IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

SPECIAL CIVIL APPLICATION No.7926 of 2006

To

SPECIAL CIVIL APPLICATION No.7951 of 2006

WITH

SPECIAL CIVIL APPLICATION No.10746 of 2007

WITH

SPECIAL CIVIL APPLICATION No.9261 of 2007

WITH

SPECIAL CIVIL APPLICATION No.27935 of 2007

WITH

SPECIAL CIVIL APPLICATION No.12181 of 2009

WITH

SPECIAL CIVIL APPLICATION No.12182 of 2009

WITH

SPECIAL CIVIL APPLICATION No.3179 of 2007

WITH

SPECIAL CIVIL APPLICATION No.7025 of 2010

WITH

SPECIAL CIVIL APPLICATION No.7953 of 2006

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SPECIAL CIVIL APPLICATION No.7954 of 2006

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SPECIAL CIVIL APPLICATION No.7955 of 2006

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SPECIAL CIVIL APPLICATION No.7970 of 2006

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SPECIAL CIVIL APPLICATION No.7971 of 2006

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SPECIAL CIVIL APPLICATION No.7973 of 2006

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SPECIAL CIVIL APPLICATION No.7974 of 2006

WITH

SPECIAL CIVIL APPLICATION No.11074 of 2006

TO

SPECIAL CIVIL APPLICATION No.11097 of 2006

WITH

SPECIAL CIVIL APPLICATION No.24952 of 2006

WITH

SPECIAL CIVIL APPLICATION No.4163 of 2012

WITH

CIVIL APPLICATION No.4040 of 2012

IN

SPECIAL CIVIL APPLICATION No.4163 of 2012

WITH

SPECIAL CIVIL APPLICATION No.4170 of 2012

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CIVIL APPLICATION No.4042 of 2012

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SPECIAL CIVIL APPLICATION No.4170 of 2012

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SPECIAL CIVIL APPLICATION No.4175 of 2012

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SPECIAL CIVIL APPLICATION No.4183 of 2012

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SPECIAL CIVIL APPLICATION No.4188 of 2012

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CIVIL APPLICATION No.4049 of 2012

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SPECIAL CIVIL APPLICATION No.4188 of 2012

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SPECIAL CIVIL APPLICATION No.4192 of 2012

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CIVIL APPLICATION No.4050 of 2012

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CIVIL APPLICATION No.4051 of 2012

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SPECIAL CIVIL APPLICATION No.4195 of 2012

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CIVIL APPLICATION No.4059 of 2012

IN

SPECIAL CIVIL APPLICATION No.4195 of 2012

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SPECIAL CIVIL APPLICATION No.4400 of 2012

TO

SPECIAL CIVIL APPLICATION No. 4412 of 2012

WITH

SPECIAL CIVIL APPLICATION No.4442 of 2012

TO

SPECIAL CIVIL APPLICATION No.4449 of 2012

WITH

CIVIL APPLICATION No.4208 of 2012

IN

SPECIAL CIVIL APPLICATION No.4449 of 2012

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SPECIAL CIVIL APPLICATION No.4451 of 2012

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CIVIL APPLICATION No.4209 of 2012

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SPECIAL CIVIL APPLICATION No.4456 of 2012

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CIVIL APPLICATION No.4213 of 2012

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SPECIAL CIVIL APPLICATION No.4456 of 2012

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SPECIAL CIVIL APPLICATION No.4957 of 2012

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SPECIAL CIVIL APPLICATION No.5699 of 2012

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SPECIAL CIVIL APPLICATION No.5700 of 2012

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SPECIAL CIVIL APPLICATION No.5701 of 2012

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SPECIAL CIVIL APPLICATION No.5701 of 2012

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SPECIAL CIVIL APPLICATION No.5702 of 2012

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SPECIAL CIVIL APPLICATION No.5703 of 2012

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CIVIL APPLICATION No.4748 of 2012

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CIVIL APPLICATION No.4750 of 2012

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SPECIAL CIVIL APPLICATION No.5705 of 2012

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SPECIAL CIVIL APPLICATION No.5708 of 2012

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CIVIL APPLICATION No.4752 of 2012

IN

SPECIAL CIVIL APPLICATION No.5708 of 2012

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SPECIAL CIVIL APPLICATION No.5709 of 2012

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CIVIL APPLICATION No.4753 of 2012

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CIVIL APPLICATION No.4757 of 2012

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CIVIL APPLICATION No.4792 of 2012

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TO

SPECIAL CIVIL APPLICATION No.5752 of 2012

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CIVIL APPLICATION No.4802 of 2012

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SPECIAL CIVIL APPLICATION No.5747 of 2012

TO

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SPECIAL CIVIL APPLICATION No.5753 of 2012

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SPECIAL CIVIL APPLICATION No.5904 of 2012

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SPECIAL CIVIL APPLICATION No.3257 of 2012

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CIVIL APPLICATION No.3038 of 2012

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SPECIAL CIVIL APPLICATION No.3283 of 2012

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CIVIL APPLICATION No.3087 of 2012

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SPECIAL CIVIL APPLICATION No.3305 of 2012

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CIVIL APPLICATION No. 3088 of 2012

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SPECIAL CIVIL APPLICATION No.3304 of 2012

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SPECIAL CIVIL APPLICATION No.3327 of 2012

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CIVIL APPLICATION No. 3110 of 2012

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SPECIAL CIVIL APPLICATION No.3327 of 2012

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SPECIAL CIVIL APPLICATION No.3329 of 2012

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SPECIAL CIVIL APPLICATION No.3330 of 2012

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CIVIL APPLICATION No. 3112 of 2002

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SPECIAL CIVIL APPLICATION No.3330 of 2012

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SPECIAL CIVIL APPLICATION No.3335 of 2012

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SPECIAL CIVIL APPLICATION No.3337 of 2012

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CIVIL APPLICATION No. 3119 of 2012

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CIVIL APPLICATION No. 3139 of 2012

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SPECIAL CIVIL APPLICATION No.3370 of 2012

WITH

SPECIAL CIVIL APPLICATION No.3491 of 2012

WITH

SPECIAL CIVIL APPLICATION No.3637 of 2012

WITH

SPECIAL CIVIL APPLICATION No.3714 of 2012

WITH

SPECIAL CIVIL APPLICATION No.3715 of 2012

For Approval and Signature:

HONOURABLE THE ACTING CHIEF JUSTICE

MR.BHASKAR BHATTACHARYA

AND

HONOURABLE MR.JUSTICE **J.B.PARDIWALA**

==========

1	Whether Reporters of Local Papers may be allowed to see the judgment ?
2	To be referred to the Reporter or not ?`
3	Whether their Lordships wish to see the fair copy of the judgment ?
4	Whether this case involves a substantial question of law as to the interpretation of the constitution of India, 1950 or any order made thereunder ?
5	Whether it is to be circulated to the civil judge ?

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AVANI EXPORTS & OTHERS

Versus

COMMISSIONER OF INCOME TAX RAJKOT & ORS.

==========

Appearance:

MR SN SOPARKAR with MS SWATI SOPARKAR, MR JAYAKUMAR WITH MR MANISH K KAJI, MR TUSHAR P HEMANI, MR MANISH J. SHAH, MR KETAN H. SHAH, MR YOGEN N. PANDYA, MR AKHILESHWAR SHARMA, ADVOCATES for the Petitioners.

MR MOHAN PARASHARAN, ASG WITH MR. G.C. SRIVASTAVA, SPECIAL COUNSEL, MR GAURAV DHINGA, MR MANISH R. BHATT, SR. COUNSEL WITH MRS. MAUNA BHATT WITH MR. MISHRA, MR. PRANAV G DESAI, MS. PAURAMI SHETH, MR. KETAN PARIKH, MR SUDHIR MEHTA, SENIOR STANDING COUNSEL FOR INCOME TAX DEPARTMENT.

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CORAM :	HONOURABLE THE ACTING CHIEF JUSTICE MR.BHASKAR BHATTACHARYA
	and
	HONOURABLE MR.JUSTICE J.B.PARDIWALA

Date : 02/07/2012

ORAL JUDGMENT

(PER : HONOURABLE THE ACTING CHIEF JUSTICE MR.BHASKAR BHATTACHARYA)

1. All these writ-applications were taken up together pursuant to the order passed by the Supreme Court of India. By the said order, the Apex court transferred these matters pending before various High Courts to this court for considering whether the severable parts of the 3rd and 4th proviso to section 80 HHC (3) of the Income Tax Act, 1961 [the Act, hereafter] are *ultra vires* Articles 14 and 19 (1) (g) of the Constitution of India. By way of consequential relief, the petitioners have prayed for direction upon the respondents not to give effect to those severable parts of the third and the fourth proviso to section 80 HHC (3) of the Act and for prohibiting them from taking any action by taking aid of those provisos.

2. The facts giving rise to the filing of these matters may be summed up thus:

2.1 In all these matters, the constitutional validity of insertion of conditions in the third and the forth provisos to section 80 HHC (3) of the Act by amendment of Taxation Laws (Second Amendment) Act, 2005 with retrospective effect is challenged. According to the petitioners, the benefit of deduction under section 80 HHC of the Act was available to them from the Assessment Year 1988-99 to the Assessment Year 2004-05. They claim that they have settled their affairs based on availability of the said benefit up to 31st March 2004 and by the amendment challenged in these writ-applications, the respondents seek to take away the benefit retrospectively after the

entire period of benefit is over on 31st March 2004. They contend that the amendment seeks to grant some conditional benefit selectively to certain assessees in January 2006 with retrospective effect for the period from A.Y. 1988-89 to A.Y. 2004-05. The petitioners allege that the impugned portion of the said amendment discriminates between the assessee falling in the same class, which is prohibited by Article 14 of the Constitution of India and at the same time, imposes new pre-conditions retrospectively for being eligible for deduction under section 80 HHC of the Act. The petitioners further contend that the said amendment denies retrospectively the deduction under section 80 HHC to the exporters having turnover of more than Rs.10 Crore although as evident from the history of deduction u/s 80 HHC, the exporters were encouraged to increase the turnover as an incentive to avail the deduction u/s 80 HHC. The petitioners point out that the amendment grants deduction with respect to export having turnover of more than Rs.10 Crore whose products are notified or eligible for both Duty Drawback Scheme and Duty Entitlement Pass Book Scheme [for short, DEPB hereafter] and the rate of duty draw back is higher than DEPB while rest of the exporters are singled out without there being any rational basis for making the aforesaid classification. The petitioners contend that the said denial is against the principle of promissory estoppel. They further contend that the amendment seeks to upset the financial structuring based on which the assessees had arranged and planned their business affairs and the amendment also

upsets the settled law laid down by the Tribunal which is binding on the petitioners and the respondents.

3. These applications have been opposed by the respondents thereby contending that the amendment made in section 80 HHC by the Taxation Law and (Amendment) Act, 2005 with retrospective effect from 1st April 1998 by way of adding second, third, forth and fifth proviso to section 80 HHC (3) and inserting clause (iiid) and (iiie) in section 28 with effect from 1st April 1998 and 1st April 2001 respectively was a beneficial legislation conferring the benefit of section 80 HHC on the assessees also in respect of the profit on the transfer of the DEPB Scheme and Duty Free Replenishment Certificate which was not available before this amendment. According to the respondents, it would appear from paragraph 3 of the Statement of Objects and Reasons made while introducing the Taxation Laws (Second Amendment) Bill 2005 that in order to extend certain tax incentive to the export business with effect from the Assessment Year 1998-99, it was proposed that the deductions allowable under section 80 HHC of the Act for export business may be extended to any profit on transfer of the DEPB Scheme or the Duty Free Replenishment Certificate subject to certain specified conditions.

3.1 The respondents further contend that the classification of the assessees on the basis of quantum of export turnover being more or less than Rs.10 Crore is a reasonable classification permitted by

Article 14 of the Constitution of India. The respondents contend that the classification in terms of quantum of income or quantum of turnover is embedded all through in the Act as can be seen from Section 44AA(2), 44AB and 139(4A). It is further contended by the respondents that the beneficial nature of the impugned amendments made by the Taxation Laws (Amendment) Act, 2005 in section 80 HHC is further clear from the first proviso to section 80 HHC(3) added by the same amendment Act providing for set off of loss worked out under clauses (a), (b) or (c) of section 80 HHC (3) against proportionate amount of ninety per cent of export incentives with effect from 1st April 1992. According to the respondents, it thus becomes clear from the fact that based on the ratio of the Supreme Court decision in the case of **IPCA LABORATORIES v/s DCIT** reported in **266 ITR 521 (SC**) it had been held in several decisions that in case the result of computation under section 80 HHC (3) (a), (b) and (c) is a loss, no deduction was at all admissible with reference to the export incentives under the proviso to section 80 HHC (3) of the Act. According to the respondents, by the proposed amendment, the law was rationalized in favour of the assessees by overruling the above decisions, which were in favour of the Revenue and consequently, retrospectiveness of such legislation beneficial to the assessee is not questionable. The respondents have, therefore, prayed for dismissal of the writ-applications.

4. Mr. S.N. Soparkar, Mr. Manish J. Shah, Mr. Ketan H. Shah, Mr. Jayakumar, Mr. Tushar Hemani and Mr. Akhileshwar Sharma, learned advocates made submissions in support of the petitioners while Mr. Mohan Parasaran, learned Additional Solicitor General, Mr. G.C. Srivastava, Mr. Gaurav Dhingra, Mr. Manish R Bhatt with Ms. Mauna R Bhatt, Mr. Pranav G Desai, Ms. Paurami Sheth, Mr. Ketan Parikh, Mr. Sudhir Mehta and Mr. Mishra appeared on behalf of the respondents to oppose the writ-applications.

5. The sum and substance of the contentions made by the learned counsel on behalf of the petitioners may be enumerated below:-

5.1. **The impugned Amendment is arbitrary and unreasonable:**

According to the learned counsel for the petitioners, the benefit, which was conferred from A.Y. 1998-99 to A.Y. 2004-05, was obviously the basis of entire financial structuring of the petitioners' business including the pricing of export, payments of dividends, distribution of profits etc. They contend that the impugned amendment purports to retrospectively take away the benefit on the basis that exporter having turnover of more than Rs.10 Crore will get the benefit if he has evidence to prove that he had an option to choose either duty drawback or DEPB and that he chose DEPB, even when he was entitled to higher benefit under the duty drawback scheme. This, according to the learned counsel for the petitioners, is an absurd

condition which no sensible person can ever exercise the option to choose a scheme under which he would get lesser benefit. Moreover, according to the learned advocates for the petitioners, to impose such condition retrospectively and requiring such person to prove that he had such an option in past and he had exercised it to avail lesser benefit is totally arbitrary, capricious, unjust, unfair, discriminatory and violative of both Article 14 & Article 19 (1) (g) of the Constitution. In support of such contention, the learned advocates for the petitioners rely upon the following decisions:-

(1) **MARADIA CHEMICALS LTD. VS. UNION OF INDIA** reported in (**2004) 4 SCC 311 : AIR 2004 SC 2371**

(2) **MALPE VISHWANATH ACHARYA & ORS.** Vs. **STATE OF MAHARASHTRA & ANR.** reported in **1998 (2) SCC 1 : 1998 SC 602**.

(3) **WELFARE ASSOCIATION A.R.P**. reported in (**2003) 9 SCC 358 : AIR 2003 SC 1266**

5.2. **The Amendment is violative of Article 14:**

On the above aspect, the learned counsel for the petitioners submit that the impugned amendment places two assessees of the same class on different footing and the amendment, in fact, seeks to take away the deduction from one retrospectively and continues to give the benefit to others although both are in the same class. Learned counsel

for the petitioners contend that the impugned amendment thus violates Article 14 of the Constitution of India inasmuch as it is unreasonably discriminatory and leads to class legislation, which is not permissible by the Constitution of India. They contend that in the case of some assessees whose export turnover is more than Rs.10 Crore and who have claimed deduction u/s. 80 HHC on DEPB / DFRC in their return of income and the assessments have become final by the Respondents accepting the same cannot be reopened after a period of 6 years (31st March 2005) if no assessment is made u/s. 143 (3) and after a period of 4 years (31st March 2003) if the assessments are made under Section 143 (3). In this class of assessee, according to the petitioners, the deduction is granted without compliance of the conditions imposed by the Taxation Laws (Second Amendment) Act, 2005, since the assessments of these assessees cannot be reopened after 31st March 2005 and 31st March 2003 as the case may be. In contrast to the above, in the case of the assessees whose turnover is more than Rs.10 Crore, and who have claimed deduction u/s. 80 HHC on DEPB/DFRC and whose assessments are pending either before the Assessing Officer or the Appellate Authority would be required to comply with those two conditions retrospectively. According to the learned counsel for the petitioners, two assessees having export turnover of more than Rs.10 Crore are discriminated inasmuch as the assessees whose assessments have become final is not required to comply with the two conditions and would avail deduction u/s. 80

HHC as against the assessees whose assessments are pending and who would be required to comply with the two conditions. According to the learned advocates for the petitioners, exporters and non-exporters constitute two separate classes but within the class of exporter, further classification based on turnover would be unreasonable and even assuming that classification based on turnover is permissible, the amendment further makes a sub-class within the class of exporters having turnover of more than Rs.10 Crore, because it results into following 4 sub-classes:-

[1]. Exporters eligible for drawback and DEPB and rate of drawback is higher;

[2]. Exporters eligible for drawback and DEPB and rate of drawback is lower;

[3]. Exporters eligible for DEPB and not drawback;

[4]. Exporter eligible only for drawback and not DEPB.

5.2.1 Learned counsel for the Petitioners further submit that the impugned amendment further classifies the exporter into two classes, first, whose assessments have become final and secondly, whose assessments are pending. Such classification, according to them, is unintelligible and not in consonance with or have no relation with deduction u/s. 80 HHC and therefore, violative of Article 14 of the Constitution. They contend that sub-classification sought to be

introduced/resulting due to impugned amendment has no rationale nexus with the object of the amendment and therefore, fails the test of Article 14. They contend that this leads to discrimination between the assessee placed in the same class by giving them unequal treatment and therefore, would be grossly violative of Article 14 of the Constitution of India and thus, the impugned amendment is *ultra vires* and bad in law.

In support of this contention, they rely upon the decision in the case of **S. K. DUTTA, ITO & ORS.** V/s **LAWRENCE SINGH INGTY** reported in **68 ITR 272(SC) = AIR 1968 SC 658.**

5.3. <u>The amendment in its present form does not entitle a single assessee to claim benefit of incentives under Section 80HHC of the Act. So it makes the section completely unworkable:</u>

While interpreting a statutory provision, according to the learned counsel for the petitioners, construction of provisions of the statute, which leads to absurdity, should not be preferred. The learned advocates for the petitioners contend that if the strict and literal construction of the statute is applied, then there is an absurd proposition that no assessee would be in a position to fulfill the twin conditions as laid down by the amendment under challenge. Resultantly, no assessee would ever get this benefit.

In support of such contention, they rely on the judgments of the Supreme Court in the following cases:

1. **CIT** vs. **HINDUSTAN BULK CARRIERS** reported in **259 ITR 449, : AIR 2003 SC 3942**.

2. **K. P. VARGHESE vs. ITO & ANR**. reported in (**1981) 131 ITR 597 (SC) @ 604 = AIR 1981 SC 1922**.

3. **CIT vs. J.H. GOKHLE** reported in **156 ITR 323(SC) : AIR 1985 SC 1698**.

5.4. <u>The burden to prove that the restrictions imposed by the Act are reasonable is on the State.</u>

According to the learned advocates for the petitioners, in any case, the amendment is completely arbitrary, irrational and unreasonable and the legislature is completely silent as to what is the rationale and object behind introducing this amendment. According to them, it is for the State to justify how the amendment is not arbitrary, unreasonable and irrational and thus, not violative of Art. 19 (1) (g) of the Constitution and the State having failed to disclose such reasons, it should be set aside.

In support of the aforesaid contention, the learned advocates for the petitioners rely on the following two judgments of the Supreme Court:

1. **MOHAMMED FARUK vs. STATE OF MADHYA PRADESH & ORS**. reported in **1969 (1) SCC 853 : AIR 1970 SC 93**.

2. **MESSRS VIRAJLAL MANILAL & CO. & ORS**. Vs. **STATE OF MADHYA PRADESH & ORS**. reported in **1969 (2) SCC 248 : AIR 1970 SC 129**

5.5. **In any case, amendment cannot have retrospective effect:**

The learned advocates for the petitioners further submit that the impugned amendment is unreasonable, arbitrary, violative of fundamental rights guaranteed under the Constitution and *ultra vires* inasmuch as though it is a substantive amendment, the same is inserted with retrospective effect. According to them, it is well settled that only procedural amendments can have retrospective effect and any amendment, which is otherwise substantive in nature, can never have a retrospective effect, unless the same is beneficial to an assessee. They contend that in the facts of the present case, the impugned explanation added to section 80-IA(4) of the Act is a substantive amendment substantially curtailing the right of an assessee to claim the deduction under section 80HHC of the Act, which was otherwise available to it. Thus, according to them, the retrospective amendment is unduly oppressive and confiscatory.

5.6. <u>Promissory Estoppel and Legitimate Expectations:</u>

Lastly, the learned advocates for the petitioners submit that it would appear from the history of section 80HHC of the Act that it was given to encourage the exports, and the petitioners, by virtue of the impugned amendment retrospectively cannot be deprived of the incentives / deductions. According to them, such an amendment is against the principle of promissory estoppel. They contend that the assessees have arranged their business affairs in the past when there were no conditions on the statute book, which is now sought to be upturned by making the amendment retrospectively and thus, is contrary to the representation as evident from history of deduction u/s. 80HHC of the Act. They contend that the principle of promissory estoppel applies in all areas of activities of a State including legislative field.

In support of such contention, they rely on the following judgments:

1. **MOTILAL PADAMPATH SUGAR MILLS LTD.** reported in **1979) 2 SCC 409 : AIR 1979 SC 621.**

2. **STATE OF PUNJAB V. NESTLE INDIA LTD.** reported in **(2004) 6 SCC 465 : AIR 2004 SC 4559.**

3. **MAHAVIR VEGETABLES (PVT.) LTD.** reported in **(2006) 3 SCC 620.**

764. UP POWER CORPORATION LTD. reported in **(2008) 2 SCC 777 : AIR 2008 SC 693.**

5. ACC LIMITED VS ASST. COMMISSIONER reported in **(2011) 46 VST 244 (CAL).**

(6) PRASAD FORMS PVT. LTD. VS. ASST. COMMISSIONER reported in **(2005) 140 STC 11 (CAL).**

6. Mr. Parasaran, the learned Additional Solicitor General, appearing on behalf of the Union of India and Mr. Bhatt, the learned Senior Advocate appearing on behalf of the Income Tax Authority have, on the other hand, opposed the aforesaid contentions of the petitioners and they have advanced their submission in the following ways:

6.1 Challenge in the petitions is restricted to the severable parts of the Third and Fourth proviso to section 80HHC (3) but not to:

(a) Insertion of section 28(iiid), 28(iiie), and,

(b) Reduction of 90% of these amounts as per clause (baa) of Explanation below to section 80HHC (4C).

According to the learned counsel, the net result is that as per Explanation (baa), the profits of the business are required to be reduced by 90% of any sum referred to in section 28(iiia) to 28(iiie) as also receipts by way of brokerage, commission, etc. and any other

receipts of similar nature included in such profits. Thus, there is no dispute that in the instant cases, profits of the business are required to be reduced by 90% of the sum referred to in section 28(iiid) and 28(iiie). The learned counsel for the Revenue point out that there is no challenge to such reduction and according to them, rightly such reduction is not challenged, for the following reasons:

[a]. When the formula of computation of deduction of section 80HHC(3) was substituted by the Finance Act [No. 2 of 1991] w.e.f. 1.4.1992, it has been specifically noted that the existing formula (pre 1.4.1992) gave a distorted figure in respect of profits when receipts like interest, commission, etc. which did not have the element of turnover were included in the profit and loss account.

[b]. As per the scheme of section 80HHC, such deduction is given on the profits derived from the export as per sub-section (1) and sub-section (3) explains the phrase "profits derived from exports" to mean the amount which bears to the profits of business in the same proportion as the export turnover to the total turnover of the business carried out by the assessee. Thus, the scheme of 80HHC for computing the profits derived from exports is thus first to exclude "independent incomes" and "export incentives" from the profits of business, but since the legislature intended to give deduction under section 80HHC in respect of "export

incentives" it provided for the deduction by way of First to Fourth Proviso appended to sub-section (3) of section 80HHC. The rationale of first excluding the export incentives from the "profits of business" and then loading it back for calculating deduction under section 80HHC by way of provisos is attributed to the concept that the export incentives are not strictly to be construed as profits of business as the effective source of these incentives are the government schemes.

[c]. After the decision of the Supreme Court in the case of **TOPMAN EXPORTS** reported in **342 ITR 49(SC)**, upholding the decision of Special Bench reported in **TOPMAN EXPORTS vs. INCOME-TAX OFFICER** reported in **[2009] 318 ITR (AT) 87**, it can be safely stated that the issue which now remains is only with regard to excess of realization over the face value of DEPB.

[d]. In the case of DEPB, any premium over and above the face value on transfer cannot be stated to be in the nature of export incentives and it would classify under the category of "independent income". Thus, any independent income in any event was required to be reduced as per explanation (baa). The rationale of treating this premium as independent income is simple, as such premium is determined by market forces of demand and supply in creating premium in the market but the dominant element of premium in such a situation would be due

to higher value of benefit available to intended buyer in the market and when such premium is created in the market due to market force of demand and supply it partakes the colour and character of independent income.

6.2 According to the learned counsel for the Revenue, to contend that the premium/profit on transfer of DEPB is a step removed from the actual activity and derivation of profits from export, reliance was placed on:

(a) **TOPMAN EXPORTS vs. INCOME-TAX OFFICER** reported in **[2009] 318 ITR (AT) 87** at page 145 [para 79].

(b) **CIT vs. K. RAVIONDRANATHAN NAIR** reported in **[2007] 295 ITR 228 (SC).**

(c) **COMMISSIONER OF INCOME TAX vs. STERLING GOODS** reported in **[1999] 237 ITR 579 (SC)** at Page 582

(d) **LIBERTY INDIA vs. COMMISSIONER OF INCOME-TAX** reported in **[2009] 317 ITR 218(SC)** at Page 232.

6.3 The learned counsel for the Revenue contend that assuming the profit is export incentive profit, by a specific exclusion in explanation (baa) the same is reduced from the Business Profits.

6.4 The learned counsel for the Revenue point out that the main averments of the petitioners are as under:

[a]. The benefit of deduction under section 80HHC in respect of profits arising from DEPB entitlements was available to them from A.Y. 1998-99 to A.Y. 2004-05.

[b]. They have already acted on the basis of such benefits available to them and their entire financial restructuring including pricing of export was based on such benefits existing since 1998.

[c]. The amendment seeks to take away the available benefits retrospectively after the entire period of benefit is over on 31st march 2004

[d]. The amendment granting conditional benefits selectively to certain assessees discriminates between the assessees falling in the same class which is violative of Article 14 of the Constitution.

[e]. The conditions stipulated in third and fourth Provisos to sub-section (3) of section 80HHC are arbitrary, capricious, unjust and discriminatory thereby violating both Articles 14 and 19(1)(g) of the Constitution.

6.5 The Revenue contends that the aforesaid averments are incorrect both factually as also legally. In the first place, it is pointed out that prior to the impugned amendments, the Income Tax Act 1961 did not at any stage grant benefit of any kind to the exporters in respect of profits derived by them from the transfer/sale of their DEPB

entitlements. This, according to the Revenue, is evident from the provisions of the Act as these existed prior to the impugned amendments.

6.6 The Revenue submits that the Ministry of Commerce, with a view to give boost to the exports, does introduce from time to time certain schemes of cash assistance or other direct/indirect incentives under the EXIM Policy of the Govt. However, such incentives do not automatically get the analogous benefit under the direct tax laws. Parliament has to step in to amend the IT Act to provide corresponding benefits under the IT Act. The incentives which were included for benefits under the IT Act prior to the impugned amendments, it is pointed out, were only the following:

(a) Profit on sale of license under Imports(Control) order 1955 made under Imports and Exports (Control) Act of 1947. (Section 28(iiia))

(b) Repayment of customs/excise duty under the Customs and Central Excise Duties Drawback Rules 1971 (Section 28(iiic))and

(c) Cash assistance under any scheme of the Government(Section 28(iiib))

6.7 In the year 1997, it is submitted, the Ministry of Commerce introduced a new scheme called Duty Entitlement Pass Book Scheme (DEPB) under the EXIM Policy announced under Section 5 of the Foreign Trade (Development and Regulation) Act of 1992. A similar scheme named Duty Free Replenishment Certificate (DFRC) was introduced in the year 2000 and both of these schemes granted a new and distinct incentive to the exporters. These Schemes did not stipulate that the exporters would be entitled to higher deduction of export profits under the IT Act 1961 if they chose to sell their entitlements to third parties. Parliament did not prefer to amend the Act to provide for higher deduction of export profits on sale of these entitlements. Thus, according to the Revenue, while the exporters were entitled to take credit against the Customs Duty leviable at the time of import of goods or to sell these licences to third parties, in either event they were not entitled to any benefit under direct taxes (S.80HHC).

6.8 In the circumstances, the Revenue contends that the tax authorities denied benefits by way of higher deduction of export profits and rejected the claims of the taxpayers in respect of these two schemes (DEPB and DFRC). As, according to the Revenue, highly irrational and legally untenable view taken by one of the Benches of ITAT that the assessees were entitled to claim such benefits under section 28(iv) was not accepted by the Revenue. (In the case of P.G.

Enterprises). This led to a spate of litigation and huge arrears of taxes became pending for realization.

6.9 The Revenue submits that it was in this backdrop that the proposal to amend the law (IT Act 1961) was moved and passed by Parliament. The amendment sought to:

(a) grant unconditional benefit of higher deduction of export profits where the sale of DEPB/DFRC was made by exporters having turnover of less than Rs. 10 crore (small and medium exporters) and

(b) grant benefit of such higher deduction subject to fulfillment of certain conditions by such exporters who have export turnover exceeding Rs. 10 Crore.

In either case, according to the Revenue, the benefits were given retrospectively from the years when such schemes came into operation.

6.10 In the light of above, the learned Counsel for the Revenue referred to debate/discussion in the House while moving the Bill and contended that the premium is simply a business profit as the income earned is not in foreign exchange but in Indian rupees and does not arise out of export activity or import activity but arises on trading of license. It is also pointed out that reduction in any event was required to be effected as per Explanation (baa) but only with a view to give

benefit, Second to Fourth Provisos were inserted.

6.11 Thus, according to the Revenue, it is factually incorrect to suggest that the petitioners were entitled to benefits of higher deduction of export profits from A.Y. 1998-99. Their claims advanced in the returns of income filed before tax authorities, according to the Revenue, were wholly untenable since those were based on a complete misunderstanding of law that the announcement of the scheme would automatically allow them not only to take credits against payment of import duty but also claim higher deduction under section 80HHC in the event of sale of such entitlements.

6.12 Thus, according to the Revenue, the impugned amendments gave certain benefit/concession to the exporters with retrospective effect, which was hitherto not available. It, the Revenue proceeded, did not seek to withdraw any benefit/concession already available nor did it seek to levy any new charge of tax retrospectively. The grant of a benefit with retrospective effect, according to the Revenue, does not create any prejudice against the taxpayer and cannot form the ground for challenging the validity of the impugned amendment.

6.13 Further, according to the Revenue, a rationale that these independent incomes would not be part of computation of section 80HHC, is also clear if explanation (ba) defining total turnover is perused and so interpreted by the Supreme court in the case of **CIT V. LAXMI MACHINE WORKS 290 ITR 667 (SC)** which confirms **CIT V.**

SUDARSHAN INDUSTRIES LIMITED 245 ITR 769 (BOMBAY).

6.14 The Revenue submits that the contention of the assessee also does not hold good as:-

A) 80HHC grants deduction for "profits derived from exports". For an assessee having both export and domestic turnover the profits of business would be embedded in both “profits derived from exports" and “profits derived from local sales".

B) Basic scheme of 80HHC is apportionment on the basis of turnover to compute the “profits derived from exports" embedded in the “profits derived from business". Thus under this section, "profits derived from exports"= "profits derived from business" X export turnover / total turnover.

C) In this scheme of apportionment, if “profits derived from business" include non turnover based receipts/ income then the scheme of 80HHC would become unworkable as illustrated from the following numerical example:

(I) Case where no non-turnover based receipts are there: Say export turnover is Rs. 500/-. Say Domestic turnover is Rs. 1500/-, i.e. Total turnover is Rs. 2000/-. Say profits from business are purely turnover based and are Rs. 200/-. In such scenario

as per the above formula “profits derived from exports"= 200 x 500/2000=50

(II) Now take a case where "profits derived from business" include non turnover based income in it be they from interest, rent, commission or be they from profit on sale of DEPB [in view of the use of the phrase other receipts of such nature used in (baa)] then the scheme of 80HHC becomes UNWORKABLE as seen from the example below: Say export turnover is Rs. 500/-. Say Domestic turnover is Rs. 1500/-, i.e. Total turnover is Rs. 2000/-. Say profits from business are now Rs. 300/- which includes turnover based Rs. 200/- and non turnover based Rs. 100/-. In such scenario as per the above formula “profits derived from exports"= 300 x 500/2000=75.

Thus, according to the Revenue, in this manner just by including non turnover based income in it's income under the head "profits from business" an assessee is artificially able to increase it's claim of deduction.

It was to overcome this unintended benefit possible due to inclusion of non-turnover based incomes that, according to the Revenue, the Explanation (baa) was amended in 1992 to provide for exclusion of

interest, rent commission and receipts of similar nature AND THUS EVEN AS PER THE SECTION AS IT ORIGINALLY STOOD IN AY 1998 assessees could not have claimed benefit of deduction u/s 80HHC on profit from sale of DEPB because these non turnover based receipts were to be excluded even as per the amendments made in 1992.

6.15 Whenever, the Revenue submits, the Legislature wanted to grant benefit of profit on sale of export incentives which was not within the normal profits of business, properly so called, a specific inclusion was made in section 28, that is to say, insertion of section 28(iiia) etc.. Thus, according to the Revenue, the provisions of section 80HHC were redesigned to restrict the tax benefit to profits derived from the export of goods which were realized in convertible foreign exchange and not in respect of any incidental income in Indian currency. Wherever the Legislature wanted to grant benefit with regard to such incidental income, for example, profit from sale of EXIM scripts, according to the Revenue, the provision was so made and formula was accordingly applied.

6.16 The Revenue points out that the main contention of the petitioners is that the benefit/deduction which was granted earlier is now sought to be withdrawn retrospectively. This contention, according to the Revenue, is wholly misconceived as can be seen from the above inasmuch as on DEPB profit no such benefit/deduction was earlier allowable. It is only because of Second to Fourth proviso,

according to the Revenue, that 90% of profits on DEPB though reduced from the profits of business [as per explanation (baa)], is sought to be again reloaded for grant of deduction under section 80HHC. Thus, it is submitted that in 2005, for the first time the statute granted deduction in respect of DEPB profit, from retrospective date of 01/04/1998, subject to fulfillment of certain conditions insofar as Third and Fourth proviso are concerned.

6.17 It is a settled position of law, the Revenue continues, that once the Legislature wants to grant benefit to a particular class of assesses, it is open for it to do so. The classification based on turnover is therefore undoubtedly a reasonable classification and in fact various Income Tax sections itself, for example 44AA (2), 44AB and 139(4A) recognize such reasonable classification based on turnover. If the Legislature, according to the Revenue, has thought it fit to grant the benefit without imposing any conditions to the assessees having turnover less than Rs. 10 crore and imposing certain conditions to be fulfilled by the assessees having turnover of more than Rs. 10 crore, the same cannot be stated to be an unreasonable classification.

6.18 Classification based on turnover, it is pointed out, has been made pursuant to recommendation of Economic Advisory Council, which is based on thorough analysis and also on the opinion rendered by the Ministry of Law and also of Dr.Rangarajan Committee Report. The impugned amendment, according to the Revenue, grants

unconditional benefits to the small and medium exporters (2nd Proviso) having export turnover of less than Rs. 10 Crore and conditional benefits to large exporters having turnover of over Rs. 10 Crore (3rd and 4th Proviso). This, the Revenue contends, is based on intelligible and reasonable classification widely recognized in matters relating to Direct Tax laws all over the world. Income tax, according to the Revenue, being a progressive levy is based on income classification in terms of both basis of taxation and the rate of tax. Persons having a certain income/turnover levels form a class by themselves. The impugned amendments, according to the Revenue, are neither unreasonable nor discriminatory nor violative of Article 14 of the Constitution. Exporters may form a broad category of taxpayers but the classification of small and medium exporters and big or large exporters depending upon their turnover levels is a reasonable classification and cannot be held to be discriminatory.

6.19 Classification based on turnover has been held to be valid in the following decisions as pointed out by the Revenue :-

(a) **THE STATE OF BOMBAY AND ANOTHER, V. THE UNITED MOTORS (INDIA) LTD. AND OTHERS** reported in **AIR 1953 SC 252** [Page 262 Para 29]

(b) **KERALA HOTEL AND RESTAURANT ASSOCIATION AND OTHERS, V. STATE OF KERALA AND OTHERS** reported in **(1990) 2 SCC 5002 = AIR 1990 SC 913 [**at Page 917 Para 8, Page 920 Para 24 and 26, Page 924 Para 34].

(c) **S KODAR vs. STATE OF KERALA** reported in **(1974) 4 SCC 422 = AIR 1974 SC 2272** at Page 2275 Para 16, 17.

(d) **BRITISH INDIA CORPORATION LTD. V/S. COLLECTOR OF CENTRAL EXCISE, ALLAHABAD AND OTHERS** reported in **AIR 1963 SC 104** [at Page 107 Para 12]

(e) **FEDERATION OF HOTEL AND RESTAURANT V. UNION OF INDIA AND OTHERS,** reported in **(1989) 3 SCC 634= AIR 1990 SC 1637** [at Para 46, 48, 54].

6.20 Parliament, according to the Revenue, has the necessary power to grant benefit/concession retrospectively to small exporters and deny similar benefits/concessions to large exporters on a reasonable classification of levels of income/turnover. Even a complete absence of third and fourth proviso could not have given any right to the petitioners to challenge the validity of the enactment on the ground sought to be raised by them. Hence, the Revenue submits that where the Proviso extends the benefits/concessions retrospectively subject to certain conditions, howsoever stringent these might appear to be, the validity of the impugned amendments cannot be assailed on the grounds of reasonableness or intelligible classification.

6.21 The question of denial of any benefit/concession or otherwise would arise in the present case, according to the Revenue, only if the Petitioners had any profits on the sale/transfer of their DEPB entitlements. It is very unlikely that any third party intending to acquire DEPB entitlement would pay anything more than the face

value of the license for the simple reason that he would get credit against the import duty only to the extent of the face value of these entitlements. Why should he pay more for acquiring credit entitlement against import of goods, the Revenue questions, when he can pay the duty in cash of a lesser amount for such imports? The petitioners, according to the Revenue, have not furnished details to show the amount of profits they derived on transfer of DEPB, which, according to them, is being denied the benefit due to the impugned amendments. In the absence of such details, the Revenue contends, the issues raised are merely academic and do not arise out of any real and substantial prejudice to the Petitioners. It is a settled principle, the Revenue submits, that the constitutional validity of an enactment cannot be addressed for academic considerations.

6.22 It is a settled position of law, according to the Revenue, that in taxing statute more laxity is permissible:-

(a) AIR 1987 SC 662 [**citation seems to be wrong**]

(b) **GOVERNMENT OF ANDHRA PRADESH AND ORS. V. SMT. P. LAXMI DEVI**. Reported in **AIR 2008 SC 1640 [**at Para 68, 69, 76]

(c) **BHAVESH D. PARISH AND OTHERS V. UNION OF INDIA AND ANOTHER,** reported in **AIR 2000 SC 2047**

6.23 It is a settled position of law, the Revenue contends, that when the Legislature enacts the law it is aware of the ground realities and

there is presumption qua constitutionality. [**K K BASKARAN v. STATE** reported in **(2011) 3 SCC 793**.

6.24 Thus, the Revenue contends, it is abundantly clear that though profit on DEPB is reduced in (baa) the benefit of deduction is sought to be given under Second to Fourth Provisos , with retrospective effect. It is also necessary to note that the insertion of Second to Fifth provisos were in fact of beneficial nature inasmuch as though the assessee was not entitled to deduction under section 80HHC in case of loss (in view of the decision in the case of **IPCA LABORATORY LTD. v DEPUTY C.I.T.** reported in **[2004] 266 ITR 521 (SC)**, by insertion of Fifth proviso this benefit is also sought to be given.

6.25 From the above, according to the Revenue, it can be seen that the object and intent of the legislation by introducing clause (iiid) and (iiie) was to clarify that the premium on sale of DEPB was business profit and not to be counted as exempt export profit and as a necessary consequence/corollary ,amendments have been made in clause (baa) read with Second to Fourth Provisos.

6.26 It is incorrect on the part of the petitioners to contend, according to the Revenue, that the conditions stipulated in clause (a) and (b) of Third proviso can never be fulfilled. For example, when an exporter has an option to choose between DEPB and duty draw back and for example rate of duty draw back is 10% and rate of DEPB is 8% and the exporter exercises option to choose DEPB having lower rate of 8%

of export value, in such a case premium is likely to be created in the market to the extent of difference of rate of duty drawback in excess of rate of DEPB., since intended buyer will get benefit of DEPB up to the rate of duty drawback applicable. In view of premium element, the exporter would have chosen DEPB.

6.27 Assuming but without admitting that the benefit is sought to be withdrawn by the 2005 Act, according to the Revenue, even retrospective levy is held to be permissible as held in the following cases:-

(a) **M/S. HIRALAL RATAN LAL V. THE SALES TAX OFFCER, SECTION III, KANPUR AND ANOTHER** reported in **(1973) 1 SCC 216 = AIR 1973 SC 1034** [Para 12, 17, 18A, 19, 20].

(b) **M/S. CHHOTABHAI JETHABHAI PATEL AND CO. V. UNION OF INDIA AND ANOTHER** reported in **AIR 1962 SC 1006** [at Para 41]

(c) **R.C. TOBACCO (P) LTD. vs. UNION OF INDIA** reported in **(2005) 7 SCC 725.**

(d) **EMPIRE INDUSTRIES LTD. AND OTHERS V. UNION OF INDIA AND OTHERS** reported **1985 3 SCC 314 = AIR 1986 SC 662** [at Para 49, 51].

(e) **NATIONAL AGRICULTURAL CO-OP. MARKETING FEDERATION vs. UNION OF INDIA** reported in **[2003] 260 ITR 548 (SC)**.

7. In order to appreciate the aforesaid questions, it will be profitable to refer first to the Statutory Resolution and Government Bill and the extract from the combined discussion on the statutory resolutions moved by Shri P. Chidambaram, which are quoted below:

"STATUTORY RESOLUTION AND GOVERNMENT BILL

> *Extract from the Combined discussion on the statutory Resolution regarding disapproval of taxation laws (Amendment) Ordinance, 2005 (No.4 of 2005) moved by Prof. Rasa Singh Rawat and consideration of the Taxation Laws (Second Amendment) Bill, 2005, moved by Shri P. Chidambaram (Resolution negatived and Bill Passed)*
>
> *SHRI P. CHIDAMBARAM: Now, I come to the sixth amendment. It is the one dealing with DEPB. This is not in the Ordinance. We did not bring it by way of an Ordinance. We are bringing it by way of a Bill and hon. Members are debating this provision. Now, this is rather a complicated question of law. I would take three or four minutes to explain this in as simple a language as possible. But please try to understand that it is a complicated question of law. You heard an hon. Member, Shri Varkala Radhakrishanan, saying that we should not have these Sections 3 and 4 because exporters do not deserve this benefit. You also heard other Members, like Shri Kashiram Rana saying that Sections 3 and 4 are necessary because exporters deserve the benefits, but we are denying the benefits to one section*

and giving the benefits to another section. So, there are two points of view. In fact, my notes here say that Shri Mohan Singh said that this provision is unnecessary for one reason and Shri Kashiram Rana said that this provision is unnecessary for another reason. Shri Varkala Radhakrishnan said that this provision is unnecessary because you are giving too many benefits to exporters (r54).

Therefore, it is not that I am giving benefit to some or not giving benefit to some. Let us look at the objective facts. DEPB came into force in the financial year 1997-98.

The first assessment year in respect of a return, in which a DEPB credit sale is claimed, is assessment year 1998-99 beginning on the 1 April, 1998. So, prior to 1 April 1998, this question did not arise. Section 80-HHC is a section which deals with deductible profits. If you come under section 80-HHC, the profits are not taxable. That section was phased out by the previous Government and the last date for operation of that section was 31.3.2005. Therefore, this situation does not arise after 1.4.2005. I hope, I am making myself clear to the hon. Members. We are now dealing with only the period 1.4.1998 to 31.3.2005. That is a period of about seven years. This problem did not arise before 1.4.1998. This problem does not arise after 1.4.2005. In this period of seven years, the relevant sections – I am not getting into an exposition of the law – are section 28 and section 80-HHC. These are the two sections which are relevant. Now, the Department's interpretation is that DEPB credit sale – I will explain what it is – is not export profit.

What is a DEPB credit sale? A DEPB credit sale is, that on your DEPB Passbook, if you have certain credits in your favour you can import items against the credit without paying duty. But you can also sell the credit to another importer. If you actually import it is part of export-import. If you sell it to another importer and make a profit on that – the premium, it is not export profit. It is a simple business profit because the income you earn is not in foreign exchange, it is in Indian rupees. It does not arise out of export activity or import activity. It arises because you are trading in a "Licence", which has a premium in the market. So, the Department took the view that it does not fall under section 28 read with section 80-HHC. I am not going into the sub-sections. Therefore this is not to be counted as exempted export profit. This must be added back as taxable profit. The assessees took a different view. Please remember, the first assessment in respect of this was filed only in the assessment year 1998-99. Some exporters paid; some exporters did not pay. Some exporters paid but disputed. Some assessing officers assessed it as taxable profit. Some assessing officers exempted it as exempted profit. That is bound to happen. When so many assessments take place all over the country, there is bound to be different assessments – income tax or sales tax or whatever. Ultimately, one case went up to the Income-tax Appellate Tribunal. The assessing officer took the view that this is not exempted profit; this is taxable profit. The assessee went in appeal. In appeal, the ITAT observed that the case falls under section 28(iv) not under section 28-(iii)(a), (iii)(b) or (iii)(c). It falls under section 28(iv). Then, the Tribunal gave a judgment, which I find as a lawyer difficult to understand. But, with great respect to the Tribunal which

is entitled to take a view, the Tribunal gave a judgment that although it falls under section 28(iv), it does not fall under section 80-HHC 'Explanation" (baa[mks55])

Therefore, it ruled on a new interpretation of the law in favour of the assessee and the Department has gone up in appeal to the Delhi High Court. Now, there are two courses open to me. I could have said: "Let us wait for the Delhi High Court's judgment. One of them will win and one of them will lose. They are bound to go to the Supreme Court. So, let us wait for the Supreme Court's judgment." It would have taken a minimum of ten years to settle this issue which arises – please remember – only between 1.4.1998 and 31.3.2005. It is today an academic issue. We are only dealing with seven assessment years. I could have waited for ten years. Thousands of rupees would have been spent by everybody fighting litigation at every level – before the Assessing Officer, before the Appellate Commissioner, before the ITAT, before the High Court and before the Supreme Court. So, we said: "All right. We will look into this matter. We will try to find a solution which does not affect the revenue and which tries to give some relief to the exporter."

Exporters, of course, have only argued that what Shri Kashiram Rana argued today very articulately saying "give exemption to all the exporters." Naturally, the Department says: "Do not give exemption to any exporter. We must collect the revenue." Therefore, we decided that this is not a matter where we can give up revenues completely. At the

same time, we must be sympathetic to small exporters. Anyway, we did not take a view. We referred it to Dr. Rangarajan's Economic Advisory Council. The Economic Advisory Council heard exporters, heard everyone and gave a report to the Prime Minister.

What did the Economic Advisory Council recommend? I am reading only the recommendations.

(1) If the export turn-over was Rs.10 crore or less, the DEPB Credit transfer income may be exempted.

(2) If the export turn-over was more than Rs.10 crore, the corresponding income may be exempt provided two conditions are satisfied: one, if an exporter had claimed DEPB credit and also tax exemption for such DEPB credit, the income should be brought to tax without the benefit of exemption. The income should be exempt if the exporter had a choice between draw-back and DEPB and the customs component of the draw back rate was higher than the DEPB rate;

(3) No penalty by way of interest or penal interest should be levied; and

(4) The arrears of tax, if any, may be collected over a period of two years.

I have accepted all the four recommendations with the improvement that the arrears, if any, will be collected not over two years but over five years. What more can I do? ... (Interruptions)

SHRI SURESH PRABHAKAR PRABHU Is it with penalty or with interest?

SHRI P. CHIDAMBARAM: There will be no penalty and no interest. I read it. I am going to collect the basic arrears over five years.

Shri Kashiram Rana asked me two questions. One, he asked: What is the basis of Rs.10 crore? The basis of this Rs.10 crore is the Economic Advisory Council's Report. They have gone into the data. They have looked at the frequency distribution of the exporters. They found that out of the 65,000 exporters – of course, not all will be covered under the DEPB credit scheme – if you keep a limit of Rs.10 crore, 60,000 exporters are out. So, all the small exporters are exempted. I am giving the exemption today. It is not there in the law as we interpret it. But we are now amending the law to give the exemption to about 60,000 exporters according to the Report of Dr. Rangarajan's Committee. This is the basis of the Rs.10 crore.

He has asked me the next question. I suppose this is the last question. Why did you give retrospective effect from 1.4.1998? My Department's officers are sitting in the gallery. If I do not give retrospective effect, they will be the happiest people because everybody has to pay tax then. We have to give retrospective effect because the period is from 1.4.1998 to 31.3.2005. What is the use of making a law today when the period is over on 31.3.2005? Therefore, we are giving retrospective effect to cover the period from 1.4.1998 to 31.3.2005 (R56).

The basis of Rs.10 crore is a reasonable basis. It is based on a thorough analysis. It is based on Ministry of Law's opinion. The Ministry of Law's opinion is that the Department's interpretation is correct. Yet, the Economic Advisory Council said the legal position may be in favour of the Department but let us give the benefit to the small exporter and we have accepted that recommendation. The Prime Minister only said, "I will refer it to a Committee." The Committee was Dr. Rangarajan's Committee. Here is the report and I have accepted the report. I have, in fact, improved upon the report by saying 'arrears will be collected not in two year, it will be collected in five years.' So, we think only a small number of big exporters will have to pay some tax if, at all, because if they can show that the DEPB benefit and the Drawback benefit, one was higher than the other, they can still come under the exemption. But, I think what we have done is a balance. We have to protect the interest of the revenue. I agree, I understand the concern of the Members of exporters but I appeal, to you to please show some concern for the revenue also. Therefore, balancing the interest of revenue and the small exporter, we have given the benefit to the small exporter. We have denied it in a limited way to the large exporter. If the large exporter satisfies both conditions he will also get the exemption. But, if he is not able to satisfy both conditions, he would have to pay some tax. There is no interest, no penalty and payment is over a period of five years. I think, Sir, we have struck a balance. Of course, we can always disagree whether the balance is correctly struck or the balance is not correctly struck but that is a judgment which the Government has made. I submit we have come to a reasonable solution to the problem.. (Interruptions) I have

explained. I have to protect the interest of the revenue also. I cannot give up revenues. When there is such large expenditure, such large claims for Sarva Siksha Abhiyan, Mid-Day Meal Scheme .....

8. It will be also profitable to refer to the provisions contained in sections 28 and section 80 HHC of the Act as it stands now which are quoted below:-

"***Profits and gains of business or profession.***

28. *The following income shall be chargeable to income-tax under the head "Profits and gains of business or profession",--*

[i] the profits and gains of any business or profession which was carried on by the assessee at any time during the previous year;

[ii] any compensation or other payment due to or received by,--

[a] any person, by whatever name called, managing the whole or substantially the whole of the affairs of an Indian company, at or in connection with the termination of his management or the modification of the terms and conditions relating thereto;

[b] any person, by whatever name called, managing the whole of substantially the whole of the affairs in India of any other company, at or in connection with the termination of his office or the modification of the terms and conditions relating thereto;

[c] any person, by whatever name called, holding an agency in India for any part of the activities relating to the

business of any other person, at or in connection with the termination of the agency or the modification of the terms and conditions relating thereto;

[d] any person, for or in connection with the vesting in the Government, or in any corporation owned or controlled by the Government, under any law for the time being in force, of the management of any property or business;

[iii] income derived b a trade, professional or similar association from specific services performed for its members;

[iiia] profits on sale of a licence granted under the Imports [Control] Order, 1955, made under the Imports and Exports [Control] Act, 1947 [18 of 1947];

[iiib] cash assistance [by whatever name called] received or receivable by any person against exports under any scheme of the Government of India;

[iiic] any duty of customs or excise re-paid or re-payable as drawback to any person against exports under the Customs and Central Excise Duties Drawback Rules, 1971;

[iiid] any profit on the transfer of the Duty Entitlement Pass Book Scheme, being the Duty Remission Scheme under the export and import policy formulated and announced under section 5 of the Foreign Trade [Development and Regulation] Act, 1922 [22 of 1992];

[iiie] any profit on the transfer of the Duty Free Replenishment Certificate, being the Duty Remission Scheme under the export and import policy formulated and announced under section 5 of the Foreign Trade [Development and Regulation]

Act, 1992 [22 of 1992];

[iv] the value of any benefit or perquisite, whether convertible into money or not, arising from business or the exercise of a profession;

[v] any interest, salary, bonus, commission or remuneration, by whatever name called, due to, or received by, a partner of a firm from such firm;

***Provided** that where any interest, salary, bonus, commission or remuneration, by whatever name called, or any part thereof has not been allowed to be deducted under clause [b] of section 40, the income under this clause shall be adjusted to the extent of the amount not so allowed to be deducted;*

[va] any sum, whether received or receivable, in cash or kind, under an agreement for--

[a] not carrying out any activity in relation to any business; or

[b] not sharing any know-how, patent, copyright, trade-mark, licence, franchise or any other business or commercial right of similar nature or information or technique likely to assist in the manufacture or processing of goods or provision for services:

***Provided** that sub-clause[a] shall not apply to--*

[i] any sum, whether received or receivable, in cash or kind, on account of transfer of the right to manufacture, produce or process any article or thing or right to carry on any business, which is chargeable under the head "Capital gains";

[ii] any sum received as compensation, from the multilateral fund of the Montreal Protocol on Substances that Deplete the Ozone layer under the United Nations Environment Programme, in accordance with the terms of agreement entered into with the Government of India.

Explanation.-- For the purposes of this clause,--

[i] "agreement" includes any arrangement or understanding or action in concert,--

[A] whether or not such arrangement, understanding or action is formal or in writing; or

[B] whether or not such arrangement, understanding or action is intended to be enforceable by legal proceedings;

[ii] "service" means service of any description which is made available to potential users and includes the provisions of services in connection with business of any industrial or commercial nature such as accounting, banking, communication, conveying of news or information, advertising, entertainment, amusement, education, financing, insurance, chit funds, real estate, construction, transport, storage, processing, supply of electrical or other energy, boarding and lodging;

[vi] any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy.

Explanation.-- For the purposes of this clause, the expression "Keyman insurance policy" shall have the meaning assigned to it in clause [10D] of section 10;

[vii] any sum, whether received or receivable, in cash or kind, on account of any capital asset [other than land or goodwill or financial instrument] being demolished, destroyed, discarded or transferred, if the whole of the expenditure on such capital asset has been allowed as a deduction under section 35AD;

Explanation 1.-- Omitted

Explanation 2.-- Where speculative transactions carried on by an assessee are of such a nature as to constitute a business, the business[hereinafter referred to as "speculation business"] shall be deemed to be distinct and separate from any other business."

Section 80HHC provides as under:

Deduction in respect of profits retained for export business.

80HHC. *(1) Where an assessee, being an Indian company or a person (other than a company) resident in India, is engaged in the business of export out of India of any goods or merchandise to which this section applies, there shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of the assessee, a deduction to the extent of profits, referred to in sub-section (1B), derived by the assessee from the export of*

such goods or merchandise:

Provided *that if the assessee, being a holder of an Export House Certificate or a Trading House Certificate (hereafter in this section referred to as an Export House or a Trading House, as the case may be,) issue a certificate referred to in clause (b) sub-section (4A), that in respect of the amount of the export turnover specified therein, the deduction under this sub-section is to be allowed to a supporting manufacturer, then the amount of deduction in the case of the assessee shall be reduced by such amount which bears to the total profits derived by the assessee from the export of trading goods, the same proportion as the amount of export turnover specified in the said certificate bears to the total export turnover of the assessee in respect of such trading goods.*

(1A) Where the assessee, being a supporting manufacturer, has during the previous year, sold goods or merchandise to any Export House or Trading House in respect of which the Export House or Trading House has issued a certificate under the proviso to sub-section (1), there shall, in accordance with the subject to the provisions of this section, be allowed in computing the total income of the assessee, a deduction to the extent of profits, referred to in sub-section (1B), derived by the assessee from the sale of goods or merchandise to the Export House or Trading House in respect of which the certificate has been issued by the Export House or Trading House.

(1B) For the purposes of sub-sections (1) and (1A), the extent of deduction of the profits shall be an amount equal to-

[i] eighty per cent thereof for an assessment year beginning

on the 1st day of April, 2001;

[ii] seventy per cent thereof for an assessment year beginning on the 1st day of April, 2002;

[iii] fifty per cent thereof for an assessment year beginning on the 1st day of April, 2003;

[iv] thirty per cent thereof for an assessment year beginning on 1st day of April, 2004,

and no deduction shall be allowed in respect of the assessment year beginning on the 1st day of April, 2005 and any subsequent assessment year.

(2)(a) This section applies to all goods or merchandise, other than those specified in clause (b), if the sale proceeds of such goods or merchandise exported out of India are received in, or brought into, India by the assessee (other than the supporting manufacturer) in convertible foreign exchange within a period of six months from the end of the previous year or, within such further period as the competent authority may allow in this behalf.

Explanation:- For the purposes of this clause, the expression "competent authority" means the Reserve Bank of India or such other authority as is authorised under any law for the time being in force for regulating payments and dealings in foreign exchange.

(b) This section does not apply to the following goods or merchandise, namely:-

(i) mineral oil; and

(ii) minerals and ores (other than processed minerals and ores specified in the Twelfth schedule)

Explanation 1.:- The sale proceeds referred to in clause (a) shall be deemed to have been received in India where such sale proceeds are credited to a separate account maintained for the purpose by the assessee with any bank outside India with the approval of the Reserve Bank of India.

Explanation 2.:- For the removal of doubts, it is hereby declared that where any goods or merchandise are transferred by an assessee to a branch, office, warehouse or any other establishment of the assessee situate outside India and such goods or merchandise are sold from such branch, office, warehouse, or establishment, then, such transfer shall be deemed to be export out of India of such goods and merchandise and the value of such goods or merchandise declared in the shipping bill or bill of export as referred to in sub-section (1) of section 50 of the Customs Act, 1962 (52 of 1962), shall, for the purposes of this section, be deemed to be the sale proceeds thereof.

(3) For the purposes of sub-section (1)-

(a) where the export out of India is of goods or merchandise manufactured or processed by the assessee, the profits derived from such export shall be the amount which bears to the profits of the business, the same proportion as the export turnover in respect of such goods bears to the total turnover of the business carried on by the assessee;

(b) where the export out of India is of trading goods, the profits derived from such export shall be the export turnover in respect of such trading goods as reduced by the direct costs and indirect costs attributable to such export;

(c) where the export out of India is of goods or merchandise manufactured or processed by the assessee and of trading goods, the profits derived from such export shall,-

i. *in respect of the goods or merchandise manufactured or processed by the assessee, be the amount which bears to the adjusted profits of the business, the same proportion as the adjusted export turnover in respect of such goods bears to the adjusted total turnover of the business carried on by the assessee; and*

ii. *in respect of trading goods, be the export turnover in respect of such trading goods as reduced by the direct and indirect costs attributable to export of such trading goods:*

Provided *that the profits computed under clause (a) or clause (b) or clause (c) of this sub-section shall be further increased by the amount which bears to ninety per cent of any sum referred to in clause (iiia) (not being profits on sale of a licence acquired from any other person), and clauses (iiib) and (iiic) of section 28, the same proportion as the export turnover bears to the total turnover of the business carried on by the assessee:*

Provided further *that in the case of an assessee having export turnover not exceeding rupees ten crores during the*

previous year, the profits computed under clause (a) or clause (b) or clause (c) of this sub-section or after giving effect to the first proviso, as the case may be, shall be further increased by the amount which bears to ninety per cent of any sum referred to in clause (iiid) or clause (iiie), as the case may be, of section 28, the same proportion as the export turnover bears to the total turnover of the business carried out by the assessee.

Provided also *that in the case of an assessee having export turnover exceeding rupees ten crores during the previous year, the profits computed under clause (a) or clause (b) or clause (c) of this sub-section or after giving effect to the first proviso, as the case may be, shall be further increased by the amount which bears to ninety per cent of any sum referred to in clause (iiid) of section 28, the same proportion as the export turnover bears to the total turnover of the business carried on by the assessee, if the assessee has necessary and sufficient evidence to prove that;-*

(a) he had and option to choose either the duty drawback or the Duty Entitlement Pass Book Scheme, being the Duty Remission Scheme; and

(b) the rate of drawback credit attributable to the customs duty was higher than the rate of credit allowable under the Duty Entitlement Pass Book Scheme, being the Duty Remission Scheme:

Provided also *that in the case of an assessee having export turnover exceeding rupees ten crores during the previous year, the profits computed under clause (a) or clause (b) or clause (c) of this sub-section or after giving*

effect to the first proviso, as the case may be, shall be further increased by the amount which bears to ninety per cent of any sum referred to in clause (iiie) of section 28, the same proportion as the export turnover bears to the total turnover of the business carried on by the assessee, if the assessee has necessary and sufficient evidence to prove that,-

(a) he had and option to choose either the duty drawback or the Duty Free Replenishment Certificate, being the Duty Remission Scheme; and

(b) the rate of drawback credit attributable to the customs duty was higher than the rate of credit allowable under the Duty Free Replenishment Certificate, being the Duty Remission Scheme.

Explanation:- For the purposes of this clause, "rate of credit allowable" means the rate of credit allowable under the Duty Free Replenishment Certificate, being the Duty Remission Scheme calculated in the manner as may be notified by the Central Government:

***Provided also** that in the case the computation under clause (a) or clause (b) or clause (c) of this sub-section is a loss, such loss shall be set off against the amount which bears to ninety per cent of-*

(a) any sum referred to in clause (iiia) or clause (iiib) or clause (iiic), as the case may be, or

(b) any sum referred to in clause (iiid) or clause (iiie), as the case may be, of Section 28, as applicable in the case of an assessee referred to in the second or the third

or the fourth proviso, as the case may be,

the same proportion as the export turnover bears to the total turnover of the business carried on by the assessee.

Explanation- For the purposes of this sub-section,-

(a) "adjusted export turnover" means the export turnover as reduced by the export turnover in respect of trading goods;

(b) "adjusted profits of the business" means the profits of the business as reduced by the profits derived from the business of export out of India of trading goods as computed in the manner provided in clause (b) of sub-section (3);

(c) "adjusted total turnover" means the total turnover of the business as reduced by the export turnover in respect of trading goods;

(d) "direct costs" means costs directly attributable to the trading goods exported out of India including the purchase price of such goods;

(e) "indirect costs" means costs, not being direct costs, allocated in the ratio of the export turnover in respect of trading goods to the total turnover;

(f) "trading goods" means goods which are not manufactured or processed by the assessee.

(3A) For the purposes of sub-section (1A), profits derived by a supporting manufacturer from the sale of goods or merchandise shall be, -

(a) in a case where the business carried on by the supporting manufacturer consists exclusively of sale of goods or merchandise to one or more Export Houses or Trading Houses, the profits of the business

(b) in a case where the business carried on by supporting manufacturer does not consist exclusively of sale of goods or merchandise to one more Export Houses or Trading Houses, the amount which bears to the profits of the business the same proportion as the turnover in respect of sale to the respective Export House or Trading House bears to the total turnover of the business carried on by the assessee.

[4] The deduction under sub-section [1] shall not be admissible unless the assessee furnishes in the prescribed form along with the return of income, the report of an accountant, as defined in the Explanation below sub-section [2] of section 288, certifying that the deduction has been correctly claimed in accordance with the provisions of this section:

Provided that in the case of an undertaking referred to in sub-section [4C], the assessee shall also furnish along with the return of income, a certificate from the undertaking in the special economic zone containing such particulars as may be prescribed, duly certified by the auditor auditing the accounts of the undertaking in the special economic zone under the provisions of this Act or under any other law for the time being in force.

[4A] The deduction under sub-section [1A] shall not be admissible unless the supporting manufacturer furnishes in the prescribed form along with his return of income,--

[a] the report of an accountant, as defined in the Explanation below sub-section [2] of section 288, certifying that this deduction has been correctly claimed on the basis of the profits of the supporting manufacturer in respect of his sale of goods or merchandise to the Export House or Trading House; and

[b] a certificate from the Export House or Trading House containing such particulars as may be prescribed and verified in the manner prescribed that in respect of the export turnover mentioned in the certificate, the Export House or Trading House has not claimed the deduction under this section;

Provided that the certificate specified in clause [b] shall be duly certified by the auditor auditing the accounts of the Export House or Trading House under the provisions of this Act or under any other law.

[4B] For the purposes of computing the total income under sub-section[1] or sub-section [1A], any income not charged to tax under this Act shall be excluded.

[4C] The provisions of this section shall apply to an assessee,--

[a] for an assessment year beginning after the 31st day of March, 2004 and ending before the 1st day of April, 2005;

[b] who owns any undertaking which manufactures or produces goods or merchandise anywhere in India [outside any special economic zone] and sells the same to any undertaking situated in a special economic zone which is eligible for deduction under section 10A and such sale shall be deemed to be export out of India for the purposes of this section.

Explanation.--For the purposes of this section,--

[a] "convertible foreign exchange" means foreign exchange which is for the time being treated by the Reserve Bank of India as convertible foreign exchange for the purposes of the Foreign Exchange Regulation Act, 1973 [46 of 1973], and any rules made thereunder;

[aa] "export out of India" shall not include any transaction by way of sale or otherwise, in a shop, emporium or any other establishment situate in India, not involving clearance at any customs station as defined in the Customs Act, 1962 [52 of 1962];

[b] "export turnover" means the sale proceeds, received in, or brought into, India by the assessee in convertible foreign exchange in accordance with clause [a] of sub-section [2] of

any goos or merchandise to which this section applies and which are exported out of India, but does not include freight or insurance attributable to the transport of the goods or merchandise beyond the customs station as defined in the Customs Act, 1962 [52 of 1962];

[ba] "total turnover" shall not include freight or insurance attributable to the transport of the goods or merchandise beyond the customs station as defined in the Customs Act, 1962 [52 of 1962];

[baa] "profits of the business" means the profits of the business as computed under the head "Profits and gains of business or profession" as reduced by--

[1] ninety per cent of any sub referred to in clauses [iiia], [iiib], [iiic], [iiid] and [iiie] of section 28 or of any receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in such profits; and

[2] the profits of any branch, office, warehouse or any other establishment of the assessee situate outside India;

[bb] Omitted.

[c] "Export House Certificate" or "Trading House Certificate" means a valid Export House Certificate or Trading House Certificate, as the

case may be, issued by the Chief Controller of Imports and Exports, Government of India;

[d] "supporting manufacturer" means a person being an Indian company or a person [other than a company] resident in India, manufacturing [including processing] goods or merchandise and selling such goods or merchandise to an Export House or a Trading House for the purposes of export;

[e] "special economic zone" shall have the meaning assigned to it in clause [viii] of the Explanation 2 to section 10A.

9. At the very outset, we propose to refer to the following observations of the Constitutional Bench of the Supreme Court in the case of **KUNNATHAT THATHUNNI MOOPIL NAIR V. STATE OF KERALA AND ANOTHER** reported in **AIR 1961 SC 552** pointing out the scope of investigation by a court while considering the question whether a Taxing Statute is *ultra vires* the provisions of the Constitution of India:

"*Article 265 imposes a limitation on the taxing power of the State in so far as it provides that the State shall not levy or collect a tax, except by authority of law, that is to say, a tax cannot be levied or collected by a mere executive fiat. It has to be done by authority of law, which must mean valid law. In order that the law may be valid, the tax proposed to be levied must be within the legislative competence of the Legislature imposing a tax and authorising the collection thereof and, secondly, the tax must be subject to the conditions laid down in Art. 13 of the Constitution.* ***One of such conditions envisaged by Art. 13(2) is that the Legislature***

shall not make any law which takes away or abridges the equality clause in Art. 14, which enjoins the State not to deny to any person equality before the law or the equal protection of the laws of the country. It cannot be disputed that if the Act infringes the provisions of Art. 14 of the Constitution, it must be struck down as unconstitutional. *For the purpose of these cases, we shall assume that the State Legislature had the necessary competence to enact the law, though the petitioners have seriously challenged such a competence.* ***The guarantee of equal protection of the laws must extend even to taxing statutes. It has not been contended otherwise.*** *It does not mean that every person should be taxed equally. But it does mean that if property of the same character has to be taxed, the taxation must be by the same standard, so that the burden of taxation may fall equally on all persons holding that kind and extent of property. If the taxation, generally speaking, imposes a similar burden on every one with reference to that particular kind and extent of property, on the same basis of taxation, the law shall not be open to attack on the ground of inequality, even though the result of the taxation may be that the total burden on different persons may be unequal. Hence, if the Legislature has classified persons of properties into different categories, which are subjected to different rates of taxation with reference to income or property, such a classification would not be open to the attack of inequality on the ground that the total burden resulting from such a classification is unequal. Similarly, different kinds of property may be subjected to different rates of taxation,* ***but so long as there is a rational basis for the classification, Art. 14 will not be in the way of such a classification resulting in unequal burdens on different classes of properties. But if the same class of property similarly situated is subjected to an incident of taxation,***

which results in inequality, the law may be struck down as creating an inequality amongst holders of the same kind of property. It must, therefore, be held that a taxing statute is not wholly immune from attack on the ground that it infringes the equality clause in Art. 14, though the Courts are not concerned with the policy underlying a taxing statute or whether a particular tax could not have been imposed in a different way or in a way that the Court might think more just and equitable. *The Act has, therefore, to be examined with reference to the attack based on Art. 14 of the Constitution."*

Bearing in mind the aforesaid observations, we first propose to consider the first question that arises for determination as to whether the amendment impugned in this application is arbitrary and unreasonable.

10. According to the learned counsel appearing on behalf of the petitioners, the benefit conferred from Assessment Year 1998-99 till Assessment Year 2004-05 was basis of the entire financial structuring of the petitioners' business including the pricing of export, payments of dividends, distribution of profits etc. and by the impugned amendment, the Revenue wants to take away the benefit on the basis that the exporter having turnover of more than Rs.10 Crore will get the benefit if he has evidence to prove that he had an option to choose either duty drawback or DEPB and that he chose DEPB, even when he was entitled to higher benefit under the duty drawback scheme. The

learned counsel for the petitioners submit that it is an absurd condition which no sensible person can ever exercise. According to them, to impose such condition retrospectively and requiring such person to prove that he had such an option in past and he had exercised it to avail the lesser benefit is totally arbitrary, capricious, unjust, unfair, discriminatory and violative of both Article 14 & Article 19 (1) (g) of the Constitution.

11. After hearing the learned counsel for the parties and after going through the impugned amendment, we find that classification based on export turnover is a recognized way of classification throughout the world. We find substance in the contention of the learned counsel for the Revenue that progressive levy is based on income classification in terms of both, the basis of taxation and the rate of tax, and on this ground, the same cannot be said to be arbitrary. In this connection, we may profitably refer to the following observations of the Supreme Court in the case of **KERALA HOTEL AND RESTURANT ASSOCIATION VS. STATE OF KERALA** reported in **AIR 1990 SC 913** dealing with the question in detail:

> *"26. It would be useful at this stage to refer to some decisions of this Court indicating the settled principles for determining validity of classification in a taxing statute. In Ganga Sugar Corporation Limited v. State of Uttar Pradesh (1980) 1 SCC 223 : (AIR 1980 SC 286), Krishna Iyer, J. speaking for the Constitution Bench held that a classification based, inter alia, on "profits of business and ability to pay tax" is constitutionally valid. Classification*

permissible in a taxing statute of dealers on the basis of different turnovers for levying varying rates of sales tax was considered by the Constitution Bench in M/ s. S. Kodar v. State of Kerala, (1974) 4 SCC 422: (AIR 1974 SC 2272), and Mathew, J. therein indicated the true perspective as under (at p. 2276 of AIR) :

"As we said, a large dealer occupies a position of economic superiority by reason of his volume of business and to make the tax heavier on him both absolutely and relatively is not arbitrary discrimination but an attempt to proportion the payment to capacity to pay and thus arrive in the end at a more genuine equality. The capacity of a dealer, in particular circumstances, to pay tax is not an irrelevant factor in fixing the rate of tax and one index of capacity is the quantum of turnover. The argument that while a dealer beyond certain limit is obliged to pay higher tax, when others bear a less tax, and it is consequently discriminatory, really misses the point namely that the former kind of dealers are in a position of economic superiority by reason of their volume of business and form a class by themselves. They cannot be treated as on a par with comparatively small dealers. An attempt to proportion the payment to capacity to pay and thus bring about a real and factual equality cannot be ruled out as irrelevant in levy of tax on the sale or purchase of goods. The object of a tax is not only to raise revenue but also to regulate the economic life of the society."

(Emphasis supplied)

27. A recent decision of this Court in P. H. Ashwathanarayana Setty v. State of Karnataka, 1989 Suppl (1) SCC 696 : (AIR 1989 SC 100) gives a fresh look to the extent of classification held valid in a taxing statute; and the scope of judicial review permitted while considering its validity on the ground of equality under

Article 14. The true position has been succinctly summarised by Venkatachaliah, J. speaking for the Court, as under (at pp. 118-119 of AIR) :

"The problem is, indeed, a complex one not free from its own peculiar difficulties. Though other legislative measures dealing with economic regulation are not outside Article 14, it is well recognised that the State enjoys the widest latitude where measures of economic regulation are concerned. These measures for fiscal and economic regulation involve an evaluation of diverse and quite often conflicting economic criteria and adjustment and balancing of various conflicting social and economic values and interests.

It is for the State to decide what economic and social policy it should pursue and what discriminations advance those social and economic policies. In view of the inherent complexity of these fiscal adjustments, courts give a larger discretion to the legislature in the matter of its preferences of economic and social policies and effectuate the chosen system in all possible and reasonable ways. if two or more methods of adjustments of an economic measure are available, the legislative preference in favour of one of them cannot be questioned on the ground of lack of legislative wisdom or that the method adopted is not the best or that there were better ways of adjusting the competing interests and claims. The legislature possesses the greatest freedom in such areas ....."

"The legislature has to reckon with practical difficulties of adjustments of conflicting interests. It has to bring to bear a pragmatic approach to the resolution of these conflicts and evolve a fiscal policy it thinks is best suited to the felt needs. The complexity of economic matters and the pragmatic solutions to be found them defy and go beyond conceptual mental models. Social

and economic problems of a policy do not accord with preconceived stereotypes so as to be amenable to predetermined solutions....."

The lack of perfection in a legislative measure does not necessarily imply its unconstitutionality. It is rightly said that no economic measure has yet been devised which is free from all discriminatory impact and that in such a complex arena in which no perfect alternatives exist, the Court does well not to impose too rigorous a standard of criticism, under the equal protection clause, reviewing fiscal services. In G. K. Krishan v. State of Tamil Nadu (AIR 1975 SC 583) this Court referred to, with approval, the majority view in San Antonio Independent School District v. Rodriguez (1973-411 US 1) speaking through Justice Stewart :

'No scheme of taxation, whether the tax is imposed on property, income or purchases of goods and services, has yet been devised which is free of all discriminatory impact. In such a complex arena in which no perfect alternatives exist, the Court does well not to impose too rigorous a standard of scrutiny lest all local fiscal schemes become subjects of criticism under the Equal Protection clause'

and also to the dissent of Marshall, J. who summed up his conclusion thus :

'In summary, it seems to me inescapably clear that this Court has consistently adjusted the care with which it will review State discrimination in light of the constitutional significance of the interests affected and the invidiousness of the particular classification. In the context of economic interests, we find that discriminatory State action is almost always sustained, for such interests are generally far removed from constitutional guarantees. Moreover, "(t) he extremes to which the court has gone

in dreaming up rational basis for State regulation in that area may in many instances be ascribed to a healthy revulsion from the court's earlier excesses in using the Constitution to protect interests that have more than enough power to protect themselves in the legislative halls."

"The observations of this Court in ITO v. K. N. Takim Roy Ryba (AIR 1976 SC 670) made in the context of taxation laws are worth recalling.

The mere fact that a tax falls more heavily on some in the same category, is not by itself a ground to render the law invaliad. It is only when within the selection, the law operates unequally and cannot be justified on the basis of a valid classification that there would be a violation of Article 14."

(Emphasis supplied)

28. In Federation of Hotel and Restaurant Association of India v. Union of India (1989) 178 ITR 97 Venkatachaliah J., delivering the majority opinion of the Constitution Bench while dealing with a similar objection to classification in a taxing statute, held as under:

"The State, in the exercise of its Governmental power, has, of necessity, to make laws operating differently in relation to different groups or class of persons to attain certain ends and must, therefore, possess the power to distinguish and classify persons or things. It is also recognised that no precise or set formulae or doctrinaire tests or precise scientific principles of exclusion or inclusion are to be applied. The test could only be one of palpable arbitrariness applied in the context of the felt needs of the times and societal exigencies informed by experience.

Classifications based on differences in the value of articles or the economic superiority of the persons of incidence are well recognised. A reasonable classification is one which includes all who are similarly situated and none who are not. In order to ascertain whether persons are similarly placed, one must look beyond the classification and to the purposes of the law."

(Emphasis supplied)

29. Thus, it is clear that the test applicable for striking down a taxing provision on this ground is one of 'palpable arbitrariness applied in the context of the felt needs of the times and societal exigencies informed by experience'; and the courts should not interfere with the legislative wisdom of making the classification unless the classification is found to be invalid by this test."

We, therefore, find no substance in the aforesaid contention of the petitioners as regards the legality of the amendment based on turnover.

12. The next question is whether the impugned amendment is violative of Article 14 of the Constitution of India because it is arbitrary. In this connection, the learned counsel for the petitioners vehemently contended before us that by the impugned amendment, two assessees of the same class are placed on different footing. They contend that in case of some of the assessees whose export turnover is more than Rs.10 Crore and who have claimed deduction u/s. 80 HHC on DEPB /

DFRC in their return of income and the assessments have become final by the Respondents accepting the same, are given the benefit of deduction without compliance of the conditions imposed by the Taxation Laws (Second Amendment) Act, 2005. They point out that in contrast to the above, in the cases of the assessees whose turnover is more than Rs.10 Crore, and who have claimed deduction u/s. 80 HHC on DEPB/DFRC and whose assessments are pending either before the Assessing Officer or the Appellate Authority would be required to comply with those two conditions retrospectively. According to the learned counsel for the petitioners, two assessees of similar description having export turnover of more than Rs.10 Crore are discriminated inasmuch as the assessees whose assessments have become final is not required to comply with the two conditions and would avail deduction u/s. 80 HHC as against the assessees whose assessments are pending and who would be required to comply with the two conditions.

13. After hearing the learned counsel for the parties, we are of the view that the benefit based on pendency of the proceedings of assessment and discrimination based thereon definitely violates Article 14 of the Constitution of India. In the matter of completion of assessment, the assessees have little role to pay. After the assessees have submitted their returns within the time fixed by law, if for any reason the respondent delays in making the assessment, taking advantage of their own delay, the Revenue cannot deprive a class of the assessees of

the benefit whereas other assessees of the same class whose assessment have already been completed would get the benefit. We, therefore, find that discrimination based on two classes, first, whose assessments have become final and secondly, whose assessment are pending, definitely violates Article 14 of the Constitution of India as there is no rationale nexus with the object of the amendment, and, therefore, such classification fails the test of Article 14 of the Constitution, being a case of 'palpable *arbitrariness'.*

14. We fully agree with the submissions made by the learned counsel for the petitioners that the burden was upon the Revenue to prove that the restrictions imposed by the amending Act are reasonable. We find that the Revenue has failed to discharge that burden by pointing out the reason for making classification based on the above two aspects which have no reasonable connection with the object of amendment.

15. The next question is whether the proposed amendment should be declared as *ultra vires* being violative of the principles of promissory estoppel and legitimate expectation.

16. According to the learned counsel for the petitioners, the benefit of section 80HHC was given to encourage exports and by virtue of the impugned amendment, they are deprived of the incentive which was promised. According to the learned counsel for the petitioners, the assessees have arranged their business affairs in the past when there were no conditions on the statute book, which is now sought to be

upturned by making the amendment retrospectively by imposing new conditions and thus, they contend that the principle of promissory estoppel applies in all areas of activities of a State including the legislative field.

17. After hearing the learned counsel for the parties and after going through the various decisions cited at the Bar, we find that although initially there was some discrepancy about the application of doctrine of promissory estoppel on the legislative field, the law is now settled that there is no estoppel against legislation. (See M/s. Vij Resins Pvt. Ltd. vs. State of J & K, reported in AIR 1989 SC 1629). The Supreme Court in the above decision pointed out that that there is no estoppel against the legislature and the *vires* of the Act cannot be tested by invoking the said plea but so far as the Government was concerned, the rule of estoppel did apply. Thus, the said decision clearly postulates that even though there may not be any promissory estoppel against the legislature, yet, if on the basis of the representation and promise made by the Government, certain concessions have been allowed, the Government may be compelled to honour its promise and allow the benefit of exemption on the basis of the doctrine of promissory estoppel even though the legislative provision need not be challenged. We, therefore, find that legislature is not bound by the doctrine of promissory estoppel and thus, we are unable to uphold the contention of the learned counsel for the petitioners that the proposed amendment should be struck down on the ground that the same is

violative of principles of promissory estoppel although individually an assessee can take the plea of promissory estoppel if the amended provision adversely affects such an assessee.

18. The last question is whether the impugned amendment should be set aside on the ground that this type of substantive amendment cannot be made with retrospective operation.

19. The learned counsel appearing on behalf of the Revenue has, however, opposed the aforesaid contention on the ground that as on DEPB profit no such benefit/deduction was earlier allowable, it cannot be branded as retrospective amendment. The learned counsel appearing on behalf of the Revenue contend that the Parliament has the necessary power to grant benefit/concession retrospectively to small exporters and deny similar benefits/concessions to large exporters on a reasonable classification of levels of income/turnover. According to them, where the Proviso extends the benefits/concessions retrospectively subject to certain conditions, howsoever stringent these might appear to be, the validity of the impugned amendments cannot be assailed on the grounds of unreasonableness or intelligible classification.

20. After hearing the learned counsel for the parties and after going through the decisions cited at the bar, we are of the view that although in taxing statute laxity is permissible and after giving a benefit to the assessee based on some specific conditions, such benefit can definitely

be curtailed but the same must be effective from a future date and not from an earlier point of time. If after inducing a citizen to arrange his business in a manner with a clear stipulation that if the existing statutory conditions are satisfied, in that event, he would get the benefit of taxation and thereafter, the Revenue withdraws such benefit and imposes a new condition which the citizen at that stage is incapable of complying whereas if such promise was not there, the citizen could arrange his affairs in a different way to get similar or at least some benefit, such amendment must be held to be arbitrary and if not, an ingenious artifice opposed to law. In the case before us, the object of the amendment, as it appears from the statements of the Finance Minister while moving the bill, is to get rid of the alleged wrong decision of the Tribunal interpreting the then provision of the Statute in a way beneficial to the assesses, which according to the Finance Minister, was never the intention of the legislature. If such be the position, the Revenue has definitely right to challenge the decision of the Tribunal as a wrong one before the higher forum; but on a plea of delay in disposal of appeal if filed, without challenging the decision of the Tribunal before High Court or Supreme Court, the Revenue cannot curtail such benefits by proposing amendment, incorporating a new provisions in the Statute from an anterior date. According to the existing law enacted by the Parliament itself, wrong orders passed by a Tribunal should be challenged by the aggrieved party before the appropriate High Court and if such party is still aggrieved by the order

of the High Court, he should move the Supreme Court.

21. Even in a case, where a taxing statute is declared invalid for some technical defect, the law is, in order to validate the tax collected under an invalid legislation, the legislature must lawfully revalidate the law. In this connection, we may appositely refer to the following observations of the constitutional bench of the Supreme Court in the case of **PRITHVI COTTON MILLS LTD VS. BROACH BOROUGH MUNICIPALITY** reported in **AIR 1970 SC192***:*

> "*. When a legislature sets out to validate a tax declared by a Court to be illegally collected under ineffective or an invalid law, the cause for ineffectiveness or invalidity must be removed before validation can be said to take place effectively. The most important condition, of course, is that the legislature must possess the power to impose the tax, for, if it does not, the action must ever remain ineffective and illegal.* ***Granted legislative competence, it is not sufficient to declare merely that the decision of the Court shall not bind for that is tantamount to reversing the decision in exercise of judicial power which the legislature does not possess or exercise. A Court's decision must always bind unless the conditions on which it is based are so fundamentally altered that the decision could not have been given in the altered circumstances.*** *Ordinarily, a Court holds a tax to be invalidly imposed because the power to tax is wanting or the statute or the rules or both are invalid or do not sufficiently create the jurisdiction.* ***Validation of a tax so declared illegal may be done only if the grounds of illegality or invalidity are capable of being removed and are in fact removed and the***

tax thus made legal. *Sometimes this is done by providing for jurisdiction where jurisdiction had not been properly invested before. Sometimes this is done by re-enacting retrospectively a valid and legal taxing provision and then by fiction making the tax already collected to stand under the re-enacted law. Sometimes the legislature gives its own meaning and interpretation of the law under which the tax was collected and by legislative fiat makes the new meaning binding upon Courts. The legislature may follow any one method or all of them and while it does so it may neutralise the effect of the earlier decision of the Court which becomes ineffective after the change of the law. Whichever method is adopted it must be within the competence of the legislature and legal and adequate to attain the object of validation. If the legislature has the power over the subject-matter and competence to make a valid law, it can at any time make such a valid law and make it retrospectively so as to bind even past transactions. The validity of a Validating law, therefore, depends upon whether the legislature possesses the competence which it claims over the subject-matter and whether in making the validation it removes the defect which the Courts had found in the existing law and makes adequate provisions in the validating law for a valid imposition of the tax."*

21.1 In the case before us, there is no defect in the original legislation but the Tribunal has interpreted the language of the valid piece of legislation in a way, which benefits the assessee. In such a case, for overcoming the adverse decision of the Tribunal, the legislature cannot delete a valid piece of legislation and incorporate a totally new one with retrospective effect. The effect of this amendment is that it is bypassing the existing law enacted by the Parliament of preferring

appeal against the order passed by the Tribunal, which is still the law of the land.

22. We, however, are, not for a moment, disputing the power of the legislature to curtail the benefit of a taxing statute conferred upon the assessee by prospective legislation but such curtailment with retrospective effect cannot be made for overcoming the effect of a judicial decision without taking recourse to the provison of appeal prescribed by law on the plea of delay. Moreover, we find that the present amendment has been made at a point of time when the application of section 80HHC has already been exhausted and the same was not even in the statute book. In such situation, it is not permissible to take away the benefit already granted through a concluded scheme by introducing fresh amendment by virtue of which an expired scheme has been revived with benefit conferred upon only a limited section and snatching the same from some other sections.

23. The present amendment is not just an amendment of a taxing statute creating a new provision retrospectively. We are quite alive to the position that a legislature has right to confer benefit prospectively or even retrospectively. Out of the five decisions cited by the Revenue on the question of power of the legislature to enact law retrospectively, except in the case of R. C. Tobacco (p) Ltd. and another vs. Union of India and another reported in (2005) 7 SCC 725, the other four cases did not involve the dispute of the present nature where a benefit

continuing for years has been withdrawn retrospectively. Thus, those four decisions do not help the Revenue in the facts of the present case.

24. So far the case of R. C. Tobacco (p) Ltd. and another vs. Union of India and another (supra), the benefit of notification granting exemption granted by a delegated authority was withdrawn by regular legislation clarifying the mistake of the delegated authority by the competent legislature. Such amendment of the substantive provision with retrospective effect was found to be valid by the Supreme Court. In that context, the Supreme Court made the following observations:

> "***21.*** *A law cannot be held to be unreasonable merely because it operates retrospectively. Indeed even judicial decisions are in a sense retrospective. When a statute is interpreted by a court, the interpretation is, by fiction of law, deemed to be part of the statute from the date of its enactment. The unreasonability must lie in some other additional factors. The retrospective operation of a fiscal statute would have to be found to be unduly oppressive and confiscatory before it can be held to be so unreasonable as to violate constitutional norms:*
>
> "*Where for instance, it appears that the taxing statute is plainly discriminatory, or provides no procedural machinery for assessment and levy of the tax, or that it is confiscatory, courts would be justified in striking down the impugned statute as unconstitutional. In such cases, the character of the material provisions of the impugned statute is such that the court would feel justified in taking the view that, in substance, the taxing statute is a cloak adopted by the legislature for achieving its*

confiscatory purposes." (See Rai Ramkrishna v. State of Bihar, SCR p. 910.)

The question to be answered therefore is whether Section 154, which is in terms retrospective, is ex facie discriminatory, or so unreasonable or confiscatory that it violates Articles 14 and 19 of the Constitution.

22. *The factors which are generally considered relevant in answering this question are: (i) the context in which retrospectivity was contemplated, (ii) the period of such retrospectivity, and (iii) the degree of any unforeseen or unforeseeable financial burden imposed for the past period.*

23. *The context in which legislation is enacted is to be distinguished from the motives which impelled it to act. The latter are irrelevant. (See K.C. Gajapati Narayan Deo v. State of Orissa SCR at p. 11; R.S. Joshi v. Ajit Mills Ltd. SCC at p. 108.) The justification put forward by the respondent for enacting Section 154 was therefore really unnecessary. Nevertheless, while we cannot for that reason analyse the justification, we may at least consider the plea as setting out the background in which the section was passed.*

24. *The particular context of the section impugned in this case was the industrial policy formulated by the Central and the State Government of Assam for the development of that State. The obvious intention behind the grant of the package of incentives including an exemption from payment of excise duties was to stimulate further industrial growth in the area with enduring benefits not only to the local populace by way of employment*

opportunities but also to the economic welfare of the State. The State Government's insistence from the very outset on the need to regulate the industries which were claiming the benefit of the exemption was to ensure that these objects were attained. According to the Union of India the exemption notification, at least as interpreted by the High Court, did not effectuate that intent. As it transpired, none of the industrial units manufacturing cigarettes were prepared to contribute to this object and their investment in the manufacture of cigarettes was co-extensive with the period of the exemption. The loss of revenue suffered by the Union and the State by the various subsidies and exemptions granted was the quid in return for which the petitioners were not prepared to suffer any quo. With the withdrawal of the exemption, all of them without exception immediately closed down their cigarette manufacturing units and a large majority have shifted out of the State. Clearly, if the grant of the exemption had operated as it was intended to, it would have been unnecessary to enact Section 154.

25. *The High Court may have been right in construing the exemption notification as it stood. Yet the respondent can contend that the words should have been used in the exemption so as to provide for sufficient safeguards to ensure that the benefit of exemption was granted only to those industries which would in turn permanently invest in the State. By the retrospective enactment this defective expression of the object of the policy, was rectified.*

26. *The exemption notifications were issued under Section 5-A of the Central Excise Act, 1944 as a delegate of Parliament. In a cabinet form of Government, the executive is expected to reflect the views of the legislature. It would be impossible for the legislatures*

to deal in detail and cater to the innumerable problems which may arise in implementing a statute. When the power of subordinate legislation is conferred by Parliament in certain matters it can only lay down the policy and guidelines and expect that what is done by the executive is in keeping with such policy. It does of course retain control over its delegate and can exercise that control by repealing the action of the delegate. Consequently, if the executive has failed to carry out the object of Parliament, such control may be exercised by retrospectively enacting what the executive ought to have achieved."

25. In the case before us, it is not one where *the executive has failed to carry out the object of the Parliament necessitating exercise of control by retrospective amendment what the executive ought to have achieved.*

In the present case, according to the Finance Minister presenting the Bill, a valid piece of legislation has been wrongly interpreted by the Tribunal. We have already pointed out that according to the existing law, if a valid piece of legislation is wrongly interpreted by the Tribunal, the aggrieved party should move higher judicial forum for correct interpretation. As pointed by the Apex Court in the case of Pritvi Cotton Mills Ltd (supra), the legislature does not possess or exercise power to reverse the decision in exercise of judicial power. Thus, we are of the view that the principles laid down in the case of R. C. Tobacco (P) Ltd. (supra) has no application to the facts of the present case. The impugned amendment granting benefit restricting it

to a class of assessee whose turnover is less than Rs. 10 Crore is permissible prospectively but the way it has been enacted, it takes away an enjoyed right of a class of citizen who availed of the benefit by complying with the requirements of the then provisions of law.

26. On consideration of the entire materials on record, we, therefore, find substance in the contention of the learned counsel for the petitioners that the impugned amendment is violative for its retrospective operation in order to overcome the decision of the Tribunal, and at the same time, for depriving the benefit earlier granted to a class of the assessees whose assessments were still pending although such benefit will be available to the assessees whose assessments have already been concluded. In other words, in this type of substantive amendment, retrospective operation can be given only if it is for the benefit of the assessee but not in a case where it affects even a fewer section of the assesses.

27. We, accordingly, quash the impugned amendment only to this extent that the operation of the said section could be given effect from the date of amendment and not in respect of earlier assessment years of the assessees whose export turnover is above Rs. 10 Crore. In other words, the retrospective amendment should not be detrimental to any of the assesses.

28. The writ-applications are, thus, disposed in terms of the above order. In the facts and circumstances, there will be, however, no order

as to costs.

28.1 In view of the above order passed in the writ-applications, the Civil Applications do not survive and are disposed of accordingly.

[BHASKAR BHATTACHARYA, ACTING C.J.]

[J.B.PARDIWALA. J.]

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