IN THE HIGH COURT OF KARNATAKA, BANGALORE

DATED THIS THE 28TH DAY OF OCTOBER, 2014

PRESENT:

THE HON'BLE Mr.JUSTICE N.KUMAR

AND

THE HON'BLE Mr.JUSTICE B.MANOHAR

INCOME TAX APPEAL NO.46 OF 2009
C/W.
INCOME TAX APPEAL NO.47 OF 2009

IN ITA NO. 46/2009

BETWEEN:

M/S SUBEX LIMITED
ADARSH TECH PARK
OUTER RING ROAD, DEVARABISANAHALLI
BANGALORE-560037
(REPRESENTED BY ITS MANAGING DIRECTOR
SRI SUBASH MENON, AGED ABOUT 44 YRS
S/O P.JAYAPALA MENON)

... APPELLANT

(BY SRI CHYTHANYA K.K., ADVOCATE)

AND:

THE INCOME TAX OFFICER
WARD 12 (2)
BANGALORE.

... RESPONDENT

(BY SRI K.V.ARAVIND, ADVOCATE)

THIS APPEAL IS FILED U/S 260-A OF I.T.ACT, 1961 ARISING OUT OF ORDER DATED 23-10-2008 PASSED IN ITA

NO. 94/BNG/2008, FOR THE ASSESSMENT YEAR 2003-2004, PRAYING TO:

I. FORMULATE THE SUBSTANTIAL QUESTIONS OF LAW STATED THEREIN,

II. ALLOW THE APPEAL AND SET ASIDE THE ORDER PASSED BY THE ITAT BANGALORE IN ITA NO. 94/BNG/2008,DATED 23-10-2008 IN THE INTEREST OF JUSTICE.

IN ITA NO.47/2009:

BETWEEN:

M/S SUBEX LIMITED
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OUTER RING ROAD, DEVARABISANAHALLI
BANGALORE-560037
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(BY SRI K.V.ARAVIND, ADVOCATE)

THIS APPEAL IS FILED U/S 260-A OF I.T.ACT, 1961 ARISING OUT OF ORDER DATED 23-10-2008 PASSED IN ITA NO. 95/BNG/2008, FOR THE ASSESSMENT YEAR 2004-2005, PRAYING TO:

III. FORMULATE THE SUBSTANTIAL QUESTIONS OF LAW STATED THEREIN,

IV. ALLOW THE APPEAL AND SET ASIDE THE ORDER PASSED BY THE ITAT BANGALORE IN ITA NO. 95/BNG/2008,DATED 23-10-2008 IN THE INTEREST OF JUSTICE.

THESE APPEALS ARE COMING ON FOR HEARING THIS DAY, ***N.KUMAR, J.,*** DELIVERED THE FOLLOWING:

J U D G M E N T

The assessee preferred these appeals against the order passed by the Tribunal.

2. As the question involved in both these appeals are one and the same and the assessee also being the same, they are taken up for consideration together and disposed of by this common order.

3. The assessee is a public limited company engaged in the business of development of software and export of software. It is an 100% EOU approved by the STP of India. The assessing officer noticed from Schedule "M" to the financial accounts that a sum of Rs.17,27,385/- was shown as rent receipt. When that was sought to be clarified, the assessee stated that they were having a

branch office at Canada for development of software product. They had entered into a non-cancelable lease for 36 months with the lessor from 01.06.2001 to 31.05.2004. As the company does not carry on any activity other than development of software in Canada and the letting out of the property is inextricably connected with its business operations, the rental income for the period had been claimed as forming part of Section 10A as per the Income Tax Act (for short the 'Act'). The assessee has paid an amount of Rs.43,38,350/- as rent from April 2002 to March 2003. The rent paid is more than the rent received. The assessee claimed that the excess rent paid should be treated as loss and should be allowed to be carried forward. The assessing authority did not accept the said explanation and brought the aforesaid amount to tax under 'income from other sources'. In appeal, the Commissioner of Income Tax (Appeals) also held the same cannot be admitted as 'income from house property' as the asseessee is not the owner of the property in question. The rent income cannot be assessed as business income as there is no direct nexus between the assessee's software

development business and the industrial undertaking with the payment of rent. Therefore, dismissing the appeal, the tribunal affirmed the finding of the assessing authority and the appellate authority. Aggrieved by the said order, the assessee is in appeal.

4. The substantial question of law that arises for our consideration in this appeal is as under:-

> *1. Whether on the facts and in the circumstances of the case, the Honourable Tribunal was right in law in holding that the rental from temporary sublease of office premises cannot be regarded as "part of the profits of the business" for the purpose of deduction under Section 10A?*
>
> *2. Whether on the facts and in the circumstances of the case, the Honourable Tribunal was right in law in holding while the rent received in respect of sublease should be charged to tax under the head 'income from other sources', the rent paid on principal lease of the very same premises should be allowed in computing the profits of the STP undertaking resulting in artificially lowering the profits of the STP undertaking eligible for deduction under Section 10A?*

5. Learned counsel for the assessee contends that Section 10A (1) of the Act has to be read with Sub section (4) of the Act. If so read, the profits of the business of the

undertaking as referred to in Section 10A(4) quantifies the deduction provided in Section 10A(1). Therefore, if the assessee for a temporary period lets out the lease premises and derives the rental income, it constitutes the profits of business of the undertaking and the assessee is entitled to the benefit of Section 10A of the Act. Therefore, the impugned order passed is contrary to law and requires to be set aside.

6. Per contra, learned counsel for the revenue submitted that the only income which falls under Section 10A of the Act is the profits and gains as are derived by undertaking from the export of articles or things or computer software and the rental income derived by the assessee would not form part of the said profits and gains and therefore, the authorities were justified in not extending the benefit.

7. Section 10A (1) and (4) reads as under:-

> "10A. 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.

(4) For the purposes of sub-sections (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."

8. As could be seen from the aforesaid provisions, the opening words of Section 10A of the Act assumes importance. It commences with the words "subject to the provisions of this section". The opening words of sub section 4 of the Act clearly state that "for the purposes of [sub-sections (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". If the assessee is entitled to deduction only profit derived under Section 10A(1) of the Act, the sub section (4) would be redundant. The sub section which came into effect on 01-04-2002 by Finance Act 2001 recognizes that the profits of the business of the undertaking would be, not only the profits and gains from the exports of articles or things or computer. in addition to that, the undertaking may have some other profits also, which is derived from business of the undertaking.

9. In the instant case, the assessee took the premises on lease. Assessee has paid a sum of Rs.43,38,350/- as rent from April 2002 to March 2003. It is shown as 'business expenses', as against the 'expenses incurred'. The assessee has received a sum of Rs.17,27,385/- as rent receipt for the relevant period. Assessee is not the owner of the said premises. Assessee is carrying on the business of development of Software in Canada. The said premises was taken for the aforesaid

business purpose. As a portion of the said premises was not used for business purpose, instead of keeping it vacant and suffering loss, it was rented out. Therefore, the said income derived from lease of the said premises constitutes "income from business". Neither it would be 'income from house property' nor 'income from other sources'. In view of the explanation used in sub Section (4) of Section 10A of the Act for the purpose of Sub section 1, the profit derived from export of articles or things or computer software shall be the amount which bears to the profits of business of the undertaking. Though the said profits are not derived from export of articles or things or computer software, by virtue of sub Section (4) it is deemed to be the profits of the business of the undertaking for the purpose of extending the benefit of exemption of payment of tax under Section 10A of the Act to a newly established undertaking in a free trade zone. In that view of the matter, the order passed by the Tribunal is un-sustainable and contrary to law. Therefore, the first substantial question of law is answered in favour of the assessee as against the revenue. The

second substantial question of law does not arise for consideration. Hence, we pass the following:

ORDER

1. The appeals are allowed.
2. The impugned order is set aside .
3. The assessing Authority is directed to extend the benefit of Section 10A of the Act, even in respect of this rental income as Income derived from business of the undertaking.

Sd/-
JUDGE

Sd/-
JUDGE

VMB