IN THE HIGH COURT OF JUDICATURE AT BOMBAY

O. O. C. J.

INCOME TAX APPEAL (LODG.) NO.2887 OF 2009

The Commissioner of Income Tax-13
Ayakar Bhavan, M.K. Road,
Mumbai 400 020. ..Appellant.

Vs.

Kalpataru Colours and Chemicals
110, Mandavi Navjivan Bldg.,
121/127, Kazi Sayyed Street,
Mumbai 400 003. ..Respondent.

....

Mr. Vimal Gupta with Mr. Suresh Kumar, Ms Padma Divakar, Mr. A.S. Shivsharan and Mr. D.K. Kamwal for the Appellant.

Mr. J.D. Mistri, Senior Advocate with Mr. A.D. Shetty, Mr. R.V. Shetty and Ms. Rita Joshi for the Respondent.

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CORAM : DR.D.Y.CHANDRACHUD &
J.P.DEVADHAR, JJ.

28 /29 June 2010.

ORAL JUDGMENT (Per. DR.D.Y.CHANDRACHUD, J.). :

A. The questions of law

1. This appeal by the Revenue under Section 260-A of the

Income Tax Act, 1961 arises out of a decision of a Special bench of the Income Tax Appellate Tribunal dated 11 August 2009. The Revenue has formulated two questions of law in the appeal:

> "a) Whether the Tribunal is justified in holding that the entire amount received on the sale of the Duty Entitlement Passbook does not represent profits chargeable under Section 28(iiid) of the Income Tax Act, 1961 and that the face value of the Duty Entitlement Passbook shall be deducted from the sale proceeds;
>
> b) Whether the Tribunal is justified in holding that the face value of the Duty Entitlement Passbook is chargeable to tax under Section 28(iiib) at the time of accrual of income i.e. when the application for Duty Entitlement Passbook is filed with the competent authority pursuant to the exports made and that the profits on the sale of Duty Entitlement Passbook representing the excess of the sale proceeds over the face value is liable to be considered under Section 28(iiid) at the time of sale;"

B. Facts

2. The appeal relates to Assessment Year 2003-04. The Appellant is a trader and exporter in dyes, chemicals and other products. In the return of income the assessee declared a total income of Rs.1.06 Crores. The assessee claimed a deduction under Section 80HHC in the amount of Rs.78.01 Crores. The total export turnover of the assessee was Rs.12.82 Crores. The assessee received

export incentives of Rs.1.89 Crores inclusive of a consideration of Rs. 1.87 Crores received on the sale of Duty Entitlement Pass Book (DEPB) credit. The export turnover of the Appellant was over Rs.10 Crores. The Assessing Officer declined to grant the benefit of a deduction under Section 80HHC on the ground that under the third proviso to sub section (3), the DEPB credit could be considered for deduction in the case of an assessee with an export turnover of more than Rs.10 Crores only on the fulfillment of two conditions viz (i)The assessee must have had an option to choose either duty drawback or DEPB; (ii) The rate of duty drawback credit attributable to customs duty should have been higher than the rate of credit allowable under the DEPB scheme. These conditions were not fulfilled. Hence, the Assessing Officer declined to grant a deduction under Section 80HHC.

3. In appeal, the Commissioner (Appeals) held that the contention of the assessee that only the premium realized on the sale of DEPB credit should be treated as a 'profit on transfer' within the

meaning of Section 28(iiid) was not acceptable. In the present case, according to the Commissioner the amount of credit was not purchased nor was it a cost. The amount was regarded to be a revenue item appearing on the credit side of the Profit and Loss Account. The premium, according to the Commissioner, represented a further gain in income. The Commissioner held that as a matter of fact the assessee did not import any material, which is a part of the export product, and had sold the DEPB credit. Hence, the question of reducing the DEPB credit from the cost of export would not arise. The Commissioner was of the view that if the so called duty was never a part of any purchase cost of material, the question of deducting it from the cost of material would not arise. The alternative contention of the assessee was that the DEBP entitlement should be considered as a cash assistance within the meaning of Section 28(iiib). On this, the finding was that DEPB is not a cash incentive. The entire sale proceeds on the sale of the DEPB credit were held to represent profit, there being no cost involved. On this ground, the findings of the Assessing Officer were confirmed.

4. A Special bench of the Tribunal was constituted by the President for determining as to whether the entire amount received on the sale of the DEPB entitlement represents profit chargeable under Section 28(iiid) of the Income Tax Act, 1961 or whether the profit referred to therein requires any artificial cost to be interpolated. The Tribunal came to the conclusion that the entire amount that is received on the sale of the DEPB entitlement does not represent a profit chargeable under Section 28(iiid) and the face value of the DEPB entitlement is liable to be deducted from the sale proceeds. According to the Tribunal the face value of the DEPB entitlement was chargeable to tax under Section 28(iiib) while the difference between the sale consideration and the face value of the DEPB entitlement would fall for classification under Section 28(iiid).

5. This appeal has been listed for hearing together with a batch of other appeals. Since certain questions of law would arise in all the appeals, we had in the interests of fairness permitted counsel

appearing on behalf of the assessees in the batch of cases to urge submissions on the question of law. Accordingly, during the course of the hearing, we have heard arguments on behalf of the intervening parties as well.

C. Submissions

(i) The Revenue

6. On behalf of the Revenue it has been submitted that (i) The assessee had not complied with the conditions prescribed in the third proviso to Section 80HHC and was therefore not entitled to the benefit that is provided therein in respect of income arising from the transfer of the DEPB entitlement; (ii) An entitlement under the DEPB can never have a cost because the computation of the benefit is based on the FOB value of exports; (iii) A DEPB entitlement is an incentive without a cost and the full extent of the DEPB credit represents an entitlement; (iv) The common element which underlies clauses (iiia), (iiib) and (iiic) of Section 28 is that any income received as and by way of an export incentive would be income classifiable under the

head of profits and gains of business or profession. For instance under clause (iiic) where a duty is paid and a drawback is obtained, the entire duty drawback is treated as income which is chargeable under the head of profits and gains of business or profession. The consideration realized under clause (iiid) on the transfer of a DEPB entitlement, could not be placed on a higher footing and the entire sale proceeds constitute a profit on the transfer of the entitlement.

(ii) The Assessee

7. On behalf of the assessees, it has been urged by counsel that (i) The plain language of Section 28(iiid) shows that it applies to a situation involving profits on the transfer of the DEPB entitlement. The expression "profits" cannot mean sale proceeds; (ii) The object of the DEPB scheme is to neutralize the cost of inputs involved in the export product. Hence, it is directly related to export profit and the sequitur is that the assessee is entitled to a deduction under Section 80HHC on the amount of the DEPB entitlement; (iii) The normal way of obtaining this benefit is to utilize the face value for the payment of

customs duty. If the assessee were to do so, the cost of the inputs would to that extent be reduced; the profits would stand increased and the assessee would be entitled to the benefit of Section 80HHC; (iv) The quantum of the benefit is the face value of the DEPB entitlement. Hence, the face value of the DEPB entitlement is a part of income and forms a part of export profits. Once it is a part of income, whether it falls under clauses (iiib), (iiic) or (iiid) of Section 28 is of no consequence and the assessee would be entitled to a deduction in respect of the face value; (v) The face value of the DEPB entitlement has a direct nexus with exports and it is only the profit element on the trading of the entitlement which is liable to be excluded on the ground that it has no nexus with profits. Both the face value of the DEPB entitlement and the trading profits are comprised in the business profits of the assessee. Explanation (baa) to Section 80HHC determines how much would be exempt for the purposes of the provision. Whatever is not directly relatable to exports has to be excluded. The face value of the DEPB entitlement cannot be excluded because it is directly relatable to exports; (vi) The

DEPB entitlement is not required to be reduced under Explanation (baa) because - (a) on a plain reading, Explanation (baa) refers to clause (iiid) of Section 28 which in turn postulates a profit generated on transfer; (b) Clause (iiid) of Section 28 is in contradistinction to clauses (iiib) and (iiic) where the full amount of the benefit is referred to; (vii) The speech of the Finance Minister on the floor of Parliament when the amendment bill was introduced would demonstrate what was required to be removed was the premium representing the excess over the face value; (viii) The judgment of the Tribunal in the case of **P & G Enterprises (P) Ltd. v. Deputy Commissioner of Income Tax**[1] allowed the benefit of Section 80HHC over the premium realized on the sale of the entitlement and it was this aspect of the decision of the Tribunal that was sought to be remedied by the amendment to Section 28; (ix) The decision of this Court in the case of **Commissioner of Income Tax v. Dresser Rand India P. Ltd.**[2] would show that what is not related to export is liable to be reduced; (x) The interpretation of the Revenue would require that export profits

1 (2005) 93 ITD 138 (Delhi)

2 (2010) 323 ITR 429 (Bom)

would not get a deduction; (xi) The interpretation suggested on behalf of the Revenue would result in a manifest absurdity. The face value of the DEPB entitlement is the quantum of benefits directly related to exports and cannot be excluded out of reckoning for computing the deduction under Section 80HHC. Mr.Mistry has also stated that he does not consider it necessary to urge any submission on the view of the Tribunal that the face value of the DEPB falls under Section 28(iiib).

D. The legislative scheme – Section 28 and Section 80HHC

8. At the outset it would be necessary to advert to the legislative scheme underlying the provisions of Section 28 on the one hand and Section 80HHC on the other.

(i) Clauses (iiia), (iiib) and (iiic) of Section 28

9. Section 28 elucidates incomes which shall be chargeable to income tax under the head of "Profits and gains of business or profession". Clauses (iiia), (iiib) and (iiic) were inserted into the Section by the Finance Act of 1990. Clause (iiia) was inserted with

retrospective effect from 1 April 1962, clause (iiib) with effect from 1 April 1967 and clause (iiic) with effect from 1 April 1972. Clauses (iiia), (iiib) and (iiic) as inserted into Section 28 provide as follows :

> "(iiia) 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);
>
> (iiib) Cash assistance (by whatever name called) received or receivable by any person against exports under any scheme of the Government of India;
>
> (iiic) 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."

10. Prior to the insertion of clauses (iiia) to (iiiic), the question as regards the taxability of export incentives was dealt with in a judgment of this Court in **Metal Rolling Works Pvt. Ltd. v. Commissioner of Income Tax**[3] and by the Allahabad High Court in **Agra Chain Manufacturing Co. v. Commissioner of Income Tax**[4]. The prevailing view of these two courts was that in the case of an assessee who is engaged in exports import entitlements received

3 (1983) 142 ITR 170 (Bom.)

4 (1978) 114 ITR 840 (Allahabad)

under incentive schemes of the Government of India would be taxable under clause (iv) of Section 28 as the value of a benefit, whether convertible into money or otherwise arising from business or the exercise of a profession. However, there appeared to be a conflict of opinion among Courts on the issue which was resolved by Parliament by the insertion of clauses (iiia), (iiib) and (iiic) by the Finance Act of 1990. While explaining the reasons underlying the amendment, circular 572 dated 3 August 1990 of the Board noted that at that point in time the incentives which were given to exporters fell into three categories (i) Cash compensatory support; (ii) Drawback of duty and (iii) Import entitlement licence. The view of the Revenue had all along been that such export incentives were revenue receipts and were taxable, whether they took the form of cash compensatory support, a drawback of duty or a profit on the sale of an import entitlement licence. Parliament stepped in to settle the question as regards the taxability of these incentives by enacting with retrospective effect that profits on the sale of an import licence, cash assistance under any scheme of the Central Government and a

drawback of duty of customs or excise would constitute income that would be chargeable to income tax under the head of profits and gains of business. Clauses (iiia), (iiib) and (iiic) therefore constitute a recognition by Parliament that the three forms in which incentives were granted by the Union Government viz. import licence, cash compensatory assistance and a drawback of duty would constitute taxable income that would be exigible to income tax.

(ii) The DEPB scheme under the Exim Policy

11. With effect from 1 April 1997 the Exim policy came to recognize an additional form of export incentives, in the nature of the Duty Entitlement Pass Book scheme. The Exim policy for the period 1 April 1997 to 31 March 2002 elucidates the nature of export incentives. The policy clarifies in Chapter VII that the Advance Licence Scheme enables the import of inputs required for export production. On the other hand, the duty exemption scheme enables post export replenishment / remission of the duty on inputs used in the export product. An advance licence is issued under the duty

exemption scheme to allow import of inputs which are physically incorporated in the export product. Paragraph 7.3(a) states that an advance licence is issued for the duty free import of inputs subject to an actual user condition.

12. The Duty Entitlement Pass Book scheme is explained in paragraph 7.14 of the policy. The scheme is "an optional facility" which is granted to exporters who are not desirous of going through the licensing route. The object of the DEPB scheme is to neutralize the incidence of customs duty on the import content of the export product. Neutralization is provided by granting a duty credit against the export product. The manner in which the DEPB scheme operates is that an exporter is allowed to apply for credit which is computed as a specified percentage of the FOB value of exports made in freely convertible currency. The export products and the rates governing the grant of DEPB credit are notified. The DEPB credit and items imported against it are made freely transferable under paragraph 7.16. The duty credit under the scheme is calculated by taking into

account what is described as a deemed import content of the export product in accordance with standard input output norms and the basic customs duty payable on such deemed import. In other words, the credit which is made available to an exporter under the DEPB scheme represents a specified percentage of the FOB value of the goods exported. The goods which are exported need not, as a matter of fact, necessarily utilize imported inputs. The policy calculates a deemed import content on the basis of standard input output norms and a credit is made available to the exporter. The credit need not be utilized by the exporter himself nor for that matter is it necessary for the exporter to utilize the goods that may be imported against the utilization of the DEPB credit. The DEPB credit is transferable.

(iii) Section 80HHC

Profits received from export

13. Under sub section (1) of Section 80HHC, a deduction is allowed to the extent of profits "derived by the assessee" from the export of goods to which the Section applies. Since the deduction is

in respect of profits derived from export, Parliament has in sub section (3) laid down a formula on the basis of which export profits have to be computed. Sub section (3) of Section 80HHC consists of three clauses. Clause (a) deals with the export of goods manufactured or processed by the assessee; clause (b) deals with the export of trading goods and clause (c) deals with the export of goods manufactured or processed by the assessee and of trading goods. Sub section (3) of Section 80HHC reads as follows :

> "(3)(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."

14. Under clause (a) of sub section (3) the expression "profits derived from export" are defined to 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. In other words, the proportion between the export turnover to the total turnover of the business is applied to the profits of the business of the assessee and the result constitutes export profits. However, where an assessee carries on the business of export of trading goods, clause (b) defines export profits to be the export turnover in respect of such trading goods which is to be reduced by the direct and indirect costs attributable to the export.

Profits of business

15. In the application of the formula to a manufacturer

exporter, clause (a) refers to the profits of the business. The expression profits of the business is elucidated in Explanation (baa) to Section 80HHC. Explanation (baa) is to the following effect :

> "(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."

16. The expression "profits of the business" means profits as computed under the head of 'profits and gains of business or profession' under Sections 28 to 44D and they are thereupon to be reduced to the extent provided by clauses (1) and (2). Clause (1) as it now stands is bifurcated in two parts. The first consists of the sums referred to in clauses (iiia), (iiib), (iiic), (iiid) and (iiie) of Section 28; and the second consists of receipts by way of brokerage, commission,

interest, rent, charges or any other receipt of a similar nature included in such profits. The first part of clause (1) provides for the exclusion of ninety percent of 'incentive profits' (those referred to in clauses (iiia) to (iiie) of Section 28) and 'independent incomes' which are not relatable to exports.

Rationale for exclusion of independent incomes and incentive profits

17. The rationale for this exclusion is explained in the judgment of the Supreme Court in the **Commissioner of Income Tax V. K. Ravindranathan Nair**[5]. The Supreme Court held that the expression "derived from" that is used in sub section (1) of Section 80HHC is narrower in its ambit than the words 'attributable to' and consequently, it is only profits that are derived from export that qualify for a deduction. The second important facet of the judgment of the Supreme Court is in explaining the provisions of Explanation (baa). The Supreme Court has observed that what the explanation

5 (2007) 295 ITR 228 (SC)

postulates is that though incentive profits and independent incomes constitute a part of the gross total income, they have to be excluded from the gross total income because such receipts have no nexus with the export turnover. In referring to "incentive profits" the Supreme Court had in contemplation clauses (iiia) to (iiie) of Section 28. Similarly, the independent incomes to which a reference has been made in the judgment of the Supreme Court are receipts by way of brokerage, commission, interest, rent, charges and any other receipt of a similar nature included in the profits of the business.

(iv) **The amendment of 2005 : Clauses (iiid) and (iiie) of Section 28**

18. The reference to clauses (iiid) and (iiie) in Explanation (baa) to Section 80HHC was brought in under the Taxation Laws (Amendment) Act 2005. The Amending Act brought about a corresponding amendment to Section 28 by the insertion of clauses (iiid) and (iiie). Clauses (iiid) and (iiie) as inserted into Section 28 by the Amending Act of 2005 are to the following effect :

> "(iiid) 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);
>
> (iiie) any profit on the transfer of the 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)."

19. Clause (iiid) contemplates that any profit on the transfer of the Duty Entitlement Pass Book scheme would be chargeable to income tax as a business profit. The circumstances in which the amendment was brought about would have a bearing on the subject matter of the controversy in the present case and will therefore need some elaboration. In **P & G Enterprises (supra)** a Bench of the Income Tax Appellate Tribunal at Delhi considered the case of an exporter to whom a credit was available under the Duty Entitlement Pass Book scheme. The DEPB credit was transferred and the receipts were shown as business receipts under Section 28(iiia). The Assessing Officer held that the receipts upon the transfer of the DEPB

entitlement fell for classification under Section 28(iv) and he excluded ninety percent of those receipts under Section 80HHC. The Commissioner (Appeals) held that the receipts were in the nature of revenue receipts and the entirety of those receipts was assessable as business receipts under Section 28(iv). The Commissioner held that those receipts were not derived from export though they may have been attributable to that business and upheld the action of the Assessing Officer in excluding ninety percent of the DEPB receipts under Explanation (baa). Before the Tribunal there was no dispute about the finding that the DEPB receipts were in the nature of revenue and that the entirety of those receipts was chargeable to tax under Section 28(iv). The Tribunal held that Section 28(iv) was not referred to in Explanation (baa) and the omission to include that provision suggested that the legislature did not intend the exclusion of ninety percent of those incomes which fell within the purview of Section 28(iv). The Tribunal was also of the view that DEPB receipts did not constitute a 'receipt of a similar nature' within the meaning of Explanation (baa) and were not therefore liable to be reduced in

computing the profits of business. The judgment of the Tribunal would therefore show that (i) The entirety of the DEPB receipts were treated as of a revenue nature; (ii) The DEPB receipts were held to fall within the purview of Section 28(iv); and (iii) Such receipts were held not to be sustainable to a reduction of ninety percent under Explanation (baa).

20. It is in this background that Parliament stepped in by amending Section 28 and correspondingly, Explanation (baa), so as to specifically bring in DEPB receipts within the fold of taxability under Section 28. The fact that the entirety of the DEPB receipts was taxable was elucidated in the judgment of the Tribunal. The Tribunal had, however, held that such receipts were not liable to sustain a reduction of ninety percent under Explanation (baa). Parliament considered it appropriate to amend Section 28 by bringing in a specific provision that would cover DEPB receipts on the one hand and by clarifying through the amendment of Explanation (baa) that DEPB receipts also constitute incentive profits which were liable to

sustain a reduction of ninety percent.

21. Parliament incorporated several provisos to sub section (3) of Section 80HHC. Under the first proviso the profits computed under clauses (a), (b) or (c) of sub section (3) have to be increased by the amount which bears to ninety percent of any sum referred to any clauses (iiia), (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. The second and third provisos to sub section (3) are of some significance in the present case and they read as follows :

> "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."

22. Parliament has made, by the second and the third provisos a classification between exporters with an export turnover not exceeding Rs.10 Crores and those exporters whose turnover exceeds that amount. For those exporters whose turnover is less than Rs.10 Crores, Parliament has legislated that the profits computed under sub section (3) of Section 80HHC are liable to a further increase by the amount which bears to ninety percent of the sum referred to in clauses (iiid) or (iiie) of Section 28, the same proportion as the export turnover bears to the total turnover. In the case of an exporter with a

turnover in excess of Rs.10 Crores, the grant of this additional benefit is, however, conditioned by the fulfillment of the two conditions which are referred to therein. Those conditions are that the assessee must have necessary and sufficient evidence that (i) he had an option to choose either duty drawback or the Duty Entitlement Pass Book scheme; and (ii) The rate of duty drawback credit attributable to customs duty was higher than the rate of credit allowable under the DEPB scheme. Before this Court, it is an admitted position, on which there is no dispute that the assessee did not fulfill the requirement of the third proviso. What the Tribunal has, however, done in the course of its decision is to observe that clause (iiid) of Section 28 would cover only the difference between the sale consideration realized by the assessee on the transfer of the DEPB credit and the DEPB credit that was the subject of transfer. As regards the DEPB credit, described as the face value, the Tribunal observed that it was liable to be brought in under Section 28(iiib).

E. **"Any profit on the transfer" of DEPB credit**

23. The submission which has been urged before the Court by the assessee is that Section 28(iiid) brings within the fold of income chargeable to tax any profit on the transfer of the Duty Entitlement Pass Book scheme. According to the assessee, the expression profit means the difference between the sale consideration realized from the transfer of the DEPB receipts and the face value of the DEPB credit that has been transferred. The Tribunal, while accepting the contention of the assessee has also held that it is only this difference which would fall within the purview of clause (iiid) and that the DEPB credit would fall within the purview of clause (iiib). (Clause (iiib) deals with a cash assistance received or receivable under any scheme of the Government of India.)

24. Export incentives, such as import licenses, cash assistance, duty drawback, DEPB credit, or duty free replenishment certificates are all intended to encourage exports. The object of these incentives is to neutralize the incidence of customs duty on the import content of the export product. Under the Income Tax Act, 1961 not only the

profits on sale of an import licence and profits on transfer of DEPB credit/DFRC, but also the duty drawback received by an assessee are considered as profits of business. Duty drawback is nothing but receiving back the amount of duty actually paid by the assessee. Similarly, the DEPB credit is a credit to be utilized in paying the customs duty on goods to be imported. When the duty drawback received by the assessee constitutes profits of business, then, it is obvious that the amount realized on transfer of the DEPB credit would also be business profits. Thus, the amount received on transfer of DEPB credit would be profits of business covered under Section 28(iiid).

25. Clause (iiia) treats as income chargeable to tax, profits on the sale of an import licence. When the licence is sold, the entire amount is received as profit. The entire amount that is received on the sale of a licence is considered as profits of business under Section 28(iiia). Similarly, the entire amount of cash assistance received or receivable by any person against exports under a scheme of the

Government of India is treated as income for the purposes of chargeability to tax. By clause (iiic) the entire duty of customs or excise repaid or repayable as drawback against exports is also treated as income that would be subject to tax. Under the Exim policy, the scheme relating to the DEPB entitlement is in the nature of an option which is made available to an exporter who does not wish to go through the licensing procedure. The transfer of a DEPB credit is similar to trading in a licence. As we have noted, when a licence is sold, the holder receives the entire amount as profit which is treated by the legislature as profits of business within the meaning of Section 28. Logically and as a matter of first principle, there would be no justification for this Court to treat the amount which is received by an exporter on the transfer of the DEPB credit any differently than the profits which are made on the sale of an import licence under clause (iiia). Both would have to be treated as profits of business under Section (iiid).

26. Prior to the insertion of clause (iiid) in Section 28, the

dispute was, whether the profits of business such as the amount received on transfer of DEPB would constitute export profit for the purposes of deduction under Section 80HHC or not. According to the exporters, the entire amount received on transfer of a DEPB credit would constitute export profit and according to the revenue it would not. Thus, there was no dispute that the entire amount received on transfer of DEPB was profits of business but the dispute was whether or not such profits would constitute export profits.

27. By the Finance Act of 2005, Parliament resolved the controversy by inserting a specific clause, namely Clause (iiid) in Section 28 to the effect that profits on transfer of DEPB i.e., the amount received on transfer of DEPB is income chargeable to tax under the head – profits and gains of business and profession. As regards the deduction under Section 80 HHC, the legislature substituted Explanation (baa) in Section 80HHC so as to exclude 90% of the profits received on transfer of DEPB from the profits of business for the purposes of Section 80HHC and inserted the second and third

provisos to Section 80HHC(3). By the second proviso it was provided that in the case of an assessee having an export turnover not exceeding Rs.10 crores, the profits computed under Section 80HHC(3) shall be increased by 90% of the sum referred to in Section 28(iiid). By the 3rd proviso it was provided that in the case of an assessee having an export turnover exceeding Rs.10 crores, the profits computed under Section 80HHC(3) shall be increased by 90% of the sum referred to in Section 28(iiid) subject to the two conditions set out therein.

28. Admittedly, in the assessment year in question, the assessee had an export turnover exceeding Rs.10 crores and did not fulfill the conditions set out in the third proviso to Section 80HHC(3), introduced by the Finance Act of 2005. As a result the assessee was not entitled to a deduction under Section 80HHC on the amount received on transfer of DEPB.

29. To get over this difficulty, the assessee contends that the

profits on transfer of DEPB in Section 28(iiid) would not include the face value of the DEPB so that the assessee gets a deduction under Section 80HHC on the face value of the DEPB. There is no merit in the above contention for the following reasons :

a) What is received on transfer of the DEPB credit is the profit, because DEPB credit under the DEPB scheme is given at a percentage of the FOB value of the exports, so as to neutralize the incidence of customs duty on the import content of the export product. The DEPB credit is also given to an exporter who has exported goods without importing raw materials required for the export. DEPB credit is given for paying customs duty on import of goods which may or may not be utilized in the export goods. When the DEPB credit is not utilized for paying customs duty but is transferred for any sum, then such sum would be profits on transfer of DEPB covered under Section 28(iiid);

b) Even the assessee has not disputed before the Court that the entire amount received on transfer of DEPB is business income chargeable to tax as profits of business. However, it is contended that the face value of the DEPB would not be covered under Section 28(iiid) because it is a credit earned by the assessee. Where the duty paid is received back as duty drawback it is also an amount earned by the assessee, but such a receipt is still considered as profits of business. Similarly, the amount realized on transfer of DEPB, be it equivalent to the face value of the DEPB; more than the face value of DEPB; or less than the face value of DEPB, would be profit on transfer of DEPB covered under Section 28(iiid);

c) The fact that the assessee had accounted for the DEPB credit immediately after making an application seeking DEPB credit would make no difference to the taxability of the entire amount received on transfer of the

DEPB credit under Section 28(iiid). What constitutes profits under Section 28(iiid) is the amount received on transfer of the DEPB credit and not the amount of credit which the assessee was entitled to under the DEPB scheme. In other words, the amount equivalent to the face value of DEPB as well as the amount received in excess of the DEPB would constitute profits of business under Section 28(iiid) and merely because, a part of such profits of business (face value) was offered to tax in the year in which the credit accrued to the assessee would not be a ground to hold that such profit was not covered under Section 28(iiid). Where the face value of the DEPB credit is offered to tax as business profits under Section 28(iiid) in the year in which the credit accrued to the assessee, then any further profit arising on transfer of DEPB credit would be taxed as profits of business under Section 28(iiid) in the year in which the transfer of DEPB credit took place. Therefore, the argument of the assessee that if the face value of the DEPB

credit is held to be covered under Section 28(iiid), it would amount to double taxation is without any merit.

30. There is another perspective from which the issue can be looked at. The DEPB credit to which an exporter is entitled is a form of an export incentive. The Supreme Court in **Ravindranathan Nair**'s case has held that all the incomes which fall within clauses (iiia) to (iiie) of Section 28 are 'incentive incomes'. As an incentive, that is made available to the exporter there is no cost that is attached to the grant of the incentive. The incentive, as we have already noted, is calculated as a percentage of the FOB value of the goods exported. The Tribunal in the present case recognized the difficulty in reducing the face value of the DEPB credit from the sale consideration when it observed, in paragraph 48 of its judgment, that "no doubt the exporter does not directly purchase the DEPB from the market by incurring any cost". Having so observed, the

Tribunal still considered it appropriate to hold that clause (iiid) would only refer to the difference between the sale consideration and the value of the DEPB credit. We find no basis or justification for the Tribunal to have done so.

31. We do not find any logical justification in bifurcating the value of the sale consideration realized by the exporter on the transfer of the DEPB credit. For one thing clause (iiid) of Section 28 must cover within its purview, the entirety of the sale consideration which is realized by the exporter on the transfer of the DEPB credit since that represents the profit which the exporter obtains on the transfer of the credit. No part of the credit that is available under the DEPB scheme can fall for classification under clause (iiib) of Section 28 which deals with cash assistance, received or receivable against any scheme of the Government of India. As the legislative history of the provision would show clause (iiib) was enacted by Parliament at a time when the export incentives that were available were (i) Import entitlement licences; (ii) Cash compensatory support; and (iii) Duty

drawback. The DEPB scheme was not even in existence when clause (iiib) came to be enacted into Section 28 by the Finance Act of 1990. The DEPB scheme was brought into existence with effect from 1 April 1997. Clause (iiid) of Section 28 was inserted by the Amending Act of 2005 with effect from 1 April 1998. The value of the DEPB credit can by no means be regarded as a cash assistance which is received or receivable by a person against exports under any scheme of the Government of India.

32. The Tribunal has relied to a considerable extent on a speech made by the then Finance Minister on the floor of Parliament in support of its conclusion that only the premium realized by an exporter on the sale of the DEPB credit would fall within the purview of clause (iiid) of Section 28 and not the face value of the DEPB. The entire approach of the Tribunal is with respect misconceived and unsustainable. The Finance Minister sought to introduce clause (iiid) in Section 28 in view of the decision of the Delhi Bench of the Tribunal in the case of **P & G Enterprises (**supra). The dispute in

that case related to taxing the entire amount received on the transfer of the DEPB credit and not the amount that was received in excess of the face value of the DEPB credit. As a matter of fact in that case the assessee had claimed that the entire receipt on the transfer of the DEPB credit including the face value of the credit as profits under Section 28(iiia). The Tribunal in that case held that the entirety of the amount would be covered by Section 28(iv). However, the view of the Tribunal was that since Explanation (baa) in Section 80HHC did not envisage the exclusion of profits covered by Section 28(iv), such profits could not be excluded while computing the deduction under Section 80HHC. Hence, there was no dispute in considering the entirety of the receipts on the transfer of the DEPB credit as profits of business. The dispute was only in not treating the receipts by way of transfer of the DEPB credit as export receipts while computing the deduction under Section 80HHC. Consequently, the entirety of the receipts on the transfer of the DEPB credit which was sought to be included in Section 28(iv) was brought in by the Parliamentary amendment in the form of an insertion of clause (iiid)

in Section 28 with retrospective effect. There was no controversy regarding the taxability of the quantum of receipts on the transfer of the DEPB credit. Hence, for these reasons we are of the view that it cannot be inferred from the speech of the Finance Minister that the insertion of clause (iiid) in Section 28 was made with a view to tax only the amount which has been received in excess of the face value of the DEPB credit.

33. The submission that prior to the insertion of clause (iiid) in Section 28, the face value of the DEPB credit realized on the transfer of such credit constituted export profits, but not the amount realized in excess of the face value of the DEPB is similarly without any basis. This is because (i) The object of DEPB was to furnish an incentive to exporters so as to adjust the credit against the customs duty payable on any goods imported into India. However, where an exporter instead of utilizing the credit transfers the credit at a premium, it cannot be said that the exporter has utilized the credit; (ii) The legislature considers that the customs duty and excise duty paid on

raw materials used in the export product, when repaid or repayable as duty drawback, would not constitute export profit. Similarly, when the DEPB credit is not utilized in the business but is transferred for value, the amount received on the transfer would be business profits and not export profits irrespective of whether the amount which is realized is equal to, larger than or less than the face value of the DEPB credit. Parliament has considered that the entirety of the amount received on the transfer of the DEPB shall constitute profits of business under Section 28(iiid). Since such profits are not export profits Parliament directed that ninety percent of those profits would be excluded while computing the deduction under Section 80HHC; (iii) Parliament considered that an exporter who instead of utilizing the DEPB credit for paying customs duty on imported goods, makes a profit by transferring the DEPB, would form a separate class and seeks to tax the receipts on the transfer of the DEPB credit as business profits and not export profits. Exporters who transfer the DEPB credit and make a profit cannot be placed on par with those exporters who utilize the credit for paying the customs duty on the imported goods;

(iv) The fact that Parliament did not consider the amount received on the transfer of the DEPB to be export profit cannot be a ground to hold that the receipts on the transfer of DEPB credit are not business profits. Counsel appearing on behalf of the assessee submits that the entire amount received on the transfer of the DEPB credit is business profit, but it was contended that what is included in Section 28(iiid) is the amount received on the transfer of the DEPB credit in excess of the face value of the DEPB and the amount received to the extent of the face value of the DEPB would be covered under Section 28(iiib). There is no merit in this contention because (a) the DEPB credit was not in existence when Section 28(iiib) was inserted by the Finance Act of 1990. DEPB credit was introduced with effect from 1 April 1997 which was after the insertion of clause (iiib) in Section 28; (b) Section 28(iiib) refers to cash assistance (by whatever name called) received by the assessee from the Government pursuant to a scheme of the Government. The amount received on the transfer of the DEPB credit is not received by the assessee from the Government pursuant to a scheme of the Government within the meaning of clause

(iiic) and (c) When Section 28(iiid) specifically deals with profits realized on the transfer of the DEPB credit, it would be impermissible as a matter of first principle to bifurcate the face value of the DEPB and the amount received in excess of the face value of the DEPB.

34. For all these reasons, we have come to the conclusion that the view of the Tribunal on the two questions of law formulated by the revenue is unsustainable. In the circumstances, we allow the appeal by answering the first question of law as formulated in the negative.

33. Insofar as the second question is concerned, we are not in agreement with the view of the Tribunal that the face value of the duty entitlement passbook realized on the transfer of the entitlement is chargeable to tax under Section 28(iiib). We have already clarified that the entirety of the sale consideration would fall within the purview of Section 28(iiid). We answer the second question of law accordingly in the aforesaid terms.

35. In view of the findings which have been recorded in this judgment, we remand the proceedings to the Assessing Officer to pass fresh orders having due regard to the questions of law which have been determined in this appeal. The Assessing Officer will furnish an opportunity of being heard to the assessee. All submissions on facts may be urged before the Assessing Officer and shall be considered in accordance with law. The Appeal is accordingly disposed of. In the circumstances of the case, there shall be no order as to costs.

(Dr. D.Y.Chandrachud, J.)

(J.P. Devadhar, J.)