IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 02.01.2019

CORAM

THE HON'BLE DR.JUSTICE VINEET KOTHARI

AND

THE HON'BLE DR.JUSTICE ANITA SUMANTH

Tax Case Appeal No.342 of 2009

M/s.Rajapalayam Mills Ltd.,
PAC Ramaswamy Raja Salai,
Rajapalayam - 626 117.

.... Appellant/Respondent

Vs

The Deputy Commissioner of Income Tax,
Circle - I, Virudhunagar

.... Respondent/Appellant

Tax Case Appeals filed under Section 260A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal, Madras 'B' Bench, Chennai, dated 31.12.2008 made in ITA No.1305/Mds/2008 for the Assessment Year 2005-06, against the order dated 08/02/2008 in PAN/GIR No.AAACR88974/2007-08 by the Commissioner of Income Tax, Appellate II, Madras, prferred against the order of Deputy Commissioner of Income Tax, Virudhunagar, dated 28/08/2007 Assessment year 2005-2006.

For Appellant : Mr.P.J.Rishikesh

For Respondent : Mr.M.Swaminathan,
Sr. Standing Counsel, assisted by Ms.Premalatha

J U D G M E N T

(Delivered by DR.ANITA SUMANTH,J)

The assessee is in appeal before us challenging an order of the Income Tax Appellate Tribunal dated 31.12.2008 relating to Assessment Year 2005-06.

2. The appellant is engaged in the business of manufacturing and export of yarn and biotechnology products. The

sole issue in the appeal relates to computation of relief under section 10B of the Income Tax Act, 1961 (in short 'Act') specifically in regard to the inclusion of income earned from the sale of cotton waste, as part of the total turnover of the appellant.

3. The appellant filed a return claiming relief under section 10B in terms of the prescribed formula as per which the profits derived from the export of articles or things or computer software shall be the amount which bears to the profits of the business of the undertaking the same proportion as the export turnover in respect of such articles or things or computer software bears to the total turnover of the business carried on by the undertaking.

4. Deduction at 100% of the profits earned was claimed that included an amount of Rs.1,13,15,824/- representing income from the sale of waste cotton/scrap. The Assessing Authority was of the view that the aforesaid amount ought to have been included in the denominator in the above formula for arriving at a proper figure of deduction under section 10B. He thus recomputed the relief sought, disallowing an amount of Rs.32,67,196/- that, according to him, had been claimed in excess. Other adjustments were made in the assessment that we are not concerned with in the present appeal.

5. The Commissioner of Income Tax (Appeals) (in short, 'CIT (A)') vide order dated 08.02.2008 reversed the above adjustment, being of the view that the income from the sale of the scrap would, at best, only go to reduce the cost of the raw material, being cotton. Thus according to him, the income from the sale of scrap would not be part of the total turnover and no restriction of the deduction claimed under section 10B was liable to be made.

6. The Revenue went on appeal before the Income Tax Appellate Tribunal (in short 'Tribunal'), which, following the decision of a co-ordinate Bench held that the inclusion of income in the total turnover would have to be balanced by the inclusion of the identical amount in the export turnover as well. The Assessing Officer was thus directed to include the income from sale of waste cotton scrap in turnover as well as total turnover subject to confirmation by the Assessing Officer that the appellant was a 100% export oriented unit. The present appeal has been filed as against the aforesaid order of the tribunal by the assessee.

7. We have heard Mr.P.J.Rishikesh, learned counsel for the appellant and Mr.M.Swaminathan, learned senior standing counsel for the Revenue.

8. This Court, vide order dated 12.06.2009 has admitted the following substantial question of law for determination:

> 'Whether in facts and circumstances of the case the Tribunal was right in holding that the income earned out of sale of waste cotton would form part of total income?'

9. We may straight away state that the direction of the Tribunal to the Assessing Officer to include the income from sale of cotton scrap in the numerator in the formula is patently incorrect in so far as admittedly the sale of scrap was in the domestic market and did not generate consideration received in or brought into India in convertible foreign exchange income as per the definition of 'export turnover' in the Explanation to section 10B.

10. That apart, section 10B is a special provision that provides for a deduction from the income generated by eligible business activity. It is thus essential to determine the business activity of an assessee first and accordingly apply the formula to the income generated by such activity alone. Seen in that light, the appellant, admittedly, is not a dealer in scrap and sale of scrap cannot thus be termed to be business activity in so far as it is concerned. The CIT(A) has thus, rightly held that, at best, the income from sale of scrap would only go to reduce the cost of acquisition of raw material.

11. Furthermore, the phrase 'total turnover' has not been defined in s.10B and would thus assume a meaning as commonly understood in commercial parlance. The total turnover of the business carried on by the undertaking would thus be the sum total of all incomes generated by the business activities carried on by the appellant. In the light of our conclusion earlier to the effect that income from the sale of scrap, or cotton scrap as in the present case, is, but only an incident of the business of manufacture of textile yarn, the assessee not being a dealer thereof, such income will not will not come within the ambit of the word 'total turnover'.

12. Finally, the provision is a complete code inserted specifically to encourage the activity of exports. Its interpretation should thus be in tandem with, and advance the aforesaid avowed object of the provision.

13. The Supreme Court, in the case of Commissioner of Income Tax VII, New Delhi V. Punjab Stainless steel Industries ((2014) 15 SCC 129), has considered the question of inclusion of income from sale of scrap in the component of 'total turnover', being the denominator in the formula for computation of relief under s.80HHC of the Act. In almost identical facts as we are faced with, the Bench concludes that the proceeds generated from sale of scrap is not liable to be included in total turnover, as turnover, as commonly understood, would include only such incomes as are generated by business activities. Though this judgement has been rendered in the context of s.80 HHC, the rationale thereof is applicable on all fours in the present case as well.

14. The substantial question of law raised is thus answered in favour of the assessee and against the Revenue. The Tax case (Appeal) is allowed. No costs.

Sd/-
Assistant Registrar(CS-III)

//True copy//

Sub Assistant Registrar

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To

1. The Income Tax Appellate Tribunal, Madras 'B' Bench, Chennai.

2. The Commissiner of Incoem Tax (Appeals)-II, Madurai.

3. the Deputy Commissioner of Incoem Tax, Virudhunagar.

+1cc to Mr.S.Premalatha, Advocate SR.No.586

+1cc to Mrs.P.J.Rishikesh, Advocate SR.No.297

TCA No.342 of 2009

SJ(CO)

GMY(30/01/2019)