IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED : 09.07.2021

CORAM :

THE HON'BLE MR.JUSTICE M. DURAISWAMY
AND
THE HON'BLE MRS.JUSTICE R. HEMALATHA

Tax Case Appeal Nos.171 to 174 of 2016

Commissioner of Income Tax II (2)
No.121, Nungambakkam High Road,
Chennai – 600 034. ... Appellant
in all appeals

Vs.

M/s.HTC Global Services India Pvt. Ltd.,
SDF II, Phase II, MEPZ,
Tambaram,
Chennai – 600 045. ... Respondent
in all appeals

Tax Case Appeals in Tax Case Appeal Nos.171 to 174 of 2016 filed under Section 260A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal, Chennai "B" Bench, dated 02.06.2015, passed in I.T.A.Nos.58/Mds/2014, 362/Mds/2014, 1280/Mds/2014 and 2021/Mds/2014 respectively.

For Appellant : Mr.Karthik Ranganathan
Senior Standing Counsel
in all appeals

For Respondent : Notice served in all appeals

COMMON JUDGMENT

(Delivered by **M. DURAISWAMY, J.**)

T.C.A.No.171 of 2016 arises against the order passed in I.T.A.No.58/Mds/2014 in respect of the Assessment Year 2008-09, T.C.A.No.172 of 2016 arises against the order passed in I.T.A.No.362/Mds/2014 in respect of the Assessment Year 2008-09, T.C.A.No.173 of 2016 arises against the order passed in I.T.A.No.1280/Mds/2014 in respect of the Assessment Year 2009-10, T.C.A.No.174 of 2016 arises against the order passed in I.T.A.No.2021/Mds/2014 in respect of the Assessment Year 2009-10, on the file of the Income Tax Appellate Tribunal, Madras, "B" Bench. The above appeals are filed by the Revenue challenging the order passed by the Income Tax Appellate Tribunal.

2.The assessee is a company engaged in the business of providing customer support, services in the form of e-mail support, voice support and chatting. During the Assessment Year 2009-10, the assessee filed return of income on 25.09.2009 claiming deduction under Section 10-B of the Income Tax Act, 1961. The return of income was taken up for scrutiny assessment and the Assessing Officer found that the assessee company had earned dividend income of Rs.24,30,229/- and claimed the same as exempt under Section 10(34) of the Act. The assessee has not claimed any expenditure for earning this dividend income, and therefore, the Assessing Officer invoked the provisions of Section 14-A read with Rule 8D Clause (ii) and (iii) as expenditure attributable to the investments whose income is exempt from tax on the dividend earned.

3.Challenging the order of assessment, the assessee preferred an appeal before the Commissioner of Income Tax (Appeals) and the Appellate Authority reworked the calculation and confirmed the disallowance under Rule 8D. Aggrieved over the order passed by the Commissioner of Income Tax (Appeals), the assessee preferred further appeal before the Income Tax Appellate Tribunal, and the Tribunal, by

its common order, upheld the order of the Commissioner of Income Tax (Appeals) and confirmed the disallowance under Rule 8D.

4.Challenging the order passed by the Income Tax Appellate Tribunal, the Revenue has filed the above appeals.

5.T.C.A.No.171 of 2016 was admitted on the following substantial questions of law :

"1.Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in treating 3% of the exempt income as the expenditure to be disallowed under section 14A of the Income Tax Act for the assessment year 2008-09 which is against the statute?

2.Is not the finding of the Appellate Tribunal bad in law when the statute prescribes for the disallowance under section 14A is in accordance with Rule 8D of the Income Tax Rules with effect from assessment year 2008-09 onwards?"

6.T.C.A.Nos.172 and 174 of 2016 were admitted on the following substantial questions of law :

"1.Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was correct in confirming to reduce the expenses relating to telecommunication and travel expenses in foreign currency from the total turnover for computing deduction under Section 10B of the Income Tax Act?

2.Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in excluding the telecommunication and travel expenditure incurred in foreign currency from the total turnover when clause (iv) to Explanation 2 to Section 10B specifically excludes the same only from the export turnover?"

7.T.C.A.No.173 of 2016 was admitted on the following substantial question of law :

"Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in confirming the order of CIT (A) and confirmed the disallowance to Rs.12,31,129/- under Rule 8D of the Income Tax Rules?"

8.Since the issues involved in all these appeals are common, Mr.Karthik Ranganathan, learned Senior Standing Counsel, appearing for the appellant/Revenue, submitted that all the appeals may be taken up together and disposed of by a common order.

9.Further, the learned Senior Standing Counsel fairly submitted that the questions of law that arise for consideration in all these appeals were already decided against the Revenue and in favour of the assessee in the following judgments :

i. [2018] 93 taxmann.com 33 (SC) [Commissioner of Income-Tax, Central-III v. HCL Technologies Ltd.], wherein, the Hon'ble Supreme Court held as follows :

> *"8.The whole controversy revolves around the claim of certain expenses attributable to the delivery of software outside India or in providing technical services from 'total turnover' by the Respondent under Section 10A of the IT Act. It is an undisputed fact that neither Section 10A nor Section 2 of the IT Act define the term 'total turnover'. However, the term 'total turnover' is given in clause (ba) of the Explanation to Section 80 HHC of the IT Act which defines the meaning of total turnover as follows:*

"(ba) 'total turnover' shall not include freight or insurance attributable to the transport of the goods or merchandise beyond the customs stations as defined in the Customs Act, 1962 (52 of 1962).

***Provided** that in relation to any assessment year commencing on or after the 1st day of April, 1991, the expression "total turnover" shall have effect as if it also included any sum referred to in clauses (iiia), (iiib), (iiic), (iiid) and (iiie) of section 28;"*

9.It is also pertinent to mention here the relevant terminologies which are as under:

"Export Turnover:

Explanation 2(iv) of Section 10A of the IT Act defines "export turnover" to mean the consideration that has been received for export of articles/things/computer software. Normally the consideration will include the freight/telecommunication charges/insurance which had been incurred to deliver the article/things/computer software outside India. However the Explanation 2(iv) specifically seeks to exclude these three categories of expenditure incurred for delivering the export of articles/things/computer software. It also seeks to exclude expenses for providing technical service, etc. outside India. Therefore, where an Indian technician goes abroad and receives fees for service, the foreign client will normally be required to reimburse the expenses as well. Therefore, out of the consideration received, the portion representing reimbursement of expenditure has to be excluded.

Export Turnover and Total turnover:

The "total turnover" has been defined in sections 80HHC and 80HHE only to exclude additional items given under section 28. But for this additional exclusion, there was no need to define "total turnover".

Export turnover is a component of total turnover. If the entire turnover represents export proceeds, then the export turnover and the total turnover are identical. It is clear that any exclusion in the export turnover in the numerator will automatically imply exclusion in the denominator as well because export turnover is always a component of total turnover.

Export Turnover/Total Turnover/Business:

Form 56F prescribes the report under Section 10A for and Annexure- A thereto refers to "export proceeds" and "sale proceeds". Both together form the total turnover of the undertaking."

10.The question arises here that when the particular term has not been defined in any particular Section, is it allowed to import the meaning of such term from the other provisions of the same Act? Section 10A of the IT Act is a special beneficial provision and the purpose of deduction under such Section is to encourage and boost the new business undertakings situated in the free trade zone of this Nation by providing suitable deductions to such business entities. Sometimes, while calculating the deduction,

disputes arise regarding the methodology of deduction which ought to be followed. Undisputedly, it is a matter of record that the Respondent is engaged in the activity of trading of generic software and providing customized software development services for domestic as well as for foreign clients through its two units situated in Software Technology Park, Gurgaon (Now Gurugram) which falls under definition of the Section 10A of the IT Act. The contention of the Respondent is that it incurred expenditure in foreign exchange in sending professionals abroad as per the agreements with the foreign constituents.

11.On an analysis of the Respondent's activity taken from its website, Assessing Officer arrived at a conclusion that Respondent has been rendering technical services outside India and, therefore, expenses incurred on such activity are required to be excluded from the export turnover while working out the deduction admissible under Section 10A of the IT Act. The Assessing Officer estimated 60% of the software development charges required to be attributed towards expenses incurred for providing technical services outside India. On appeal, learned CIT (Appeals) again made a detailed analysis of the activity of the Respondent and arrived at a conclusion that the Assessing Officer failed to bring any evidence which can indicate that Respondent was providing technical services outside India and it has

incurred expenses towards salary etc. rendering such services. Inspite that, learned CIT (Appeals), estimated 10% of software development charge as charges incurred for technical services provided outside India.

12.It is undisputed fact that the Respondent was engaged in the business of software development for its customers engaged in different activities at software development centres of the Respondent. However, in the process of such customized software development, certain activities were required to be carried out at the sight of customers on site, located outside India for which the employees of the branches of the Respondent located in the country of the customers are deployed. It is true that it is not defined that which activity will be termed as providing technical services outside India. Moreover, after delivery of such softwares as per requirement, in order to make it fully functional and hassle free functioning subsequent to the delivery of softwares in many cases, there can be requirement of technical personnel to visit the client on site. The Assessing Officer could not bring any evidence that the Respondent was engaged in providing simply technical services independent to software development for the client for which the expenditures were incurred outside India in foreign currency.

13.The Respondent company has claimed deduction under Section 10A as per certificates filed on Form No. 56F. The Respondent, while computing the deduction, has taken the same figure of export turnover as of total turnover. The Respondent cited various judicial cases but all these cases pertain to deduction under Section 80HHC. Further, the definition of total turnover has been defined in Section 80HHC and 80HHE of the IT Act. As discussed earlier, the definition of total turnover has not been defined under Section 10A of the IT Act.

14. In the above backdrop, we are of the opinion that the definition of total turnover given under Sections 80HHC and 80HHE cannot be adopted for the purpose of Section 10A as the technical meaning of total turnover, which does not envisage the reduction of any expenses from the total amount, is to be taken into consideration for computing the deduction under Section 10A. When the meaning is clear, there is no necessity of importing the meaning of total turnover from the other provisions. If a term is defined under Section 2 of the IT Act, then the definition would be applicable to all the provisions wherein the same term appears. As the term 'total turnover' has been defined in the Explanation to Section 80HHC and 80HHE, wherein it has been clearly stated that "for the purposes of this Section

only", it would be applicable only for the purposes of that Sections and not for the purpose of Section 10A. If denominator includes certain amount of certain type which numerator does not include, the formula would render undesirable results.

15.A Statute is the intention of the legislature who enacts it after having regard to various facts and circumstances. It is a cardinal principle of law that the interpretation by the Court shall be done in such a way that the intention of the legislature shall prevail and no injustice occurred with the parties. The rule of harmonious construction is the thumb rule to interpretation of any statute. An interpretation which makes the enactment a consistent whole, should be the aim of the Courts and a construction which avoids inconsistency or repugnancy between the various sections or parts of the statue should be adopted.

16.In ***Commissioner of Income Tax vs. J.H. Gotla****, (1985) 23 Taxman 14J (SC)/156 ITR 323 (SC) this Court has held as under:*

> *"46.Where the plain literal interpretation of a statutory provision produces a manifestly unjust result which could never have been intended by the Legislature, the Court might modify the language*

used by the Legislature so as to achieve the intention of the Legislature and produce a rational construction. The task of interpretation of statutory provision is an attempt to discover the intention of the Legislature from the language used....

47..If the purpose of a particular provision is easily discernible from the whole scheme of the Act which, in the present case, was to counteract, the effect of the transfer of assets so far as computation of income of the Respondent was concerned, then bearing that purpose in mind, the intention should be found out from the language used by the Legislature and if strict literal, construction leads to an absurd result, i.e. result not intended to be subserved by the object of the legislation found out in the manner indicated above, then if other construction is possible apart from strict literal construction, then that construction should be preferred to the strict literal construction. Though equity an taxation are often strangers, attempt should be made that these do not remain so always so and if a construction results in equity rather than in injustice then such construction should be preferred to the literal construction. Furthermore, in the instant case, we are dealing with an artificial liability created for counteracting the effect only of attempts by the assessee to reduce tax liability by transfer.."

17.The similar nature of controversy, akin this case, arose before the Karnataka High Court in CIT vs. Tata Elxsi Ltd. (2012) 204 Taxman 321/17/taxmann.com 100/349 ITR 98. The issue before the Karnataka High Court was whether the Tribunal was correct in holding that while computing

relief under Section 10A of the IT Act, the amount of communication expenses should be excluded from the total turnover if the same are reduced from the export turnover? While giving the answer to the issue, the High Court, inter-alia, held that when a particular word is not defined by the legislature and an ordinary meaning is to be attributed to it, the said ordinary meaning is to be in conformity with the context in which it is used. Hence, what is excluded from 'export turnover' must also be excluded from 'total turnover, since one of the components of 'total turnover' is export turnover. Any other interpretation would run counter to the legislative intent and would be impermissible.

18.Accordingly, the formula for computation of the deduction under Section 10A of the Act would be as follows:

$$\text{Export Profit} = \text{total Profit of the Business} \times \frac{\text{Export turnover as defined in Explanation 2 (IV) of Section 10A of IT Act / Export turnover as defined in Explanation 2(IV) of Section 10A of the IT Act + domestic sale proceeds}}{}$$

19.In the instant case, if the deductions on freight, telecommunication and insurance attributable to the delivery of computer software under Section 10A of the IT Act are allowed only in Export Turnover but not from the Total Turnover then, it would give rise to inadvertent, unlawful, meaningless and illogical result which would

cause grave injustice to the Respondent which could have never been the intention of the legislature.

20.Even in common parlance, when the object of the formula is to arrive at the profit from export business, expenses excluded from export turnover have to be excluded from total turnover also. Otherwise, any other interpretation makes the formula unworkable and absurd. Hence, we are satisfied that such deduction shall be allowed from the total turnover in same proportion as well.

21.On the issue of expenses on technical services provided outside, we have to follow the same principle of interpretation as followed in the case of expenses of freight, telecommunication etc., otherwise the formula of calculation would be futile. Hence, in the same way, expenses incurred in foreign exchange for providing the technical services outside shall be allowed to exclude from the total turnover.

22.In view of above discussion, we are of the considered view that these instant appeals are devoid of merits and deserve to be dismissed. Accordingly, all the connected matters and interlocutory applications, if any, are disposed of with no order as to costs."

ii. [2021] 123 taxmann.com 378 (Madras) [Principal Commissioner of Income Tax, Corporate Circle-2(1), Chennai v. Envestor Ventures Ltd.], wherein, the Division Bench of this Court held as follows :

> *"21.We cannot approve even the larger disallowance proposed by the Assessee himself in the computation of disallowance under Rule 8D made by him. These facts are akin to the case of Pragati Krishna Gramin Bank (supra) decided by Karnataka High Court. The legal position, as interpreted above by various judgments and again reiterated by us in this judgment, remains that the disallowance of expenditure incurred to earn exempted income cannot exceed exempted income itself and neither the Assessee nor the Revenue are entitled to take a deviated view of the matter. Because as already noted by us, the negative figure of disallowance cannot amount to hypothetical taxable income in the hands of the Assessee. The disallowance of expenditure incurred to earn exempted income has to be a smaller part of such income and should have a reasonable proportion to the exempted income earned by the Assessee in that year, which can be computed as per Rule 8D only after recording the satisfaction by the Assessing Authority that the apportionment of such disallowable expenditure under section 14A made by the Assessee or his claim that no*

expenditure was incurred is validly rejected by the Assessing Authority by recording reasonable and cogent reasons conveyed to Assessee and after giving opportunity of hearing to the Assessee in this regard.

22.We, therefore, dispose of the present appeal by answering question of law in favour of the Assessee and against the Revenue and by holding that the disallowance under rule 8D of the IT Rules read with Section 14A of the Act can never exceed the exempted income earned by the Assesee during the particular assessment year and further, without recording the satisfaction by the Assessing Authority that the apportionment of such disallowable expenditure made by the Assessee with respect to the exempted income is not acceptable for reasons to be assigned the Assessing Authority, he cannot resort to the computation method under Rule 8D of the Income-tax Rules, 1962."

10.The ratio laid down by the Hon'ble Supreme Court of India in the judgment reported in *[2018] 93 taxmann.com 33 (SC)* covers the questions of law that arise for consideration in T.C.A.Nos.173 and 174 of 2016 and the judgment of the Division Bench of this Court reported in *[2021] 123 taxmann.com 378 (Madras)* covers the questions of law that

arise for consideration in T.C.A.Nos.171 and 172 of 2016.

11.In view of the submissions made by the learned Senior Standing Counsel appearing for the appellant/Revenue and the ratio laid down by the Hon'ble Supreme Court of India in the judgment reported in *[2018] 93 taxmann.com 33 (SC) (cited supra)* and by the Division Bench of this Court in the judgment reported in *[2021] 123 taxmann.com 378 (Madras)*, the questions of law are decided against the Revenue and in favour of the assessee.

12.Accordingly, the Tax Case Appeals are dismissed. No costs.

[M.D., J.] [R.H., J.]
09.07.2021

Index : Yes / No
Internet : Yes
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To

1.The Income Tax Appellate Tribunal, Chennai "B" Bench

2.The Commissioner of Income Tax II (2)
No.121, Nungambakkam High Road,
Chennai – 600 034.

M. DURAISWAMY, J.
and
R. HEMALATHA, J.

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T.C.A. Nos.171 to 174 of 2016

09.07.2021