Commissioner of Income Tax Vs Hemsons Industries

Court: Andhra Pradesh High Court

Date of Decision: July 27, 2001

Acts Referred: Central Sales Tax Act, 1956 â€" Section 5(3)
Income Tax Act, 1961 â€" Section 148, 15C, 256, 45, 54D

Citation: (2001) 171 CTR 527 : (2001) 251 ITR 693

Hon'ble Judges: S.R. Nayak, J; S. Ananda Reddy, J

Bench: Division Bench

Advocate: J.V. Prasad, for the Appellant; None, for the Respondent

Judgement

S.R. Nayak, J.
The Income Tax Appellate Tribunal, Hyderabad, herein has referred the following questions u/s 256 of the Income Tax

Act, 1961 (for short ""the Act""), to this court for opinion at the instance of the Commissioner of Income Tax, Andhra Pradesh-II Hyderabad.

1. Whether, on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was justified in law in holding that the assessee''s

activity of decortication of groundnuts was an industrial undertaking engaged in manufacture or production activity and therefore entitled to benefit

u/s 80HH ?

2. Whether, on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal ought to have taken cognisance of the fact that

claim u/s 80HH was not made u/s 80HH in Form No. 10C which consequently disentitled the assessee to claim the benefit during appeal-

proceedings for the first time ?

3. Whether, on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was justified in law in holding that for the

purpose of Section 54D it is not necessary for industrial undertaking to be engaged in manufacture or production ?

4. Whether, on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal ought to have held that the benefit of section 54D

is not available to the assessee in respect of sale of land as corresponding asset of land was not acquired as required by Section 54D ?

2. The assessee carries on business of purchase and sale of groundnuts, decortication of groundnuts into kernel and selling the same. The assessee

at the relevant point of time had a factory on lease at Anantapur and its own factory at Kadiri. For the assessment year 1984-85, the assessee filed

its return of income showing an income of Rs. 2,15,886. The assessment was completed on August 18, 1996, at a total income of Rs. 4,72,760

by the Income Tax Officer. At this stage itself, it may be noticed that along with the return the assessee did not file an audit report. The Income Tax

Officer opining that the requirements of Section 80HH were not satisfied, declined to grant the benefit under the said Section as claimed by the

assessee. The assessee made a claim of exemption u/s 54D in respect of a sum of Rs. 6,24,817 towards compensation and solatium received by it

out of compulsory acquisition of the land on the ground that the compensation money was utilised for setting up of a new factory. The Income Tax

Officer disallowed the claim on the ground that the assessee did not acquire the land at Gooty, but the land was taken only on tease. Further, the

Income Tax Officer held that capital gains arising on the sale of the building could not be exempted u/s 54D on the ground that the assessee is not

an industrial undertaking engaged in manufacturing activity. On appeal, the Commissioner of Income Tax (Appeals) confirmed the finding of the

Income Tax Officer. On second appeal by the assessee to the Appellate Tribunal, the Tribunal opined that the decortication of groundnuts

constituted a manufacturing activity and in so opining it placed reliance on the decision of this court in OMKARMAL AGARWAL Vs.

COMMISSIONER OF Income Tax, A. P., and of the Madras High Court in Commissioner of Income Tax, Madras Vs. M.R. Gopal, and also

the judgment of the Supreme Court in Ganesh Trading Co., Karnal Vs. State of Haryana and Another, . Further, the Tribunal found that the

assessee had taken a site on lease at Kadiri and constructed a new building and installed machinery worth of Rs. 2 lakhs and this was done by

transferring the capital from the Anantapur factory. It was also found, as a matter of fact, that no machinery from the Anantapur factory has been

transferred to the Kadiri factory. In the premise of these established facts, the Tribunal applying the ratio of the judgment in Textile Machinery

Corporation Limited, Calcutta Vs. The Commissioner of Income Tax, West Bengal, , came to the conclusion that the Kadiri factory was an

independent entity and, therefore, the assessee is entitled to the relief envisaged u/s 80HH of the Act for the assessment year 1984-85. At this

stage, it is also relevant to note that the case of the assesses that the acquisition had taken place on September 10, 1983, and within three years it

established an industrial undertaking at Gooty is not disputed by the Department. The Tribunal recording the findings as stated above, allowed the

appeal of the assessee.

3. The respondent though served with notice remains unrepresented. We have heard learned standing counsel for the Income Tax Department.

4. Learned standing counsel placing reliance on the judgments in Deputy Commissioner of Sales Tax (Law), Board of Revenue (Taxes),

Ernakulam Vs. Pio Food Packers, ; Sterling Foods, A Partnership Firm represented by its Partner Shri Ramesh Dalpatram Vs. State of Karnataka

and Another, and Namputhiris Pickle Industries v. State of Kerala [1994] 92 STC 1 (Ker) would contend that the decortication of groundnuts into

kernel does not involve any manufacturing activity and, therefore, the assessee is not entitled to the relief envisaged u/s 80HH of the Act. Secondly,

learned standing counsel would contend that the construction of the factory at Gooty tantamounts to reconstruction of an old business. In support

of this plea, learned standing counsel would place reliance on Textile Machinery Corporation Limited, Calcutta Vs. The Commissioner of Income

Tax, West Bengal, . Thirdly, learned counsel would contend that since, admittedly, the assessee did not file the audit report along with the return, it

is not entitled to the relief u/s 80HH. In support of this contention, learned counsel would place reliance on an unreported judgment of this court in

R. C. No. 27 of 1989, dated July 29, 1997.

5. it should be noticed at the threshold that the question whether decortication of groundnuts into kernel involves a manufacturing activity or not is

essentially a question of fact. The learned Tribunal on consideration of the judgment of this court in OMKARMAL AGARWAL Vs.

COMMISSIONER OF Income Tax, A. P., and that of the Madras High Court in Commissioner of Income Tax, Madras Vs. M.R. Gopal, and

also of the Supreme Court in Ganesh Trading Co., Karnal Vs. State of Haryana and Another, , came to the conclusion that the decortication of the

groundnuts into kernel involves manufacturing activity. The only thing to be seen is whether that view of the Tribunal is perverse or based on some

acceptable material evidence.

6. In OMKARMAL AGARWAL Vs. COMMISSIONER OF Income Tax, A. P., the question that fell for consideration of this court was

whether the business in buying raw cotton, ginning it, and converting it into lint with the aid of machinery, and selling lint and cotton seed involved

manufacturing activity or not. This court on consideration of the decisions in The Commissioner of Income Tax Vs. Ramlal and Sons, Barmer, ;

Commissioner of Income Tax, Punjab, Jammu and Kashmir and Himachal Pradesh, Simla Vs. Ram Sarup, and JUMMARLAL SURAJKARAN

Vs. COMMISSIONER OF Income Tax, ANDHRA PRADESH., opined that ginning kapas and converting it into lint with the aid of machinery

involves a manufacturing process.

7. In Commissioner of Income Tax, Madras Vs. M.R. Gopal, the Madras High Court has held that the process employed in converting boulders

into small stones with the aid of machinery is a manufacturing process and therefore such an undertaking is an industrial undertaking and

consequently such undertaking is entitled to the exemption u/s 15C of the Act. The court observed thus (page 598) :

Section 15C exempts from tax the newly established industrial undertakings, and the Section would apply only if the profits or gains charged to

tax are derived from any industrial undertaking, and further if the undertaking employs ten or more workers in a manufacturing process carried on

with the aid of power or employs 20 or more workers in a manufacturing process carried on without the aid of power. To qualify himself for the

benefit of this Section the assessee must establish that the profits and gains are derived from an industrial undertaking and that the undertaking

employed the required number of people in a manufacturing process carried on with the aid of power or without power. What is an industry?

Webster''s New International Dictionary gives various meanings to the word, one of which is : ''Systematic labour or habitual employment;

especially human exertion employed for the creation of value, regarded by some as a species of capital or wealth ; labour.'' Another meaning is :

''Any department or branch of art, occupation or business ; especially one which employs much labour and capital and is a distinct branch of trade

; as, the sugar industry ; the iron industry ; the cotton industry.'' ''Undertaking'' also has different shades of meaning ; and, according to Webster, it

means : ''Anything undertaken ; any business, work, or project to which one engages in, or attempts, an enterprise.'' There is here no doubt that

labour is employed, capital is utilised and a form of wealth is produced in the shape of small chips of stones by the aid of machinery. The process

of making chips is obviously also an enterprise, an occupation, or a business, and, therefore, is an undertaking. In fact, the only ground on which

the departmental officers have held the process in question as not an industrial undertaking is that it did not involve a manufacturing process.

8. In Ganesh Trading Co., Karnal Vs. State of Haryana and Another, , the question as to whether paddy and rice can be considered as identical

goods for the purpose of imposition of sales tax under the provisions of the General Sales Tax Act of Punjab and Haryana fell for consideration.

Under the concerned Sales Tax Act, exemption from payment of sales tax was provided if the very paddy in respect of which purchase tax was

levied was sold and not if that paddy was converted into rice and sold. It was contended in that case that paddy and rice were identical goods and

therefore when the law grants an exemption in respect of paddy, that exemption is also available to transactions relating to rice. This argument was

built upon the hypothesis that rice was nothing but dehusked paddy and therefore rice and paddy are identical goods. This contention was rejected

by the Supreme Court. The Supreme Court has opined that conversion of paddy into rice involves manufacturing activity. While opining so, the

Supreme Court observed thus (page 626):

It was contended on behalf of the appellants that the essential question that we have to decide is whether the goods sold differed in identity from

the goods purchased. It was urged that merely because paddy was dehusked and rice produced, there was no change in the identity of the goods.

Identity of goods is one of the essential elements to be borne in mind in deciding the nature of the transaction. It was so decided in Tungabhadra

Industries Ltd. Vs. The Commercial Tax Officer, Kurnool, . In that case, the question arising for decision was whether hydro-genated oil continued

to be groundnut oil. This court held that the hydro-genated groundnut oil continued to be groundnut oil. In arriving at that conclusion this court took

into consideration that the essential nature of the goods had not changed after the groundnut oil had been subjected to chemical process. Similar

view was taken by this court in State of Gujarat v. Sakarwala Brothers [1967] 19 STC 24 (SC). Therein the question whether patasa, harda and

alchidana could be considered as ''sugar''. This court held that when sugar was processed into patasa, harda and alchidana, it did not change its

essential characteristic. Its identity continued to be the same. Now, the question for our decision is whether it could be said that when paddy was

dehusked and rice produced, its identity remained. It was true that rice was produced out of paddy but it is not true to say that paddy continued to

be paddy even after dehusking. It had changed its identity. Rice is not known as paddy. It is a misnomer to call rice as paddy. They are two

different things in ordinary parlance. Hence quite clearly when paddy is dehusked and rice produced, there has been a change in the identity of the

goods. In this view it is not necessary for us to refer to the decisions of some of the High Courts read to us at the time of hearing.

9. In all these three cases, the goods which were subjected to certain processes, lost their identity speaking in commercial parlance after

undergoing those processes. Therefore, the courts have held that those processes involved manufacturing activity. In the case on hand, no doubt,

after deco-rtication of the groundnut into kernel, one may not find'' any qualitative difference in the kernel itself. In other words, there will not be

any qualitative difference in the kernel as such before or after decortication. But, that fact itself cannot be a ground to hold that decortication of the

groundnut into kernel does not involve manufacturing process. However, the fact remains that after the process, the original produce, i.e.,

groundnuts lost their original identify speaking in commercial parlance. In the case decided by the Supreme Court in Ganesh Trading Co., Karnal

Vs. State of Haryana and Another, , undoubtedly, after dehusking there was no change in the quality of the rice as such, but the process of

dehusking was itself held to be a manufacturing process because the paddy which was subjected to the process of dehusking lost its identity after

the process. If that is the rationale of the judgment, the same rationale can be applied to the present case also and it can be said that the

decortication of the groundnut involves manufactur ing process.

10. The decisions cited by learned standing counsel for the Department in Deputy Commissioner of Sales Tax (Law), Board of Revenue (Taxes),

Ernakulam Vs. Pio Food Packers, ; Sterling Foods, A Partnership Firm represented by its Partner Shri Ramesh Dalpatram Vs. State of Karnataka

and Another, and Namputhiris Pickle''s case [1994] 92 STC 1 (Ker) are not of much help to the Department.

11. In Deputy Commissioner of Sales Tax (Law), Board of Revenue (Taxes), Ernakulam Vs. Pio Food Packers, , what fell for consideration was

whether the process adopted by the assessee to convert pineapple fruits into pineapple slices for the purpose of being sold in sealed cans for

consumption involved manufacturing activity or not. The Supreme Court opined that the process did not involve manufacturing activity. The reason

given by the Supreme Court in so opining is quite apposite. It reads (page 66) :

The dealer and the consumer regard both as pineapple. The only difference is that the sliced pineapple is a presentation of fruit in a more

convenient form and by reason of being canned it is capable of storage without spoiling. The additional sweetness in the canned pineapple arises

from the sugar added as a preservative. On a total impression, it seems to us, the pineapple slices must be held to possess the same identity as the

original pineapple fruit"".

12. In Sterling Foods'' case [1986] 63 STC 239 the apex court was called upon to decide whether raw shrimps, prawns and lobsters"" after

suffering processing of cutting heads and tails, peeling, deveining, cleaning and freezing retain their original character or identity or become a new

commodity to attract the applicability of Section 5(3) of the Central Sales Tax Act. In that case, the assessee was purchasing raw shrimps, prawns

and lobsters for the purpose of fulfilling the existing contracts for export'' and after the said purchase, the assessee was subjecting the purchased

goods to the process of cutting heads and tails, peeling deveining, cleaning and freezing before export. In such a fact-situation, the Supreme Court

opined that even after the above process of cutting heads and tails, peeling deveining, cleaning and freezing, the goods remained the same goods in

commercial parlance and, therefore, the process to which the purchased raw shrimps, prawns and lobsters were subjected did not involve

manufacturing activity.

13. In Namputhiris Pickle Industries'' case [1994] 92 STC 1 the Kerala High Court while dealing with the question whether the chillies and chilli

powder possess substantial identity and character, opined that both of them possess the same identity and character. The court opined that when

chillies are made into powder, they do not change in substantial identity or character or essential nature. It is very pertinent to notice that the Kerala

High Court has arrived at such an opinion mainly on the ground that both chillies and chilli powder be used or consumed, in their natural form. The

judgments on which learned standing counsel for the Department placed reliance can be distinguished on facts also. One common feature of all

these cases is that the goods involved could be used''and consumed even before subjecting them to the manufacturing processes. Whereas the

groundnuts before decortication are not fit for consumption, and only after decortication, the end product, i.e., kernel, would be .fit for

consumption. Be that as it may, as opined at the threshold, the only question that arises for our consideration is whether the finding of fact recorded

by the learned Tribunal could be said to be perverse. We do not think so.

14. This takes us to whether the benefit u/s 80HH could be denied to the assessee solely on the ground that the assessee did not file the audit

report with the return. The Tribunal placing reliance on the judgment in Addl. Commissioner of Income Tax Vs. Murlidhar Mathura Prasad, , has

opined that the requirement of filing audit report with the return is only directory and not mandatory and if such report is not produced with the

return, it is only a curable defect. However, learned standing counsel for the Department would place reliance on an unreported judgment of this

court in RC No. 27 of 1989, dated July 29, 1997. We have perused that judgment. In that case, the judgment of the Punjab and Har-yana High

Court in Commissioner of Income Tax Vs. Jaideep Industries, and the judgment of the Bombay High Court in Commissioner of Income Tax Vs.

Shivanand Electronics, , were placed before this court for consideration. The Punjab and Haryana High Court held that the filing of the audit report

along with the return is a mandatory requirement and if it is not so filed, then, no deduction would be granted ; whereas the Bombay High Court

has opined that if the audit report is not filed along with the return, but if it is filed before the completion of the assessment, then, deduction could be

granted. This court on consideration of both the judgments has held : ""In view of what is stated supra, we hold that the assessment order of the

Income Tax Officer passed on January 2, 1985, on the basis of the material available on record was correct as the provision contained u/s

80J(6A) of the Act is mandatory and can be stretched only up to the point of passing of the assessment order so as to enable the assessee to file

the audit report before the assessment order is passed, but not later to that.

15. From the above observation of this court, it is quite clear that the mere fact that the assessee failed to enclose the audit report along with the

return itself would not disentitle him to claim the benefit, and, on the other hand, if he files the audit report before the assessment order is passed,

he will be entitled to the deduction. Admittedly, in this case, the petitioner filed the audit report before conclusion of the assessment proceedings for

the assessment years 1981-82 and 1984-85. As regards the assessment year 1979-80 also, it was filed in the reassessment proceedings in

response to the show-cause notice u/s 148 of the Act.

16. The relief u/s 54D of the Act is disallowed mainly on the ground that in establishing the factory at Kadiri, the capital from Anan-tapur factory

has been diverted. Even according to the Department, no machinery from the Anantapur factory has been transferred to the Kadiri factory and the

Kadiri factory was constructed on a land secured on lease and new machineries have been erected thereon. The Tribunal on appreciation of the

facts recorded the finding that the Kadiri factory is an independent factory and it is not a reconstruction of the existing unit.

17. Sub-section (1) of Section 54D reads :

(1) Subject to the provisions of Sub-section (2), where the capital gain arises from the transfer by way of compulsory acquisition under any law of

a capital asset, being land or building or any right in land or building, forming part of an industrial undertaking belonging to the assesses which, in

the two years immediately preceding the date on which the transfer took place, was being used by the assessee for the purposes of the business of

the said undertaking (hereafter in this Section referred to as the original asset), and the assessee has within a period of three years after that date

purchased any other land or building or any right in any other land or building or constructed any other building for the purposes of shifting or re-

estabhishing the said undertaking or setting up another industrial undertaking, then, instead of the capital gain being charged to Income Tax as the

income of the previous year in which the transfer took place, it shall be dealt with in accordance with the following provisions of this section, that is

to say :

(i) if the amount of the capital gain is greater than the cost of the land, building or right so purchased or the building so constructed (such land,

building or right being hereafter in this Section referred to as the new asset), the difference between the amount of the capital gain and the cost of

the new asset shall be charged u/s 45 as the income of the previous year ; and for the purpose of computing in respect of the new asset any capital

gain arising from its transfer within a period of three years of its purchase or construction, as the case may be, the cost shall be nil ; or

(ii) if the amount of the capital gain is equal to or less than the cost of the new asset, the capital gain shall not be charged u/s 45 ; and for the

purpose of computing in respect of the new asset any capital gain arising from its transfer within a period of three years of its purchase or

construction, as the case may be, the cost shall be reduced by the amount of the capital gain.

18. Sub-section (1) of Section 54D provides the relief from tax in the case of persons owning industrial undertakings in respect of capital gain

arising on compulsory acquisition of any land or building used by them for the purposes of the business of the undertaking. The relief will be

available in cases where the land or building which is acquired, was used by the taxpayer for the purposes of the business of the industrial

undertaking during the two years immediately preceding the date of compulsory acquisition and the taxpayer purchases any other land or building

or constructs any other building, within three years from the date of compulsory acquisition, for the purposes of shifting or re-establishing the

industrial undertaking or setting up another industrial undertaking. In such cases, the capital gain will not be charged to tax to the extent it is utilised

for purchasing or, as the case may be, constructing the new asset. In other words, in a case where the amount of the capital gain exceeds the cost

of purchase or construction, only the excess amount will be chargeable to tax. Where the new asset is transferred within a period of three years of

its purchase or construction, then, for the purposes of determining the amount of capital gain arising from the transfer of the new asset (i) the cost of

the new asset will be taken as nil if the amount of the capital gain arising from the transfer of the old asset exceeded the cost of the new asset ; and

(ii) the cost of the new asset will be reduced by the amount of the capital gain arising from the transfer of the old asset if such capital gain was equal

to or less than the cost of the new asset. Section 54D, granting an exemption, must be construed liberally and the expression ""industrial

undertaking"" occurring therein must be given its popular meaning. An undertaking mentioned in Section 54D must be one maintained by a person

for the purpose of carrying on his business. The demonstrative objective ""industrial"" qualifying the word ""undertaking"" unmistakably and with

precision shows that the undertaking must be one, which partakes of the character of a business. The word ""business"" connotes some real,

substantial and systematic or organised course of activity with a set purpose. Since the word ""business"" is of wide import, the words ""industrial

undertaking"" should be understood to have been used in Section 54D in a wide sense, taking in its fold any project or business a person may

undertake. In P. Alikunju, M.A. Nazeer Cashew Industries Vs. Commissioner of Income Tax, , where the assessee invested the compensation

money received on acquisition of its ice factory by the Government in the construction and running a lodging house, it was held, that running of a

lodge by the assessee could be said to be an industrial undertaking within the meaning of section 54D of the Act and, therefore, it would be entitled

to exemption u/s 54D.

19. In the instant case, admittedly, the assessee has set up an industrial undertaking at Gooty by investing a sum of Rs. 1,88,530 on a land secured

by it on lease during the assessment years 1985-86 and 1986-87. Therefore, the reason given by the Department to deny the benefit u/s 54D that

the assessee has not purchased the land at Gooty for establishing the factory is untenable. The finding recorded by the Tribunal that the factory set

up at Gooty is a new factory is based on acceptable evidence. The Tribunal is the final fact-finding authority and the factual findings recorded by it

cannot lightly be interfered with unless in a given case they are shown to be perverse and based on ""no evidence"".

20. In the result and for the foregoing reasons, we answer the questions against the Revenue and in favour of the assessee.