

IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATE: 02.03.2021

CORAM:

THE HON'BLE MR. JUSTICE M.DURAI SWAMY
AND
THE HON'BLE MRS.JUSTICE T.V.THAMILSELVI

T.C.A.No.795 of 2013

The Commissioner of Income Tax,
Chennai.

... Appellant

Vs.

M/s.Covansys (India) Pvt. Ltd.,
(now merged with M/s.Computer Science
Corporation India Pvt Ltd),
Unit 13, Block 2, SDF Building, MEPZ,
Tambaram, Chennai - 600 045.

... Respondent

Appeal preferred under Section 260A of the Income Tax Act, 1961, against the order of the Income Tax Appellate Tribunal, Chennai, "D" Bench, dated 23.12.2011 in I.T.A.No.1570/Mds/2011, against the order of the Commissioner of Income Tax (Appeals)-III, Chennai dated 11-01-2011 in ITA.No.140/07-08/A-III, PAN.No.AAACC1351M for the Assessment Year 2002-2003 and against the order of the Assistant Commissioner of Income Tax, Company Circle 1(3), Chennai dated 30-08-2007 in AAACC1351M/CM4-149 for the Assessment year 2002-2003.

For Appellant : Mr.T.Ravi Kumar,
Senior Standing Counsel

For Respondent : Mr.R.Venkata Narayanan

JUDGMENT

(Judgment was delivered by M.DURAI SWAMY, J.)

Challenging the order passed in I.T.A.No.1570/Mds/2011 in respect of the assessment year 2002-03 on the file of the Income Tax Appellate Tribunal, Chennai "D" Bench, the Revenue has filed the above appeal.

2.The assessee - Company is engaged in the business of development of Computer Software and renders training and software development services in Chennai, Mumbai, Bangalore and

also in Hyderabad. The assessee filed its return of income on 31.12.2002 declaring taxable income of Rs.8,89,04,154/-. After claiming deduction under Section 80HHE amounting to Rs.31,02,08,097 and also deduction under Section 10B amounting to Rs.24,22,46,315/- and claimed a refund of Rs.1,98,46,156/-. An intimation dated 29.03.2003 under Section 143(1)(a) was issued, granting a refund of Rs.2,12,43,455/-, which included interest amounting to Rs.14,71,067/-. A notice under Section 143(2) was issued on 16.09.2003 and the gain from exchange fluctuation/deduction under Section 80HHE was claimed at Rs.2,87,27,351/- and therefore, the assessee was asked to explain why the exchange gain of units excluding Chennai should be excluded from the eligible profit for the purpose of Section 80HHE. The Assessing Officer found that exchange fluctuation pertains to export of computer software and followed the assessment order passed for the year 1999-00 and 2001-02 by treating the foreign exchange fluctuation would not be eligible for calculating 80HHE deduction, instead the gains would be taxed under the head "income from other sources".

3.The other issue with regard to the gain from exchange fluctuation deduction under Section 10B, the Assessing Officer found that the exchange fluctuation relating to export of computer software and based on the decision for the assessment year 1999-00 and 2000-01, which was similar to the present assessment year, followed the same and held that exchange fluctuation gain was to be taxed separately as it was not derived from software exports and therefore, the exchange fluctuation was not to be regarded as eligible profit of the business while computing Section 10B and taxed under the same head "income from other sources".

4.The issue with regard to loss from Mumbai, Bangalore and Hyderabad unit and income from Chennai unit alone was to be considered in computing Section 80HHE. The Assessing Officer followed the decisions rendered in the assessment year 1999-00 and held that loss from Mumbai, Bangalore and Hyderabad units was to be reduced while computing eligible profit of business under Section 80HHE.

5.In respect of the issue with regard to the total turnover for the purpose of calculating Section 80HHEE, the assessee has considered only the total turnover of the Chennai unit and had excluded turnover of Hyderabad, Bangalore and Mumbai unit while calculating deductions under Section 80HHE in the return of income filed. The Assessing Officer held that Hyderabad unit was not engaged in the business of software development but were providing software training and followed the order passed in the assessment year 1999-00 and excluded the same from the total turnover.

6.The next issue with regard to the software expenses amounting to Rs.1,11,69,398/- which related to Chennai Unit-I & II, Bangalore and the sum of of Rs.1,82,21,841/- was capitalized in the books of accounts and the assessee had claimed the same as revenue expenditure while computing the taxable income, the Assessing Officer followed the assessment order passed in the year 1999-00 and 2000-01 and held that software expenses of Rs.2,93,98,239/- incurred was not eligible for deduction as revenue expenditure, but allowed depreciation at the rate of 25% on the same. On various disallowances, the Assessing Officer had arrived at a total taxable income at Rs.15,74,66,739/-.

7.The Commissioner of Income Tax passed an order under Section 263 holding that exemption under Section 10B was granted in respect of the Chennai Unit - II and there was a mistake in computation of deduction and the higher amount of exemption was granted, which the assessee was otherwise not entitled to. The CIT further held that the Assessing Officer failed to disallow the expenditure under Section 14A in respect to dividend income amounting to Rs.6,21,80,887/- which was exempted under Section 10(33), therefore, the assessment made was erroneous and prejudicial to the interest of the Revenue, after issuing show cause notice, the CIT directed the Assessing Officer to quantify the amount of exemption under Section 10B and also to quantify the exemption for the purpose of Section 14A after providing opportunity to the assessee. Aggrieved by the same, the assessee filed an appeal before the Commissioner of Income Tax (Appeals), which was partly allowed. Aggrieved by the order of the CIT (Appeals), both the assessee and the Revenue preferred appeals before the Income Tax Appellate Tribunal and the Tribunal partly allowed the Revenue's appeal and dismissed the assessee's appeal. Aggrieved by the same, the Revenue has filed the above appeal.

8.The above appeal has been admitted on the following substantial question of law:

"Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in directing the Assessing Officer to recompute the deduction under Section 10B by excluding telecommunication and other expenses incurred in foreign currency both from export turnover and total turnover?"

9.When the appeal is taken up for hearing, Mr.R.Venkata Narayanan, learned counsel appearing for the respondent relied upon the following judgments:

(i)[2018] 93 taxmann.com 33 (SC) [Commissioner of Income-tax, Central - III Vs. HCL Technologies Ltd.]

"...

10. The question arises here that when the particular term has not been defined in any particular section, is it allowed to import the meaning of such term from the other provisions of the same Act? Section 10A of the IT Act is a special beneficial provision and the purpose of deduction under such Section is to encourage and boost the new business undertakings situated in the free trade zone of this Nation by providing suitable deductions to such business entities. Sometimes, while calculating the deduction, disputes arise regarding the methodology of deduction which ought to be followed. Undisputedly, it is a matter of record that the respondent is engaged in the activity of trading of generic software and providing customized software development services for domestic as well as for foreign clients through its two units situated in Software Technology Park, Gurgaon (Now Gurugram) which falls under the definition of the Section 10A of the IT Act. The contention of the respondent is that it incurred expenditure in foreign exchange in sending professionals abroad as per the agreements with the foreign constituents.

...

19. In the instant case, if the deductions on freight, telecommunication and insurance attributable to the delivery of computer software under Section 10A of the IT Act are allowed only in Export Turnover but not from the Total Turnover then, it would give rise to inadvertent, unlawful, meaningless and illogical result which would cause grave injustice to the Respondent which could have never been the intention of the legislature.

20. Even in the common parlance, when the object of the formula is to arrive at the profit from export business, expenses excluded from export turnover have to be excluded from total turnover also. Otherwise any other interpretation makes the formula unworkable and absurd. Hence, we are satisfied that such deduction shall be allowed from the total turnover in same proportion as well.

21. On the issue of expenses on technical services provided outside, we have to follow the same principle of interpretation as followed in the case of expenses of freight, telecommunication etc., otherwise the formula of calculation would be futile. Hence, in the same way, expenses incurred in foreign exchange for providing the technical services outside shall be allowed to exclude from the total turnover."

(ii)(2019) 417 ITR 0441 (Mad) [M/s.Polaris Consulting & Services Ltd., (formerly known as M/s.Polaris Software Lab Limited) Vs. Deputy Commissioner of Income Tax], wherein a Division Bench of this Court held as follows:

"...

16.On a perusal of the nature of the contract and the various steps, which been enumerated therein, we find that the element of 'technical services' have been rendered as integral part of the software development process. There was no material available before the Assessing Officer to split up the transaction into two or to bisect the transaction to find out an element of 'technical services'. As rightly pointed out by the assessee, this exercise has been done by the Assessing Officer based on the notes to the accounts in the financial statements, which would be impermissible. What is required to be examined is the nature of services rendered by the assessee to the foreign entity. Thus, we are fully satisfied that the 'technical services' rendered by the assessee is not on a 'standalone basis', but it is an integral part of the software development and up to step No.(8), as mentioned above, the assessee is bound to render all assistance to the foreign entity. Therefore, the artificial split up of the transaction by the Assessing Officer, that too without any materials on his file, is wholly unsustainable.

17.For the above reasons, we are constrained to set aside the order passed by the Tribunal and answer the Substantial Question of Law No.1 in favour of the assessee."

(iii)Un-reported judgment of this Bench dated 19.01.2021 dated T.C.A.Nos.1470 to 1472 of 2010 [Commissioner of Income Tax, Chennai Vs. M/s.S.R.A. Systems Ltd., No.100, Valluvar Kottam High Road, Nungambakkam, Chennai], this Bench held as follows:

"...

5.As the issue of allowability of deduction under Section 10A is common to all the three Assessment Years, all the three Tax Appeals are taken up together and disposed of by this common judgment. For the Assessment Year 2000-01, the assessee had filed its return of income on 29.11.2000. The assessee claimed that it was eligible for deduction under Section 10B. The return was processed on 28.03.2002. Subsequently, the Assessing Officer had reason to believe that income

chargeable to tax had escaped assessment on account of the assessee Company being ineligible for deduction under Section 10A. Subsequently, a notice dated 22.03.2007 was issued under Section 148 and after giving an opportunity of hearing, the scrutiny assessment order was passed on 17.12.2007, disallowing the entire claim of deduction under Section 10B. Further, the expenditure incurred for the renovation and repairs of the rented premises of the assessee Company was disallowed by the Assessing Officer on the ground that such expenses were in the nature of capital expenditure. The Assessing Officer in his re-assessment order noted that in terms of Section 10B(ii) an undertaking in order to be eligible for deduction under Section 10B must not be formed by splitting up or reconstruction of a business already in existence. Further, the Assessing Officer held that deduction under Section 10B was not available to the assessee Company in view of the provisions of Section 10B(iii) which stipulate that eligible business is not formed by transfer to a new business of plant and machinery previously used for any purpose. The Assessing Officer found that the assessee had not complied with both these conditions, hence, it was not entitled to any deduction under Section 10B.

6. For the Assessment Year 2002-03, in the case of the assessee Company itself, the Income Tax Appellate Tribunal "C" Bench, Chennai had dealt with the applicability of Clauses (ii) and (iii) of Section 10A (2) in its order dated 16.05.2008 in I.T.A.No.2255/Mds/06. The Tribunal, after taking into consideration the decision of Apex Court reported in 107 ITR 195 [Textile Machinery Corporation Limited Vs. CIT] held as follows:

"... this is not a case of setting up of a new business, but only transfer of business place of existing business to a new place located in STPI area and thereafter, getting the approval from the authorities, the assessee become entitled to deduction under Section 10A. Merely because by shifting the business from one place to another and keeping some of the plant and machinery as those are bearing charge of financial institution, does not violate Clause (ii) and (iii) of Sub Clause (2) to Section 10A of the Income Tax Act."

7. The order passed by the Income Tax Appellate Tribunal was challenged by the Department in T.C.A.No.1916 of 2008 and the Hon'ble Division Bench of

this Court by its judgment dated 26.10.2018 confirmed the order of the Income Tax Appellate Tribunal dated 16.05.2008 made in I.T.A.No.2255/Mds/06 for the Assessment Year 2002-03 and dismissed the appeal. In view of the judgment of the Hon'ble Division Bench of this Court, it is clear that the applicability of Clauses (ii) and (iii) of Sub Clause (2) to Section 10B of the Act, the impugned order passed by the Income Tax Appellate Tribunal is proper. In view of the order passed by the Income Tax Appellate Tribunal dated 16.05.2008 in I.T.A.No.2255/Mds/06 and the judgment passed by the Hon'ble Division Bench of this Court on 26.10.2018 in Tax Case Appeal No.1916 of 2008, the assessee Company would be entitled to deduction under Section 10A and disallowance made by the Assessing Officer was not correct. Since the order passed under Section 263 itself has been set aside, the cause of action for re-assessment does not survive."

10.Mr.T.Ravi Kumar, learned Senior Standing Counsel appearing for the appellant fairly submitted that the issues involved in the present appeal are covered by the decision relied upon by the learned counsel for the respondent.

11.In view of the submissions made by the learned counsel on either side, we are convinced that the Question of Law involved in the present appeal is covered by the decisions relied upon by the learned counsel for the respondent, cited supra. Following the decisions of the Hon'ble Supreme Court and the decisions of this Court, the Question of Law is decided against the Revenue and in favour of the assessee. The appeal is liable to be dismissed. Accordingly, the Tax Case Appeal is dismissed. No costs.

Sd/-
Assistant Registrar(CS-VII)

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Sub Assistant Registrar

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To

1.The Income Tax Appellate Tribunal,
Chennai, "D" Bench.

2.The Commissioner of Income Tax
(Appeals)-III, Chennai.

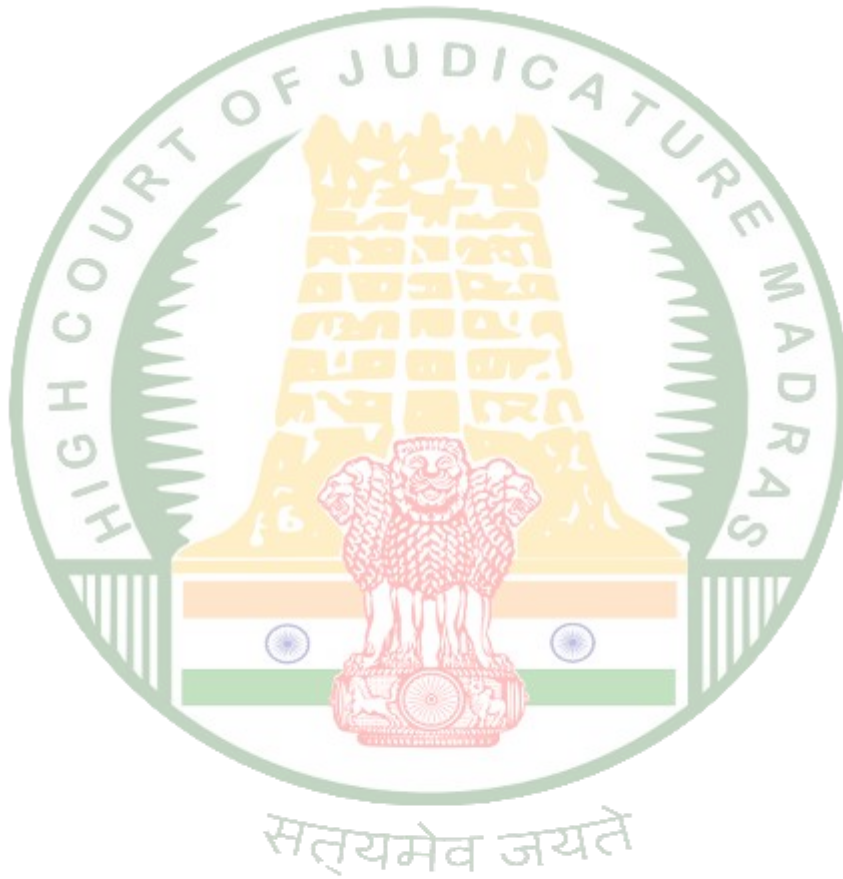
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3.The Assistant Commissioner of
Income Tax
Company Circle I(3), Chennai-34.

+1cc to Mr.T.Ravikumar, Advocate, S.R.No.12592
+1cc to Mr.Subbaraya Aiyar, Advocate, S.R.No.13490

T.C.A.No.795 of 2013

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