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

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Date of Decision: 20.02.2023

+ **ITA 105/2023**

PR. COMMISSIONER OF INCOME TAX-7 Appellant
Through: Mr Puneet Rai, Sr Standing Counsel
with Mr Ashwini Kumar, Standing
Counsel.

versus

M/S STERLING AGRO INDUSTRIES LTD Respondent
Through: None.

CORAM:

HON'BLE MR. JUSTICE RAJIV SHAKDHER

HON'BLE MS. JUSTICE TARA VITASTA GANJU

[Physical Hearing/Hybrid Hearing (as per request)]

RAJIV SHAKDHER, J. (ORAL):

CM Appl.8120/2023

1. Allowed, subject to just exceptions.

CM Appl.8121/2023 *[Application filed on behalf of the appellant seeking
condonation of delay of 56 days in filing the appeal]*

2. This is an application seeking condonation of delay. According to the
appellant/revenue, the period of delay involved is 56 days.

3. For the reasons stated in the application, the delay is condoned.

4. The application is disposed of.

ITA 105/2023

5. We have heard Mr Puneet Rai, learned senior standing counsel, who
appears on behalf of the appellant/revenue.

5.1 Mr Rai says that apart from the record placed before us, nothing further needs to be filed.

6. Admit.

6.1 As proposed, the following question of law is taken up for consideration by this Court:

(i) Given the facts and circumstances of the case, has the Income Tax Appellate Tribunal [in short, “Tribunal”] erred in deleting the addition made by the Assessing Officer on account of disallowance of deduction under Section 80IA of the Income Tax Act, 1961 [in short, “Act”], amounting to Rs. 12,63,07,697/-, ignoring the mandate of provisions of Section 80IA(5) of the Act?

7. This appeal concerns Assessment Year (AY) 2016-17 and is directed against the order dated 22.07.2022 passed by the Tribunal.

8. Mr Puneet Rai concedes that insofar as the proposed issue is concerned, the judgment of the Madras High Court rendered in *Velayudhaswamy Spinning Mills P. Ltd. and Anr. vs. Assistant Commissioner of Income Tax*, 2010 SCC OnLine Mad 6191, which was followed in *Principal Commissioner of Income-tax-3, Coimbatore vs. Prabhu Spinning Mills (P.) Ltd.*, (2016) 76 taxmann.com 8 (Madras), is in favour of the assessee, and against the revenue.

8.1 Mr Rai, however, seeks to place reliance on the judgment of the Karnataka High Court rendered in *Microlabs Ltd. vs. Assistant Commissioner of Income-tax, Bangalore*, (2015) 56 taxmann.com 160 (Karnataka) to burnish the appellant/revenue’s stand in the instant appeal.

9. Before we proceed further, it may be relevant to note certain broad

facts which, in our view, are necessary for the adjudication of the instant appeal.

9.1 The respondent/assessee had filed its return of income under Section 139 of the Act on 14.10.2016. In the said return, the respondent/assessee had quantified its taxable income as Rs. 22,12,03,720/-. This return was revised on 03.05.2017, whereby the total taxable income was reduced marginally and pegged at Rs. 21,29,69,700/-.

9.2 It appears that the respondent/assessee's case was taken up for scrutiny and a notice was served under Section 143(2) of the Act on the respondent/assessee on 14.07.2017.

9.3 The record also shows that an assessment order was framed under Section 143(3) of the Act. This order was passed on 29.12.2018. While framing the assessment, the Assessing Officer (AO) disallowed Rs. 12,63,07,697/-, which was claimed by the respondent/assessee as deduction under Section 80IA of the Act, while determining its total income, which was quantified at Rs. 33,92,77,400/-.

10. Being aggrieved, the appellant/revenue carried the matter in appeal to the Commissioner of Income Tax (Appeals) [in short, "CIT(A)"]. The CIT(A) agreed with the respondent/assessee and allowed the appeal.

10.1 This time around, the appellant/revenue was aggrieved and hence instituted an appeal in the Tribunal. The Tribunal, *via* the impugned order, dismissed the appeal of the appellant/revenue. It is in these circumstances that the appellant/revenue has filed the instant appeal under Section 260A of the Act.

11. We may note that before the Tribunal, two issues were raised. Firstly, which AY would qualify as "the initial AY". Secondly, as to whether

unabsorbed losses/depreciation could be notionally carried forward for the purposes of determining profit for the eligible business under Section 80IA of the Act.

11.1 Insofar as the first issue is concerned, the Tribunal, *inter alia*, relied upon the Central Board of Direct Taxes [in short, “CBDT”] circular no.1/2016 dated 15.02.2016.

11.2 The said circular, *inter alia*, emphasized the fact that the initial AY was the year which the assessee chooses to opt for, and was not the year when the eligible business commenced or the point in time when the manufacturing activity was carried out in the first instance.

11.3 The Tribunal, in support of its reasoning, also relied upon the judgment of the Madras High Court in ***Prabhu Spinning Mills (P.) Ltd.***

11.4 Likewise, insofar as the second issue was concerned, the Tribunal ruled in favour of the respondent/assessee.

12. Mr Rai says that since the ***Mircrolabs Ltd.*** case is pending in the Supreme Court, in which the Karnataka High Court has taken a decision in favour of the appellant/revenue, the appellant/revenue’s appeal is sustainable.

13. We have examined in detail the facts of this case as noted above, and also the ratio of the three judgments cited before us.

13.1 As noted right in the beginning, there are two judgments of the Madras High Court, which are relevant for the purposes of determining the issue at hand, i.e., the ***Velayudhaswamy Spinning Mills (P.) Ltd.*** case and the ***Prabhu Spinning Mills (P.) Ltd.*** case.

13.2 We may note that insofar as the issue proposed by the revenue is concerned, the Division Bench of the Madras High Court in the ***Prabhu***

Spinning Mills (P.) Ltd. case has followed its own decision in the *Velayudhaswamy Spinning Mills (P.) Ltd.* case. The Division Bench has noted that they have followed the said decision in a number of cases. The large part of the discussion in the *Prabhu Spinning Mills (P.) Ltd. case* veered around what would be the initial AY of the eligible business. The court, after noting the CBDT's circular no.1/2016 dated 15.02.2016, concluded that the assessee had an option of choosing its initial AY and, in this regard, adverted to a plain language of sub-section (2) of Section 80IA of the Act. Although this issue is not proposed before us, the reasoning of the Division Bench of the Madras High Court in the *Prabhu Spinning Mills (P.) Ltd.* case is unimpeachable.

13.3 Insofar as the proposed issue is concerned, the following observations made by the Division Bench of the Madras High Court in the *Velayudhaswamy Spinning Mills (P.) Ltd.* case, being relevant, are extracted hereafter:

"16. From a reading of sub-section (1), it is clear that it provides that where the gross total income of an assessee includes any profits and gains derived by an undertaking or an enterprise from any business referred to in subsection (4), i.e., referred to as the eligible business, there shall, in accordance with and subject to the provisions of the section, be allowed, in computing the total income of the assessee, a deduction of an amount equal to 100 per cent, of the profits and gains derived from such business for ten consecutive assessment years. Deduction is given to eligible business and the same is defined in sub-section (4). Sub-section (2) provides option to the assessee to choose 10 consecutive assessment years out of 15 years. Option has to be exercised, if it is not exercised, the assessee will not be getting the benefit. Fifteen years is outer limit and the same is beginning from the year in which the undertaking or the enterprise develops and begins to operate any infrastructure activity, etc. Sub-section (5) deals with quantum of deduction for an eligible business. The words "initial assessment year" are used in sub-section (5) and the same is not defined under the provisions. It is to be noted that "initial assessment year" employed in sub-section (5) is different from the words "beginning from the year" referred to in sub-section (2). The important factors are to

be noted in sub-section (5) and they are as under:

- “(1) It starts with a non obstante clause which means it overrides all the provisions of the Act and other provisions are to be ignored;*
- (2) It is for the purpose of determining the quantum of deduction;*
- (3) For the assessment year immediately succeeding the initial assessment year;*
- (4) It is a deeming provision;*
- (5) Fiction created that the eligible business is the only source of income; and*
- (6) During the previous year relevant to the initial assessment year and every subsequent assessment year.*

17. *From a reading of the above, it is clear that the eligible business were the only source of income, during the previous year relevant to the initial assessment year and every subsequent assessment years. When the assessee exercises the option, the only losses of the years beginning from initial assessment year alone are to be brought forward and no losses of earlier years which were already set off against the income of the assessee. Looking forward to a period of ten years from the initial assessment is contemplated. It does not allow the Revenue to look backward and find out if there is any loss of earlier years and bring forward notionally even though the same were set off against other income of the assessee and the set off against the current income of the eligible business. Once the set off is taken place in earlier year against the other income of the assessee, the Revenue cannot rework the set off amount and bring it notionally. A fiction created in sub-section does not contemplates to bring set off amount notionally. The fiction is created only for the limited purpose and the same cannot be extended beyond the purpose for which it is created.*

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19. *From a reading of the above, the Rajasthan High Court held that it is not at all required that losses or other deductions which have already been set off against the income of the previous year should be reopened again for computation of current income under section 80-1 for the purpose of computing admissible deductions thereunder. We also agree with the same. We see no reason to take a different view.*

20. *The standing counsel appearing for the Revenue is unable to bring to our notice any relevant material or any compelling reason or any contra judgment of other courts to take a different view. He only relied heavily on the Memorandum explaining the provisions in the Finance (No.*

2) Bill, 1980, [1980] 123 ITR (St.) 154 to support this case and the same reads as follows:

“Clause 30(iii). In computing the quantum of ‘tax holiday’ profits in all cases, taxable income derived from the new industrial units, etc., will be determined as if such units were an independent unit owned by a taxpayer who does not have any other source of income. In the result, the losses, depreciation and investment allowance of earlier years in respect of the new industrial undertaking, ship or approved hotel will be taken into account in determining the quantum of deduction admissible under the new section 80-1 even though they may have been set off against the profits of the taxpayer from other sources.”

21. *We are not agreeing with the counsel for the Revenue. We are, therefore, of the view that loss in the year earlier to the initial assessment year already absorbed against the profit of other business cannot be notionally brought forward and set off against the profits of the eligible business as no such mandate is provided in section 80-IA(5).”*

14. As would be evident, the Division Bench of the Madras High Court in the ***Velayudhaswamy Spinning Mills (P.) Ltd.*** case has broken down sub-section (5) of Section 80IA of the Act and analysed as to what would be the important indices of the said provision. This is evident upon a reading of paragraph 16 of the said judgement.

14.1 According to us, the indices noted in paragraph 16 of the said judgement clearly and distinctly emerge even on a plain reading of the said provision.

14.2 The argument advanced before us on behalf of the appellant/revenue, which was also the submission put forth before the Madras High Court, proceeded on the following lines: Because sub-section (5) of Section 80IA opens with a non-obstante clause, therefore, loss or unabsorbed depreciation which has already been set off prior to the initial year against the other business [i.e. business apart from the eligible business], should be notionally

carried forward and adjusted against the profits of the eligible business in order to determine the deduction that an assessee can avail under Section 80IA of the Act.

14.3 According to us, there is nothing to suggest in Sub-clause (5) of Section 80IA of the Act that the profits derived by an assessee from the eligible business can be adjusted against “notional losses which stand absorbed against profits of other business.” The deeming fiction created by sub-section (5) of Section 80IA does not envisage such an adjustment. The fiction which has been created is simply this: the eligible business will be the only source of income. There is no fiction created, that losses which have already been absorbed, will be notionally carried forward and adjusted against the profits derived from the eligible business to quantify the deduction that the assessee could claim under Section 80IA of the Act.

14.4 A perusal of the judgment rendered in the ***Microlabs Ltd.*** case would show that the Karnataka High Court gave weight to the fact that sub-section (5) of Section 80IA commenced with a non-obstante clause. It was based on this singular fact that the Karnataka High Court chose to veer away from the view expressed by the Madras High Court in the ***Velayudhaswamy Spinning Mills (P.) Ltd.*** case. This aspect emerges on an appraisal of paragraph 6 of the judgement of the Karnataka High Court rendered in ***Microlabs Ltd. case.***

14.5 We have read the aforementioned portion of the judgement along with Mr Rai. For the sake of convenience, the same is extracted hereafter:

6. It is stated that the non-obstante clause in sub-section (5) means it overrides all the provisions of the Act and other provisions are to be ignored. In the absence of non obstante clause, what the judgment of the Madras Court states is the legal position, because of the non obstante clause, the set off amount against other income of the assessee has to be ignored and

because of the fiction created in the sub-section notionally, the set losses is to be treated as "losses being carried forward and after deducting the said losses, the profit prior to business is to be calculated," i.e., precisely what the Special Bench has stated and the relevant portion of the judgment reads as under:

"From the reading of the above, it is clear that the eligible business were the only source of income, during the previous year relevant to initial assessment year and every subsequent assessment years. When the assessee exercises the option, the only losses of the years beginning from initial assessment year alone are to be brought forward and no losses of earlier years which were already set off against the income of the assessee. Looking forward to a period often years from the initial assessment is contemplated. It does not allow the Revenue to look backward and find out if there is any loss of earlier years and bring forward notionally even though the same were set off against other income of the assessee and the set off against the current income of the eligible business. Once the set off is taken place in earlier year against the other income of the assessee, the Revenue cannot rework the set off amount and bring it notionally. Fiction created in sub-section does not contemplates to bring set off amount notionally. Fiction is created only for the limited purpose and the same cannot be extended beyond the purpose for which it is created."

15. We are unable to persuade ourselves to agree with the view taken by the Karnataka High Court in the ***Microlabs Ltd.*** case. We respectfully agree with the view taken by the Madras High Court in the ***Velayudhaswamy Spinning Mills (P.) Ltd.*** case, which has been followed in the ***Prabhu Spinning Mills (P.) Ltd.*** case as well.

16. We have given our own reasons as to how sub-section (5) of Section 80IA should operate.

17. There is another additional reason why we agree with the view of the Tribunal. The Tribunal has noted that in earlier AYs, the AO has neither disallowed the claim nor adjusted notional depreciation/losses of previous years set off against other income in the years prior to the initial AY.

18. Accordingly, the question of law is answered against the appellant/revenue and in favour of the respondent/assessee.
19. The appeal is disposed of in the aforesaid terms.
20. The Registry will dispatch a copy of this judgement to the respondent/assessee *via* all permissible modes including email.

RAJIV SHAKDHER, J

TARA VITASTA GANJU, J

FEBRUARY 20, 2023/pmc

Click here to check corrigendum, if any