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Section 10A deduction available before setting off domestic tariff area unit's current year as well as brought forward loss

In brief

The Delhi High Court (the HC), in its recent decision in the case of TEI Technologies Pvt. Ltd,[1] (the assessee) has held that section 10A of Income-tax Act, 1961 (the Act), though worded as a deduction, is essentially an exemption. Further, the deduction under section 10A the Act should be computed before setting-off the current year's loss of the domestic tariff area (DTA) unit as well as the brought forward loss of the DTA unit.

Facts

- The assessee had a unit in an export processing zone (EPZ), which was eligible for exemption under section 10A of the Act. The assessee also had a DTA unit.
- In the return of income for assessment year (AY) 2002-03 and AY 2003-04, the assessee computed the deduction under section 10A of the Act before setting-off the current year's loss and brought forward loss of the DTA unit.
- During the course of assessment proceedings, the assessing officer (AO) adjusted the current year's loss of DTA unit against profit of EPZ unit. To the remaining amount, the AO added the amount arising from disallowances of

[1] CIT *v.* TEI Technologies Pvt. Ltd. [TS-665-HC-2012(Del)]

other expenses. Against the resultant amount, the AO set-off the brought forward loss of the DTA unit and assessed the income at NIL.

- Accordingly, the claim for deduction under section 10A of the Act was rejected as the assessed income was NIL.

- The assessee filed an appeal against the order of the AO with the Commissioner of Income-tax Appeals (CIT(A)). The assessee argued that section 10A of the Act was an exemption provision. Therefore, the profit of the EPZ unit would form part of the total income subject to deduction of the exempted profits under section 10A. This exemption was to be given before the computation of gross total income. Accordingly, the approach adopted by the AO was erroneous as the level of gross total income was arrived at before computing the amount of exemption under section 10A of the Act.

- The CIT(A) upheld the action of the AO by following the decision of the Bangalore Bench of the Tribunal in the case of Mindtree Consulting Pvt. Ltd.[2]

- Aggrieved with the order of CIT(A), the assessee appealed before the Tribunal. In view of the decision of the Bangalore Tribunal in the case of Yokogawa India Ltd.[3], the appeal of the assessee was allowed.

- Aggrieved, by the order of the Tribunal, the revenue authorities preferred an appeal before the HC.

Issues before the HC

- Whether the loss incurred in the current year by the DTA unit should be set-off before computing the deduction under section 10A of the Act for EPZ unit

- Whether the brought forward loss of the DTA unit should be set-off before computing the deduction under section 10A of the Act for the EPZ unit

HC ruling

- Even after the amendment by the Finance Act, 2000, section 10A of the Act (change from exemption to deduction) has been retained in Chapter III (Incomes not forming part of total income) of the Act as opposed to placing it under Chapter VI-A (Deductions from gross total income) of the Act.

- Section 10A of the Act provides that deduction shall be allowed from 'total income'. Determination of the total income is the last point before the tax is charged. Upon determination of the total income, there would be no scope for any further deduction. Accordingly, the term 'total income' in the context of section 10A of the Act would mean profits and gains of the undertaking as understood in its commercial sense[4].

- Relief under section 10A of the Act is to be given before the computation of profits and gains of business or profession. This proposition was supported by the income-tax return form[5].

[2] Mindtree Consulting (P) Ltd. *v* ACIT [2005] 102 TTJ 691 (Bangalore)
[3] ACIT *v*. Yokogawa India Ltd. [2007] 111 TTJ 548 (Kar.)

[4] CIT *v.*Yokogawa India Ltd (2012) 341 ITR 385 (Kar)
[5] CIT *v* Yokogawa India Ltd (2012) 341 ITR 385 (Kar)

- In the case of Yokogawa India Ltd.[6], the Karnataka HC has held that section 10A of the Act is an exemption section. However, the Bombay HC in the cases of Hindustan Unilever Ltd[7] and Black and Veatch Consulting Pvt. Ltd.[8] had held that section 10A of the Act is a deduction section. However, both the high courts held that deduction under section 10A should be computed before adjusting the losses of the DTA unit.

- In light of the ambiguity as to whether section 10A of the Act is an exemption or a deduction section, the chapter heading may be used as an aid to interpret the statute. Section 10A of the Act is placed in Chapter III of the Act which deals with Incomes not forming part of total income.

- In light of the above, the HC held that section 10A of the Act is an exemption section and that deduction under the section should be given before setting off both the current year's as well as the brought-forward loss and unabsorbed depreciation of the non-EPZ unit.

Conclusion

This decision is relevant for companies which have taken a position not to set-off losses of the DTA unit against the profits of units eligible for deduction under sections 10A, 10B or 10AA of the Act.

The HC's discussion of amendments over time to section 10A of the Act would be very useful reference for any defence of claims for tax holiday.

[6] CIT *v.* Yokogawa India Ltd (2012) 341 ITR 385 (Kar)
[7] Hindustan Unilever Ltd. *v.* DCIT and Anr., [2010] 325 ITR 102 (Bombay)
[8] CIT *v.* Black and Veatch Consulting Pvt Ltd [2012] (Bombay)

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