IN THE INCOME TAX APPELLATE TRIBUNAL,
MUMBAI BENCH 'E', MUMBAI

Before Shri D.K. Agarwal, J.M. and Shri T.R. Sood, A.M.

I.T.A. No.1924/Mum/08
Assessment Year : 2005-06

M/s. Tricom India Limited, Tricom House, Gandhi Estate, Andheri Kurla Road, Safed Pool, Andheri East, Mumbai 400 072. PAN: AAACT 2807 R	**Vs.**	Asst. Commissioner of Income-tax, Central Circle 41, Mumbai.
(Appellant)		(Respondent)

Appellant by : Shri Vijay Mehta

Respondent by : Shri Jagadish

O R D E R

Per T. R. Sood (AM):

In this appeal assessee has raised the following ground:

"On the facts and circumstances of the case and in law, the learned CIT(A) Mumbai, erred in confirming the disallowance of Rs. 61,45,377/- made by the Assessing Officer on account of appellant's claim u/s.10B of the I.T.Act."

2. Brief facts of the case are that the assessee was engaged in the business of providing I.T. (Information Technology) enabled services and BPO transactions processing and had claimed deduction u/s.10B of the Income0tax Act, 1961 amounting to Rs.5,43,83,495/- . Upon examination of details of profits, it was found that profit declared by the assessee included the following items:

(i) Interest	..	Rs.57,36,314/-
(ii) Interest on F.D.	..	Rs. 1,10,874/-
(iii) Misc. Income	..	Rs. 2,98,189/-

		Rs. 61,45,377/-
		=========

The Assessing Officer was of the opinion that under Section 10B(1), deduction was allowable only on profits derived from export of articles or things or computer software. Therefore, no deduction was possible on the above noted items on interest income. On enquiry it was submitted that assessee was having several

units in various Software Technology Part (S.T.P.), therefore, satisfied the conditions of section 10B. These units generated surplus funds which were deposited in short term deposits with the banks etc. It was submitted that the company was treating interest income etc. as business profit and therefore deduction u/s.10B should be allowed in this respect also. Reliance was placed on the decision of the Hon'ble Madras High Court in the case of CIT vs. N.S.C. Shoes(258 ITR 749) and CIT v. Punit Commercial (245 ITR 550). A.O. did not find any force in this submission and held that Hon'ble Supreme Court has clearly held that in the case of CIT vs. Sterling Foods (237 ITR 579) that whenever the expression derived from was used then only profits derived from such undertakings could be made eligible for the purpose of various deductions. Ultimately he held that taxable income as per return at 'Nil' but added a sum of Rs. 61,45,377/- to the business income on account of denial of deduction u/s.10B.

3. Before the learned CIT(A), similar submissions were reiterated and further reliance was placed on the decision of the Bangalore Bench of the Tribunal in the case of CIT v. Himmat Singika Seida. Learned CIT(A) did not find force in the submission and decided the issue against the assessee vide para 2.3 and 2.4 which are as under:

> "I *have examined the facts and considered the contentions of the appellant. Section 10B of the Act contains special provisions in respect of newly established 100% export-oriented undertakings. Sub-section (4) of section 10B provides as overleaf:*
>
> *"10B special provisions in respect of newly established hundred percent export-oriented undertakings.*
>
> *(1) .....*
> *(2)....*
> *(3).....*
> *4. For the purposes of sub-section (1), 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 proportions 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.*

2.4 Therefore a plain reading of sub-section (4) of section 10B makes it clear that the deduction is allowable in respect of the profit "derived from" export of articles or things or computer software. It is settled law that the usage of the term "derived from" requires a direct and proximate connection between eligible activity and income. The yardstick to be applied, therefore, to income arising on account of interest or miscellaneous income is whether or not the source of income is integrally connected with the eligible activity. In the present case, the appellant is parking the surplus with tanks money market instruments for convenience and for deriving higher interest income and therefore, there is no direct link. The same holds true in the case of interest from FDS which has no direct and proximate relation with the eligible activity. The miscellaneous income represents income from sale of scrap of Rs. 23,239/-, having again no relation to the eligible activity. The interest received on allotment money again, cannot be said to have any direct nexus with the eligible activity. Thus, there being no direct and proximate connection between the interest income and miscellaneous income with the eligible activity, the AO has rightly denied the appellant's claim of deduction u/s.10B on Rs. 61,45,377/-

4. Further, the arguments regarding netting of interest was rejected by the CIT(A) vide para 3.1 of his order, which is as under:

"I have considered the facts, the Bombay High Court in the case of CIT v. Punit Commercial Ltd. (supra) did not go into the larger question of law on whether or not interest income, on facts, constituted income from other sources. In the present case, interest expenses incurred have been in connection with the export business of the appellant and deduction for the same has been allowed in computing the profit or business. There is, therefore, no merit in the contention of the appellant that interest expenses, being business expenditure, be reduced from interest income, which constitutes income from other sources. This ground of appeal is, therefore, dismissed."

5. Before us, learned counsel for the assessee referred to page 19 of the paper book and pointed out that interest income was offered as business income and then he referred to the last page of the assessment order and pointed out that the same has been assessed as business income. According to him, once such income was assessed as 'business income' then the same was entitled to deduction u/s.10B(1), particularly in the light of the decision of the Hon'ble Bombay High Court in the case of CIT v. Indo Swiss Jewels ltd. (284 ITR 389) and CIT v. Lok Holdings (308 ITR 356). He argued that concept of "derived from' will have

different connotations with reference to different provisions of the Act. For example, while considering the deduction u/s.80H, 80HH, 80I and 80IA, etc. the expression "derived from" would have different consequences because the deductions in these sections have been prescribed as an amount of 'profits derived from units/undertakings:, whereas in section 10A, 10B and 80HHC in addition to use of expression 'derived from' a further formula has been prescribed for determination of deduction. He submitted that section 10B(1) of the Act, prescribes that income derived from export would be eligible for deduction but further section 10B(4) provides that for the purpose of sub-section (1) profit derived from articles or things for computer software shall be the amount which bears to the profits of the business of undertaking the same proportion as the export turnover in respect of such articles or things or computer software bears to the total turnover of business of the undertaking.

6. The above provision clearly shows that a separate formula has been given for allowing deduction u/s. 10B(4) and therefore, it would not be correct to test each and every item of income on the anvil of phrase "derived from" in order to find out the eligibility thereof. Instead formula given u/s.10B(4) has to be followed. In this respect he referred to the decision of Bombay Bench of the tribunal in the case of Living Stones Jewellery P.Ltd. v. DCIT (31 SOT323). He also relied on the decision of the Bombay Bench in the case of J.P. Morgan India P.Ltd.v. DCIT (33 SOT 327), wherein again interest from fixed deposit as well as staff loan was treated as profits and gains from business eligible for deduction u/s.10A of the Act. He also referred to the decision of the Special Bench in the case of Topman Exports vs. ITO (318 ITR (AT) 87and particularly the observations made at page 134 and 135 wherein it was observed that if the contention of the learned Departmental Representative regarding derived from was accepted, then explanation u/s.4C would become redundant. Therefore, in view of the particular

formula given in section 10B(4) the expression derived from was not required to be given any effect.

7. On the other hand, the learned Departmental Representative submitted that once the expression 'derived from' was used by the legislature then only profits from a particular business undertaking were eligible for deduction and not all kinds of profits were eligible for deduction. He agreed that the Mumbai Bench of the Tribunal has taken the view in the case of Living Stones Jewellery P. Ltd. v. DCIT (supra) that interest is eligible for deduction u/s.10A but that decision was rendered without noticing the binding precedent from the Hon'ble Madras High Court in the case of CIT v. Menon Impex P. Ltd., (259 ITR 403), wherein it was held that interest received from the deposits made in banks was not eligible for deduction u/s.10A by following the decision of the Hon'ble Supreme Court in the case of Cambay Electric Supply Industrial Co. Ltd. v. CIT (113 ITR 84) and CIT v. Sterling Foods 237 ITR 579 (SC). Since, there is no contrary decision available from any other High Court, this becomes binding precedent and has to be followed. Further, the provisions of sec.10A and 10B are almost similar and therefore, the Tribunal was bound to follow this decision in the case before us.

8. In the rejoinder, the learned counsel for the assessee referred to the decision of the Hon'ble Madras High Court in the case of Menom Impex Pvt. Ltd. (supra) and pointed out that the same was rendered for the assessment year 1985-86 when section 10B was differently worded and section 10B(4) giving specific formula of deduction was not on statute and therefore, this decision cannot be followed.

9. We have considered the rival submissions carefully. In the light of the material on record as well as the written submissions filed by the learned counsel for the assessee and citations quoted by both the parties. Section 10B(1) and 10B(4) *reads as under :*

> *"10B(1) Subject to the provisions of this ection, a deduftion of such profits and gains as are derived by a hundred per cent export-oriented 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 articles or things or computer software, as the case may be, shall be allowed from the total income of the assessee."*
>
> *"10B(4) For the purposes of sub-section (1) the profits derived from export of articles or things or computer software shall be the amount which hears 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."*

Section 10B(4) in the present form was not there on the statute when Section 10B was originally enacted by the Finance Act, 1988. The present Sub-section (4) was brought on the Statute by the finance act 2000 with effect from 1.4.2001.

10. Let us first of all deal with the decision of the Hon'ble Bombay High Court in the case of Indo Swiss Jewels Ltd. (supra). In that case the interest from surplus funds was returned as income from business and deduction u/s.80HH and 80I was claimed. However, the Assessing Officer denied the deduction and assessed the same as 'income from other sources'. We do not know any facts beyond this. We would like to refer to the decision of the Hon'ble Supreme Court in the case of Pandian Chemicals Ltd. v. CIT (262 ITR 278), wherein it was held as under:

> *"Interest derived by the industrial undertaking of the assessee on deposits made with the Electricity Board for the supply of electricity for running the industrial undertaking could not be said to flow directly from the industrial undertaking itself and was not profit or gains derived by the undertaking for the purpose of the special deduction under section 80HH."*

From the above it is clear even interest from electricity deposit was not held eligible for deduction u/s.80-HH, then obvious by interest from surplus funds would not in any case can be held to be eligible for deduction u/s.80HH and 80I. Recently, in the case of Liberty India vs. CIT, 317 ITR 218, the concept 'derived from' has been again upheld and it was held that u/s.80I, 80*A and 80IB, the

incentives from DEPB Licenses etc. could not be held to be profits derived from industrial undertaking. In this case, one of the argument taken was that languages of sec. 80IB was different from section 80I. But despite the difference of language the expression "derived from" was given full effect.

11. The learned counsel for the assessee has vehemently argued that in this case interest from deposit was offered as business income and was also assessed as business income and therefore, automatically once it is assessed as business income then the same becomes eligible for deduction u/s.10B.

On careful consideration we find that though these arguments look attractive but not correct. For this we have to refer to the famous decision of the Hon'ble Supreme Court in the case of CIT vs. Sterling Foods (supra). In that case the question arose whether receipt from sale of import entitlements was eligible for deduction u/s.80HH.

The Hon'ble Supreme Court noted that identical question came before the Hon'ble High Court for an earlier year and the High Court had answered the question against the assessee in Sterling Foods vs. CIT (150 ITR 292). It was further noted that in this year, the Hon'ble High Court has taken a different view. If we go through the decision of Hon'ble Karnataka High Court in the case carefully, which is reported at 190 ITR 275, then we find that a different view has taken by the Hon'ble Karnataka High Court because section 28 had itself been amended by the Finance Act, 1990 with effect from April 1, 1962 by insertion of clause (iiia) and clause (iiib) with effect from 1.4.1967. After noting this amendment the Hon'ble High Court reproduced the provisions of clause (iiia) and (iiib) and then observed as under:

> *"Section 28 provides for what income shall be chargeable to income tax under the head "Profits and gains of business or profession". Therefore, by the amendment effected to section 28, what was held by this court not to be an income arising out of profits and gains of business or profession, by operation of law, has become such income. Therefore, once it becomes income, automatically, the benefits conferred* by *section 80HH will be attracted to the case of the assessee."*

From the above, it is clear that Hon'ble High Court was of the view that once the income from sale of import license was to be treated as business income under the Act in view of clause (iiia) of section 28, then automatically benefits conferred by section 80HH would be available.

12. The Hon'ble Supreme Court did not agree with this logic (reported at 237 ITR 579) and the decision of Hon'ble Karnataka High Court was reversed. It was observed that it is not the criteria how the income is assessed but because of the expression "derived from" what was required is that such business profit for being eligible to a deduction should have direct nexus to the profits and gains of such industrial undertakings. In fact it was held as under:

> *"Held, reversing the decision of the High Court, that the provisions of section 28 as amended made no difference. The word "derive" is usually followed by the word "from" and it means: "get, to trace from a source: arise from, originate in, show the origin or formation of". The source of import entitlements could not be said to be the industrial undertaking of the assessee. The source of the import entitlements could only be said to be the Export Promotion Scheme of the Central Government whereunder the export entitlements became 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 was not direct but only incidental. The industrial undertaking exported processed sea foods. By reason of such export, the Export Promotion Scheme applied. Thereunder, the assessee was entitled to import entitlements, which it could sell. The sale consideration therefrom could not be held to constitute a profit and gain derived from the assessee's industrial undertaking. The receipts from the sale of import entitlements could not be included in the income of the assessee for the purpose of computing the relief under section 80HH of the Income-tax Act, 1961."*

13. We further find that similar view has been taken by the Hon'ble Supreme Court again in the case of Liberty India vs. CIT(supra). In this case the question was whether profit from Duty Entitlement Pass Book Scheme (DEPB) and Duty Draw Back Scheme could be said to be profit derived from business of industrial undertaking eligible for deduction under section 80-IB of the Income-tax Act, 1961. It can be seen that DEPB and Duty Drawback etc.,

are covered by clause (iiid) to section 28 which means necessarily they have to be treated as business income under the provisions of the Act, still the deduction was denied u/s. 80I/80IA/80IB because these items were held to be not derived from the business of industrial undertaking/export activity.

14. Therefore, it is clear that merely because the income has been assessed as business income will not automatically confer the benefits of a particular deduction once there is a rider provision that such income should be derived from a particular source. In the case before us admittedly the interest income was generated from interest on FDRs etc., from the surplus funds and, therefore, the same cannot be held to have been derived from the export of I.T. Services.

15. We are unable to agree with the submissions of the learned counsel for the assessee that even the Special Bench of the Tribunal in the case of Topman Exports v. ITO (supra), the concept 'derived from' was given 'go by'. Section 80HHC has very clearly given the definition of business profits under clause (baa) to Explanation to Section (4C). Under this clause the 90% of the incentives provided under section 28(iiia), (iiib), (iiic) and (iiid) etc. were to be reduced from the profits of the business. This is so because such incentives were required to be added to the business profits in view of the first proviso to sub-section (3) of section 80HHC and the DEPB licences fall under section 28(iiid). Since the Special Bench was considering the issue regarding DEPB license, therefore it has referred to the first proviso and the meaning of business profits and it cannot be said that expression 'derived from' will have no effect where separate formula for calculation of deduction has been given. Interestingly it was also noted that in this case also one of the issue involved was deduction u/s.80HHC in respect of interest income in the case of Kalpataru Colour & Chemicals which was adjudicated along with other appeals. After considering the decision of the Hon'ble High Court in the case of CIT v. Indo Swiss Jewels as well as the decision of the Special Bench in the case of

Lalsons Enterprises v. DCIT (supra) as well as the decision of the Hon'ble Delhi High Court in the case of CIT v. Sriram Honda Power Equipments (289 ITR 475) and CIT v. Delhi Brass and Metal Works Ltd. (313 ITR 352). In this case in page 95 of the report reads as under :

> *"In order to cover any activity under the ambit of business, it must be continued on regular business with the intention of earning income therefrom. Interest income will fall under the head "Profits and gains of business or profession" if the assessee carries on the business of finance and the earning of interest is its main business or if the business is different from that of financing but interest income results in carrying o the main business activity and is incidental to it. The necessary pre-requisite condition is not the deployment of business funds but the nature of activity which results in such income. If the funds of the business are parked for safe keeping or with a view to earn interest income de hors the main business activity, the interest resulting thereform cannot assume the character of business income but would fall under the head "Income from other sources" and only the deductions permissible under section 57 will be permissible. In order to qualify for deduction under clause (iii) of this section which is the residual clause, the expenditure must be wholly and exclusively laid out for earning such income."*
> *The Tribunal held as under:*
>
> *"Held accordingly, on the facts, that the interest income could not be considered for deduction under section 80HHC. Nothing had been shown that there was some business exigency necessitating the deployment of funds. It was a case of simple parking of surplus funds with third parties and the bank, having no relation with the export business. The interest income had been rightly taxed under the last head of income and no amount was deducible against this income. Hence, it was also ineligible for deduction under section 80HHC."*

Therefore, it cannot be said that in the case of Topman Exports (supra) the Special Bench has already held that once a separate formula for giving deduction is there, then expression "derived from" would have no meaning.

16. We also find that the case of ITO v. Banyan Chemicals Pvt. Ltd. 310 ITR (AT)384(Ahd.)(TM) which is a Third Member decision (which has equal force as to the Special Bench), it was held that expression 'derived from' has to be applied in the case of 10B(4) also. At page 391 after extracting section 10B(1) and 10B(4) it was observed as under:

> "*On a plain reading of these two sub-sections of section 10B, it is evident that a deduction is to be allowed on such profits and gains as are derived by an undertaking from the export of articles or things and as computed under*

sub-section (4) thereof. The words "profit and gains as are derived by" are narrower than the profits attributable or arising from the business of an assessee or an undertaking. The term "derived" has been subject matter of judicial interpretation in various decisions, viz. CIT v. Sterling Foods (1999) 237 ITR 579 (SC) and Pandian Chemicals Ltd. v. CIT [2003] 262 ITR 278 (SC). In Sterling Foods [1999] 237 ITR 579 (SC), it is held that the word 'derive' means, 'get to trace from a source; arise from, originate in, show the origin or formation of". In this case, the court dealt with the nature of import entitlements and it is held that the source of the import entitlements could only be said to be the Export Promotion Scheme of the Central Government, whereunder the export entitlements become available. It held that there must be, for the application of the words, "derived from", a direct nexus between the profits and gains and the industrial undertaking and in the instant case, the nexus was not direct but only incidental. By reason of such export, the Export Promotion Scheme applies, whereunder, the assessee was entitled to import entitlements, which it could sell. The sale consideration therefrom could not be held to constitute a profit and gain derived from the assessee's industrial undertaking."

17. In this case, the issue was that assessee had deposited certain amounts in EEFC account. It was held when the export proceedings were realized and deposited in the EEFC account then such gain from foreign exchange would be eligible for deduction u/s. 10B of the Act. But any gain received later on from withdrawal from EEFC account would not be part of such sales and cannot therefore, be profit arising from export of goods.

18. In our view once a foreign exchange is deposited in EEFC account and withdrawal is made later on then perhaps the gains could be attributed to the interest portion also because once the foreign exchange is deposited for a particular period, at the time of withdrawal it would have two elements, viz. interest as well as profits/loss on account of fluctuation in the rate of exchange. It has been clearly held in this case that on a later withdrawal from EEFC such gain could not be said to have been derived from export of goods. This means interest portion was also found to be not eligible for deduction u/s. 10B because the same was not derived from export of goods.

19. We are unable to agree with the submission of the learned counsel for the assessee that after insertion of section 10B(4) by the Finance Act 2000 with effect from 2001, the decision in the case of Menon Impex (supra) would not be

applicable. This is so, because section 10B(4) merely gives the formula to make the deduction proportionate. Say if there is export turnover of Rs. 50 and total turnover is also Rs.100/- then the total business profit has to be divided by 50/100, because the total turnover (i.e. export turnover + domestic turnover). But the expression 'derived from' cannot be ignored in Section 10B(1) because the expression involves only these items of profit eligible for deduction which are derived from such undertaking.

20. We have also gone through the decisions of the Co-ordinate Bench of the Tribunal in the case of J.P. Morgan India Pvt. Ltd. v. DCIT (supra) and Living Stones Jewellery Pvt. Ltd., v. DCIT (supra) and find that both the decisions are distinguishable because both the decisions have not considered mandatory decision available from the Hon'ble Madras High Court in the case of CIT v. Menon Impex v. CIT(supra). In addition the benefit of Third Member decision in the case of Ito v. Banyan Chemicals Ltd. (supra) was also not available in this case.

21. In any case the decision in the case of Menon Impex v. CIT(supra) was followed by the Hon'ble Madras High Court in the case of India Comnet International v. ITO (304 ITR 322). This decision was rendered for the assessment year 2002-03 when sub-section (4) had already been inserted on the Statute. Further in this case it was also argued that since the interest income was derived from funds retained by the bank to meet the exigencies of the business and that the entire transaction would constitute an integrated whole and the same could not be bifurcated into different areas. Reliance was also placed on the decision of the Hon'ble Supreme Court in the case of CIT v. Baby Marine Exports (290 ITR 323) for the proposition that section 10A was beneficial provisions and, therefore, should be construed liberally. But these submissions were not accepted by the Court. From the above, it is clears that at present only one decision is available and whereby interest income was held to be not eligible for deduction u/s.

10A/10B. Therefore, we are bound to follow this decision as the learned counsel simply tried to distinguish this and could not point out to a different decision from the apex court or other courts. In these circumstances, we find nothing wrong with the order of the learned CIT(A) and confirm the same.

22. In the result, the appeal is dismissed.

Order pronounced on this 1st day of December, 2009.

Sd.	Sd.
(D.K. Agarwal)	(T. R. Sood)
Judicial Member	Accountant Member

Mumbai dated the 1st December, 2009.
Kn
Copy to:

1. The Assessee
2. The Revenue
3. The CIT, Central IV, Mumbai
4. The CIT(A), Central-III, Mumbai
5. The D.R.'E' Bench, Mumbai

/True copy/

By order

Asst. Registrar, ITAT, Mumbai

FIT FOR REPORTING

(D.K. Agarwal)	(T.R. Sood)
Judicial Member	Accountant Member

S.No.	Details	Date	Initials	Designation
1	Draft dictated on	27.11.09		Sr.PS/PS
2	Draft Placed before author	27.11.09/1.12.09		Sr.PS/PS
3	Draft proposed & placed before the Second Member			JM/AM
4	Draft discussed/approved by Second Member			JM/AM
5.	Approved Draft comes to the Sr.PS/PS			Sr.PS/PS
6.	Kept for pronouncement on			Sr.PS/PS
7.	File sent to the Bench Clerk			Sr.PS/PS
8	Date on which the file goes to the Head clerk			
9	Date of Dispatch of order			