

* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

+ **ITA NOS. 591/2008**

% **Reserved on: 1st May, 2012**

Date of Decision: 1st June, 2012

THE COMMISSIONER OF INCOME TAX V ...Appellant
Through Ms. Rashmi Chopra, Sr.
Standing Counsel.

VERSUS

NAGESH KNITWEARS P. LTD. ...Respondent
Through Mr. Salil Aggarwal & Mr.
Prakash Kumar, Advocates.

ITA NOS. 993/2008, 994/2008, 996/2008, 1010/2008 & 955/2009,

THE COMMISSIONER OF INCOME TAX V ...Appellant
Through Ms. Rashmi Chopra, Sr.
Standing Counsel.

VERSUS

ORIENT CRAFTS LTD. ...Respondent
Through Mr. Salil Aggarwal & Mr.
Prakash Kumar, Advocates.

ITA NOS. 832/2009

THE COMMISSIONER OF INCOME TAX V ...Appellant
Through Mr. Kiran Babu, Sr. Standing
Counsel.

VERSUS

VOGUE SETTERS ...Respondent
Through Mr. Salil Aggarwal & Mr.
Prakash Kumar, Advocates.

CORAM:
HON'BLE MR. JUSTICE SANJIV KHANNA
HON'BLE MR. JUSTICE R.V. EASWAR

SANJIV KHANNA, J.:

Revenue has preferred these appeals under Section 260A of the Income Tax Act, 1961 (Act, for short) in which the issue and contention which requires examination is whether the premium received on sale of export quota is covered by Section 28(iia) to 28(iic) and accordingly, has to be included while computing the deduction as per the provisos to sub-Section (3) of Section 80HHC of the Act.

2. The assesseees and the assessment year involved are different and we only record that the assesseees have succeeded in all cases before the tribunal. As an identical or similar legal issues and question of law arise for our consideration, the appeals are being disposed of by this common order. Before we examine facts of each individual cases, we deem it appropriate to refer to and examine the legal position.

3. Section 28(iia) to 28(iie) read as under:

“28. Profits and gains of business or profession.—
The following income shall be chargeable to income tax under the head “Profits and gains of business or profession”,—

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(iii-a) profits on sale of a licence granted under the Imports (Control) Order, 1955, made under the Imports and Exports (Control) Act, 1947 (18 of 1947);

(iii-b) cash assistance (by whatever name called) received or receivable by any person against exports under any scheme of the Government of India ;

(iii-c) any duty of customs or excise repaid or repayable as drawback to any person against exports under the Customs and Central Excise Duties Drawback Rules, 1971;

(iii-d) any profit on the transfer of the Duty Entitlement Pass Book Scheme, being the Duty Remission Scheme under the export and import policy formulated and announced under Section 5 of the Foreign Trade (Development and Regulation) Act, 1992 (22 of 1992);

(iii-e) any profit on the transfer of Duty Free Replenishment Certificate, being the Duty Remission Scheme, under the export and import policy formulated and announced under section 5 of the Foreign Trade (Development and Regulation) Act, 1992 (22 of 1992);”

4. Sub-Section (3) of Section 80HHC and the Explanation (baa) read as under :

“Section 80HHC- Deduction in respect of profits retained for export business.—

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(3) For the purposes of sub-section (1),--

(a) where the export out of India is of goods or merchandise manufactured or processed by the assessee, the profits derived from such export shall be the amount which bears to the profits of the business, the same proportion as the export turnover in respect of such goods bears to the total turnover of the business carried on by the assessee ;

(b) 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 ;

(c) where the export out of India is of goods or merchandise manufactured or processed by the assessee and of trading goods, the profits derived from such export shall,--

(i) in respect of the goods or merchandise manufactured or processed by the assessee, be the amount which bears to the adjusted profits of the business, the same proportion as the adjusted export turnover in respect of such goods bears to the adjusted total turnover of the business carried on by the assessee ; and

(ii) in respect of trading goods, be the export turnover in respect of such trading goods as reduced by the direct and indirect costs attributable to export of such trading goods :

Provided that the profits computed under clause (a) or clause (b) or clause (c) of this sub-section shall be further increased by the amount which bears to ninety per cent of any sum referred to in clause (iiia) (not being profits on sale of a licence acquired from any other person), and clauses (iiib) and (iiic) of section 28, the same proportion as the export turnover bears to the total turnover of the business carried on by the assessee.

6. Provided further that in the case of an assessee having export turnover not exceeding rupees ten crores during the previous year, the profits computed

under clause (a) or clause (b) or clause (c) of this sub-section or after giving effect to the first proviso, as the case may be, shall be further increased by the amount which bears to ninety per cent. of any sum referred to in clause (iiid) or clause (iiie), as the case may be, of section 28, the same proportion as the export turnover bears to the total turnover of the business carried on by the assessee :

Provided also that in the case of an assessee having export turnover exceeding rupees ten crores during the previous year, the profits computed under clause (a) or clause (b) or clause (c) of this sub-section or after giving effect to the first proviso, as the case may be, shall be further increased by the amount which bears to ninety per cent. of any sum referred to in clause (iiid) of section 28, the same proportion as the export turnover bears to the total turnover of the business carried on by the assessee, if the assessee has necessary and sufficient evidence to prove that,—

(a) he had an option to choose either the duty drawback or the Duty Entitlement Pass Book Scheme, being the Duty Remission Scheme ; and

(b) the rate of drawback credit attributable to the customs duty was higher than the rate of credit allowable under the Duty Entitlement Pass Book Scheme, being the Duty Remission Scheme :

Provided also that in the case of an assessee having export turnover exceeding rupees ten crores during the previous year, the profits computed under clause (a) or clause (b) or clause (c) of this sub-section or after giving effect to the first proviso, as the case may be, shall be further increased by the amount

which bears to ninety per cent. of any sum referred to in clause (iiie) of section 28, the same proportion as the export turnover bears to the total turnover of the business carried on by the assessee, if the assessee has necessary and sufficient evidence to prove that,—

(a) he had an option to choose either the duty drawback or the Duty Free Replenishment Certificate, being the Duty Remission Scheme ; and

(b) the rate of drawback credit attributable to the customs duty was higher than the rate of credit allowable under the Duty Free Replenishment Certificate, being the Duty Remission Scheme.

Provided also that in case the computation under clause (a) or clause (b) or clause (c) of this subsection is a loss, such loss shall be set off against the amount which bears to ninety per cent of—

(a) any sum referred to in clause (iiia) or clause (iiib) or clause (iiic), as the case may be, or

(b) any sum referred to in clause (iiid) or clause (iiie), as the case may be, of section 28, as applicable in the case of an assessee referred to in the second or the third or the fourth proviso, as the case may be,

the same proportion as the export turnover bears to the total turnover of the business carried on by the assessee.

Explanation.—For the purposes of this clause, “rate of credit allowable” means the rate of credit allowable under the Duty Free Replenishment Certificate, being the Duty Remission Scheme

calculated in the manner as may be notified by the Central Government ; ' ;

Explanation.--For the purposes of this sub-section,--

(a) "adjusted export turnover" means the export turnover as reduced by the export turnover in respect of trading goods ;

(b) "adjusted profits of the business" means the profits of the business as reduced by the profits derived from the business of export out of India of trading goods as computed in the manner provided in clause (b) of sub-section (3) ;

(c) "adjusted total turnover" means the total turnover of the business as reduced by the export turnover in respect of trading goods ;

(d) "direct costs" means costs directly attributable to the trading goods exported out of India including the purchase price of such goods ;

(e) "indirect costs" means costs, not being direct costs, allocated in the ratio of the export turnover in respect of trading goods to the total turnover ;

(f) "trading goods" means goods which are not manufactured or processed by the assessee.

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Explanation.--For the purposes of this sub-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 ;”

5. Prior to 1st January, 2005, the export of textiles and clothing was governed by the bilateral agreements entered into between the Government of India and United States of America, countries of European Union and Canada. In view of the said international agreements, policies were framed from time to time for allocation of quota amongst exporters to ensure the effective administration of the quota system and for optimizing the export revenue in the interest of the country. Under the Garments and Knitwear Export Entitlement (Quota) Policies, quotas in various categories were allocated to exporters wanting to export readymade garments. Some of the export quotas permits/certificates were issued on the basis of past performance/exports made in earlier years. Export quota permits/certificates were issued by the Government of India or Apparel Export Promotion Council (AEPC).

6. It appears that a category of export quota permits/certificates could be sold by the holder/acquirer to a third person, who then on the basis of export quota permit could make exports. The issue/question is whether the profit earned/consideration received on the sale of export quota permit/certificate should be included under the provisos to Section 80HHC(3) which refer to amounts/incomes covered by Section 28(iia) to (iie) of the Act.

7. The profit or proceeds received from sale of quota permits is not income derived from export. The first or the proximate source of the said income is the payment made by the third party in India, to whom the export quota certificate/permit was transferred for consideration.

8. The next question which arises for consideration is whether and if the premium earned on sale of quota permits would fall under any of the clauses of Section 28(iia) to (iie). Sale of export quota is not covered under Clause 28(iia), as it applies to sale, profit on sale of a licence granted under the Import (Control) Order, 1955. Export quota permits were not issued under the said Order. Export quota sale earnings are not cash assistance or duty on customs or excise repaid or repayable as drawback. It has no concern with excise or customs duty paid on exports. Export quota permits were not issued on the said basis/criteria. Thus the earnings from sale of export quota would not

fall under 28(iiib) and (iiic). Section 28(iiid) and 28(iiie) were introduced by Taxation Laws (Amendment) Act, 2005, with retrospective effect from 1st April, 1998 and 1st April, 2001 respectively. These clauses have to be accordingly considered only in cases where assessment years 1998-99 and 2001-02 onwards are involved. Duty Entitlement Passbook Scheme entitles the importers to set off customs duty payable on the import from the credit available under the said Scheme. It is only the profit earned on the transfer which is exigible and covered by Section 28(iiid) and not the original amount mentioned and recorded in the Duty Entitlement Passbook Scheme. The original/principal amount is covered by Section 28(iiib) as held in *ACG Associated Capsule Private Limited versus Commissioner of Income Tax, Central IV, Mumbai* (2012) 3 SCC 321. Premium received is on the sale of export quota. It is a profit earned on transfer to a third party but the quota certificate was not issued under the Duty Entitlement Passbook Scheme and did not have any connect/link with the customs duty paid/payable on imports. (iiie) of Section 28 deals with profit on transfer of duty free replenishment certificate, which entitles a person to import goods for replenishment. What is covered by the said clause is only the profit earned on transfer and not the amount credited under the Scheme. The said clause is not

applicable as export quotas were different and not like or similar to free replenishment certificates.

9. Clause 28(iv) deals with value of any benefit or perquisites whether convertible to money or not arising from business or the exercise of profession. This provision is similar to a residuary clause. Profit earned from sale of export quota would fall under Section 28(iv) because it is a benefit earned by an assessee which was arising from the business.

10. The tribunal in the impugned order has held that in terms of Office Memorandum dated 23rd February, 1998 issued by the Central Board of Direct Taxes to the Joint Secretary, Prime Minister's Office, the premium received on export quota can be equated with items mentioned in Section 28(iia) to 28(iic), i.e., profit on sale of import licence, cash assistance and duty drawback. The said notification has been treated as a circular and the Assessing Officer has been directed to compute deduction under Explanation (baa) to Section 80HHC by including 10% profit earned from quota on sale in the business profits and thereafter the deduction should be increased in terms of the provisos to Section 80HHC(3). The question raised, whether the premium received on sale of export quota is to be accounted for under the provisos to the Section 80HHC(3). If the said premium fall and is

covered under Section 28(iia) to (iie), it may be entitled to benefit under the provisos to Section 80HHC(3), subject to other conditions being satisfied. Satisfaction of the other condition is not an issue in these appeals, but the question is whether the premium/profit on sale of the export quota is covered by Section 28(iia) to (iie) for the purpose of Section 80HHC(3) of the Act.

11. The Office Memorandum, in question dated 23rd February, 1998 reads as under:

“The undersigned is directed to refer to PMO’s DO No. 247/JS(5)/98 dated Feb 2, 1998 on the subject cited above. In the representation enclosed therein, a clarification has been sought by AEPC as to whether the premium received for the transfer of export quota would be treated as a part of export profit eligible for deduction u/s 80HHC of the Income Tax Act or not.

(ii) deduction u/s 80HHC is allowed on export profits with a view to encourage earnings in convertible foreign exchange. Since the premium payment on export quotas under electronic transfer system does not involve any earnings in foreign exchange, this amount does not qualify for deduction u/s 80HHC.

(iii) Technically, export premium can be equated with the items mentioned in section 28(iia) (profit on sale of import licenses) section 28(iic) (duty drawback).

(iv) Therefore, the present item viz the premium on sale of export quota statutorily receive the same

treatment as profit on sale of import license, cash assistance and duty drawback.”

12. It is not possible to agree with the learned counsel for the Revenue that the aforesaid instructions is not a circular issued by the Board under Section 119 of the Act. The Office Memorandum refers to the clarification sought by the AEPC, whether the premium received on transfer of the export quotas could be treated as a part of export proceeds eligible for deduction under Section 80HHC. In paragraphs 3 and 4, it is stated that technically export premium can be equated with the items mentioned in the clauses (iiia) to (iiic) of Section 28 and they will statutorily receive the same treatment.

13. The next question, which arises for consideration is whether the aforesaid circular even if it is contrary to the Act is binding on the Revenue. Learned counsel for the Revenue has relied upon decision of the Supreme Court in *Commissioner of Central Excise, Bolpur versus Ratan Melting & Wire Industries*, (2008) 13 SCC 1. In the said case, Constitution Bench of five Judges referred to the earlier Constitution Bench judgment in *CCE versus Dhiren Chemical Industries*, (2002) 2 SCC 127 and reference was made to paragraph 6 in the case of *Kalyani Packaging Industry versus Union of India*, (2004) 6 SCC 719 wherein it has been observed as under:

“6. We have noticed that para 9 (para 11 in SCC) of *Dhiren Chemical case* [(2002) 2 SCC 127 : (2002) 139 ELT 3] is being misunderstood. It, therefore, becomes necessary to clarify para 9 (para 11 in SCC) of *Dhiren Chemical case* [(2002) 2 SCC 127 : (2002) 139 ELT 3] . One of us (Variava, J.) was a party to the judgment of *Dhiren Chemical case* [(2002) 2 SCC 127 : (2002) 139 ELT 3] and knows what was the intention in incorporating para 9 (para 11 in SCC). It must be remembered that law laid down by this Court is law of the land. The law so laid down is binding on all courts/tribunals and bodies. It is clear that circulars of the Board cannot prevail over the law laid down by this Court. However, it was pointed out that during hearing of *Dhiren Chemical case* [(2002) 2 SCC 127 : (2002) 139 ELT 3] because of circulars of the Board in many cases the Department had granted benefits of exemption notifications. It was submitted that on the interpretation now given by this Court in *Dhiren Chemical case* [(2002) 2 SCC 127 : (2002) 139 ELT 3] the Revenue was likely to reopen cases. Thus para 9 (para 11 in SCC) was incorporated to ensure that in cases where benefits of exemption notification had already been granted, the Revenue would remain bound. The purpose was to see that such cases were not reopened. However, this did not mean that even in cases where the Revenue/Department had already contended that the benefit of an exemption notification was not available, and the matter was sub judice before a court or a tribunal, the court or tribunal would also give effect to circulars of the Board in preference to a decision of the Constitution Bench of this Court. Where as a result of dispute the matter is sub judice, a court/tribunal is, after *Dhiren Chemical case* [(2002) 2 SCC 127 : (2002) 139 ELT 3] , bound to interpret as set out in that judgment. To hold otherwise and to interpret in the manner suggested would mean that courts/tribunals have

to ignore a judgment of this Court and follow circulars of the Board. That was not what was meant by para 9 of *Dhiren Chemical case* [(2002) 2 SCC 127 : (2002) 139 ELT 3] .”

14. Thereafter, in *Ratan Melting & Wire Industries* (supra) it has been held:

“7. Circulars and instructions issued by the Board are no doubt binding in law on the authorities under the respective statutes, but when the Supreme Court or the High Court declares the law on the question arising for consideration, it would not be appropriate for the court to direct that the circular should be given effect to and not the view expressed in a decision of this Court or the High Court. So far as the clarifications/circulars issued by the Central Government and of the State Government are concerned they represent merely their understanding of the statutory provisions. They are not binding upon the court. It is for the court to declare what the particular provision of statute says and it is not for the executive. Looked at from another angle, a circular which is contrary to the statutory provisions has really no existence in law.

8. As noted in the order of reference the correct position vis-à-vis the observations in para 11 of *Dhiren Chemical case* has been stated in *Kalyani case*. If the submissions of learned counsel for the assessee are accepted, it would mean that there is no scope for filing an appeal. In that case, there is no question of a decision of this Court on the point being rendered. Obviously, the assessee will not file an appeal

questioning the view expressed vis-à-vis the circular. It has to be the Revenue Authority who has to question that. To lay content with the circular would mean that the valuable right of challenge would be denied to him and there would be no scope for adjudication by the High Court or the Supreme Court. That would be against the very concept of majesty of law declared by this Court and the binding effect in terms of Article 141 of the Constitution.”

15. Reading of these two paragraphs elucidates that circulars can be issued by the Board and sometimes grant benefit beyond the statutory enactment. Revenue will be bound by the said circular, but this does not mean that if the circular is contrary to the Act, Revenue cannot file an appeal or challenge the same. Paragraph 8 in the case of ***Ratan Melting & Wire Industries*** (supra) clarifies that Revenue cannot be denied the right to challenge a decision on interpretation or question of law, even if there is a beneficial circular in favour of the assessee on the said aspect. The High Court or the Supreme Court can also adjudicate and once they give a decision, it will apply to all cases. However, the earlier cases, which have been decided, cannot be reopened. The decision will be only applicable to cases sub judice before the Court or the tribunal and effect will be given to the law as elucidated regardless of what has been stated in the circular.

16. Recently again in *State of Tamil Nadu vs. India Cements Ltd.* (2011) 13 SCC 247, the Supreme Court quoted from *Ratan Melting and Wire Industries (Supra)*, but ultimately dismissed the appeal of the Revenue observing that in the said case the Revenue had not claimed or stated that the circular was contrary to the statute.

17. The circular quoted above states that export premium can be equated with the items mentioned in Section 28(iia) to (iic) and, therefore, it will statutorily receive the same treatment as profit on sale of import license, cash assistance and duty drawback. The question which arises is whether the same treatment referred to is only with reference to Explanation (baa) but also with reference to provisos to Section 80HHC (3). This has not been clarified or stated in the circular. Also which specific sub-clause i.e. (iia) or (iib) or (iic) to Section 28 will apply is not stated. Explanation (baa) to Section 80HHC specifically refers to receipts under clauses (iia) to (iie) of Section 28 or receipts in nature of brokerage, commission, interest, rent, charges or any other receipt of similar nature included in such profit. The last part is residuary and will cover and include receipt of similar nature mentioned earlier. We may, however, notice that while referring to clauses (iia) to (iie) to Section 28 in the Explanation (baa), the word used is “sum” and for other incomes the

word used is “receipt” and in the residuary part the word again used is “receipt”. There may or may not be merit in the contention that the word “sum” or “receipt” convey different intention or meaning, but the said aspect is not relevant and need not be examined. What the circular postulates and states at best is that premium earned on sale of export quota would be given the same treatment i.e. will be treated as profits of business. The said amount, therefore, would be exigible under Explanation (baa). The circular has not clarified that the receipt of premium/profit on the sale of export quota would be given the same treatment only under Explanation (baa) but not under provisos to Section 80HHC(3). The Assessing Officer has accordingly included 10% of the profit received on sale of export quota in the profits of business under the Explanation (baa). First proviso to Section 80HHC(3), on the other hand, specifically refer to Section 28 (iiia) to (iiic) and then the second proviso refers to clauses (iiid) and (iiie) to Section 28 and conditions which have to be satisfied. The third proviso deals with the cases where turnover exceeds Rs.10 crores and certain other stipulations and requirements which are to be fulfilled. The provisos do not refer to the residuary or other incomes included in Explanation (baa). In view of the specific language of the provisos to Section 80HHC (3), it is not possible to hold that in terms of the circular, the assessee is covered and entitled to benefit under the

provisos to Section 80HHC(3) of the Act. We note that it is not understood how and when will an assessee comply with the conditions stipulated in the third proviso, if applicable, in the case of profit on sale of export quota. On the provisos and Section 28(iia) to (iie) in *ACG Associated Capsule* (supra) distinction has been drawn between the principal amount and profit on sale of import license/DEPB and it has been held:-

“2. On the first issue, the High Court has held, relying on its judgment in *CIT v. Kalpataru Colours and Chemicals* [(2010) 328 ITR 451 (Bom)] , that the entire amount received by an assessee on sale of the Duty Entitlement Pass Book (for short “the DEPB”) represents profit on transfer of DEPB under Section 28(iii-d) of the Income Tax Act, 1961 (for short “the Act”). We have already decided this issue in favour of the assessee in a separate judgment in *Topman Exports v. CIT* [(2012) 3 SCC 593] and other connected matters and we have held that not the entire amount received by the assessee on sale of DEPB, but the sale value less the face value of the DEPB will represent profit on transfer of DEPB by the assessee. The first issue is, therefore, decided accordingly.”

18. This brings us to the facts of the individual cases.

ITA No. 591/2008

19. This appeal relates to Nagesh Knitwears Pvt. Ltd. and pertains to the assessment years 2003-04. By order dated 28th October, 2009, the following substantial question of law was framed:-

“Whether the amount received by the assessee from the sale of quota for export of goods could be equated with income mentioned in Sections 28(iia) or Section 28 (iv) of the Income Tax Act, 1961 so as to be eligible for deduction under Section 80HHC of the Act?”

20. The Assessing Officer noticed that the assessee had earned export quota premium of Rs. 27,68,991/- in the assessment year 2003-

04. 10% of the said amount was taken into consideration under Explanation (baa) to Section 80HHC. However, the export quota premium was not taken into consideration while applying proviso to sub Section 3 to Section 80HHC on the ground that it does not fall within Section 28(iia), (iib) and (iic).

21. The assessee succeeded in the first appeal with the CIT (Appeals) holding that the export quota premium should be given the same treatment of DEPB under clauses (a) (b) or (c) to sub Section 3 to Section 80HHC for the assessment year 2003-04.

22. The tribunal by the impugned order dated 6th July, 2007 has observed as under:-

“2.9 The issue raised is whether the premium on sale of export quota has to be increased in the ratio of export turnover to total turnover in terms of proviso to section 80HHC(3). The proviso states that the sums referred in clauses (iiia) (iiib) & (iiic) of section 29, 90% of which has been deducted from the profit of business as per Explanation (baa), have to be further added to the profit derived from export, in the ratio of export turnover to total turnover. The argument of the assessee is that the nature of premium on sale of export quota is the same as the sale of import licenses as mentioned in clause (iiia) of section 28. The assessee has relied on the letter of CBDT F.No.133/131/97 TPL dated 23.2.1998, in which it has been clarified that the premium on sale of import quota statutorily received the same treatment as profit on sale of export licenses, cash assistance and duty drawback. It has therefore, been pleaded that provision to section 80HHC(3) will also apply to the premium on sale of export quota. The argument of the revenue is that the sale letter was only an OM written by an officer of CBDT to PMO and does not have the force of binding nature of circular and therefore, the nature of premium on sale of export quota is not the same as profit on sale of import licenses, etc.

2.10 In our view, it is not necessary for us to go into the issue whether the letter under reference from CBDT is a circular or not. We find that the A.O. has already treated the premium on sale of export quota as being of the same nature as profit on sale of import licenses as mentioned in section 28 (iiia) because he has already deducted 90% of the premium on sale of export quota from the profit of business as per Explanation (baa). Under the provisions of Explanation (baa) only 90% of the sums referred in clauses (iiia) (iiib) (iiic) of section 28 etc. or any receipts of similar nature are required to be excluded. As the A.O. had deducted 90% of premium on sale of export quota as per Explanation (baa), he has already treated the

nature of premium on sale of export quota as that of the sum referred in section 28 (iiia), which relates to receipts from sale of import licenses. Once, the A.O. has treated the nature of premium on sale of export quota as being the same as receipts from sale of import licenses mentioned in section 28 (iiia), he cannot deny the benefit of increase as mentioned in proviso to section 80HHC(3) as per which 90% of sum mentioned in section 28(iiia) in the ratio of export turnover to total turnover has to be added to the profit computed u/s 80HHC(3). The Chandigarh bench of the tribunal in case of M/s. Gateway Pvt. Ltd. (supra), has also allowed the claim of the assessee in relation to premium on sale of export quota while computing deduction u/s 80HHC. In view of the foregoing discussion, we are of the view that the assessee is entitled to the benefit of increase to the profit as provided in the proviso to section 80HHC(3) in relation to premium on sale of export quota on the facts of the case. Accordingly, we set aside the order of CIT(A) and allow the claim of the assessee.”

23. We may note that there appears to be an error in the last sentence of paragraph 2.10 quoted above because the Revenue had preferred an appeal before the tribunal and the respondent-assessee was satisfied with the findings/directions given by the CIT (Appeals).

24. As held above, premium on sale of export quota is not covered by clauses 28(iiia) to (iiie) and, therefore, the same cannot be taken into consideration. The question of law mentioned above, therefore, is answered in negative i.e. in favour of the appellant-Revenue and against the respondent-assessee.

ITA No.955/2009

25. This appeal relates to Orient Crafts Ltd. and pertains to the assessment year 2003-2004. Vide order dated 7th October, 2009, the following substantial question of law was framed:-

“Whether the amount received by the Assessee from the sale of quota for export of goods could be equated with income mentioned in Section 28(iia) to 28 (iie) or Section 28 (iv) of the Income Tax Act, 1961 so as to be eligible for a deduction under Section 80HHC of the Act?”

26. Though the language or the question of law as framed is different, but the issue and question involved is the same.

27. In this year, the Assessing Officer observed that the assessee had received premium of Rs. 17,79,510/- on sale of quota rights received from AEPC. He held that the above proceeds were not directly related to the export of goods and should be reduced from ‘the profit and gains from business or profession’. However, 10% of the sale proceeds of the quota have to be added to arrive at profit of business as per the Explanation (baa) to Section 80HHC. Accordingly, the Assessing Officer computed deduction under Section 80HHC.

28. The assessee succeeded in the first appeal and then before the tribunal. The tribunal relying upon the aforesaid circular has held that

premium on sale of export quota should be given the same treatment as items mentioned in Section 28 (iiia) to (iiic) and then deduction under Section 80HHC should be recomputed under Explanation (baa) and the provisos to Section 80HHC(3).

29. In view of the position explained above, it is held that the premium/profit on sale of export quota is not covered by Section 28 (iiia) to (iiie) of the Act and accordingly the deduction under the provisos to Section 80HHC (3) has to be computed. The question of law is answered in favour of the Revenue and against the assessee.

ITA Nos.993/2008 & 994/2008

30. These appeals by the Revenue in the case of Orient Crafts Ltd. pertain to the assessment years 2001-02 and 2000-01, respectively. By the order dated 17th May, 2010 following two substantial question of law were framed:

“a) Whether the proceeds from the sale of an export quota is covered by the provisions of section 28(iiia) of the Act so as to be taken into consideration while computing deduction under section 80HHC (3) of the said Act?

b) Whether the Income Tax Appellate Tribunal had erred in law in holding that assessment order passed under section 143(3) of the Income Tax Act, 1961 was not prejudicial to the interest of the revenue and thereby holding that the proceedings under section 263 of the said Act were without jurisdiction?”

31. Further on 22nd May, 2012, an additional substantial question of law was framed which reads as under:

“ Whether the Income Tax Appellate Tribunal (ITAT) has erred in setting aside the order passed by the Commissioner of Income Tax under Section 263 of the Income of the Income Tax Act, 1961?”

32. In the two assessment years, the Assessing Officer had in the order under Section 143(3) accepted the computation made by the assessee under Section 80HHC of the Act. The Assessing Officer treated the premium/profit earned on sale of export quota as covered under Section 28(iia) to (iic).

33. The Commissioner of Income Tax, however, issued notice under Section 263 in exercise of power of revision and held that the Assessing Officer had wrongly included premium of Rs.1,16,62,320/- and Rs.73,49,341/- on the sale of quota rights for the assessment years 2000-01 and 2001-02 as covered by Section 28(iia) to (iic) and had computed the deduction. The Commissioner of Income Tax referred to the decision of the Supreme Court in *Commissioner of Income-tax Vs. Sterling Foods* (1999) 237 ITR 579 and held that under the proviso to Section 80HHC(3), the three categories mentioned in Section 28(iia), (iib) and (iic) have to be included. He held that deduction under

Section 80HHC has to be computed by reducing business profit by 90% from the receipts on sale of quota rights. He also observed that the Assessing Officer had not verified facts and no details of export incentives or receipt were taken on record. The Assessing Officer did not examine the provisions of Section 28 (iiia/b/c). The Assessing Officer was directed to make fresh assessment and treat the sale of quota rights as “other receipts” under Explanation (baa) to Section 80HHC. He was also asked to verify the receipts on account of export incentives shown for the purpose of deduction under Section 80HHC offered for taxation and ensure that the receipts not covered under Section 28 (iiia/b/c) were excluded while applying the provisos to Section 80HHC(3).

34. The Assessing Officer, thereafter recomputed deductions under Section 80HHC and passed assessment orders for the two years. These were made subject matter of challenge by the assessee, who succeeded in the first appeal. It was observed that the Assessing Officer had excluded 90% of the profit on sale of export license while computing deduction under Explanation (baa) to Section 80HHC. It was held that as per the provisos to Section 80HHC(3), the profit has to be computed after increasing the amount which bears to 90% of the same referred to in 28 (iiia) i.e. profit on sale of export license, but this had not been

allowed and followed by the Assessing Officer. The assessee, therefore, succeeded in the first appeal.

35. The tribunal by order dated 7th September, 2007 in ITA 2210 & 2211/Del/2005 held that the Commissioner was not justified in invoking his power under Section 263 as the view taken by the Assessing Officer was plausible. They referred and relied upon ***Malabar Industrial Company Limited Vs. CIT*** (2000) 243 ITR 83 (SC) and the decision of Delhi High Court in ***Nabha Investments Pvt. Ltd. Vs. Union of India & Others*** (2000)246 ITR 41. The tribunal also examined the case on merits and came to the conclusion that the addition was not justified in view of the circular issued by the Board. On correct interpretation of law, the assessee was entitled to include premium or profit on sale of export quota in Section 28 (iiia/b/c). Accordingly, the twin conditions i.e. order of the Assessing Officer should be erroneous and prejudicial to the interest of the Revenue, were not satisfied.

36. As far as Section 263 is concerned, we have examined the said Section in depth and detail in ***ITO Vs. D G Housing Projects Ltd.*** decided on 1st March, 2012, in ITA No. 179/2011 and observed as under:-

“10. Revenue does not have any right to appeal to the first appellate authority against an order passed by the Assessing Officer. Section 263 has been enacted to empower the CIT to exercise power of revision and revise any order passed by the Assessing Officer, if two cumulative conditions are satisfied. Firstly, the order sought to be revised should be erroneous and secondly, it should be prejudicial to the interest of the Revenue. The expression ‘prejudicial to the interest of the Revenue’ is of wide import and is not confined to merely loss of tax. The term ‘erroneous’ means a wrong/incorrect decision deviating from law. This expression postulates an error which makes an order unsustainable in law.

11. The Assessing Officer is both an investigator and an adjudicator. If the Assessing Officer as an adjudicator decides a question or aspect and makes a wrong assessment which is unsustainable in law, it can be corrected by the Commissioner in exercise of revisionary power. As an investigator, it is incumbent upon the Assessing Officer to investigate the facts required to be examined and verified to compute the taxable income. If the Assessing Officer fails to conduct the said investigation, he commits an error and the word ‘erroneous’ includes failure to make the enquiry. In such cases, the order becomes erroneous because enquiry or verification has not been made and not because a wrong order has been passed on merits.

12. Delhi High Court in *Gee Vee Enterprises v. Additional Commission of Income-Tax, Delhi-I*, (1975) 99 ITR 375, has observed as under:-

“The reason is obvious. The position and function of the Income-tax Officer is very different from that of a civil court. The statements made in a pleading proved by the minimum amount of evidence may be accepted by a civil court in the absence of any rebuttal. The civil court is neutral. It simply gives decision on the basis of the pleading and evidence which comes before it. The Income-tax Officer is not only an adjudicator but also an investigator. He cannot remain passive in the face of

a return which is apparently in order but calls for further inquiry. It is his duty to ascertain the truth of the facts stated in the return when the circumstances of the case are such as to provoke an inquiry. The meaning to be given to the word “erroneous” in section 263 emerges out of this context. It is because it is incumbent on the Income-tax Officer to further investigate the facts stated in the return when circumstances would make such an inquiry prudent that the word “erroneous” in section 263 includes the failure to make such an inquiry. The order becomes erroneous because such an inquiry has not been made and not because there is anything wrong with the order if all the facts stated therein are assumed to be correct.”

13. In the said judgment, Delhi High Court had referred to earlier decisions of the Supreme Court in *Rampyari Devi Sarogiv. CIT* (1968) 67 ITR 84 (SC) and *Tara Devi Aggarwal v. CIT* (1973) 88 ITR 323 (SC), wherein it has been held that where Assessing Officer has accepted a particular contention/issue without any enquiry or evidence whatsoever, the order is erroneous and prejudicial to the interest of the Revenue. After reference to these two decisions, the Delhi High Court observed:-

“These two decisions show that it is not necessary for the Commissioner to make further inquiries before cancelling the assessment order of the Income-tax Officer. The Commissioner can regard the order as erroneous on the ground that in the circumstances of the case the Income-tax Officer should have made further inquiries before accepting the statements made by the assessee in his return.”

14. The aforesaid observations have to be understood in the factual background and matrix involved in the said two cases before the Supreme Court. In the said cases, the Assessing Officer had not conducted any enquiry or examined evidence whatsoever. There was total absence of enquiry or verification. These cases have to be distinguished from other cases (i) where there is enquiry but the findings

are incorrect/erroneous; and (ii) where there is failure to make proper or full verification or enquiry.

15. In the case of *Commissioner of Income Tax v. Sunbeam Auto Ltd.* (2011) 332 ITR 167 (Del), Delhi High Court was considering the aspect, when there is no proper or full verification, and it was held as under:-

“We have considered the rival submissions of the counsel on the other side and have gone through the records. The first issue that arises for our consideration is about the exercise of power by the Commissioner of Income-tax under section 263 of the Income-tax Act. As noted above, the submission of learned counsel for the Revenue was that while passing the assessment order, the Assessing Officer did not consider this aspect specifically whether the expenditure in question was revenue or capital expenditure. This argument predicates on the assessment order, which apparently does not give any reasons while allowing the entire expenditure as revenue expenditure. However, that by itself would not be indicative of the fact that the Assessing Officer had not applied his mind on the issue. There are judgments galore laying down the principle that the Assessing Officer in the assessment order is not required to give detailed reason in respect of each and every item of deduction, etc. Therefore, one has to see from the record as to whether there was application of mind before allowing the expenditure in question as revenue expenditure. Learned counsel for the assessee is right in his submission that one has to keep in mind the distinction between “lack of inquiry” and “inadequate inquiry”. If there was any inquiry, even inadequate that would not by itself give occasion to the Commissioner to pass orders under section 263 of the Act, merely because he has a different opinion in the matter. It is only in cases of “lack of inquiry” that such a course of action would be open. In *Gabriel India Ltd.* [1993] 203 ITR 108 (Bom), law on this aspect was discussed in the following manner (page 113):

“... From a reading of sub-section (1) of section 263, it is clear that the power of suo motu revision can be exercised by the Commissioner only if, on examination of the records of any proceedings under this Act, he considers that any order passed therein by the Income-tax Officer is ‘erroneous in so far as it is prejudicial to the interests of the Revenue’. It is not an arbitrary or unchartered power, it can be exercised only on fulfilment of the requirements laid down in sub-section (1). The consideration of the Commissioner as to whether an order is erroneous in so far as it is prejudicial to the interests of the Revenue, must be based on materials on the record of the proceedings called for by him. If there are no materials on record on the basis of which it can be said that the Commissioner acting in a reasonable manner could have come to such a conclusion, the very initiation of proceedings by him will be illegal and without jurisdiction. The Commissioner cannot initiate proceedings with a view to starting fishing and roving enquiries in matters or orders which are already concluded. Such action will be against the well-accepted policy of law that there must be a point of finality in all legal proceedings, that stale issues should not be reactivated beyond a particular stage and that lapse of time must induce repose in and set at rest judicial and quasi-judicial controversies as it must in other spheres of human activity. (See *Parashuram Pottery Works Co. Ltd. v. ITO* [1977] 106 ITR 1 (SC) at page 10) ... From the aforesaid definitions it is clear that an order cannot be termed as erroneous unless it is not in accordance with law. If an Income-tax Officer acting in accordance with law makes a certain assessment, the same cannot be branded as erroneous by the Commissioner simply because, according to him, the order should have been written more elaborately. This section does not visualise a case of substitution of the judgment of the Commissioner for that of the Income-tax Officer, who passed the order unless the decision is held to be erroneous. Cases may be visualised where the Income-tax Officer while making an assessment examines the accounts, makes enquiries, applies his mind to the facts and circumstances of the case and determines the

income either by accepting the accounts or by making some estimate himself. The Commissioner, on perusal of the records, may be of the opinion that the estimate made by the officer concerned was on the lower side and left to the Commissioner he would have estimated the income at a figure higher than the one determined by the Income-tax Officer. That would not vest the Commissioner with power to re-examine the accounts and determine the income himself at a higher figure. It is because the Income-tax Officer has exercised the quasi-judicial power vested in him in accordance with law and arrived at a conclusion and such a conclusion cannot be formed to be erroneous simply because the Commissioner does not feel satisfied with the conclusion ... There must be some prima facie material on record to show that tax which was lawfully exigible has not been imposed or that by the application of the relevant statute on an incorrect or incomplete interpretation a lesser tax than what was just has been imposed ... We may now examine the facts of the present case in the light of the powers of the Commissioner set out above. The Income-tax Officer in this case had made enquiries in regard to the nature of the expenditure incurred by the assessee. The assessee had given detailed explanation in that regard by a letter in writing. All these are part of the record of the case. Evidently, the claim was allowed by the Income-tax Officer on being satisfied with the explanation of the assessee. Such decision of the Income-tax Officer cannot be held to be 'erroneous' simply because in his order he did not make an elaborate discussion in that regard.” ”

16. Thus, in cases of wrong opinion or finding on merits, the CIT has to come to the conclusion and himself decide that the order is erroneous, by conducting necessary enquiry, if required and necessary, before the order under Section 263 is passed. In such cases, the order of the Assessing Officer will be erroneous because the order passed is not sustainable in law and the said finding must be recorded. CIT cannot remand the matter to the Assessing Officer to decide whether the findings

recorded are erroneous. In cases where there is inadequate enquiry but not lack of enquiry, again the CIT must give and record a finding that the order/inquiry made is erroneous. This can happen if an enquiry and verification is conducted by the CIT and he is able to establish and show the error or mistake made by the Assessing Officer, making the order unsustainable in Law. In some cases possibly though rarely, the CIT can also show and establish that the facts on record or inferences drawn from facts on record *per se* justified and mandated further enquiry or investigation but the Assessing Officer had erroneously not undertaken the same. However, the said finding must be clear, unambiguous and not debatable. The matter cannot be remitted for a fresh decision to the Assessing Officer to conduct further enquiries without a finding that the order is erroneous. Finding that the order is erroneous is a condition or requirement which must be satisfied for exercise of jurisdiction under Section 263 of the Act. In such matters, to remand the matter/issue to the Assessing Officer would imply and mean the CIT has not examined and decided whether or not the order is erroneous but has directed the Assessing Officer to decide the aspect/question.

17. This distinction must be kept in mind by the CIT while exercising jurisdiction under Section 263 of the Act and in the absence of the finding that the order is erroneous and prejudicial to the interest of Revenue, exercise of jurisdiction under the said section is not sustainable. In most cases of alleged “inadequate investigation”, it will be difficult to hold that the order of the Assessing Officer, who had conducted enquiries and had acted as an investigator, is erroneous, without CIT conducting verification/inquiry. The order of the Assessing Officer may be or may not be wrong. CIT cannot direct reconsideration on this ground but only when the order is erroneous. An order of remit cannot be passed by the CIT to ask the Assessing Officer to decide whether the order was erroneous. This is not permissible. An order is not erroneous, unless the CIT hold and records reasons why it is erroneous. An order will not become erroneous because on remit, the

Assessing Officer may decide that the order is erroneous. Therefore CIT must after recording reasons hold that the order is erroneous. The jurisdictional precondition stipulated is that the CIT must come to the conclusion that the order is erroneous and is unsustainable in law. We may notice that the material which the CIT can rely includes not only the record as it stands at the time when the order in question was passed by the Assessing Officer but also the record as it stands at the time of examination by the CIT [see *CIT v. Shree Manjunathesware Packing Products*, 231 ITR 53 (SC)]. Nothing bars/prohibits the CIT from collecting and relying upon new/additional material/evidence to show and state that the order of the Assessing Officer is erroneous.

18. It is in this context that the Supreme Court in *Malabar Industrial Co. Ltd. v. Commissioner of Income Tax*, (2000) 243 ITR 83 (SC), had observed that the phrase ‘prejudicial to the interest of Revenue’ has to be read in conjunction with an erroneous order passed by the Assessing Officer. Every loss of Revenue as a consequence of an order of the Assessing Officer cannot be treated as prejudicial to the interest of Revenue. Thus, when the Assessing Officer had adopted one of the courses permissible and available to him, and this has resulted in loss to Revenue; or two views were possible and the Assessing Officer has taken one view with which the CIT may not agree; the said orders cannot be treated as an erroneous order prejudicial to the interest of Revenue unless the view taken by the Assessing Officer is unsustainable in law. In such matters, the CIT must give a finding that the view taken by the Assessing Officer is unsustainable in law and, therefore, the order is erroneous. He must also show that prejudice is caused to the interest of the Revenue.”

37. In the present case, a reading of the order passed by the Commissioner of Income Tax expositis that the order passed by the

Assessing Officer was erroneous and prejudicial to the interest of the Revenue. In paragraph 6, 7, 9 and 10 the Commissioner of Income Tax has observed as under:-

“6. The assessee’s submissions are carefully considered. Explanation (baa) of section 80HHC clearly states that any receipts which is not directly related to the export of goods out of India has to be reduced from the ‘profits and gains of business or profession’ to arrive at ‘profit of business’ for computation of deduction u/s 80HHC. Since sale of quota is only incidental to export and source of the same is the Govt. Scheme and not the export of goods, 90% of the same is to be reduced while computing ‘profit of business’ of the assessee. In this regard reliance is placed on the decision of the Hon’ble Supreme Court in the case of ***Commissioner of Income-tax Vs. Sterling Foods*** [237 ITR 579] wherein it was held that for the application of words “derived from”, a direct nexus between the profits and gains and the industrial undertaking was required. It was also held by the Apex Court that the source of the import entitlements were the scheme of Central Government and not the industrial undertaking and the nexus was not direct but only incidental. In the present case also there was no direct nexus and the source of quota was the Government Scheme. Thus, the sale proceeds of quota rights have to be reduced to arrive at ‘profit of business’ as per Explanation (baa) to section 80HHC.

7. However, following the principle of strict construction for deeming fictions, the same cannot be added back as it does not fall under any of the three categories mentioned in clauses (iiia) (iiib) or (iiic) of section 28 as required by the proviso to sub section (3) of section 80HHC. On this issue, the liberal interpretation of any statute cannot be relied upon in view of the judgment of the

Hon'ble Supreme Court in the case of NOVO Pan India [73 ELT 769] wherein it was held that

“The principal that in case of ambiguity, a taxing statute should be construed in favour of the assessee assuming that the said principle is good and sound-does not apply to the construction of an exception or an exempting provision; they have to be construed strictly. A person invoking an exception or any exemption provision to relieve him of the tax liability must establish clearly that he is covered by the said provision. In case of doubt or ambiguity, benefit of it must go to the State. This is for the reason explained in Mangalore Chemicals and other decisions, viz. each such exception/exemption increases the tax burden on other member of the community correspondingly. Once, of course, the provision is found applicable to him, full effect must be given to it.’

Hence deduction u/s 80HHC has to be computed accordingly by reducing profit of business by 90% of the receipts from sale of quota rights.

8. x x x x x x x

9. Moreover, on perusal of the record, it is seen that the assessment was completed even though there were no details on record of export incentives received by the assessee during the year. The assessee was allowed the claim of deduction under Section 80HHC without even verifying as to whether the receipts on account of export incentive fall within the provisions of section 28(iiiia/b/c) of the Act on merit the deduction.

10. In view of the above discussion, it is clear that the impugned assessment order is erroneous and prejudicial to the interest of Revenue as it failed to apply the provisions relating to the deduction under section 80HHC correctly. Therefore, the said assessment order is hereby cancelled under section 263 of the Income-tax

Act, 1961 and the A.O. is directed to make fresh assessment as per the provisions of law. While making the fresh assessment, the A.O. is directed to treat the receipt on sale of quota rights as “Other Receipts” as mentioned in explanation (baa) of the section 80HHC. He is also directed to verify that the receipt on account of export incentives shown for the purpose of deduction under section 80HHC are offered for tax in the Profit & Loss account; and that none of these receipts include any item which is not covered by the provisions of section 28 (iiia/b/c), such as DEPB etc.”

38. Accordingly, we answer the substantial question of law framed in ITA Nos.993/2008 and 994/2008 as under:-

(i) As held above, proceeds from sale of an export quota is not covered by Section 28(iiia) to (iiie), and the same cannot be taken into consideration. The first question of law is answered in negative i.e. in favour of the Revenue and against the respondent-assessee.

(ii) The tribunal was wrong in holding that the order passed by the Commissioner of Income Tax under Section 263 was bad and contrary to the provisions of the Act. The question of law is answered in negative i.e. in favour of the Revenue and against the respondent-assessee.

(ii) The third question is also answered in negative i.e. in favour of the Revenue and against the respondent-assessee.

ITA Nos.996/2008 & 1010/2008

39. These appeals by the Revenue relates to assessment years 2000-01 and 2001-02 in the case of Orient Crafts Ltd. The substantial question of law framed on 1st May, 2012 reads as under:

“Whether Income Tax Appellate Tribunal was right in holding that 90% of the profits on sale of export quota are covered under the first proviso to Section 80HHC (3) of the Income Tax Act?”

40. For the reasons stated above, the question of law framed is answered in negative i.e. in favour of the Revenue and against the respondent-assessee.

ITA 832/2009

41. This appeal has been preferred against Vogue Setters and relates to the assessment year 2003-04. By order dated 10th September, 2009, the following substantial question of law was framed:-

“Whether the amount received by the Assessee from the sale of quota for export of goods could be equated with income mentioned in Sections 28 (iia) to 28 (iie) or Section 28 (iv) of the Income Tax Act, 1961 so as to be eligible for a deduction under Section 80HHC of the Act.”

42. In the said assessment year, the assessee had earned premium of Rs.12,26,140/- on sale of export quota. The Assessing Officer held that this premium is covered by Section 28 (iia/b/c) and accordingly

computed deduction under Section 80HHC but without giving benefit of provisos under sub Section (3) to Section 80HHC. He observed that the export turnover in the previous year was exceeding Rs.10 crores and the assessee had not complied with the several conditions mentioned in the provisos. The sale proceeds received from sale of quota rights were excluded from benefit under the provisos to Section 80HHC(3) as this was not the regular business income of the assessee.

43. The CIT (Appeals) referred to the circular issued by the CBDT and held that the premium received on sale of export quota represents export incentive and should be treated as covered by Section 28 (iiia/b/c). He did not specifically go into the question whether or not the assessee meets and satisfies the requirements mentioned in the provisos to Section 80HHC(3). The appeal filed by the Revenue before the tribunal met with an order of dismissal dated 31st October, 2008. The tribunal has also not gone into the question whether or not the conditions stipulated in the proviso to Section 80HHC were satisfied.

44. In the light of what we have argued and answered, the question of law is answered in negative i.e. in favour of the Revenue and against the assessee.

45. The appeals are accordingly allowed to the extent indicated above.

-sd-
(SANJIV KHANNA)
JUDGE

-sd-
(R.V. EASWAR)
JUDGE

June 1, 2012

VKR/NA