Pragati Aroma Oil Distillers Private Ltd. (formerly known as M/s. Hindustan Essential Oil Company) — Income Tax Appeal No. 502/2015

2026:BHC-OS:10531-DB Bhogale 3.itxa-502-2015.odt IN THE HIGH COURT OF JUDICATURE AT BOMBAY ORDINARY ORIGINAL CIVIL JURISDICTION INCOME TAX APPEAL NO.502 OF 2015 Pragati Aroma Oil Distillers Private Ltd. (formerly known as M/s. Hindustan Essential Oil Company) A company incorporated under Having its office at R. No.6, 2nd Floor, Anand, Bhanva, 17, Babu Genu Road, Mumbai-400021 ... Appellant Versus The Deputy Commissioner of Income Tax-14(2) Having his office at Room No.302, 3rd Floor, Earnest House, Nariman Point, Mumbai-400 021 .... Respondent **** Adv. Naresh Jain a/w Adv. Mansvi Singh, Adv. Priyanshi Jain and Adv. Bhavesh Bhatia, for the appellant. Adv. Sushma Nagaraj (through VC) a/w Adv. Abhinav Palshikar, for the respondent. **** CORAM : M. S. KARNIK & S. M. MODAK, JJ. DATE : 23rd APRIL, 2026 JUDGMENT (PER M. S. KARNIK, J.) :

1. This is an appeal filed under of the Income Tax Act, 1961 ("the ", for short), preferred by the appellant- 1 Bhogale 3.itxa-502-2015.odt assessee challenging the order dated 25th November 2014 passed by the Income Tax Appellate Tribunal ("ITAT", for short), in ITA No.873/Mum/2013 for the Assessment Year ("AY", for short) 2009-10, dismissing the appeal filed by the appellant.

2. This appeal was admitted on the following substantial question of law: > "Whether in the facts and circumstances of the case and in law, the Appellate Tribunal was justified in comparing and adopting net profit margin of sister concern Pragati Aroma Oil Distillers Pvt. Ltd. (as existed during the relevant Assessment Year), even in the absence of any arrangement as contemplated in read with of the Income Tax Act, 1961?" >

3. The appellant is a private limited company incorporated under the , engaged in the manufacture and export of perfumery compounds and essential oils. The appellant was originally known as M/s. Hindustan Essential Oil Company and was later converted into a private limited company. With effect from 1st April 2009, the company was amalgamated with Pragati Aroma Oil Distillers Private Limited. For the purposes of this appeal, "the appellant" refers to M/s. > (i) Although the Commissioner of Income Tax (Appeals) ("CIT(A)", for short) and the ITAT had allowed 3 Bhogale 3.itxa-502-2015.odt the Appellant's claim under for AY 2003-04, AY 2004-05, AY 2006-07 and AY 2007-08, the AO disallowed the same for the relevant assessment year vide order dated 9th December 2011, on the basis that the claim had been disallowed in earlier assessment proceedings and that the Revenue's appeal against the said relief is pending before the High Court. > (ii) The AO further held that the claim of deduction under was in contravention of read with and of the Act, alleging the use of non-market factors to inflate the profits of the eligible unit, on the following grounds: > (a) The Appellant did not charge interest at arm's length rates on loans advanced by partners. > (b) The Appellant reported an abnormally high gross profit of Rs.2,32,72,277/- on sales of Rs.5,83,65,060/-, with substantial purchases made from group entities or concerns directly or indirectly controlled by such entities. 4 Bhogale 3.itxa-502-2015.odt (c) There was no clear correlation between inputs and outputs; the activity undertaken > appeared to be in the nature of mere processing rather than manufacturing, thereby calling into question the eligibility of the unit for deduction under of the IT Act. > (iii) That the said claim of deduction was in contravention of read with and of the IT Act.

7. Aggrieved by the said order of the AO dated 9 th December 2011, the appellant filed an appeal with the CIT(A). The ITAT, vide order dated 25th November, 2014 dismissed the appeal of the appellant, recording that the contention of appellant that no comparable case was examined by the AO has no merit as it has been noted that on asking of the AO, the appellant furnished the GP/NP of the last three years of the sister concern and found that in the instant year the net profit earned by the sister concern itself was 19.03%, which led the ITAT to the conclusion that the appellant had disclosed profit in excess of what could be reasonably expected.

10. Aggrieved by the ITAT order dated 25th November, 2014, the present appeal was filed, challenging the said order. 6 Bhogale 3.itxa-502-2015.odt

11. Mr. Naresh Jain, learned counsel appearing on behalf of the appellant advanced the following submissions: > (i) That could not be applied to the present case, as it requires for there to exists some arrangement between the assessee and other persons which results in an artificial inflation of profits by the EOU and the tribunal, while holding applicable, failed to provide any finding of arrangement between the assessee and its sister concern, which led to the supposed inflation of profits. > (ii) That extraordinary profits alone cannot lead to the conclusion that there is an arrangement between the parties and that drawing such a conclusion would be akin to penalising efficient functioning. > (iii) That the amalgamation of the assessee with its sister concern Pragati Aroma does not amount to existence of an arrangement between them in terms contemplated under , considering that 7 Bhogale 3.itxa-502-2015.odt the said amalgamation took place at the end of the Assessment Year in question and was effective from 1 st April, 2009 and that for the entire year, the assessee operated independently. > (i) That, in the context of the applicability of , the ITAT has rightly applied the said section by observing that the Assessee and Pragati Aroma Oil Distillers Pvt. Ltd. shared a close relation, being regulated under the same management and dealing in the same business and that, as such, the course of business was so arranged that the business transaction between them produced more than ordinary profits. (ii) That, mere absence of a formal or written 1 [2012] 26 taxmann.com 336 (Bom.) 2 [2014] 50 taxmann.com 26 (Delhi-Trib.) 3 [2015] 61 taxmann.com 106 (Hyderabad-Trib.) 9 Bhogale 3.itxa-502-2015.odt > arrangement between the parties would not render inapplicable, considering that what has been contemplated under the said section is that the course of business must be so arranged that the business transaction between them produces profits to the assessee that are more than what may be ordinarily expected to arise in such eligible business.

13. Heard learned counsel for the parties.

14. of the IT Act provides incentive to promote exports by granting tax benefit to 100% EOUs. of the IT Act reads thus :- > "SECTION 10B(1) Special provisions in respect of newly established hundred per cent export-oriented undertakings. 10B. (1) Subject to the provisions of this section, a deduction of such profits and gains as are derived by a hundred per cent export-oriented undertaking from the export of

articles or things or computer software for a period of ten consecutive assessment years beginning with the assessment year relevant to the previous year in which the undertaking begins to manufacture or produce articles or things or computer software, as the case may be, shall be allowed from the total income of the assessee: 10 > Provided also that no deduction under this section shall be allowed to an assessee who does not furnish a return of his income on or before the due date specified under sub-section (1) of . (2) This section applies to any undertaking which fulfills all the following conditions, namely :- > (i) it manufactures or produces any articles or things or computer software; > (ii) it is not formed by the splitting up, or the reconstruction, of a business already in existence : > Provided that this condition shall not apply in respect of any undertaking which is formed as a result of the re- establishment, reconstruction or revival by the assessee of the business of any such undertaking as is referred to in , in the circumstances and within the period specified in that section; > (iii) it is not formed by the transfer to a new buishness of machinery or plant previously used for any purpose. 11 > Bhogale 3.itxa-502-2015.odt Explanation. - The provisions of Explanation 1 and Explanation 2 to sub-section (2) of shall aply for the purpose of clause (iii) of this sub-section as they apply for the purposes of clause (ii) of that sub-section."

15. empowers the AO to recompute the profits if there appears to be a close connection between the assessee and another entity and such connection produces more than ordinary profits. It is an anti-abuse provision to prevent assesses from seeking deduction on artificially inflated profits. For the facility of convenience, has been extracted below :- > "80-IA Deductions in respect of profits and gains from industrial undertakings or enterprises engaged in infrastructure development, etc. (10) Where it appears to the Assessing Officer that, owing to the close connection between the assessee carrying on the eligible business to which this section applies and any other person, or for any other reason, the course of business between them is so arranged that the business transacted between them produces to the assessee more than the ordinary profits which might be expected to arise in such eligible business, the Assessing Officer shall, in computing the profits and gains of such eligible business for the purposes of the deduction under this section, take the amount of profits as may be reasonably deemed to have been derived therefrom: Schmetz India (P■.) (supra) this Court held that extraordinary profits alone cannot lead to the conclusion that there is an arrangement between the parties as this would penalise efficient functioning. The paragraph No.8 of the decision is quoted below for ready reference :- 15 Bhogale 3.itxa-502-2015.odt "8. So far as questions (a) & (b) are concerned, we find that the Tribunal has considered the entire evidence and on facts come to the conclusion that the profits earned by Kandla division of the respondent-assessee is not abnormally high due to any arrangement between the respondent-assessee and its German Principal. The Tribunal correctly held that extraordinary profits cannot lead to the conclusion that this is an arrangement between the parties. This would penalize efficient functioning. Further, the authorities have also recorded a finding that the industrial sewing machine needles imported and traded by the Mumbai division are different from those manufactured & exported by the Kandla division. Consequently, this also negatives any arrangement between the parties to show extraordinary profits in respect of its Kandla division so as to claim deduction under of the Act. These are findings one of fact. The appellant-revenue have not been able to show that the findings are perverse or arbitrary. In the circumstances, questions (a) and (b) as formulated by the appellant/revenue do not raise substantial questions of law in the present facts and are therefore dismissed."

21. As regards the close connection between the assessee- appellant and its sister concern, we agree with the submission of the learned counsel for the appellant that merely the fact that the appellant merged with its sister concern does automatically indicate an arrangement between them to invite the rigours of , considering that the Assessee's amalgamation with its sister concern took place at the end of the Assessment Year and was only effective from 1st April 2009 and amalgamation at 16 Bhogale 3.itxa-502-2015.odt the end of the relevant financial year cannot be considered as an arrangement for the purpose of .

25. For the aforesaid reasons the substantial question of law is decided in favour of the appellant-assesseee and against the respondent-revenue. Therefore, the impugned order dated 25th November 2014 passed by the ITAT is quashed and set aside. The appeal stands allowed in terms of prayer clauses (a) and (b). No order as to costs. (S. M. MODAK, J.) (M. S. KARNIK, J.) Signed by: Pradnya Bhogale Designation: PA To Honourable Judge Date: 24/04/2026 16:41:05 19