DEPB	-	-	8,78,942/-
Total	19,84,531/-	2,87,093/-	9,94,243/-

3. That the Ld. CIT(A) has erred in law and on the facts while directing to Assessing officer to reduce profits eligible for deduction u/s 10B and 80IB of VSGM E.O.U., Auro Wvg-II and Anant-III by proportionate Head office expenses.

4. That the Ld. CIT(A) has erred in law and on facts while taxing the capital receipt amounting to Rs. 9,94,79,992/- on account of Sales Tax Exemption/Subsidy received from Government of Punjab as the revenue receipt of the assessee.

5. Without prejudice to the ground (4) above, the Ld. CIT (A) has erred in law and on facts while taxing the capital receipt amounting to Rs. 9,94,79,992/- on account of Sales Tax Exemption/Subsidy received from Government of Punjab as 'Income from other Sources'.

6. That the Ld. CIT(A) has erred in law and on the facts while confirming the action of the Assessing officer for disallowing foreign traveling expenses of wife of Chairman & Managing Director amounting to Rs.9,43,502/-.

7. The Ld. CIT(A) has erred in law and on facts while disallowing 4/5<sup>th</sup> of expenses amounting to Rs.5,35,646/- by treating these expenses as expenses covered u/s 35D of Income Tax Act.

Revenue has raised the following grounds in ITA No. 575/Chd/2009 for A.Y. 2005-06:

1. That the Id. CIT(A) has erred in law and facts in directing the A.O. to consider interest income received by the assessee on delayed payments from customers as 'Business Income' instead of Income from Other Sources' as considered by the A.O.

2. (i) That the Id. CIT(A) has erred in law and facts in directing the A.O. to treat the interest received from the customers and suppliers to be the income derived

from industrial undertaking and eligible for exemption u/s 10B and deduction u/s 80IB.

(ii) That the Id. CIT(A) has erred in law and facts in directing the A.O. to allow deduction u/s 80IB and exemption 10B on profits after excluding loss debited in the accounts in respect of which the Insurance claims were received.

(iii) That the Id. CIT(A) has erred in law and facts in directing the A.O. not to reduce foreign exchange fluctuation gain from eligible profits of units eligible for deduction u/s 80IB and exemption u/s 10B.

3. The Id. CIT(A) has erred in law and facts in directing the A.O. to allocate the eligible head office income to the respective unit for calculating deduction u/s 80IB and exemption u/s 10B.

4. That the Id. CIT(A) has erred in law and facts in allowing the deduction u/s 80IB on profits of unit named Vardhman Spinning & General Mills (100% EOU) eligible for exemption u/s 10B.

5. That the Id. CIT(A) has erred in law and facts in deleting the addition of Rs. 17,73,346/- made u/s 14A by the A.O. on proportionate basis out of personal, administrative and financial expenses for earning of dividend income.

6. That the Id. CIT(A) has erred in law and facts in vacating the addition of Rs.20 lac made by the Assessing Officer u/s 35D on account of expenses incurred in connection with the demerger scheme on account of inseparable charges to give effect to demerger scheme.

7. That the Id. CIT(A) has erred in law and facts in directing the Assessing Officer to consider expenses incurred on post implementation review of the BPCS and TIM system as revenue expenditure instead of Capital expenditure.

8. That the Id. CIT(A) has erred in law and facts in treating the income from Sale of Shares amounting to Rs. 3,53,86,594/- as income from Capital gain instead of income from speculative Business as considered by the Assessing Officer in view of explanation to section 73.

9. That the order of the Id. CIT(A) be set aside and that of the A.O. be restored.

3. For the A.Y. 2002-03 the assessee has filed a letter dt. 18/09/2012 received vide receipt no. 3897 dt. 24/09/2012 by this Tribunal, stating that the Ground Nos. 3, 5 & 8 may be permitted to argue and sought to withdraw the Application filed under section 158A of Income Tax Act, 1961 vide letter dt. 01/12/2007, hence the same is allowed to be withdrawn.

4. The assessee has taken two additional grounds which reads as under:

1. *"That the authorities below erred in computing indirect cost relating to trading goods in as much 10% of the items covered by explanation (baa) to Section 80HHC have not been deducted from the indirect cost."*

2. *That the authorities below have erred in treating reimbursement under technology up gradation fund scheme (TUFFS) as revenue receipt instead of capital receipt."*

5. Since the above grounds is purely of legal in nature following the judgment of Hon'ble Supreme Court in the case of M/s Hero Exports Ltd. Vs. CIT order dt. 20/11/2007 and NTPC Vs. CIT (Supreme Court) 229 ITR 383, therefore both the additional grounds are hereby admitted and dealt with later in this order.

**6. Issue No. 1 : The issue of reduction of 90% of other income under section 80HHC:**

A.Y. 2002-03

Ground No. 1 and 2 of the Revenue's Appeal

Ground No. 2 and 3 of the Assessee's Appeal

A.Y. 2003-04

Ground No. 3 of the Revenue's Appeal

Ground No. 4(e), 4(f) and 4(g) of the Assessee's Appeal

A.Y. 2004-05

Ground No. 5 and 7 of the Revenue's Appeal

Ground No. 6(i), 6(ii), 6(iii) of the Assessee's Appeal

A.Y. 2005-06

Ground No. 2 of the Assessee's Appeal

6.1 The above mentioned grounds deal with reduction of 90% of other income for the purpose of computation of deduction under 80HHC and effect of claims received, interest received provision written back and foreign exchange fluctuation in computation of deduction under section 80HHC.

6.2 Brief facts of the case are that the Assessing Officer while computing deduction under section 80HHC also reduced 90% of Rs. 291.10 lacs which represents claim received, excess provision written back, previous year income and misc. income. The Assessing Officer has noted that these receipts are in the nature of "any other receipt" as referred to in clause (baa) of Explanation to Section 80HHC and necessarily 90% of these receipts have to be reduced from the profit of the business.

6.3 Referring to the provisions of clause (baa), the A.O, has stated that the expression "any receipt" and "any other receipt" of a similar nature shows that the receipt mentioned are not exhaustive in nature but only illustrative. Referring

to the Board Circular No. 621 dated 19.12.1991, she has argued that if such receipts as mentioned above, are included in the "profit of the business", it would give a distorted figure of export profits. She has further observed that as per the provisions laid down in the Explanation (baa) to Section 80HHC, such receipts, which do not have element of turnover but are included in the Profit & Loss Account, should be reduced by 90% before being included in the profit of the business.

6.4 The assessee gave item wise explanation for various incomes excluded by the Assessing Officer and has argued that the assessee has already excluded 90% of interest, commission, brokerage and profit on sale of licenses/ DEPB etc. while calculating deduction under section 80HHC and these items which have been excluded in view of the provisions of Explanation (baa) to Section 80HHC. The nature of these incomes as stated by the Counsel are as follows:

1. Claims received	Rs. 52.92 Lacs
2. Excess provision written back	Rs. 149.36 Lacs
3. Previous year income	Rs. 4.65 Lacs
4. Miscellaneous income	<u>Rs. 84.17 lacs</u>
Total	Rs. 291.10 Lacs

6.5 The assessee has further argued that on similar set of facts, the CIT(A)-I, Ludhiana, in the assessee's own case for assessment years 2000-01 and 2001-02 held that claims received, excess provision written back and misc. income are in the nature of business income and as such 90% of the same are not to be deducted from the profit of the business for the purposes of computation of deduction under section 80HHC of the Act.

6.6 Ld.CIT (A) agreed that excess provision written back and previous year income are necessarily a part of the profit of the business and does not come under the ambit of "any other receipt" of similar nature as per clause (baa) of Explanation to Section 80HHC, however, the claim received and misc. income are necessarily "any other receipts" and 90% of the amount representing these items are to be reduced from the profit of the business. The misc. income represents rent received from employees, discount from suppliers etc. These fall certainly under any other receipt, and as far as the misc. income is concerned,

6.7 The Ld.CIT(A) disagreed that misc. income are in the nature of business income and 90% of the same are to be reduced from the profit of the business and directed not to reduce 90% of the excess provision written back, previous year income and claim received.

6.8 Before us, Ld. DR relied on the order of the Ld. CIT(A) to the extent of the addition confirmed and argued that the claims received excess provision written back added by the Assessing Officer needs to be upheld.

6.9 The Ld. AR brought us to our notice that the issue is squarely covered in favour of the assessee and against the Revenue by the order of the Tribunal dt. 05/01/2016 in the assessee's own case in ITA NO. 212/CHD/2005 for the A.Y. 2001-02 (Mahavir Spinning Mills Ltd.).

6.10 We have gone through the order wherein the claims received, excess provisions written back and misc. income, foreign exchange fluctuation were allowed to the assessee relying on the judgment of Hon'ble Punjab & Haryana High Court in the case of CIT Vs. Metal Man Auto Pvt. Ltd. 336 ITR 434 and VMT spinning Co. Ltd in ITA654/CHD/2005 for the year 2001-02 wide order dated 31-07-2006.

6.11 As a result, the ground no 1,2 of 202-03 and similar issue for the other years of the revenue stands dismissed and ground number 1 of 202-03 and similar issue for the other years of the assessee is allowed.

## **7. Issue No. 2 : Allocation Expenses under section 14A:**

A.Y. 2002-03  
Ground No. 3 of the Revenue's Appeal  
Ground No. 7 of the Assessee's Appeal

A.Y. 2003-04  
Ground No. 1 of the Revenue's Appeal

A.Y. 2004-05  
Ground No. 8 of the Revenue's Appeal

A.Y. 2005-06  
Ground

No. 5 of the Revenue's Appeal

7.1 The assessee has earned dividend income of Rs. 1.8 Crores and claimed it under section 10(33) of Income Tax Act, 1961. The Assessing Officer disallowed an amount of Rs. 24.57 lacs under section 14A.

7.2 The Ld. CIT(A) based on the analysis of the balance sheet and the fund position concluded that the assessee had enough reserves and surplus of its own for investment and the investments were made purely out of the assessee's own funds and deleted the addition made by the AO.

7.3 The similar matter was considered by the ITAT in the case of the assessee for the assessment year 2001-02 in ITA No. 1174/CHD/2013 vide order dt. 16/04/2014 wherein it has been held that the disallowance was made on surmises and there was no merit in the disallowances made wrongly on the premise that borrowed funds were used for investment purpose. The Tribunal has affirmed the confirming of disallowance of Rs. 1,00,000/- made by the Ld. CIT(A). In the instant year the Ld. CIT(A) has confirmed an amount of Rs. 2,00,000/- being the expenses incurred for earning of the dividend income. Following the same rationale we hereby uphold the order of the Ld. CIT(A).

7.4 As a result, the appeal of the Revenue and the cross appeal of the Assessee on this ground stands dismissed.

### **8. Issue No. 3 : Calculation of indirect cost of Trading Goods:**

A.Y. 2002-03  
Ground No. 4 of the Assessee's Appeal

A.Y. 2003-04  
Ground No. 4(c) and 4(d) of the Assessee's Appeal

A.Y. 2004-05  
Ground No. 6(vi) of the Assessee's Appeal

8.1 In these grounds of appeal the assessee stated that the Ld. A.O. has erred in law and on facts while apportioning proportionate personnel expenses/administrative expenses/financial expenses and depreciation not relating to trading activities of the assessee's business for calculating indirect cost of trading exports while calculating deduction u/s 80HHC of the Income Tax Act, 1961.

8.2 The A.O. noted that for computing deduction u/s 80HHC the assessee considered costs which were claimed to be directly relatable to trading goods as direct cost of trading goods and costs that do not relate to trading goods in any way were ignored. Costs in respect of wages of workers, salary of technical staff, loss on sale of fixed assets etc. were claimed to be relating to manufacturing activities only.

8.3 Further, the costs which are common for both trading and manufacturing goods were apparently apportioned in the ratio of export turnover of trading goods to total turnover for the purposes of computing deduction u/s 80HHC. The A.O. asked the assessee to prove with documentary evidence as to how the costs under the head heads financial, administrative and personnel relate only to manufacturing activity. It was explained before the A.O. that the assessee had reduced salary of technical employees, wages of workers and trainee allowance from the cost of trading goods as these did not relate to trading activities.

8.4 Similarly FBN interest on manufacturing goods and interest on term loan to arrive at financial expenses to be apportioned for computation of indirect cost of trading goods was reduced for computing expenses which were to be apportioned between trading and manufacturing activities because such expenses related only to manufactured goods only. The A.O., however, did not accept the contention of the assessee. The A.O. noted that as per the provisions of Section 80HHC, the deduction is to be given for the business as a whole and the profit is to be computed in *the* manner as laid down in Sub-Section (3) of Section 80HHC. She, therefore, observed that the deduction claimed by the assessee unit-wise is not as per the provisions of Section 80HHC. She further observed that the definition of direct cost and indirect cost have been provided by the Income Tax Act, 1961 in Explanation (d) to Section 80HHC(3).

8.5 By referring to these definitions of direct cost and indirect cost as given in Explanation (d) and Explanation (e) to Section 80HHC, she held that the assessee was not justified in reducing the indirect cost allegedly relating to the manufacturing activity first and doing the allocation of the remaining costs in the proportion of trading turnover to total turnover in view of the provisions of Section 80HHC. She also did not accept the argument of the assessee that costs of only those units which did the trading export alone be taken into

computation of indirect cost for the purposes of computing indirect cost of trading goods for the purposes of computing deduction u/s 80HHC. She accordingly worked out the indirect cost of trading exports in view of her conclusions as above and recomputed the deduction u/s 80HHC.

The written submissions of the assessee with regard to the ground of appeal before the Ld. CIT(A) are reproduced hereunder: -

*The Ld. Assessing Officer has erred in law and in fact while increasing the costs of trading goods to Rs. 10,24,37,872/- instead of Rs.9,80,74,074/- declared by the assessee while calculating profit/(loss) on trading goods for deduction u/s 80HHC of the Income tax Act. It is hereby submitted that the total expenditure of the units which have done trading must be segregated into the following: -*

- a. *Direct expenses solely attributable to the trading.*
- b. *Direct expenses solely relating to the manufacture of the goods and not pertaining to trading goods.*
- c. *Common costs relating to both trading and manufactured goods.*

*We are also reproducing relevant section 80HHC(3) clause (b) for your honour's reference: -*

*"where the export out of India is of trading goods, the profits derived from such export shall be the export turnover in respect of such trading goods as reduced by the direct costs and indirect costs attributable to such export"*

*The relevant word is 'indirect costs attributable' to trading goods and therefore direct costs relating to manufacturing of goods cannot be included in indirect costs attributable to trading goods. Thus, only the common costs for trading and manufacturing goods should be allocated to calculate 'proportionate indirect costs attributable to trading goods'.*

*Hence, the assessee has rightly excluded from total expenses, the direct expenses solely relating to manufacturing goods like*

- a. *personnel expenses relating to the technical employees,*
- b. *administrative expenses under the heads like loss on sale of fixed assets, sundry balance written off,*
- c. *financial expenses such as debenture interest/term loan for expansion.*

8.6 The Ld. CIT(A) held that the assessee also filed copy of the order of the Hon'ble ITAT Chandigarh Bench in appeal No.737/Chd/2004 in the case of DCIT-I, Ludhiana vs. Mahavir Spinning Mills Ltd. for the assessment year 2000-01. In view of this decision it was submitted that the Hon'ble ITAT has held in this case that the indirect cost and direct cost of trading goods has to be worked out keeping in view the decision of the Hon'ble Special Bench of ITAT in the case of Surendra Engineering Corporation vs. ACIT 86 ITD 121 (Mum.) (SB). And directed the A.O. to consider the direct cost and indirect cost as worked out by the assessee and allow deduction u/s 80HHC accordingly.

8.7 Since the matter travelled up to Tribunal in the earlier years in the assessee's own case for the A.Y. 2001-02 in ITA No. 249/CHD/2008 and 280/CHD/2008 dt. 28/12/2012, wherein it was directed to work out the indirect cost of the trading goods by calculating head wise expenditure claimed by the assessee and to compute the deduction allowed to the assessee under section 80HHC of the Act, following the same we hereby uphold the order of the Ld. CIT(A) directing the Assessing Officer to recomputed the profits.

8.8 The appeal of the assessee on this ground is treated as set aside.

**9. Issue No. 4 :Exclusion of Export Turnover and Total Turnover of EOU Unit while calculating 80HHC:**

A.Y. 2002-03

Ground No. 5 of the Assessee's Appeal

A.Y. 2003-04

Ground No. 4(a), 4(b), of the Assessee's Appeal

A.Y. 2004-05

Ground No. 6(iii) of the Assessee's Appeal

9.1 The ground of the assessee relates to exclusion of 100% of export turnover of EOU from export turnover (ETO) while calculating the deduction under section 80HHC.

9.2 Ld. CIT(A) has observed that the Hon'ble ITAT in assessee's own case for the assessment year 1998-99 in ITA No. 476/CHD/2006 dt. 27/04/2007 has confirmed the action of the A.O. for exclusion of the entire export turnover and the total turnover of 100% EOU from export turnover as well as total turnover of the business for calculating deduction under section 80HHC. Therefore, instead of 90%, 100% of export turnover and total turnover of the 100% EOU of the assessee is required to be reduced from the export turnover and total turnover of the business of the assessee for calculation of deduction under section 80HHC. If this issue is to be decided in line with the findings of the Hon'ble ITAT in assessee's own case as above, technically this would result into enhancement. Though the Ld. Counsel for the assessee, during appeal proceedings, objected to such enhancement and submitted that the decision of the Hon'ble ITAT has been further challenged by the assessee, the request of the assessee in not

following the decision of the Jurisdictional Bench of the ITAT in assessee's own case for the assessment year 1998-99 cannot be accepted. In view of the above, the A.O. is directed to reduce 100% of the export turnover and total turnover of the EOUs of the assessee from the export turnover and the total turnover of the business of the assessee respectively for computing deduction under section 80HHC.

9.3 This issue has been dealt in the ITA No. 212/CHD/2005 for the A.Y. 2001-02 while dealing with the Ground No. 4(para 14) by the ITAT Chandigarh. The decision was based on the judgment of Bombay High Court in the case of CIT Vs. Hindustan Lever Ltd. in ITA No. 5794/2010 dt. 01/04/2014 (Bom).

9.4 Since the issue stand settled at this juncture the Assessing Officer is directed to follow the judgment of the Hon'ble Bombay High Court.

9.5 This ground of appeal is allowed for statistical purposes.

#### **10. Issue No. 5: Non Exclusion of other income while calculating 10B:**

A.Y. 2002-03  
Ground No. 6(i) of the Assessee's Appeal

A.Y. 2003-04  
Ground No. 3(e) of the Assessee's Appeal

A.Y. 2004-05  
Ground No. 4 of the Assessee's Appeal  
Ground No. 3 of the Revenue's Appeal

A.Y. 2005-06  
Ground No. 2(i) and 2(ii) and 2(iii) of the Department Appeal

10.1 Brief facts of the case are that the Assessing Officer has increased the total turnover of the undertaking for calculating exemption under section 10(B) by adding excise duty and export turnover of the trading goods.

10.2 The Assessing Officer has relied on the decision of the Hon'ble Supreme Court in the case of Chowringhee Sales Bureau(P) Ltd. Vs. CIT 87 ITR 542(Supreme Court) and Sinclair Murray & Co. (P) Ltd. Vs. CIT 97 ITR 615 (Supreme Court) to hold that Excise Duty is includible in the turnover of the assessee.

10.3 The Ld. CIT(A) held that the exclusion of excise duty from the total turnover may be applicable in case of deduction under section 80HHC but not while computing deduction under section 10(B) of the Income Tax Act, 1961, in view of provisions of Section 10(B)(4).

10.4 It was argued that this issue has been covered by the order of the Tribunal in assessee's own case in ITA No. 212/CHD/2005 for the A.Y. 2001-02. He relied on the decision in the case of Phatla Cotgin Vs. CIT 303 ITR 411 (P&H High Court).

10.5 We have gone through the judgment in the case of Laxmi Machine Works (2007), 290 ITR 667 (Supreme Court) and find it squarely applicable to the instant case. The Assessing Officer is directed to re-compute the eligible profits as per the guidelines laid down.

10.6 As a result this ground of appeal raised by the Assessee and of the Revenue are allowed for statistical purposes.

## **11. Issue No. 6: Allocation of Head Office Expenses:**

A.Y. 2002-03  
Ground No. 6(ii) of the Assessee's Appeal

A.Y. 2003-04  
Ground No. 3A of the Assessee's Appeal  
Ground No. 2 and 6 of the Revenue's Appeal

A.Y. 2004-05  
Ground No. 4 of the Revenue's Appeal

A.Y. 2005-06  
Ground No. 3 of the Assessee's Appeal  
Ground No. 3 of the Revenue's Appeal

11.1 The issue relates to apportionment of expenses namely personnel, administrative, financial to various units. The order of the CIT(A) is as under:

*11.2 Ld. A.O. has erred in law and facts while reducing profits of undertaking for calculating exemption u/s 10B by allocating head office expenses amounting to Rs.39,35,236/- in the case of Anant Spinning Mills Unit-II and Rs.44,80,344/- in the case of Anant Spinning Mills Unit-III.*

*11.3 The A.O. noted that the assessee for the relevant period, debited the following administrative, personnel and financial expenses to the head office: -*  
Personal Expenses: 29870107  
Administrative : 52590075

Financial : (7787780)  
Total : 74672402

11.4 The A.O. discussed that the assessee is not an entity separate from its manufacturing units. Observing that the head office is incurring expenses on behalf of the manufacturing units, the A.O. held that in order to arrive at the actual profits derived from industrial undertaking it was imperative that all the expenses are taken into account by the units. She further observed that the expenses incurred at head office but which actually relate to the units are to be included in the expenses of the units and profits of the units is to be computed correctly. She accordingly allocated out of the head office expenses mentioned above, the following expenses, to the various units in proportion of the turnover: -

	Arisht-I	Anant-II	Anant-III
Turnover (in crores)	31.36	48.93	54.33
Percentage of share to the total turnover	3.46%	5.27%	6%

11.5 The written submissions of the assessee with regard to the above mentioned ground of appeal are given as under: -

11.6 The Ld. Assessing Officer has proportionately allocated personnel and administrative expenses of head office to the respective units in which deduction u/s 10B & 80IB is claimed in the ratio of turnover of these units to the total turnover. While doing so, Ld. Assessing Officer calculated total expenditure relating to units claiming deduction u/s 10B out of total expenditure of Rs.746.72 lacs as follows: -

Name of Unit	Deduction	Amt. of exp. Allocated
Anant Spinning Mills, Unit-2	10B	39,35,236
Anant Spinning Mills, Unit-3	10B	44,80,344
Arisht Spinning Mills, Unit-1	80IB	25,84,278/-

11.7 In this connection, it is submitted that section 10B and 80IB of Income Tax Act refers to deduction in computing the total income of the assessee at a specified percentage of profits 'derived' from an industrial undertaking. From the reading of this section it is clear that deduction is available only in respect of profits and gains derived from the industrial undertaking. Income and expenditure of Head Office cannot be in any way termed as 'profits and gains derived from' the industrial undertaking.

In this connection we rely upon following judgements: -

PUNJAB CONCAST STEEL LTD. VS. ACIT T49 ITD 430 (CHD)

Section 80-1(6) does not also give a handle to the revenue authorities to reallocate the expenses in various units. In our considered view, the entire exercise embarked upon by the assessing officer and the Ld. CIT (A) regarding allocation of expenses was not called for and the aforesaid sections, namely, section 80-1(8) and section 80-1 (6) do not clothe the revenue authorities to re-allocate the expenses particularly when the assessee has been maintaining regular books of account and production record in respect of each unit and the assessee's claim under section 80-1 has been accepted in the past. We therefore, hold that there was no justification for re-allocating various expenses as done by the revenue authorities to compute deduction under section 80-1 of the Act.

CIT VS. JIYAJEERAO COTTON MILLS LTD. 179 TAXMAN 51 (CAL)].

There are many expenditures of the company which are not only in respect of priority industry but also in respect of other industries under the management of the company. One of such expenditures is the payment made to the managing agents. The revenue's contention that the proportionate income of the managing agency by way of commission must be deducted from the profits of the priority industry to find out the profits and gains of priority industry for the purpose of computation of relief under section 80-1 is not acceptable.

Without prejudice to our submissions above, it is respectfully submitted that while apportioning the head office expenses of Rs.7.47 crores, Ld. Assessing Officer had not considered the other income of Rs.4.05 crores earned by the head office and expenditure net of income was Rs.3.42 crores (7.47 crores - Rs. 4.05 crores) and proportionate expenses out of this net amount of Rs.3.42 crores to units claiming deduction u/s 10B on the basis of reasoning of turnover of units adopted by the Ld. A.O., comes to Rs. 18.02 lacs instead of Rs.39.35 lacs in case of Anant - 2, Rs.20.52 Lacs instead of 44.80 Lacs in case of Anant - 3 and Rs. 11.83 Lacs instead of Rs.25.84 Lacs in case of Arisht - 1 apportioned by Ld. A.O. Copy of the profit and loss account of the head office of the company is enclosed at Annexure G relevant page - 17.

The Ld. CIT (A)-I have also decided this ground in favour of the assessee vide order dated 10.11.2004 on its appeal No.64/IT/CIT(A)-I/04-05 for Assessment Year 2001-02. Copy enclosed at Annexure H relevant page 35

Ld. CIT(A) held that in addition to the above it is submitted by the Ld. Counsel by enclosing copy of the order dated 26.12.2007 for the assessment year 1998-99, that the A.O. on similar issue while deciding the set aside matter by the ITAT in the case of Vardhman Spinning & General Mills, has worked out such deduction taking into account the expenses net of income of the head office. It is, therefore, the contention of the Ld. Counsel that alternatively the claim of the assessee should be considered in respect of the expenses net of income of the head office.

Ld. CIT(A) considered the contention of the Ld. Counsel for the assessee and perused the relevant record. It is an undisputed position that the head office incurs expenses on behalf of all the units of an assessee.

Therefore, the correct income of the units cannot be worked out unless the proportionate expenses from the head office are taken into account. However, as duly submitted by the Ld. Counsel, in the case of Vardhman i Spinning & General Mills Ltd. for the assessment year 1998-99 while giving effect to the order of the ITAT, on similar issue, the A.O. has allocated head office expenses net of the income. This appears to be quite in order and , logical. Therefore, in the case of the assessee also the A.O. is directed to allocate the expenses net of income of the head office (expenses of Head Office (-) income, if any, of head office) in the proportion of the turnover of these units as already done in the assessment order and to work out and allow deduction u/s 10B in respect of these units accordingly. This ground of appeal is disposed off in the above manner.

11.2 Before us the Ld. AR argued that expenses like charity and donation provision for fall in value of investments prior period expenses should not be apportioned. We find no reason to give special treatment when the entire expenditures have been apportioned.

11.3 We have gone through the order of the Ld. CIT(A) which was relied on the order of the ITAT Chandigarh for the A.Y.1998-99 in assessee's own case. Since the order of the Ld. CIT(A) is based on the order of the ITAT in assessee's own case in the absence of any contrary findings, we decline to interfere in the order of the Ld. CIT(A).

11.4 As a result this ground of appeal of the Assessee and of the Revenue is dismissed.

**12. Issue No. 7: Treatment of Loss on export of trading goods for computation of deduction under section 80HHC:**

A.Y. 2003-04

Ground No. 4 of the Revenue's Appeal

12.1 The brief background of the issue is that the Assessing Officer has not adjusted the profits of eligible business for deduction under section 80HHC with the amount of loss on export of trading goods.

12.2 It was argued before the Ld. CIT(A) that the deduction under section 80HHC(3)(c)(i) was computed by taking the profits of the business instead of adjusted profits of the business. The Assessing Officer omitted to adjust the profits of the business by the amount of loss on sale of trading exports.

12.3 Before us the Ld. DR relied on the assessment while Ld. AR relied on the case of IPCL Laboratories Vs. DCIT (2004) 266 ITR 521 (Supreme Court). With the judgment of the Hon'ble Supreme Court the matter stand settled, the relevant portion of the Hon'ble Supreme Court is as under:

*" With the adoption of the dual system for computing export profit, the computation of the disclaimed export turnover also required modification. The Finance Act has therefore amended section 80HHC in order to provide that ,where the export or trading house disclaims the tax concession in favour of the supporting manufacturer, the concession to the export or trading house will be reduced by the amount which bears to the total export profits of trading goods the same proportion as the disclaimed export turnover bears to the total export turnover of trading goods. The formula in such cases will now be-*

80HHC concession=

Export profits-[Export profits on trading goods x disclaimed export turnover]  
Total export turnover

..... submitted that if even both profits and losses are to be taken into account then on a disclaimer the losses will also have to be considered as negative profits and as per the Board circular the calculation would be as follows:

"80HHC concession=

$$\frac{\text{Export profits} - [\text{Export profits on trading goods} \times \text{disclaimed export turnover}]}{\text{Total export turnover of trading goods}}$$

..... submitted that even on this calculation the assessee is entitled to deduction of Rs. 3,78,80,937/-. We are unable to accept this submission. The calculation as per the Board circular would not be as claimed. The Board circular nowhere provides for negative profits.

The Board circular also shows that only positive profits can be considered for purposes of deduction. We, therefore, see no substance in the appeal. The same stands dismissed. There shall be no order as to costs. "

12.4 Keeping in view the above judgment, this ground of Revenue's appeal is allowed.

### **13. Issue No. 8. Deduction under section 80IB on balance profits of EOU Unit:**

A.Y. 2003-04

Ground No. 5 of the Revenue's Appeal

A.Y. 2004-05

Ground No. 2 of the Revenue's Appeal

A.Y. 2005-06

Ground No. 4 of the Revenue's Appeal

13.1 The Assessing Officer observed that one unit of the assessee is a 100% EOU and also claiming deduction under section 80IB on the grounds that double deduction is not allowable as per under section 80AB.

13.2 The Ld. CIT(A) agreed the Assessing Officer's contention that where the income of a unit is taken to be exempt under the provisions of Section 10B of the Act, no part of its income is included in the gross total income and therefore no deduction could be allowed under any other Section of Income Tax Act, 1961 included in Chapter XVI. The Ld. CIT(A) agreed with the contention of the assessee that deduction under section 80IB is claimed only on the domestic profits of the undertaking. It was held that the export profits claimed under section 10B are not included in claiming exemption under section 80IB.

13.3 The Ld. CIT(A) has referred the matter to the Assessing Officer to verify the claim. Since the principle has been laid down by the Ld. CIT(A) that only

domestic profits are eligible for deduction under section 80IB, we see no reason to interfere in the order of the Ld. CIT(A).

13.4 As a result, the grounds of appeal of the Revenue become infructuous.

**14. Issue No. 9: Deduction under section 80IB on Misc. Income:**

A.Y. 2003-04

Ground No. 7 of the Revenue's Appeal

Ground No. 5 of the Assessee's Appeal

14.1 The assessee has received rent from employees and DEPB benefit. The Assessing Officer observed that rent receipts have commercial connection with the profits of the industrial undertaking and there is no direct nexus between the profits and manufacturing activity of the unit. The Assessing Officer observed that these are receipts and not profits derived from the business. Regarding DEPB the Assessing Officer held that they are export incentives and not derived from the Industrial undertakings. The Assessing Officer relied on the decision of Hon'ble Supreme Court in the case of Sterling Foods 237 ITR 579.

14.2 The CIT(A) held against the assessee that DEPB is not covered as profits derived from industrial undertaking and also the rent receipt. The Ld. CIT(A) relied on the decision of the jurisdictional High Court in the case of Liberty India Ltd 207 CTR 243.

14.3 Before us, Ld. DR relied on the decision of Sterling Foods 237 ITR 579 whereas Ld. AR relied on the decision of the ITAT order dt. 05/01/2016 in case of Mahavir Spinning Mills Ltd. in ITA No. 212/CHD/2005 for the A.Y. 2001-02.

14.4 We have gone through the order and find that the order of 2001-02 dealt with insurance claims, misc. income, and sundry balances. We have gone through the judgment of Hon'ble Supreme Court in the case of Liberty India Ltd. wherein it has been held as under:

*"DEPB and Duty Drawback are not eligible for deduction u/s 80-IB*

*The assessee claimed that profit from Duty Entitlement Passbook Scheme (DEPB) and Duty Drawback Scheme are "derived from the business of the Industrial Undertaking" and consequently eligible for deduction u/s 80-IB. On appeal by the assessee, HELD, rejecting the plea:*

(1) The Act broadly provides for two types of tax incentives, namely, investment linked incentives and profit linked incentives. Ch VI-A essentially belongs to the category of "profit linked incentives";

(2) When ss. 80-IA/80-IB refer to profits derived from eligible business, it is not the ownership of that business which attracts the incentives but the generation of profits (operational profits). It is for this reason that Parliament has confined deduction to profits derived from eligible businesses;

(3) Each of the eligible business in sub-sections (3) to (11A) constitutes a stand-alone item in the matter of computation of profits. That is the reason why the concept of "Segment Reporting" stands introduced in the Indian Accounting Standards (IAS) by the Institute of Chartered Accountants of India (ICAI);

(4) Ss. 80-IB/80-IA are a Code by themselves as they contain both substantive as well as procedural provisions. S. 80-IB allows deduction of profits and gains derived from the eligible business. The words "derived from" is narrower in connotation as compared to the words "attributable to". By using the expression "derived from", Parliament intended to cover sources not beyond the first degree;

(5) Though the object behind DEPB etc is to neutralize the incidence of customs duty payment on the import content of export product DEPB credit/duty drawback receipt do not come within the first degree source as the said incentives flow from Incentive Schemes enacted by the Government or from s. 75 of the Customs Act. Such incentives profits are not profits derived from the eligible business u/s 80-IB. They are 'ancillary profits' of such undertakings;

(6) Even as per AS-2 and the ICAI Guidance Note, duty drawback, DEPB benefits, rebates etc. cannot be credited against the cost of manufacture of goods but have to be shown as an independent source of income beyond the first degree nexus between profits and the industrial undertaking."

14.5 Respectfully following the judgment of the Hon'ble Supreme Court, the issue of DEPB and rent as held by the Ld. CIT(A) is hereby confirmed.

14.6 As a result, this ground of appeal of the Revenue is allowed and of the Assessee is hereby dismissed.

#### **15. Issue No. 10: Reduction of scrap sales from total turnover for 80HHC:**

A.Y. 2004-05

Ground No. 6 of the Revenue's Appeal

15.1 The assessee included sale of scrap in total turnover while computing deduction under section 80HHC. The Assessing Officer has excluded entire scrap sale from total turnover and profits of the business for calculating that deduction under section 80HHC. The Assessing Officer relied on the judgment in the case of Mahavir Cycles Industries to exclude the profits of scrap.

15.2 Ld. CIT(A) relied on the decision of ITAT Chandigarh in the case of Kangaroo Industries in ITA 23/CHD/2007 for the A.Y. 2004-05 wherein it was held

that the case of manufacturing, sale of scrap is not to be reduced from the total turnover and profits of the business.

15.3 Before us, Ld. AR relied on the case of R.N. Gupta 351 ITR 369 wherein it was held as under:

*“(i) Whether in facts and circumstances of the case, the action of the Id. authorities below in ignoring the fact that scrap is incidental to manufacturing of finished good and no expense is incurred for the same and therefore the entire scrap sale forms part of business profit and thus includible for the computation purposes u/s 80 HHC is legally unsustainable in the eyes of law?*

*(ii) Whether in fact and circumstances of the case, the action of the authorities below in acting on its own presumptions and ignoring the law laid down by this Hon'ble Court in CIT v/s Bicycle Wheels (India) is legally unsustainable in the eyes of law?*

*(iii) Whether in fact and circumstances of the case, the action of the authorities below, the impugned orders Annexure A-1 and A-3 are legally sustainable in the eyes of law?*

Though the assessee has framed the aforesaid three questions of law, yet it is question No.(i) which arises for consideration of this Court.

The assessee is engaged in manufacturing of goods for export. In the process of manufacturing, the scrap is generated, which is a bi-product of manufacturing activity. The Assessing Officer has not accepted the explanation of the assessee that no expenses are incurred for generation of scrap, and therefore, expenditure should be taken as nil for not accepted. The Assessing Officer has disallowed the deductions claimed by the assessee under Section 80 HHC of the Income Tax Act, 1961.

The learned Commissioner of Income Tax (Appeals) accepted the appeal of the assessee relying upon a judgment of this Court in CIT, Ludhiana Vs. Bicycle Wheels 335 ITR 388 that scrap is generated in the course of manufacturing of goods. The scrap is systematically sold by the assessee forming part of its business. It was held that value of scrap generated goes on to increase the profits of organization and that there is no profit element embedded in the value of scrap. Thus, the order of the Assessing Officer was set aside. But in further appeal before the Tribunal at the instance of Revenue, the Tribunal recorded the following findings:-

*"9. As regards the inclusion of value of scrap sale in the profits of the business for computing the relief u/s 80HHC, the entire value of scrap sales cannot be included in the profits of the business. What can be included in the profits of the business for working out the relief u/s 80HHC is the profit element in respect of sales of scrap and not the total sales of scrap. On the facts of the case, the profit element on sale of scrap is estimated at 7.5 percent. The AO is directed to include 7.5 percent of sales of scrap in the profits of the business for working out the relief u/s 80HHC. In this view of the matter, the order of the Id. CIT(A) directing the AO to include the total sales of scrap in the profits of business is vacated. The AO is directed to include only 7.5 percent being estimated element of profit in the sale of scrap in the profits of the business for working out the relief u/s 80HHC.*

Learned counsel for the assessee has vehemently argued that the order of the Tribunal runs counter to the judgment of this Court in Mahavir Cycle Industries Vs. The Commissioner of Income Tax, Ludhiana and another, - I.T.A. No.823 of 2008 decided on 08.04.2011, wherein reliance has been placed upon an earlier order of this Court in Bicycles Wheels' case (supra) as well as the order of the Kerala High Court in The Commissioner of Income Tax, Cochin v. Kar Mobiles Limited - Income Tax Appeal No.773 of 2009 decided on 15.01.2010. Therefore, it is

contended that the findings recorded by the Tribunal runs counter to the judgments of this Court.

Mr. Katoch, learned counsel for the revenue has argued that the scrap value has to be included in the total turn-over but cannot be included in business profit as only the profit after deducting the expenses of generation of scrap can be added in the business profit.

We find that the argument raised by Mr. Katoch is wholly untenable. The expenditure is incurred by the assessee not for generation of the scrap but for generation of the finished product. There is and cannot be any expenses which are incurred for generation of scrap. Scrap is bi-product of the manufacturing activity. Therefore, there are no expenses which could be excluded from the sale of scrap. Since the question of law stands answered by this Court in favour of assessee in the above mentioned judgments, therefore, the first substantial question of law is answered in favour of the assessee and against the Revenue."

15.4 Following the ratio of the above decision of the Hon'ble jurisdictional High Court the appeal of the Revenue on this ground is dismissed.

## **16. Issue No. 11: Sales Tax Subsidy - Capital Receipt or not:**

A.Y. 2002-03  
Ground No. 8 of the Assessee's Appeal

A.Y. 2003-04  
Ground No. 1 of the Assessee's Appeal

A.Y. 2004-05  
Ground No. 2, 3 and 6(iv) of the Assessee's Appeal

A.Y. 2005-06  
Ground No. 4 and 5 of the Assessee's Appeal

16.1 The excerpts from the order of Ld. CIT(A) is as under:

5. This issue has been discussed in para 14.0 on page 21 of the assessment order. During the relevant period the assessee received Sales-tax subsidy of Rs.4,89,49,449/- from the Govt. of Punjab. In the revised return filed on 29.10.2004, the assessee claimed this receipt as a capital receipt and accordingly reduced this amount from its income. The A.O. has referred to the Scheme as per copy of the notification No.INC-11/15/43/96-5/IB/4176 dated 01.06.1996 of Department of Industries and Commerce to explain the nature of the subsidy received by the assessee. The A.O. also referred to a number of decisions in support of her contention that the nature of the Sales-tax subsidy received by the assessee is revenue. She accordingly recomputed the income of the assessee company by considering the above mentioned amount as a revenue receipt.

6. In appeal, the Ld. Counsel for the assessee filed written submissions which are reproduced as under: -

The Ld. Assessing Officer vide the impugned order disallowed the claim of assessee for treating the amount of sales tax exemption/subsidy as capital receipt. The Ld. Assessing officer while disallowing the amount of sales tax exemption/subsidy held that the Punjab Scheme is similar to that of Andhra Scheme. She further held that the Punjab scheme is different from Maharashtra Scheme and therefore the judgment of Hon'ble Special Bench, Mumbai in the case of Reliance Industries is not applicable in present case. The points of distinction as noted by the Ld. AO and our explanation to the same are as under:

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1. The Ld. Assessing officer noted that the Punjab Scheme is different from Maharashtra Scheme. Punjab government Scheme provides incentive after the unit starts commercial production. Under Maharashtra Scheme the unit become entitle to incentive during the setting up of unit stage itself.

In this connection, it is submitted that Ld. AO had erred in holding so. In the Punjab scheme also, industry was eligible for sales tax incentive since inception. Only the application for eligibility certificate under Punjab scheme was to be made within 6 months from date of starting commercial production. It is further submitted that both in Maharashtra as well as Punjab scheme, eligibility certificate was issued effective from the date of commencement of commercial production. Further Hon'ble IT AT, Special Bench in the case of Reliance Industries Ltd held that the purpose and object of the scheme under which the exemption/subsidy is given is of more fundamental importance than the fact that the exemption/subsidy was received after the commencement of production or conditional upon it. (Please refer Para 37 at page 312 of the Order of Hon'ble Bench in the case of DCIT V. Reliance Industries Limited (2004) 88 ITD 273 (Mum)(SB)).

2. The Ld. Assessing Officer further noted that the Punjab Scheme is Different from Maharashtra scheme as the eligibility period under Punjab scheme is counted from the date of commencement of commercial production i.e. commercial sale of product.

In this connection it is submitted that the under both the schemes the assessee is entitled to subsidy / exemption from sales tax since its inception but eligibility certificate was issued effective from the date of commencement of its commercial production. There is no difference between the date of commencement of eligibility certificate under both the scheme as the period of exemption starts from the date of commencement of commercial production.

3. The Ld. Assessing Officer further noted that under Maharashtra Scheme, the purpose of scheme was to fund a part of the cost of setting up of industry in the backward area, while in the Punjab Scheme the purpose of scheme is not to fund a part of cost of setting up of unit but to lend a helping hand to the industrial undertaking in running its business more profitably.

In this connection it is submitted that under Punjab Scheme the object of incentive was to build a conducive industrial climate to attract fresh investment and also facilitate the growth and expansion of the existing industry. The industrial unit was granted incentive according to location and fixed capital invested. Based upon the above the unit was granted the incentive of sales tax exemption for seven years to the extent of notified capital invested. From the above it is clear that like Maharashtra Scheme (where the unit get subsidy/exemption from sales tax in order to accelerate the flow of investment in the industry and infrastructure) the unit get exemption/subsidy for setting up of industry.

From the factual position given above, it is clear that the amount of sales tax subsidy/exemption given by government of Punjab is of capital nature and it is an incentive given to spurt industrial growth and generation of employment opportunities to its unemployed youth through rapid industrialization of the state. Therefore the amount of sales tax subsidy/exemption received by the company being a capital receipt should be exempted from tax.

6.1 In addition to the above written submissions of the assessee it was contended by the Ld. Counsel that the ratio of the decision of the Hon'ble Punjab & Haryana High Court in the case of Abhishek Industries Ltd. 286 ITR 1, would not apply in the case of the assessee. It is submitted that in case of Abhishek Industries (supra), the assessee failed to establish on record that the subsidy given by the Punjab Govt, in the form of Sales-tax exemption was a capital receipt. It is further submitted that the SLP filed by that assessee against the above referred judgement by the

Hon'ble Punjab & Haryana High Court has been admitted by the Hon'ble Supreme Court. In view of the above, it is contended that the addition made by the A.O. by considering the Sales-tax subsidy as revenue receipt may be deleted.

7. I have carefully considered the contention of the Ld. Counsel for the assessee and perused the relevant record. Though the A.O. has referred to the provisions of the Scheme under which the subsidy as above was received by the assessee and also referred to a number of decisions in support of her stand that the receipt of the subsidy was a revenue receipt in the hands of the assessee, it is seen that the issue is squarely covered by the decision of the Hon'ble Jurisdictional High Court of Punjab & Haryana in the case of the Abhishek Industries (supra). The Ld. Counsel has contended that the ratio of the decision would not apply in the case of the assessee. However, I do not agree with this contention and it is to be considered that the ratio of this

decision applies in the facts & circumstances of the assessee's case with full force. Filing of SLP against this decision before the Hon'ble Supreme Court, as further contended by the Ld. Counsel, would also not help the case of the assessee so far any decision of the Apex Court overruling such decision is there. In view of the above, this ground of appeal of the assessee is dismissed and the action of the A.O. is upheld. We have gone through the orders and arguments, we find that the matter has already been dealt in the case of Mahavir Spinning Mills Ltd. Vs. ACI in ITA No. 212-CHD/2005 wherein it has been held as under:

36. Ground No. 10 of the appeal reads as under:

10. That the dl CIT(A) has erred in law and facts in entertaining the claim of the assessee, filed after the expiry of period stipulated under the provision of section 139(5) of the IT. Act.

37. / The issue involved **is** regarding the assessee's claim **for** treating the amount of Rs. 3,60,81,695/- representing exempt sale tax as capital receipt. The assessee made this claim vide letter dated 26.3.2004. It appears that the assessee has not submitted revised return u/s 139(5) of the Act within the stipulated time, and therefore, the Assessing officer did not consider the same. On appeal, the CIT(A) directed the Assessing officer to check up the relevant Sales Tax Rules of the Punjab Government and allow the relief admissible to the assessee as per law.

38. Now the Revenue has challenged the above action of the CIT(A) in this appeal.

39. It if. observed that the issue in hand is covered in favour of the assessee by our order dated 21.10.2015 in the case of Vardhman Acrylic Limited, Ludhiana Vs. Addl. CIT and Others in ITA No. 773/Chd/2012 and Others relating to assessment year 2006-07. While deciding a similar issue, we have held as under:-

"7. We have heard the learned representatives of both the parties, perused the findings of the authorities below and considered the material available on record. We have carefully perused the order of IT. A.T. in the case of Bhushan Limited (supra) and come to a conclusion that this is one of the cases which was before the Hon'ble High Court on the same issue of sales tax subsidy. However, the only difference in the facts of the case of Bhushan Limited (supra) and the current assessee is that in the case of Bhushan Limited (supra), the sales tax subsidy was received from the Government of West Bengal under "West Bengal Incentive Scheme 1999", while in the case of the assessee in question, the subsidy has been received from the Government of Gujarat under the "New Incentive Policy-Capital investment Incentive to Premier/Prestigious Unit Scheme 1995-2000". Therefore, in order to compare the policies of two different States, we have very carefully gone through the schemes of both the Governments produced before us. Since as per the directions of the Hon'ble High Court, we

have to Judge the nature and purpose of the sales tax subsidy received by the assessee. We see that the scheme of the Gujarat Government has **aimed to** trigger off accelerated industrial development and economic growth. For **this** purpose, to provide special package to certain types of industries, the scheme was formulated. To be eligible to get the benefit of this scheme mainly the criteria has been laid down with regard to the fixed capital investment, project related infrastructural investment, social infrastructural investment and common and public purpose infrastructure. All these requirements are towards capital investments. Further a closer look at the clause relating to ineligible investment shows that short term investment or investment of revenue nature are **not** eligible for this scheme. A certificate of being declared as Permanent Prestigious Unit has been given to the assessee dated 18.5.2002, whereby the details of investment of the project and employment are given. We have also gone through the scheme of the Bengal Government which was in question before the Chandigarh Bench of the I.T.A.T. in the case of Bhushan Limited (supra). Though both the schemes of Gujarat Government and West Bengal Government are not verbatim, the sum and substance of both the schemes are same. As directed by the Hon'ble High Court on the basis of judgment in the case of Ponny Sugars & Chemicals Ltd. (supra), the nature of the sales tax subsidy is to be decided on the basis of character of the receipt in the hands of the assessee. We see that the sales tax subsidy received by the assessee is capital in nature and is not subjected to tax. In arriving at this conclusion, we are guided by the order of the I.T.A.T. in the case of Bhushan Limited (supra), in which the Coordinate Bench of the I.T.A.T. in the same set of facts and circumstances has held as under:

"24. The Hon'ble Supreme Court in the case of Ponni Sugars & Chemicals Ltd. (supra) considering its earlier decision in the case of Sahney Steels & Press Works Ltd. (supra) directed that the test is that the character of the receipt in the hands of assessee has to be determined with respect to the purpose for which subsidy is given. In other words, in such cases, one has to apply the purpose test. The point of time at which subsidy is paid, is not relevant. The source is immaterial. The form of subsidy is immaterial.

#### **25. Considering the facts of the case and the West Bengal**

Incentive Scheme, 1999 in the light of the judgement of the Hon'ble Supreme Court in the case of Ponni Sugars & Chemicals Ltd. (supra), it is clear that the unit of assessee was set up as per scheme formulated by Government of West Bengal and assessee has been allowed remission of sales tax for 12 years upto 100% of gross fixed capital investment/asset of the approved project. The incentive scheme was available for location of the unit. No incentive is available to units located in group 'A'. The unit of assessee is located in group 'B' (Hooghly). The subsidy would help the growth of industry and not to supplement profit. Subsidy is determined with reference to the fixed capital investment/asset and not profit. No working capital is considered in the scheme. The Id. DR says that the subsidy is given for 12 years after production and as such it is revenue in nature. The arguments of Id. DR cannot be accepted in view of the above facts because the scheme is made to encourage the promotion of industries/setting up in the State of West Bengal. The incentives are provided to approved projects only. The purpose of giving subsidy is thus, to promote and set up industries in State of West Bengal. The eligibility certificate was issued before commencement of production, therefore subsidy based on fixed capital investment. The time of 12 years after commencement of the production is not relevant. The source of subsidy out of sales tax is immaterial. The form of subsidy is also not relevant. The object/purpose of assistance under the subsidy scheme was to enable the assessee to set up new unit in State of West Bengal. Therefore, the receipt of the sales tax subsidy in the hands of assessee was capital in nature. The decisions relied on by Id. DR would not support the case of the revenue. The decision cited by Id. counsel for the

assessee clearly support the submission of Id. counsel for the assessee that the sales tax subsidy received by the assessee are capital in nature. We may also nxyte here that the same scheme under West Bengal Incentive Scheme, 1999 under reference was subject matter of consideration before IT AT Kolkatta Bench in the case of Keventer Agro Ltd. (supra) and the Tribunal also decided the issue in favour of the assessee holding that the West Bengal Incentive Scheme, 1999 categorically encourage the promotion of industries in the State of West Bengal.

26. Considering the facts and circumstances of the case in the light of decision of the Hon'ble Supreme Court in the case of Ponni Sugars & Chemicals Ltd. (supra) and considering the above discussion, we are of the view that sales tax subsidy received by the assessee is capital receipt in nature and are not subjected to tax. The additions made by the Assessing Officer on account of receipt of sales tax subsidy are accordingly deleted in all the assessment years in appeals. The issue remanded to the Tribunal is thus, decided in favour of the assessee and against the revenue in all the appeals under reference. "

<sup>8</sup>Respectfully following the order of the Coordinate Bench of the Tribunal, we hereby hold that the sales tax subsidy received by the assessee is capital in nature and, therefore, not taxable.

9- The appeal of the assessee is allowed. '

16.2 Further in the case of Mahavir Spinning Mills Ltd. Vs. JCIT in ITA No. 344/CHD/2009 for the A.Y. 1997-98 the coordinate Bench of ITAT held as under:

*That the sales tax exemption/incentive received by the company constitutes capital receipt and should not be taken into account while computing its total income".*

3. Vide its order dated 31.10.2006 the I.T.A.T. admitted the above ground but decided the same against the assessee by following the judgment of the Hon'ble Punjab & Haryana High Court in the case of CIT Vs. Abhishek Industries Limited (2006), 286 ITR1 (P&H). The assessee went in appeal before the Hon'ble High Court, whereby the High Court vide its order dated 18.12.2014 remanded back the matter to the file of the I.T.A.T. holding that the issue of sales tax subsidy being capital or revenue in nature is to be decided in view of the judgment of Hon'ble Supreme Court in the case of CIT Vs. Ponni Sugars & Chemicals Limited (2008), 306 ITR 392 (SC).

4. Now, the sole issue before us is to decide whether the sales tax subsidy received by the assessee is capital or revenue in nature. By the order of the Hon'ble Punjab & Haryana High Court in same circumstances a bunch of cases were sent back to the file of the I.T.A.T. to decide the issue taking into consideration the judgment of Ponni Sugars & Chemicals Limited (supra).

5. The same issue was decided in assessee's sister concerns' case i.e. Vardhman Textiles Limited in iutia.773/Chd/2012 together with ITA No.987/Chd/2006, ITA No.341/Chd./2007, ITA No.756/Chd/2011 (M/s Steel Strips Wheels Limited) and ITA No.896/Chd/2006 (M/s Indian Acrylics Limited) vide consolidated order dated 21.10.2015. In this order, in the cases of Steel Strips Wheels Limited in ITA No.987/Chd/2006, ITA No.341/Chd/2007 and ITA No.756/Chd/2011 and in the case of Indian Acrylics Ltd. in ITA No.896/Chd/2006, the issue with regard to sales tax subsidy from Punjab Government was considered. However, the detailed

discussions were made in the case of Vardhman Acrylic Limited in ITA No.773/Chd/2012, in which the issue was that of subsidy received from Gujarat Government. The appeal in the case of Steel Strips Ltd. (supra) and Indian Acrylics (supra) were decided in favour of the assessee. Since in the present case also the assessee has received sales tax subsidy from Punjab Government, which was the issue in Steel Strips Ltd. (supra) and Indian Acrylics Ltd. (supra). However, in order to make this order self-contained, we are reproducing the findings given in these cases together with that of Vardhman Acrylic Limited (supra), which reads as under :

"7. We have heard the learned representatives of both the parties, perused the findings of the authorities below and considered the material available on record. We have carefully perused the order of I.T.A.T. in the case of Bhushan Limited (supra) and come to a conclusion that this is one of the cases which was before the Hon'ble High Court on the same issue of sales tax subsidy. However, the only difference in the facts of the case of Bhushan Limited (supra) and the current assessee is that in the case of Bhushan Limited (supra), the sales tax subsidy was received from the Government of West Bengal under "West Bengal Incentive Scheme 1999", while in the case of the assessee in question, the subsidy has been received from the Government of Gujarat under the "New Incentive Policy-Capital investment Incentive to Premier/Prestigious Unit Scheme 1995-2000". Therefore, in order to compare the policies of two different States, we have very carefully gone through the schemes of both the Governments produced before us. Since as per the directions of the Hon'ble High Court, we have to judge the nature and purpose of the sales tax subsidy received by the assessee. We see that the scheme of the Gujarat Government has aimed to trigger off accelerated industrial development and economic growth. For this purpose, to provide special package to certain types of industries, the scheme was formulated. To be eligible to get the benefit of this scheme mainly the criteria has been laid down with regard to the fixed capital investment, project related infrastructural investment, social infrastructural investment and common and public purpose infrastructure. All these requirements are towards capital investments. Further a closer look at the clause relating to ineligible investment shows that short term investment or investment of revenue nature are not eligible for this scheme. A certificate of being declared as Permanent Prestigious Unit has been given to the assessee dated 18.5.2002, whereby the details of investment of the project and employment are given. We have also gone through the scheme of the Bengal Government which was in question before the Chandigarh Bench of the I.T.A.T. in the case of Bhushan Limited (supra). Though both the schemes of Gujarat Government and West Bengal Government are not verbatim, the sum and substance of both the schemes are same. As directed by the Hon'ble High Court on the basis of judgment in the case of Ponny Sugars & Chemicals Ltd. (supra), the nature of the sales tax subsidy is to be decided on the basis of character of the receipt in the hands of the assessee. We see that the sales tax subsidy received by the assessee is capital in nature and is not subjected to tax. In arriving at this conclusion, we are guided by the order of the I.T.A.T. in the case of Bhushan Limited (supra), in which the Coordinate Bench of the I.T.A.T. in the same set of facts and circumstances has held as under:

"24. The Hon'ble Supreme Court in the case of Ponni Sugars & Chemicals Ltd. (supra) considering its earlier decision in the case of Sahney Steels & Press Works Ltd.(supra) directed that the test is that the character of the receipt in the hands of assessee has to be determined with respect to the purpose for which subsidy is given. In other words, in such cases, one has to apply the purpose test. The point of time at which subsidy is paid, is not relevant. The source is immaterial. The form of subsidy is immaterial.

25. Considering the facts of the case and the West Bengal Incentive Scheme, 1999 in the light of the judgement of the Hon'ble Supreme Court in the case of Ponni Sugars & Chemicals Ltd. (supra), it is clear that the unit of

assessee was set up as per scheme formulated by Government of West Bengal and assessee has been allowed remission of sales tax for 12 years upto 100% of gross fixed capital investment/asset of the approved project. The incentive scheme was available for location of the unit. No incentive is available to units located in group 'A'. The unit of assessee is located in group 'B' (Hooghly). The subsidy would help the growth of industry and not to supplement profit. Subsidy is determined with reference to the fixed capital investment/asset and not profit. No working capital is considered in the scheme. The Id. DR says that the subsidy is given for 12 years after production and as such it is revenue in nature. The arguments of Id. DR cannot be accepted in view of the above facts because the scheme is made to encourage the promotion of industries/setting up in the State of West Bengal. The incentives are provided to approved projects only. The purpose of giving subsidy is thus, to promote and set up industries in State of West Bengal. The eligibility certificate was issued before commencement of production, therefore subsidy based on fixed capital investment. The time of 12 years after commencement of the production is not relevant. The source of subsidy out of sales tax is immaterial. The form of subsidy is also not relevant. The object/purpose of assistance under the subsidy scheme was to enable the assessee to set up new unit in State of West Bengal. Therefore, the receipt of the sales tax subsidy in the hands of assessee was capital in nature. The decisions relied on by Id. DR would not support the case of the revenue. The decision cited by Id. counsel for the assessee clearly support the submission of Id. counsel for the assessee that the sales tax subsidy received by the assessee are capital in nature. We may also note here that the same scheme under West Bengal Incentive Scheme, 1999 under reference was subject matter of consideration before ITAT Kolkatta Bench in the case of Keventer Agro Ltd. (supra) and the Tribunal also decided the issue in favour of the assessee holding that the West Bengal Incentive Scheme, 1999 categorically encourage the promotion of industries in the State of West Bengal.

26. Considering the facts and circumstances of the case in the light of decision of the Hon'ble Supreme Court in the case of Ponni Sugars & Chemicals Ltd. (supra) and considering the above discussion, we are of the view that sales tax subsidy received by the assessee is capital receipt in nature and are not subjected to tax. The additions made by the Assessing Officer on account of receipt of sales tax subsidy are accordingly deleted in all the assessment years in appeals. The issue remanded to the Tribunal is thus, decided in favour of the assessee and against the revenue in all the appeals under reference."

8. Respectfully following the order of the Coordinate Bench of the Tribunal, we hereby hold that the sales tax subsidy received by the assessee is capital in nature and, therefore, not taxable.

9. The appeal of the assessee is allowed.

**ITA No.897/Chd/2006 :**  
**ITA No.341/Chd/2007 :**  
**ITA No.756/Chd/2011 :**  
**(M/s Steel Strips Wheels Limited.)**  
**&**  
**ITA No.896/Chd/2006 :**  
**(M/s Indian Acrylics Limited)**

"11. In these cases, the assesses have received sales tax subsidy from Punjab Government under the scheme named, 'Industrial Policy & Incentive Code, 1996'. We have gone through the said policy and found that the scheme though not verbatim as that of West Bengal or Gujarat schemes, but the sum and substance of all these schemes are the same, therefore, relying on our finding given in ITA No.773/Chd/2012, we hold that the sales tax subsidy received by the assessee is capital in nature."

6. *Respectfully following the order of Coordinate Bench, the issue is decided in favour of the assessee.*

7. *In the result, the appeal of the assessee is allowed.*

16.3 Since the matter is already stands adjudicated by this Tribunal, the appeal of the assessee on this ground is allowed.

## **17. Issue No. 12: Deduction under 3<sup>rd</sup> Proviso to 80HHC**

A.Y. 2002-03

Ground No. 9 of the Assessee's Appeal

A.Y. 2003-04

Ground No. 4(i) of the Assessee's Appeal

A.Y. 2004-05

Ground No. 6(v)(a) of the Assessee's Appeal

17.1 The Assessing Officer has not allowed deduction under section 80HHC(3)(c)(iii) on export incentives. The assessee submitted before the Ld. CIT(A) that this amendment is not applicable as company adoption to choose duty drawback or DEPB being duty remission scheme. He argued that the Assessing Officer had reduced total DEPB amounting to Rs. 4.10 Crores instead of losses from transfer of DEPB amounting to Rs. 12.34 Crores from export incentives while calculating deduction under proviso to Section 80HHC(3). He further argued that amendment relating to export incentives is not applicable and DEPB of Rs. 4.10 Crores included duty drawback of Rs. 36.15 Lacs on which no restriction to allow deduction under section 80HHC have been laid in taxation provisions.

17.2 Ld. CIT(A) has confirmed the addition based on the earlier order in the assessee's own case, relying on the decision of Hon'ble jurisdictional High Court in the case of Liberty India Ltd. (supra).

17.3 Before us the assessee brought to our notice the order of Hon'ble jurisdictional High Court in the case of Guru Nanak Exports in C.W.P No. 11328 of 2009 dt. 03/10/2012 wherein the amendment brought with retrospective effect has been held ultra-vires with regard to the retrospective nature of the amendment.

17.4 Since the amendment is not applicable to the case of the assessee before us this ground of appeal of the assessee is hereby allowed.

**18. Issue No. 14: Inclusion of Excise duty, Export Turnover of Traded Goods in total turnover for Calculating deduction under section 10B**

A.Y. 2003-04

Ground No. 3(d) of the Assessee's Appeal

A.Y. 2004-05

Ground No. 5(ii) the Assessee's Appeal

18.1 The Assessing Officer has included Excise duty in the total turnover of the assessee and profits on trades goods in the profit of the under taking for the purpose of calculation of deduction ignoring assessee's contention.

18.2 The Ld. CIT(A) has confirmed the order of the Assessing Officer.

18.3 Similar issue has been ruled in favour of the assessee by the order of the Tribunal in the case of VMT Spinning Co. Ltd. in ITA No. 690/CHD/2007 dt. 29/05/2008 wherein the order of the Ld. CIT(A) directing the Assessing Officer to exclude the profits attributable to the trading export activities and also the turnover of the trading export activity from the total turnover has been upheld. Respectfully following the above order, the appeal of the assessee on this ground is allowed.

**19. Issue No. 15: Exclusion of 90% of Sale Value of DEPB instead of profit for 80HHC**

A.Y. 2003-04

Ground No. 4(h) of the Assessee's Appeal

A.Y. 2004-05

Ground No. 6(v)(b) the Assessee's Appeal

19.1 This matter has been dealt while dealing with the issue of "Deduction under 3<sup>rd</sup> Proviso to 80HHC" above and the rationale with regard to ultra-vires of the proviso is applicable. Hence, the appeal of the assessee on this ground is hereby allowed.

**20. Issue No. 16: Disallowance on account of Foreign Travelling Expenses:**

A.Y. 2004-05

Ground No. 7 the Assessee's Appeal

20.1 The Assessing Officer disallowed 50% of the Travelling expenses amounting to Rs. 4,35,000/-. It was explained that the expenses were incurred for foreign travelling to Swiss, Brazil, Poland, Bangkok and Germany by various officials of the company. Owing to the non production of any evidence Assessing Officer disallowed the said amount.

20.2 Even before the Ld. CIT(A) no evidence in support of the same has been filed. Even before us no evidence has been filed except a table pertaining to period, amount and purpose. No correspondence of whatever could not be furnished. Hence, we decline to interfere in the order of the Ld. CIT(A).

20.3 As a result this ground of appeal of the assessee is dismissed.

**21. Issue No. 17: Disallowance on account of Foreign Travelling Expenses of wife of CMD:**

A.Y. 2004-05

Ground No. 8 the Assessee's Appeal

A.Y. 2005-06

Ground No. 6 of the Assessee's Appeal

21.1 The Assessing Officer disallowed an amount of Rs. 2,95,671/- debited towards the foreign travelling expenses of wife of CMD. The assessee contested that the wife of CMD also attends telephone calls note the messages for CMD in his absence.

21.2 The Ld. AR relied on the judgment of JK Industries Vs. CIT (2011) 11 Taxmann 72 wherein such amount was allowed since the tour has been sanctioned by the Board of Directors. However, no such resolution was produced before us in the instant case hence, keeping in view the facts and circumstances specific to this case and since no specific role of the spouse in the corporate meeting could be elicited, the disallowance made by the Ld. CIT(A) is hereby confirmed.

21.3 As a result, this ground of appeal of the assessee is dismissed.

**22. Issue No. 18: Disallowance of line/bay charges:**

A.Y. 2004-05

Ground No. 9 the Assessee's Appeal

22.1 The Assessing Officer disallowed line / bay charges incurred in Year 1996-97 in the current year. The assessee submitted that the company paid the amount to PSEB as line charges and same was claimed as Revenue expenditure in the A.Y 1996-97 and not charged in that year and charged to P&L Account of year 2004-05. It was submitted that the matter is pending before the appellate authorities. Since the assessee is following mercantile system of accounting for the current year the expenses incurred in the year 1996-97 cannot be allowed during this year.

22.2 This ground of appeal of the assessee is dismissed.

**23. Issue No. 19: Treating of interest reimbursement under TUFs Scheme :**

23.1 This is the additional ground taken for the first time before the Tribunal for the A.Y. 2002-03, 2003-04, 2004-05 and 2005-06.

**23A. Issue No. 13. Reducing 10% of other income from indirect cost for 80HHC:**

This is the additional ground taken for the first time before the Tribunal for the A.Y. 2002-03.

23.2 These issues pertain to the treatment of interest reimbursement on the technology up-gradation fund scheme and reduction of 10% of other income from indirect cost for 80HHC. The assessee has relied on the judgment in the case of Avery Cycle Industries Ltd. Vs. CIT 162 taxmann 429 and the order of the Tribunal in Mahavir Spinning Mill Ltd. Vs. ACIT in ITA No. 537/CHD/2004 dt. 25/01/2008 for the A.Y. 2000-01. Further the assessee also relied on the judgment in the case of VMT Spinning Co. Ltd. Vs. ACIT in ITA No. 682/2007.

23.3 Since the additional grounds taken by the assessee are legal in nature following the above mentioned judgments the same are being admitted.

23.4 Ld. DR argued that the grounds have not been before the Ld. CIT(A) hitherto, an opportunity to be provided to the Revenue to prove to the entire gamut of the issues.

23.5 As the Revenue did not get the benefit of going through the issues and the grounds have been taken for the first time before us, the matter is remanded to the file of Ld. CIT(A) for adjudication and pass a speaking order for all the years in a comprehensive manner. The assessee would be at liberty to make submissions as deemed fit before the Ld. CIT(A).

23.6 As a result this ground of appeal of the Assessee is allowed for statistical purposes.

#### **24. Issue No. 20: Treating of interest income has incurred from other sources :**

A.Y. 2003-04

Ground No. 2 of the Assessee's Appeal

A.Y. 2004-05

Ground No. 1 of the Assessee's Appeal

A.Y. 2005-06

Ground No. 1 of the Assessee's Appeal

Ground No. 1 of the Revenue's Appeal

24.1 The Assessing Officer observed that the assessee has netted of interest income received during the year against the interest paid. Placing reliance on the decision of Hon'ble Supreme Court in the case of Tuticorin Alkali Chemicals and Fertilizers Ltd. Vs. CIT 227 ITR 172 and held that the entire interest is to be taxed under the head "Income From Other Sources".

24.2 Ld.CIT(A) relying on the decisions of the ITAT Chandigarh Bench directed the Assessing Officer to consider the interest income earned by the assessee from FDRs as "Income from other sources" and income received on account of interest income on delayed payments from the customers be considered as "income from business". For the sake of brevity the relevant part of the order of the Ld. CIT(A) is reproduced hereunder:

*"I have carefully considered the contention of the Ld. Counsel for the assessee and perused the relevant record. So far, the interest received by the assessee from FDRs is concerned, in view of the decision of the Hon'ble Jurisdictional Bench of ITAT Chandigarh Bench in the case of M/s Nucon Switchgears (supra), relied upon by the A.O. such interest has to be treated as income of the assessee from other sources. For the interest received by the assessee from the customers on account of delayed payments etc. in a recent case decided by the Hon'ble Jurisdictional Punjab & Haryana High Court in the case of Phatela Cotgin Industries(P) Ltd. Vs. CIT reported t 166 Taxman 9(P&H) it has been held such interest income on belated payments on account of sale to customers of manufactured goods is even "derived" from industrial undertaking and distinct*

from interest received from fixed deposits. In view of the ratio of this binding decision, such an interest income has to be considered to be business income of an assessee. In view of the above, the A.O. is directed to consider the interest income earned by the assessee from FDRs etc. as income from other sources and whereas the income on account of interest on delayed payments from customers etc. should be considered by the A.O. as business income of the assessee."

24.3 Before us Ld. AR relied on the judgment of ACG Associated Capsules Ltd. 343 ITR 89 (Supreme Court) the relevant extract of the judgment is reproduced hereunder:

The assessee filed an appeal against the assessment order before the Commissioner of Income-Tax (Appeals), who confirmed the order of the Assessing Officer excluding ninety per cent of the gross interest and gross rent received by the assessee while computing the profits of the business for the purposes of Section 80HHC. Aggrieved, the assessee filed an appeal before the Income Tax Appellate Tribunal (for short 'the Tribunal'). The Tribunal held, relying on the decision of the Delhi High Court in Commissioner of Income-Tax v. Shri Ram Honda Power Equip [(2007) 289 ITR 475 (Delhi)], that netting of the interest could be allowed if the assessee is able to prove the nexus between the interest expenditure and interest income and remanded the matter to the file of the Assessing Officer. The Tribunal also remanded the issue of netting of the rent to the Assessing Officer with the direction to find out whether the assessee has paid the rent on the same flats against which rent has been received from the staff and if such rent was paid then such rent is to be reduced from the rental income for the purpose of exclusion of business income for computing the deduction under Section 80HHC.

Against the order of the Tribunal, the Revenue filed an appeal before the High Court and the High Court has directed that on remand the Assessing Officer will decide the issue in accordance with the judgment of the High Court in Commissioner of Income-Tax v. Asian Star Co. Ltd. [(2010) 326 ITR 56 (Bom)] in which it has been held that while determining the profits of the business as defined in Explanation (baa) to Section 80HHC, ninety per cent of the gross receipts towards interest and not ninety per cent of the net receipts towards interest on fixed deposits in banks received by the assessee would be excluded for the purpose of working out the deduction under Section 80HHC of the Act.

4. Learned counsel for the assessee submitted that it will be clear from the Explanation (baa) that ninety per cent of any receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in such profits will be excluded for determining the profits and gains of business or profession. He argued that as the net receipts and not the gross receipts towards interest and rent are included in profits and gains of business or profession, ninety per cent of such net interest and net rent and not ninety per cent of gross interest and gross rent are to be excluded for determining the profits of the business under Explanation (baa) to Section 80HHC of the Act.

5. In support of this argument, learned counsel for the assessee relied on the decision of this Court in Distributors (Baroda) P. Ltd. v. Union of India and Others [(1985) 155 ITR 120] in which a Constitution Bench of this Court has held that only the dividends computed in accordance with the provisions of the Act, which is included in the gross total income of the domestic company, shall be taken into account for working out the relief under Section 80M of the Act.

He cited the judgment in Commissioner of Income-Tax v. Shri Ram Honda Power Equip (supra) in which the Delhi High Court has taken a view that the word 'interest' in Explanation (baa) to Section 80HHC connotes 'net interest' and not 'gross interest' and, therefore, in deducting such interest, the Assessing Officer will have to take into account the net interest, i.e. gross interest as reduced by

expenditure incurred for earning such interest. He submitted that the Karnataka High Court in *Commissioner of Income-Tax v. Gokuldas Exports, etc.* [(2011) 333 ITR 214 (Karn)] has taken a similar view relying on the decision of the High Court in *Commissioner of Income-Tax v. Shri Ram Honda Power Equip (supra)*.

6. Learned counsel for the assessee referred to the Memorandum to Finance (No.2) Bill, 1991 explaining the rationale of Explanation (baa) in which inter alia it is stated that as some expenditure might be incurred in earning such incomes, which in the generality of cases is part of common expenses, and thus ad-hoc 10 per cent deduction from such incomes have been provided for to account for these expenses. He submitted that the High Court has not correctly appreciated the Memorandum and has held, relying on the Memorandum, that gross interest and gross rent have to be deducted under Explanation (baa) to Section 80HHC to avoid a distorted figure of export profits.

7. Learned counsel for the Revenue, on the other hand, relied on the reasons given by the Bombay High Court in *Commissioner of Income-Tax v. Asian Star Co. Ltd.* (supra) and submitted that the Bombay High Court has rightly held that ninety per cent of the gross amount received towards interest and rent have to be excluded from the profits and gains of business for computing the profits of the business as defined in Explanation (baa) to Section 80HHC of the Act. He also relied on the Memorandum to the Finance (No.2) Bill 1991 in support of his submission that ninety per cent of the gross interest and gross rent has to be deducted from the profits of the assessee under Explanation (baa).

8. Before we deal with the contentions of learned counsel for the parties, we may extract Explanation (baa) to Section 80HHC of the Act.

"Explanation:- For the purposes of this section,- (baa) "profits of the business" means the profits of the business as computed under the head "Profits and gains of business or profession" as reduced by-

(1) ninety per cent of any sum referred to in clauses (iiia), (iiib), (iiic), (iiid) and (iiie) of Section 28 or of any receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in such profits; and (2) the profits of any branch, office, warehouse or any other establishment of the assessee situate outside India".

9. Explanation (baa) extracted above states that "profits of the business" means the profits of the business as computed under the head "Profits and Gains of Business or Profession" as reduced by the receipts of the nature mentioned in clauses (1) and (2) of the Explanation (baa).

Thus, profits of the business of an assessee will have to be first computed under the head "Profits and Gains of Business or Profession" in accordance with provisions of Section 28 to 44D of the Act. In the computation of such profits of business, all receipts of income which are chargeable as profits and gains of business under Section 28 of the Act will have to be included. Similarly, in computation of such profits of business, different expenses which are allowable under Sections 30 to 44D have to be allowed as expenses. After including such receipts of income and after deducting such expenses, the total of the net receipts are profits of the business of the assessee computed under the head "Profits and Gains of Business or Profession" from which deductions are to be made under clauses (1) and (2) of Explanation (baa).

10. Under Clause (1) of Explanation (baa), ninety per cent of any receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in any such profits are to be deducted from the profits of the business as computed under the head "Profits and Gains of Business or Profession". The expression "included any such profits" in clause (1) of the Explanation (baa) would mean only such receipts by way of brokerage, commission, interest, rent, charges or any other receipt which are included in the profits of the business as computed under the head "Profits and Gains of Business or Profession". Therefore, if any quantum of the receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature is allowed as expenses under Sections 30 to 44D of the Act and is not included in the profits of business as computed under the head "Profits and Gains of Business or Profession", ninety per

cent of such quantum of receipts cannot be reduced under Clause (1) of Explanation (baa) from the profits of the business. In other words, only ninety per cent of the net amount of any receipt of the nature mentioned in clause (1) which is actually included in the profits of the assessee is to be deducted from the profits of the assessee for determining "profits of the business" of the assessee under Explanation (baa) to Section 80HHC.

11. For this interpretation of Explanation (baa) to Section 80HHC of the Act, we rely on the judgment of the Constitution Bench of this Court in *Distributors (Baroda) P. Ltd. v. Union of India and Others*(supra). Section 80M of the Act provided for deduction in respect of certain intercorporate dividends and it provided in sub-section (1) of Section 80M that "where the gross total income of an assessee being a company includes any income by way of dividends received by it from a domestic company, there shall, in accordance with and subject to the provisions of this Section, be allowed, in computing the total income of the assessee, a deduction from such income by way of dividends an amount equal to" a certain percentage of the income mentioned in this Section. The Constitution Bench held that the Court must construe Section 80M on its own language and arrive at its true interpretation according to the plain natural meaning of the words used by the legislature and so construed the words "such income by way of dividends" in sub-section (1) of Section 80M must be referable not only to the category of income included in the gross total income but also to the quantum of the income so included. Similarly, Explanation (baa) has to be construed on its own language and as per the plain natural meaning of the words used in Explanation (baa), the words "receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in such profits" will not only refer to the nature of receipts but also the quantum of receipts included in the profits of the business as computed under the head "Profits and Gains of Business or Profession" referred to in the first part of the Explanation (baa). Accordingly, if any quantum of any receipt of the nature mentioned in clause (1) of Explanation (baa) has not been included in the profits of business of an assessee as computed under the head "Profits and Gains of Business or Profession", ninety per cent of such quantum of the receipt cannot be deducted under Explanation (baa) to Section 80HHC.

12.If we now apply Explanation (baa) as interpreted by us in this judgment to the facts of the case before us, if the rent or interest is a receipt chargeable as profits and gains of business and chargeable to tax under Section 28 of the Act, and if any quantum of the rent or interest of the assessee is allowable as an expense in accordance with Sections 30 to 44D of the Act and is not to be included in the profits of the business of the assessee as computed under the head "Profits and Gains of Business or Profession", ninety per cent of such quantum of the receipt of rent or interest will not be deducted under clause (1) of Explanation (baa) to Section 80HHC. In other words, ninety per cent of not the gross rent or gross interest but only the net interest or net rent, which has been included in the profits of business of the assessee as computed under the head "Profits and Gains of Business or Profession", is to be deducted under clause (1) of Explanation (baa) to Section 80HHC for determining the profits of the business.

13. The view that we have taken of Explanation (baa) to Section 80HHC is also the view of the Delhi High Court in *Commissioner of Income-Tax v. Shri Ram Honda Power Equip* (supra) and the Tribunal in the present case has followed the judgment of the Delhi High Court. On appeal being filed by the Revenue against the order of the Tribunal, the High Court has set aside the order of the Tribunal and directed the Assessing Officer to dispose of the issue in accordance with the judgment of the Bombay High Court in *Commissioner of Income-Tax v. Asian Star Co. Ltd.* (supra).

We must, thus, examine whether reasons given by the High Court in its judgment in *Commissioner of Income-Tax v.*

*Asian Star Co. Ltd.* (supra) were correct in law.

14. On a perusal of the judgment of the High Court in *Commissioner of Income-Tax v. Asian Star Co. Ltd.* (supra), we find that the reason which weighed with the

High Court for taking a different view, is that rent, commission, interest and brokerage do not possess any nexus with export turnover and, therefore, the inclusion of such items in the profits of the business would result in a distortion of the figure of export profits. The High Court has relied on a decision of this Court in *Commissioner of Income-Tax v. K.*

*Ravindranathan Nair [(2007) 295 ITR 228 (SC)]* in which the issue raised before this Court was entirely different from the issue raised in this case. In that case, the assessee owned a factory in which he processed cashew nuts grown in his farm and he exported the cashew nuts as an exporter. At the same time, the assessee processed cashew nuts which were supplied to him by exporters on job work basis and he collected processing charges for the same. He, however, did not include such processing charges collected on job work basis in his total turnover for the purpose of computing the deduction under Section 80HHC (3) of the Act and as a result this turnover of collection charges was left out in the computation of profits and gains of business of the assessee and as a result ninety per cent of the profits of the assessee arising out of the receipt of processing charges was not deducted under clauses (1) of the Explanation (baa) to Section 80HHC. This Court held that the processing charges was included in the gross total income from cashew business and hence in terms of Explanation (baa), ninety per cent of the gross total income arising from processing charges had to be deducted under Explanation (baa) to arrive at the profits of the business. In this case, this Court held that the processing charges received by the assessee were part of the business turnover and accordingly the income arising therefrom should have been included in the profits and gains of business of the assessee and ninety per cent of this income also would have to be deducted under Explanation (baa) under Section 80HHC of the Act. In this case, this Court was not deciding the issue whether ninety per cent deduction is to be made from the gross or net income of any of the receipts mentioned in clause (1) of the Explanation (baa).

15. The Bombay High Court has also relied on the Memorandum explaining the clauses of the Finance Bill, 1991 contained in the circular dated 19.12.1991 of the Central Board of Direct Taxes to come to the conclusion that the Parliament intended to exclude items which were unrelated to the export turnover from the computation of deduction and while excluding such items which are unrelated to export for the purpose of Section 80HHC, Parliament has taken due note of the fact that the exporter assessee would have incurred such expenditure in earning the profits and to avoid a distorted figure of export profits, ninety per cent of the receipts like brokerage, commission, interest, rent, charges are sought to be excluded from the profits of the business. In our considered opinion, it was not necessary to refer to the explanatory Memorandum when the language of Explanation (baa) to Section 80HHC was clear that only ninety per cent of receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in such profits computed under the head profits and gains of business of an assessee could be deducted under clause (1) of Explanation (baa) and not ninety per cent of the quantum of any of the aforesaid receipts which are allowed as expenses and therefore not included in the profits of business of the assessee.

16. In the result, we allow the appeal and set aside the impugned order of the High Court and remand the matter to the Assessing Officer to work out the deductions from rent and interest in accordance with this judgment. No costs.

CIVIL APPEAL No. 4534 OF 2008 This is an appeal against the order dated 19.01.2007 of the Delhi High Court in I.T.A. No. 541 of 2006.

2. The facts of this case very briefly are that Bharat Rasayan Limited (for short 'the assessee') filed a return of income tax claiming a deduction of Rs.72,76,405/- under Section 80HHC of the Act. In the assessment order, the Assessing Officer held that ninety per cent of the gross interest has to be excluded from the profits of the business of the assessee under Explanation (baa) to Section 80HHC of the Act and deducted ninety per cent of the gross interest of Rs.50,26,284/- from the profits of the business of the assessee. The assessee preferred an appeal contending that only ninety per cent of the net interest should have been deducted from the profits of the business of the assessee under Explanation (baa)

to Section 80HHC, but the Commissioner of Income Tax (Appeals) rejected this contention of the assessee. Aggrieved, the assessee filed an appeal before the Income Tax Appellate Tribunal (for short 'the Tribunal') and the Tribunal allowed the appeal of the assessee and held that the assessee was entitled to deduct the expenses from the interest received and only ninety per cent of the net amount of interest could be excluded under Explanation (baa) to Section 80HHC and remitted the matter to the Assessing Officer to examine whether there is factually an excess between the interest paid and interest received and take a fresh decision. The Revenue filed an appeal against the order of the Tribunal before the High Court, but by the impugned order the High Court following its decision in Commissioner of Income-Tax v. Shri Ram Honda Power Equip (supra) sustained the order of the Tribunal and dismissed the appeal.

3. We have held in our judgment in the case of M/s ACG Associated Capsules Pvt. Ltd. v. Commissioner of Income Tax that ninety per cent of not the gross interest but only the net interest, which has been included in the profits of the business of the assessee as computed under the heads 'Profits and Gains of Business or Profession' is to be deducted under clause (1) of Explanation (baa) to Section 80HHC for determining the profits of the business. Since, the view taken by the High Court in the impugned order is consistent with our aforesaid view, we find no merit in this appeal and we accordingly dismiss the same. There shall be no order as to costs.

24.4 Respectfully following the judgment of the Hon'ble Supreme Court the matter is referred to the file of the Assessing Officer to allow the netting of the interest if the assessee is able to prove the nexus between interest expenditure in the interest income.

24.5. As a result this ground of appeal of the Assessee and of the Revenue is allowed for statistical purposes.

**25. Issue No. 21: Disallowance of 4/5<sup>th</sup> expenses under section 35D:**

A.Y. 2005-06

Ground No. 7 of the Assessee's Appeal

Ground No. 6 of the Revenue's Appeal

25.1 The Assessing Officer has disallowed Rs. 20 Lacs on notional basis owing to the demerger of textile unit of M/s Vardhman Spinning General Mills Ltd. to Mahavir Spinning Mills Ltd. The Assessing Officer on examination of the legal and professional charges disallowed Rs. 5,36,646/- incurred in connection with demerger scheme in addition to Rs. 20 Lacs made on account of expenses incurred on demerger.

25.2 The Ld. CIT(A) has deleted the disallowance made on notional basis and confirmed Rs. 5,36,646/- as the assessee has not contravened the findings of the Assessing Officer.

25.3 Before us the Ld. AR argued that in the absence of any material found contra the notional disallowance and the disallowance out of legal and professional expenses cannot be upheld.

25.4 Ld. DR argued that the expenses on account of legal and profession fees have to be amortized as per section 35D.

25.5 As held in the case of Digital Equipment India Pvt. Ltd. Vs. DCIT 103 TTJ 329, we hereby uphold the action of Ld. CIT(A) in deleting the adhoc disallowance made by the Assessing Officer.

25.6 As a result this ground of the Revenue's appeal is dismissed with regard to Rs. 20 Lacs and that of the Assessee stands dismissed with regard to Rs. 5,36,646/.

## **26. Issue No. 22: Software expenses – Revenue or Capital:**

A.Y. 2005-06

Ground No. 7 of the Revenue's Appeal

26.1 The Assessing Officer has treated the amount of expenditure incurred for implementation review of BPCS and TIM Software Systems pertaining to the back office functions as capital in nature.

26.2 The Ld. CIT(A) followed the rationale of Special Bench of ITAT decision in the case of Amway Enterprises Vs. DCIT 111 ITD 112 (Del). While treating the expenditure as revenue in nature it was held that, if the advantage to the assessee consists merely in facilitating assessee's trading operations and enabling the management and conduct of the assessee's business to be carried on more efficient way it should be treated as Revenue expenditure.

26.3 We have gone through the facts on record and the arguments of both the parties. We find that the software implementation expenditure being in nature of augmenting efficiency should be treated as Revenue expenditure in nature.

26.4 As a result this ground of appeal of the Revenue is dismissed.

**27. Issue No. 23: Sale of Shares- capital gains or speculation income**

A.Y. 2005-06

Ground No. 8 of the Revenue's Appeal

27.1 The assessee has earned income of Rs. 3.5 Crores out of sale of shares. The Assessing Officer held that the Long Term Capital Gain earned by the assessee be treated as income from speculation business in the context of Explanation to Section 73 .

27.2 The Ld. CIT(A) deleted the addition on the grounds that the assessee doesn't fall under the Explanation to Section 73.

27.3 We have gone through the facts on record. The shares have been held as investments in the listed group company namely Vardhman Acrylics Ltd. and in IDBI. Hence, relying on the rationale of DCIT Vs. Jindal Exports Ltd. 101 ITD 129 (Del) wherein it is held that every transaction may give rise to capital gains or income assessable under any other head.

27.4 In the facts and circumstances of the case we find that the transactions cannot be treated as speculative in nature and we hereby uphold the order of the Ld. CIT(A).

27.5 As a result the appeal of the Revenue on this ground is dismissed.

28. In the result appeals of the Assessee and the Revenue are partly allowed.

Order pronounced in the open court.

**Sd/-**  
**(DIVA SINGH)**  
**JUDICIAL MEMBER**  
Dated : 04/05/2018  
AG

**Sd/-**  
**(B.R.R.KUMAR)**  
**ACCOUNTANT MEMBER**

Copy to: The Appellant, The Respondent, The CIT, The CIT(A), The DR