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Dr.VKJ/ASBJ/BVJ:

30-10-2017 **ITA No.812/2007**

The Commissioner of Income Tax and Another

Vs.

M/s. Hewlett Packard Global Soft Ltd.

O R D E R

Mr. K.V. Aravind, Adv. for Appellants-Revenue
Mr.T. Suryanarayana, Adv. for Respondent-Assessee

BY THE Court

(Per Dr. Vineet Kothari J)

1. The following Questions have been referred on **10/04/2017** by the Division Bench of this Court for answer by Full Bench.

> *" (i) Whether in the facts and in the circumstances of the case, Tribunal was justified in holding that interest from Fixed Deposits, accrued interest on Fixed Deposits, interest received from Citibank, Hong kong and interest on staff loans should be treated*

as business income of the assessee even though the assessee is not carrying any banking/financial activity?

(ii) Whether the Assessing Officer was correct in holding that the interest income cannot be held to be derived from eligible business of the assessee (software development) for the purpose of claiming deduction under Section 10A of the Income Tax Act, 1961?"

2. The conflict of opinion of the Two Division Benches has resulted in the aforesaid Reference to the Full Bench. The earlier view was taken in favour of the assessee by the first Division Bench in **I.T.A.No.428/2007** ***(The Commissioner of Income Tax and Another Vs. M/s. Motorola India Electronics (P) Ltd.)*** on **11/12/2013.** The subsequent Division Bench taking a different view on **10/04/2014** in the present

I.T.A.No.812/2007 referred the aforesaid Questions of Law for consideration by the Full Bench.

3. The first Division Bench in its decision dated **11/12/2013** held that the Respondent - assessee, a 100% Export Oriented Unit (EOU) which is exporting Software like the Respondent - assessee in the present case was entitled to 100% deduction under Section 10-A of the Income Tax Act, 1961 ('**Act**' for short) in respect of the interest income earned by it during the relevant Assessment Year from **Exchange Earner's Foreign Currency (EEFC) Account** and the same would be construed as "Business Income of the assessee derived from the Undertaking" within the meaning of Section 10-A of the Act. The Division Bench held that the Profits of the business of the Undertaking includes the Profits and Gains from export of the articles as well as all other incidental incomes derived from the business of the Undertaking and what is exempted under Section 10-

A/10-B of the Act is not merely Profits and Gains from the export of articles but also the income from the business of the Undertaking.

4. The Division Bench held that the assessee – ***M/s. Motorola India Electronics (P) Limited*** was a 100% Export Oriented Unit which has exported Software and earned the income and a portion of that income is deposited in EEFC Account and yet another portion of the amount was invested within the country by way of Fixed Deposits and yet another portion was invested by way of loans to the sister concerns and on which the assessee derived interest or the consideration received from sale of Import Entitlements which was permissible in law and therefore the interest received and the consideration received by the sale of Import Entitlements was to be construed as income of the business of the Undertakings and the Division Bench held that there is a direct nexus between this income and the income of the business of the

Undertaking, though it does not partake the character of a Profit and Gains from the sale of articles but it is the income which is derived from the consideration realized from export of articles. The assessee was thus held entitled to 100% deduction for the Assessment Year 2001-02 under Section 10-A/10-B of the Act.

5. However, the subsequent Division Bench took a different view on **10/04/2014** in the present **I.T.A.No.812/2007** and relying upon certain Supreme Court decisions referred therein, held that the Undertaking/Assessee could have more sources of income other than the profits and gains as are derived by them from the export of articles or things or Computer Software and such Undertakings contemplated under Section 10-A(1) of the Act are entitled to seek benefit of deduction only in respect of the profit derived from export of articles or things or Computer Software.

6. The subsequent Division Bench further held that the expression "Total Turnover of the business carried on by the Undertaking" would mean only the turnover of the export business of the Undertaking and not any other activity from the Undertaking which earns profit, which could be a part of total income of the assessee. The Division Bench, therefore, proceeded to take a view that the Respondent assessee/Undertaking, **M/s. Hewlett Packard Globalsoft P.Ltd.** which invested its surplus funds in Banks and received interest thereon and also interest on the staff loans, such interest earned by the Undertaking/assessee had no direct nexus with the business of the Undertaking and in other words the business of the Undertaking as contemplated under Section 10-A of the Act is only the export of articles or things or Computer Software and interest on surplus amount in Bank deposit or loans to staff could not have

any nexus with the business of the Undertaking as contemplated under Section 10-A(4) of the Act.

7. The Division Bench, therefore, held that they were unable to agree with the view taken by the earlier Division Bench in the case of Respondent Assessee – **M/s. Motorola India Electronics (P) Ltd.(supra)** and thus the matter was required to be referred to the Full Bench for its opinion.

8. We have heard the learned counsels, Mr. K.V. Aravind for the Revenue and Mr. T. Suryanarayana for the Respondent - Assessee.

9. The Scheme of the Income Tax Act, 1961 is that the said Act is divided into XXIII Chapters, comprising of Section 1 to Section 298 and Fourteen Schedules to the Act. We are mainly concerned with **Chapter II** (Basis of Charge - Section 4 to Section 9-A); **Chapter III** (Incomes which do not form part of Total Income – Section 10 to

Section 13-B) **Chapter IV** (Computation of Total Income, providing for different Heads of Income - Part-D - Profits and Gains of Business or Profession – (Section 28 to Section 44DB) and **Chapter VI-A** (Deductions to be made in computing Total Income, **Part A** – General, comprising of Section 80-A to 80-B and **Part B** – Deductions in respect of certain payments, comprising of Section 80C to 80GGC and **Part C** – Deductions in respect of certain incomes – comprising of Section 80H to Section 80TT.

10. Out of this broad scheme of the Act, since the cited cases before us mostly pertain to **Part C** of **Chapter VI-A** which deals with the deductions to be made in computing Total Income under **Section 80-H, 80HH, 80HHC etc,** we would deal with these provisions when relevant case laws are discussed by us.

11. As against the **Chapter VI-A** relating to Deductions from Gross Total Income as provided in

Chapter VI-A of the Act, Section 10-A and 10-B contained in **Chapter III** of the Act provide for exemptions or 100% deduction in **Chapter III** which deals with "**Incomes which do not form part of the Total Income**" and **Section 10-A** deals with **"Special provisions in respect of the newly established Undertakings in Free Trade Zone, etc.(FTZ)"** and **Section 10-AA** deals with "**Special provisions in respect of newly established Units in Special Economic Zones (SEZs)**" and **Section 10-B** deals with "**Special provisions** in respect of newly established **100% Export Oriented Units (100% E.O.Us)".**

12. Before coming to the crux of the controversy, let us have a look at the brief factual background of the Respondent assessee for the Assessment Year 2001-02 in question.

13. The Respondent assessee during the relevant year operated four Units set up under the Scheme formulated by the Government in the name of Software Technology Parks of India **(STPI)** for 100% Export of the Computer Software Units. The Government of India to promote the fast growing Industry of Software and Software Technology in our country, made a special provision for providing incentive in the form of Tax Exemption by inserting Section 10-A in **Chapter III** of the Act which provision is quoted herein below and the same provided for a 100% deduction of Profits and Gains derived by an Undertaking from the export of articles or things or Computer Software for a period of ten consecutive Assessment Years from the beginning of its setting up, if such Undertaking begins to manufacture or produce such Articles or things or Computer Software in its Export Undertaking. The said provision was substituted by Finance Act, 2000, with effect from

01/04/2001 in place of the earlier Section 10-A, which was inserted by Finance Act, 1981.

14. Section 10-B of the Act was also substituted by the Finance Act, 2000, with effect from **01/04/2001** in place of earlier provisions of Section 10-B of the Act inserted by Finance Act, 1988 with effect from **01/04/1989** and it provided for such 100% deduction of profits and gains derived by a 100% Export Oriented Undertaking set up in specified Zones like STPI etc. from the export of articles or things or Computer Software for a period of Ten consecutive Assessment Years, beginning with the Assessment Year relevant to the previous year in which the Undertaking begins to manufacture or produce such Articles.

15. There is no dispute of facts before us as found by the Income Tax Tribunal with the Respondent – assessee, as a 100% Export Oriented Unit had four Units

set up in the Software Technology Park of India (STPI) Scheme and it had no other Units from which it carried on any other activity other than the 100% export of Software projects during the Assessment Year 2001-02 under consideration.

16. The assessee earned during the said Assessment Year 2001-02, interest income of `4,68,037/- on the Short Term Deposits made by it to the tune of `6,46,88,606/- out of its Surplus Funds temporarily parked in the Current Account held in Citi Bank, Hong Kong and also earned interest of `6,02,309/- from the Advances of loans to its staff members. The deduction in respect of both the said interest income was claimed as a 100% deduction under Section 10-A of the Act during the said relevant year as income from "Profits and Gains" of export business. But, the Assessing Authority under the Act held that such interest income was not entitled to

100% deduction under Section 10-A of the Act, but such interest income was taxable under Section 56 of the Act, as 'Income from Other Sources' and that is the bone of contention between the assessee and the Revenue before us.

17. The learned counsel for the Revenue, Mr. Aravind relying upon the following judgments under Sections 80-HH, 80-HHC and 80-I of the Act which scheme of Deductions under **Chapter VI-A** of the Act is different from the scheme of Exemptions from tax under Sections 10-A and 10-B in **Chapter III** of the Act, submitted that the interest income derived by the Respondent assessee cannot be said to be "Profits and Gains" as derived by an Undertaking from the export of articles and therefore such interest income earned from Banks and staff loans has to be taxed under Section 56 of the Act as "Income from other Sources" and 100%

deduction treating them as "profits and gains of business" is not allowable under 80-A of the Act.

18. The relevant extracts of the judgments mainly relied upon by the learned counsel for the Revenue are quoted below for ready reference.

19. ***In Pandian Chemicals Ltd. Vs. Commissioner of Income Tax [(2003, 262 ITR. 278 (SC)],*** the Hon'ble Supreme Court dealing with a controversy with regard to interest on deposits with Electricity Board held that the same could not be treated as 'Profits and Gains derived from Industrial Undertaking" for the purposes of Section 80-HH of the Act. The relevant paragraphs 4 and 6 of the judgment are quoted below for ready reference.

> *"4. Section 80HH of Income Tax Act grants deduction in respect of profits and gains "**derived from**" an industrial undertaking. The contention of the appellant before us is that*

interest earned on the deposit made with the Electricity Board (assessee) for the supply of electricity to the appellants industrial undertaking should be treated as income derived from the industrial undertaking within the meaning of section 80HH. It is submitted that without the supply of electricity the industrial undertaking could not run and since electricity was an essential requirement of the industrial undertaking, the industrial undertaking could not survive without it. It is further pointed out that for the purpose of getting this essential input, the ***statutory requirement was that the deposit must be made*** *as a precondition for the supply of electricity. Consequently, according to the appellant,* ***the interest on the deposit should be treated as income derived from the industrial undertaking*** *within the meaning of section 80HH.*

5……

*6. The word "**derived**" has been construed as far back in 1948 by the **Privy Council** in CIT*

v. Raja Bahadur Kamakhaya Narayan Singh (1948) 16 ITR 325 (PC) when it said :

> *"The word derived is not a term of art. Its use in the definition indeed demands an enquiry into the genealogy of the product. But the enquiry should stop as soon as the effective source is discovered. In the genealogical tree of the interest land indeed appears in the second degree, but the immediate and effective source is rent, which has suffered the accident of non-payment. And rent is not land within the meaning of the definition."*

This definition was approved and reiterated in 1955 by a ***Constitution Bench*** *of this Court in the decision of Mrs. Bacha F. Guzdar Vs. CIT (1955) 27 ITR 1 (SC). It is clear, therefore, that the words 'derived from' is s.80HH of the IT Act, 1961 must be understood as something* ***which has direct or immediate nexus*** *with the appellant's industrial undertaking. Although electricity may be required for the*

purposes of the industrial undertaking, the deposit required for its supply is a step removed from the business of the industrial undertaking. The derivation of profits on the deposit made with Electricity Board cannot be said to flow directly from the industrial undertaking itself."

20. In ***Liberty India Vs. Commissioner of Income Tax [(2009) 317 ITR 218],*** the Hon'ble Supreme Court dealing with the controversy of profit from Duty Exemption Payback Scheme (DEPB), Duty drawback incentives dealing with deduction under 80-IB of the Act held that the profit derived on sale of such DEPB and Duty draw back Entitlements by the assessee could not be said to be Profits and Gains "derived from" which are "ancillary" as compared with the words "attributable to" and therefore such profits on sale of DEPB/Duty drawback Entitlements was not deductible under Section 80-IB of the Act. The relevant discussion as found in

paragraph 16 of the judgment is quoted below for ready reference.

> *"16. **DEPB is an incentive**. It is given under Duty Exemption/Remission Scheme. **Essentially, it is an export incentive.** No doubt, the object behind DEPB is **to neutralize the incidence of customs duty payment** on the import content of export product. This neutralization is provided for by credit to customs duty against export product. Under DEPB, an exporter may apply for credit as percentage of FOB value of exports made in freely convertible currency. Credit is available only against the export product and at rates specified by DGFT for import of raw materials, components etc. DEPB credit under the Scheme has to be calculated by taking into account the deemed import content of the export product as per basic customs duty and special additional duty payable on such deemed imports. Therefore, in our view, DEPB/duty drawback are incentives which flow from the Schemes framed by Central*

Government or from s. 75 of the Customs Act, 1962, ***hence, incentive profits are not profits derived from the eligible business under*** *S.80-IB. They belong to the category of ancillary profits of such undertakings."*

21. Likewise, in ***Commissioner of Income Tax Vs. Sterling Foods [(1999) 237 ITR 579]*** again the Hon'ble Supreme Court in a case arising under Section 80-HH of the Act held that the nexus between the sale consideration of Import Entitlements and the Industrial Undertakings was not direct but only incidental and therefore the same would not constitute "profits and gains" derived from assessee's Industrial Undertaking for the purpose of computing deduction under Section 80-HH of the Act. The observations made in paragraph 9 of the judgment are quoted below:

"9. We do not think the source of the import entitlements can be said to be the

industrial undertaking of the assessee. The source of the import entitlements can in the circumstances, only be said to be the export promotion scheme of the Central Government whereunder the export entitlements become available. There must be, for the application of the words "derived from", a direct nexus between the profits and gains and the industrial undertaking. In the instant case the nexus is not direct but only incidental. The industrial undertaking exports processed sea food. By reason of such export, the export promotion scheme applies. Thereunder, the assessee is entitled to import entitlements, which it can sell. The sale consideration therefrom cannot, in our view, be held to constitute a profit and gain derived from the assessee's industrial undertaking."

22. In ***Totgars Co-operative Sale Society Ltd. Vs. Income Tax Officer [(2010) 322 ITR 283]***, which judgment was relied upon by the Division Bench of this Court for

the later years also while deciding ***I.T.A. No.100066/2016 (Principal CIT Vs. The Totagar's Co-operative Societies Sales Ltd. Sirsi, Karnataka)*** on **16/06/2017,** the Hon'ble Supreme Court held that the profits and gains of business attributable to one of the activities specified in Section 80-P(2)(a) of the Act which gave 100% deduction from tax to the Co-operative Societies engaged in specified types of activities did not include the interest earned by it by investing Surplus Funds in Short Term Deposits and Government Securities which would be taxable under Section 56 of the Act as "Income from other Sources". The relevant extract of the Supreme Court judgment is quoted below for ready reference.

> *"To say that the source of income is not relevant for deciding the applicability of s.80P would not be correct because weightage has to be given to the words "the whole of the amount of profits and gains of business" attributable to one of the activities*

specified in s.80P(2)(a). An important point needs to be mentioned. The words "the whole of the amount of profits and gains of business" emphasise that the income in respect of which deduction is sought ***must constitute the operational income and not the other income*** *which accrues to the society. In this particular case, the evidence shows that the assessee-society earns interest on funds which are not required for business purposes at the given point of time. Therefore, on the facts and circumstances of this case, such interest income falls in the category of "other income" which has been rightly taxed by the Department under s.56.- The Totgars Co-operative Sale Society Ltd. vs. ITO (2010) 228 CTR (Kar) 526 affirmed.*

Assessee, a co-operative society, being engaged in providing credit facilities to its members and marketing the agricultural produce of the members, interest earned by it by investing surplus funds in short-term deposits and Government securities fell

under the head "Income from other sources" taxable under s.56 and ***it cannot be said to be attributable to the activities of the society*** *and, therefore, the interest income did not qualify for deduction under s.80P(2)(a)(i)."*

23. The Division Bench following the aforesaid judgment later again held that the said judgment of the Hon'ble Supreme Court will apply to the same Assessee even for subsequent assessment years despite the amendment in law and even if the interest income was earned by the assessee Co-operative Society from the deposits made with the Co operative Banks and not with the other Scheduled or Nationalized Banks as was done in the earlier years involved before the Hon'ble Supreme Court and such 100% deduction would not be available to the assessee Society even with reference to Section 80-

P(2)(a) or (d) of the Act for those subsequent assessment years as well.

24. Before adverting to the judgments cited by the learned counsel for the Respondent assessee and his contentions in brief, let us extract the relevant portion of the Section 10-A applicable in the facts and circumstances of the present case to its relevant extent herein below.

> ***10A [Special provision in respect of newly established undertakings in free trade zone, etc.***
>
> ***10A. (1)*** *Subject to the provisions of this section, a deduction of such profits and gains as are* ***derived by an undertaking*** *from the export of articles or things or computer software for a period of ten consecutive assessment years beginning with the assessment year relevant to the previous year in which the undertaking begins to*

manufacture or produce such articles or things or ***computer software,*** *as the case may be, shall be allowed from the total income of the assessee:*

....

....

10-A(2) *This section applies to any undertaking which fulfils all the following conditions, namely:-*

(i) it has begun or begins to manufacture or produce articles or things or computer software during the previous year relevant to the assessment year-

(a) commencing on or after the 1st day of April, 1981, in any free trade zone; or

(b) commencing on or after the 1st day of April, 1994, ***in any electronic hardware technology park,*** *or, as the case may be,* ***software technology park;***

(c) commencing on or after the 1st day of April, 2001 in ***any special economic zone;***

(ii) it is not formed by the splitting up, or the reconstruction, of a business already in existence:

Provided that this condition shall not apply in respect of any undertaking which is formed as a result of the re-establishment, reconstruction or revival by the assessee of the business of any such undertakings as is referred to in section 33B, in the circumstances and within the period specified in that section;

(iii) it is not formed by the transfer to a new business of machinery or plant previously used for any purpose.

…….

10-A(4) *For the purposes of [sub-section (1) and (1A)],* ***the profits derived from 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."

25. The learned counsel for the Respondent assessee, Mr.T. Suryanarayana submitted that the entire profits and gains of the Undertaking of the Respondent assessee who was exclusively engaged in the business of manufacture and export of Software Programmes and projects was entitled to exemption or 100% deduction under Section 10-A of the Act as the entire income earned by such Undertaking including the interest earned from Banks and staff loans which was just incidental to the normal business activity of export of software and such interest would also therefore constitute part of the profits and gains of the Undertaking and would be entitled to such exemption.

26. The learned counsel for the Respondent assessee also urged that in fact, the question of applying the formula under Section 10-A(4) for giving proportionate deduction would not arise in such circumstances where the assessee was engaged wholly in 100% export of its Software Programmes and would not apply to exclude such exemption in respect of the interest income because the interest income of the Undertaking does not form part of 'Total Turnover of the assessee' in contra-distinction with 'export turnover of the assessee' because the assessee is engaged in 100% export of articles and the assessee admittedly satisfies all other relevant conditions for applicability of Section 10-A of the Act to the respondent assessee.

27. He submitted that the judgment of the Division Bench in the case of **M/s. Motorola India Electronics (P) Ltd.(supra)** of this Court which has been differed with by

the subsequent Division Bench giving rise to the present Reference to the Full Bench gives the correct interpretation of Section 10-A/10-B of the Act and the same has been consistently followed at later stages by the other High Courts.

28. The learned counsel for the Respondent assessee relied upon the following decisions in this regard.

29. In ***Riviera Home Furnishing vs. Additional Commissioner of Income Tax, Range 15 [(2016) 65 Taxmann.com 287(Delhi)]***, the Division Bench of Delhi High Court dealing with a case of Export Oriented Undertaking, for the Assessment Year 2008-09, in respect of interest received by an assessee on Fixed Deposit Receipts (FDRs.) which were under lien with Bank for facilitating Letter of Credit and Bank Guarantee

facilities held that such interest received on FDRs would qualify for deduction under Section 10-B of the Act. The relevant paragraphs 9 and 15 of the said decision are quoted below.

> ***"****9. The question as to what can constitute as profits and gains derived by a* ***100% EOU from the export of articles and computer software*** *came for consideration before the Karnataka High Court in CIT v. Motorola India Electronics Pvt. Ltd. (2014) 46 Taxmann.com 167 (Kar). The said appeal before the Karnataka High Court was by the Revenue challenging an order passed by the ITAT which held that the interest payable on FDRs was part of the profits of the business of the undertaking and therefore includible in the income eligible for deduction Sections 10A and 10B of the Act. There the Assessee had earned interest on the deposits lying in the EEFC account as well as interest earned on inter-corporate loans given to sister concerns out of the funds of the undertaking. There was*

a restriction on the Assessee in that case from making pre-payment of its external commercial borrowings ('ECB'). It could repay only to the extent of 10% of the outstanding loan in a year. This made the Assessee ***temporarily park the balance funds as deposits or with various sister concerns as inter corporate deposits*** *until the date of repayment. The Assessee contended that the interest derived from the business of the industrial undertaking was eligible for exemption within the meaning of Section 10B and applied the formula under Section 10B(4) of the Act for determining the profits from exports. The Assessee's contention that the expression* ***"profits of the business of the undertaking"*** *in Section 10B(4) was wider than the expression* ***"profits and gains derived by"*** *the Assessee from a 100% EOU occurring in Section 10B(1) was accepted by the ITAT.* ***The ITAT noticed that unlike Section 80 HHC,*** *where there was an express exclusion of the interest earned from the 'profits of business of undertaking',* ***there***

was no similar provision as far as Sections 10A and 10B were concerned.

15. In the considered view of the Court, the submissions made on behalf of the ***Revenue proceed on the basic misconception regarding the true purport of the provisions of Chapter VIA*** *of the Act and on an incorrect understanding of Section 80A(4) of the Act. The opening words of Section 80A(4) read* ***"Notwithstanding anything to the contrary contained in section 10A or section 10AA or section 10B or section 10BA*** *or in any provisions of this Chapter…..". What is sought to be underscored, therefore, is that* ***Section 80A, and the other provisions in Chapter VIA, are independent of Sections 10A and 10B of the Act****. It appears that the object of Section 80A(4) was to ensure that a unit which has availed of the benefit under Section 10B will not be allowed to further claim relief under Section 80IA or 80IB read with Section*

80A(4). The intention does not appear to be to deny relief under Section 10B(1) read with Section 10B(4) or ***to whittle down the ambit of those provisions*** *as is sought to be suggested by Mr. Manchanda. Also, he is not right in contending that the decisions of the High Courts referred to above have not noticed the decision of the* ***Supreme Court in Liberty India. The Karnataka High Court in CIT v. Motorola India Electronics Pvt. Ltd. (supra) makes a reference to the said decision****. That decision of the Karnataka High Court has been cited with approval by this Court in Hritnik Exports (supra) and Universal Precision Screws (supra). In Hritnik Exports (supra) the Court quoted with approval the observations of the Special Bench of the ITAT in Maral Overseas Ltd. (supra) that* ***"Section 10A/10B of the Act is a complete code providing the mechanism for computing the 'profits of the business' eligible for deduction u/s 10B of the Act.*** *Once an income forms part of the business of the income of the eligible*

undertaking of the assessee, ***the same cannot be excluded from the eligible profits for the purpose of computing deduction u/s 10B of the Act."***

30. The said judgment, in our opinion, rightly distinguishes the judgments on the interpretation of Section 80-HH, 80-IA etc. under **Chapter VI-A** of the Act in view of Section 80-A (4) of the Act which, with a non-obstante clause which starts with "Notwithstanding anything to the contrary contained in Section 10-A or Section 10-AA or Section 10-B or Section 10-BA or in any provisions of this Chapter" proceeds to enumerate the various deductions under **Chapter VI-A** of the Act.

31. Similarly the Division Bench of the Calcutta High Court in ***Commissioner of Income Tax, Kolkata-IV Vs. Hindustan Gum & Chemicals Ltd. [(2016) 72 Taxmann.com.90(Calcutta)]*** again held that interest earned on Surplus Business Funds deposited with Banks

for short periods will be part of profits of business for the purposes of Section 10-B of the Act. The relevant portion of the judgment in para.3 relied upon in the decision of the Division Bench of this Court in the case of **M/s. Motorola India Electronics (P) Ltd.(supra)** is quoted below for ready reference.

> **"***3. A bare reading of sub-section (1) suggests that 100 % export oriented undertakings are entitled to a deduction of profits and gains derived from the export of articles for a period of 10 years. The aforesaid entitlement is, however, subject to the provisions of Section 10B. In other words, subject to the provisions contained in the other parts of the Section 10B, the benefit is available to an assessee. It was not disputed that the only relevant provision to be taken into account is sub-section (4) which we already have quoted. Sub-section (4) provides the quantum of deduction which can be availed by an assessee.* ***The quantum of deduction is***

dependent upon the total turnover of the business of the undertaking and the export turnover of the undertaking. *Once these two figures are available, one has to divide the total turnover by the export turnover in order to work out the percentage of the export turn over, vis-à-vis the total turn over. Suppose total turn over is Rs.100/- and total export turn over is for Rs.10/-, then the export turn over is 10 % of the total turnover. Then one has to find out the total profit of the business of the undertaking. Suppose the total profit of the business of the undertaking is Rs.100, in that case, deduction available to the assessee under Section 10 sub-section (1) of Section 10B shall be 10% of Rs.100, i.e. to say Rs.10/-. This is the formula which has been provided by subsection (4) for the purpose of working out the benefit or deduction under subsection (1). Total turnover shall naturally include receipt on account of interest. The legislature does not appear to have provided for excluding the amount of interest from the total turnover as has been done in the case of 80HHC by*

explanation (baa) of sub-section (4C) thereof. ***In that case, 90% of the income arising out of interest has to be excluded from the profits of the business for the purpose of arriving at deduction available under Section 80HHC. But an identical provision is not there. Therefore, that provision cannot be imported by implication.*** *The submission that the amount earned from interest was not intended to be taken into account for the purpose of giving benefit under subsection (1) of Section 10B may be correct. But the amount of deduction available to a 100% export oriented undertaking is necessarily dependent upon the formula provided in subsection (4). There is, as such, no scope for any controversy that part of the money was earned from interest and not from export. This question came up before the Karnataka High Court and was answered in the case of* ***CIT v. Motorola India Electronics (P.) Ltd. [2014] 46 taxmann.com 167/225 Taxman 11 (Kar.)(Mag.)*** *as follows:*

"In the instant case, the assessee is a 100% EOU, which has exported software and earned the income. A portion of that income is included in EEFC account. Yet another portion of the amount is invested within the country by way of fixed deposits, another portion of the amount is invested by way of loan to sister concern which is deriving interest or the consideration received from sale of the import entitlement, which is permissible in law. Now the question is whether the interest received and the consideration received by sale of import entitlements is to be construed as income of the business of the undertaking. There is a direct nexus between this income and the income of the business of the undertaking. Though it does not partake the character of a profits and gains from the sale of an article, it is the income which is derived from the consideration realized by export of articles. In view of the definition of income from Profits and

Gains incorporated in Sub-section (4), the assessee is entitled to the benefit of exemption of the said amount as contemplated under Section 10B of the Act. Therefore, the Tribunal was justified in extending the benefit to the aforesaid amounts also. We do not find any merit in these appeals. Therefore, the first substantial question of law raised in ITA No.428/2007 is answered in favour of the revenue and against the assessee and the first substantial question of law in ITA No.447/2007 is answered in favour of the assessee and against the revenue.

In the light of the aforesaid findings, the second question of law in both the appeals do not arise for consideration."

32. The Division Bench of Bombay High Court in ***Commissioner of Income Tax-IV Vs. Symantee Software India (P) Ltd. [MANU/MH/2575/2014]*** rightly held, in our opinion, that the provisions of **Chapter VI-A** in the

context of 'Deductions' cannot be allowed to be telescoped in Section 10-A and the deduction under Section 10-A has to be given effect to at the prior stage of computing the profits and gains of the business, whereas **Chapter VI-A** comes in for application after the Gross Total Income is determined by adding the income under various independent Heads of Income in **Chapter IV** comprising of Sections 14 to 59 of the Act.

33. The relevant extract from paragraphs 19 to 21 of Bombay High Court decision is also quoted below for ready reference.

> *"19. There is some substance in the contention of Mr. Kaka that if the deduction shall be allowed from the total income of the Assessee in the manner set out by section 10A and the computation is also provided in that provision itself namely sub-section (4), then there is a complete Code which is evolved and formulated by the Legislature.*

20. In relation to this, we also find support in the ***judgment of this Court in the case of Black and Veatch Consulting Pvt. Ltd.*** *This Court has observed and held as under:*

> *"Section 10A is a provision which is in the nature of a deduction and not an exemption. This was emphasized in a judgment of a Division Bench of this Court, while construing the provisions of Section 10B, in Hindustan Unilever Ltd. Vs. Deputy Commissioner of Income Tax MANU/MH/0417/2010: [2010] 325 ITR 102 (Bom) at paragraph 24. The submission of the Revenue placed its reliance on the literal reading of Section 10A under which a deduction of such profits and gains as are derived by an undertaking from the export of articles or things or computer software for a period of ten consecutive assessment years is to be allowed from the total income of the assessee. The deduction* ***under***

Section 10A, in our view, has to be given effect to at the stage of computing the profits and gains of business. This is anterior to the application of the provisions of Section *72 which deals with the carry forward and set off of business losses.* ***A distinction has been made by the Legislature while incorporating the provisions of Chapter VI-A.*** *Section 80A(1) stipulates that in computing the total income of an assessee, there shall be allowed from his gross total income, in accordance with and subject to the provisions of the Chapter, the deductions specified in Sections 80C to 80U. Section 80B(5) defines for the purposes of Chapter VIA "gross total income" to mean the total income computed in accordance with the provisions of the Act, before making any deduction under the Chapter.* ***What the Revenue in essence seeks to attain is to telescope the provisions of Chapter***

VI-A in the context of the deduction which is allowable under Section 10A, which would not be permissible unless a specific statutory provision to that effect were to be made. *In the absence thereof, such an approach cannot be accepted. In the circumstances, the decision of the Tribunal would have to be affirmed since it is plain and evident that the deduction under Section 10A has to be given at the stage when the profits and gains of business are computed in the first instance."*

21. Therefore, when this Court has held that Chapter VIA provides for deduction to be made in computing the total income and section 80HH deals with deduction in respect of profit and gains from the newly established undertaking or Hotel business in backward areas, then the attempt of the Revenue to telescope Chapter VIA in the context of the deduction, which is permissible under section

10A falling in Chapter III, cannot be countenanced."

34. We are of the considered opinion that the above referred decisions relied upon by the learned counsel for the Revenue, Mr. Aravind do not cover the cases under Sections 10-A and 10-B of the Act which are special provisions and complete code in themselves and deal with profits and gains derived by the assessee of a special nature and character like 100% Export Oriented Units (EOUs.) situated in Special Economic Zones (SEZs), STPI, etc., where the entire profits and gains of the entire Undertaking making 100% exports of articles including software as is the fact in the present case, the assessee is given 100% deduction of profit and gains of such export business and therefore incidental income of such undertaking by way of interest on the temporarily parked funds in Banks or even interest on staff loans would

constitute part of profits and gains of such special Undertakings and these cases cannot be compared with deductions under Sections 80-HH or 80-IB in **Chapter VI-A** of the Act where an assessee dealing with several activities or commodities may *inter alia* earn profits and gains from the specified activity and therefore in those cases, the Hon'ble Supreme Court has held that the interest income would not be the income "derived from" such Undertakings doing such special business activity.

35. The Scheme of Deductions under Chapter VI-A in Sections 80-HH, 80-HHC, 80-IB, etc from the 'Gross Total Income of the Undertaking', which may arise from different specified activities in these provisions and other incomes may exclude interest income from the ambit of Deductions under these provisions, but exemption under Section 10-A and 10-B of the Act encompasses the entire income derived from the business of export of such eligible Undertakings including interest income derived

from the temporary parking of funds by such Undertakings in Banks or even Staff loans. The dedicated nature of business or their special geographical locations in STPI or SEZs. etc. makes them a special category of assessees entitled to the incentive in the form of 100% Deduction under Section 10-A or 10-B of the Act, rather than it being a special character of income entitled to Deduction from Gross Total Income under Chapter VI-A under Section 80-HH, etc. The computation of income entitled to exemption under Section 10-A or 10-B of the Act is done at the prior stage of computation of Income from Profits and Gains of Business as per Sections 28 to 44 under Part-D of **Chapter IV** before 'Gross Total Income' as defined under Section 80-B(5) is computed and after which the consideration of various Deductions under **Chapter VI-A** in Section 80HH etc. comes into picture. Therefore analogy of Chapter VI Deductions cannot be telescoped or imported in Section 10-A or 10-

B of the Act. The words 'derived by an Undertaking' in Section 10-A or 10-B are different from 'derived from' employed in Section 80-HH etc. Therefore all Profits and Gains of the Undertaking including the incidental income by way of interest on Bank Deposits or Staff loans would be entitled to 100% exemption or deduction under Section 10-A and 10-B of the Act. Such interest income arises in the ordinary course of export business of the Undertaking even though not as a direct result of export but from the Bank Deposits etc., and is therefore eligible for 100% deduction.

36. We have to take a purposive interpretation of the Scheme of the Act for the exemption under Section 10-A/10-B of the Act and for the object of granting such incentive to the special class of assessees selected by the Parliament, the play-in-the-joints is allowed to the Legislature and the liberal interpretation of the

exemption provisions to make a purposive interpretation, was also propounded by Hon'ble Supreme Court in the following cases:-

I] In *Bajaj Tempo Ltd., Bombay Vs. Commissioner of Income Tax, Bombay, [(1992) 3 SCC 78],* the Hon'ble Supreme Court held that:-

> ***"5.*** *... ..Since a* ***provision intended for promoting economic growth has to be interpreted liberally, the restriction on it, too, has to be construed so as to advance the objective of the section and not to frustrate it.*** *But that turned out to be the, unintended, consequence of construing the clause literally, as was done by the High Court for which it cannot be blamed, as the provision is susceptible of such construction if the purpose behind its enactment, the objective it sought to achieve and the mischief it intended to control is lost sight of. One way of reading it is that the clause excludes any undertaking formed by transfer to it of any building, plant or*

machinery used previously in any other business. No objection could have been taken to such reading but when the result of reading in such plain and simple manner is analysed then it appears that ***literal construction would not be proper. ...”***

II] In R.K. Garg v. Union of India, [(1981) 4 SCC 675] = [1982 SCC (Tax) 30 p.690], the Hon’ble Apex Court has held as under:-

“8. *Another rule of equal importance is that* ***laws relating to economic activities should be viewed with greater latitude than laws touching civil rights*** *such as freedom of speech, religion etc. It has been said by no less a person than* ***Holmes, J.****, that the legislature should be allowed some* ***play in the joints, because it has to deal with complex problems*** *which do not admit of solution through any* ***doctrinaire or strait-jacket formula*** *and this is particularly true in case of legislation*

dealing with economic matters, where, having regard to the nature of the problems required to be dealt with, greater play in the joints has to be allowed to the legislature. The court should feel more inclined to give judicial deference to legislative judgment in the field of economic regulation than in other areas where fundamental human rights are involved. Nowhere has this admonition been more felicitously expressed than in ***Morey v. Doud [351 US 457 : 1 L Ed 2d 1485 (1957)]*** *where* ***Frankfurter, J.****, said in his inimitable style:*

> *"In the utilities, tax and economic regulation cases, there are good reasons for judicial self-restraint if not judicial deference to legislative judgment. The legislature after all has the affirmative responsibility. The courts have only the power to destroy, not to reconstruct. When these are added to the complexity of economic regulation, the uncertainty, the liability to error, the bewildering conflict of the experts, and the number of*

times the judges have been overruled by events — self-limitation can be seen to be the path to judicial wisdom and institutional prestige and stability."

The Court must always remember that "legislation is directed to practical problems, that the economic mechanism is highly sensitive and complex, that many problems are singular and contingent, that laws are not abstract propositions and do not relate to abstract units and are not to be measured by abstract symmetry"; "that exact wisdom and nice adaption of remedy are not always possible" and that "judgment is largely a prophecy based on meagre and uninterpreted experience". Every legislation particularly in economic matters is essentially empiric and it is based on experimentation or what one may call trial and error method and therefore it cannot provide for all possible situations or anticipate all possible abuses. There may be crudities and inequities in complicated experimental economic legislation but on that

account alone it cannot be struck down as invalid."

37. On the above legal position discussed by us, we are of the opinion that the Respondent assessee was entitled to 100% exemption or deduction under Section 10-A of the Act in respect of the interest income earned by it on the deposits made by it with the Banks in the ordinary course of its business and also interest earned by it from the staff loans and such interest income would not be taxable as 'Income from other Sources' under Section 56 of the Act. The incidental activity of parking of Surplus Funds with the Banks or advancing of staff loans by such special category of assessees covered under Section 10-A or 10-B of the Act is integral part of their export business activity and a business decision taken in view of the commercial expediency and the interest income earned incidentally cannot be de-linked from its profits and gains derived by the Undertaking

engaged in the export of Articles as envisaged under Section 10-A or Section 10-B of the Act and cannot be taxed separately under Section 56 of the Act.

38. We therefore affirm and agree with the view expressed by the first Division Bench of this Court in the case of **M/s. Motorola India Electronics (P) Ltd.(supra)** and we do not agree with the view taken by the subsequent Division Bench on **10/04/2014** in the present case.

39. Both the questions thus framed above are answered in favour of the Respondent Assessee and against the Revenue in the terms indicated above and the matter is sent back to the Division Bench for deciding this Appeal in accordance with the aforesaid opinion.

(Dr.VINEET KOTHARI)
JUDGE

(A.S. BOPANNA)
JUDGE

(B. VEERAPPA)
JUDGE

BMV*