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Commissioner of Income Tax, Bombay City-III Vs Indian Card Clothing Co. Pvt. Ltd.

Court: Bombay High Court

Date of Decision: July 13, 1976

Acts Referred: Income Tax Act, 1922 â€" Section 15C

Citation: (1977) 110 ITR 103

Hon'ble Judges: V.D. Tulzapurkar, J; R.M. Kantawala, J

Bench: Division Bench

Advocate: R.J. Joshi, for the Appellant; F.N. Kaka, for the Respondent

Judgement

Tulzapurkar, J.
The question that has been referred to us for our opinion in this reference u/s 66(1) of the Indian Income Tax Act, 1922, at

the instance of the commissioner of Income Tax, Bombay City-III Bombay, runs thus :

Whether, on the facts and in the circumstances of the case, the industrial undertaking of the assessee-company satisfied the requirement of section

15C(2)(i), namely, that it was not formed by the transfer, to a new business, of building, machinery or plant, previously used in any other business

?

2. The question relates to the assessment year 1961-62, the corresponding previous year being the year ended March 31, 1961. Thee assessee

private limited company. It commenced manufacturing operations on October 2, 1958. In the year in which it commenced manufacturing finish

products its total block was worth Rs. 28,33,733, out of which buildings and lands accounted for Rs. 1,46,530. The plant and machinery which

were without any dispute not used in any other business previously were valued at Rs. 8,69,627 while the reconditioned machinery was worth a

little more than Rs. 5 lakhs. It appears that thereafter the assessee purchase new as well as recondition machinery-the latter imported from the

U.K. - in the next two years. At the end of the accounting period relevant to the assessment year 1961-62, the machinery which was not used

previously was valued at Rs. 17,22,682 while the reconditioned machinery was valued at Rs. 14,95,715. The assessee-company claimed

exemption before the Income Tax Officer provided for in section 15C on the ground that the company was carrying on an industrial undertaking,

whose profits qualified for exemption under that provision. The Income Tax Officer accepted the claim of the assessee-company and allowed the

exemption of profits amounting Rs. 2,31,855.

3. Acting u/s 33B of the Act the Commissioner of Income Tax took the view that the order of the Income Tax Officer was erroneous and

prejudicial to the interest of the revenue, inasmuch as, according to him, the Income Tax Officer had wrongly applied the provisions of section 15C

in the assessment of the company for the year 1961-62. He, therefore, directed the Income Tax Officer to modify the assessment by withdrawing

the exemption. His reasoning for the conclusion was that from the figures taken from the depreciation schedule submitted by the company the

second-hand machinery was worth over Rs. 19 lakhs as against Rs. 12,09,771 worth of new machinery. Negativing the contention urged on behalf

of the assessee that reconditioned machinery could not be regarded as second-hand machinery, he took the view that the recondition machinery

could not be regarded as new one and he further took the view that it was not necessary that the previous use such second-hand machinery must

be in India. He held that the assessee-company by using in its manufacture, machinery of the value of Rs. 19,31,532, which was second-hand has

been formed by the transfer to a new business, of machinery or plant previously used in another business and that, therefore, the company was not

an industrial undertaking to which section 15C of the Act applied. Aggrieved by the order passed by the commissioner of Income Tax, the

assessee-company preferred an appeal to the Tribunal. Since the figures given by the commissioner in his order differed from the figures as given

by the company, a reconciliation statement was filed by the company before the Tribunal which gave particulars about purchase of new machinery

by the assessee-company during the three years as well as the reconditioned machinery that had been purchased by it during the said years.

According to this reconciliation statement it was clear that at the end of the accounting period relevant to the assessment year 1961-62 the

machinery which was not used previously was of the value of Rs. 17,22,682 while the reconditioned machinery was of the value of Rs. 14,95,715.

In the appeal, several contentions were urged on behalf of the assessee-company. In the first place, it was urged that the company was an

industrial undertaking which was entitled to the relief u/s 15C ; secondly, it was an industrial undertaking formed by the transfer, to a new business,

of building, machinery or plant previously used in any other business ; and thirdly, that though it had used the reconditioned machinery imported

from the U.K., such machinery formed 13% of the total block in the first year of its operation, 20% in the second year of its operation and 24% in

the third year of its operation. It was also contended that the reconditioned machinery could not be treated as machinery previously used for any

other business for the purpose of section 15C, both on the ground that such machinery was required to be used previously in India before the

company disqualified itself from getting relief contemplated by section 15C and that the reconditioned machinery could contemplated by section

15C and that the reconditioned machinery could not be regarded as second-hand machinery. It was urged that having regard to the scheme of

section 15C machinery, whose transfer would disqualify an undertaking for the relief, would be machinery previously used in any other business in

India or in any other business which was liable to Indian Income Tax that in any case machinery, whose transfer would disqualify an undertaking

from getting relief, should be big enough to form an undertaking by itself. The Tribunal held that the company was an industrial undertaking which

was entitled to get the relief u/s 15C because it could not be said to be an undertaking which had been formed by the transfer, to a nw business, of

building, machinery or plant previously used in any other business. Though the learned Accountant Member did not accept the assessee''s

contention that the machinery, whose transfer would disqualify an undertaking for the relief, should be the machinery previously used in any other

business in India or in any other business which was liable to Indian Income Tax, he came to the conclusion that the company could not be

regarded as an industrial undertaking which had been formed by the transfer, to a new business. of building, machinery or plant previously used in

any other business in that behalf, after referring to the valuation of new purchase of machinery and of the reconditioned machinery, both in the year

in which production had been commenced by the assessee as well as in relevant accounting periods, he held that the reconditioned machinery

undoubtedly formed an important part of the company''s block but it was not the nucleus around which the new undertaking was formed and the

preponderance of entirely new machinery continued year after year and even in the year of account relevant to the assessment year 1961-62 the

reconditioned machinery formed a smaller part of the total block. The learned Judicial Member did not express any opinion on the other

contentions that were urged on behalf of the assessee but concurred in the view of the learned Accountant Member that it could not by any stretch

of imagination be said that it was an industrial undertaking which had been formed by the transfer, to a new business, of building, plant or

machinery previously used in any other business, of business on the basis of relative valuation. As stated above, at the instance of the

Commissioner of Income Tax, Bombay City-III, Bombay, the question mentioned at the commencement of the judgment has been referred to us

for our opinion.

4. Mr. Joshi, appearing for the revenue, has contended before us that the Tribunal had at least recorded a finding to the effect that the

reconditioned machinery which was used by the assessee-company in its manufacture in the year of account relevant to the assessment year 1961-

62 formed an important part of the company"s block and, according to him, if the reconditioned machinery formed an important part of the

company"s block, it would be clear that without such reconditioned machinery, which formed an important part of the company"s block, the

assessee-company would not have been in a position to manufacture its products and, therefore, the company should be regarded as an industrial;

undertaking formed by the transfer, to a new business, of building, plant or machinery previously used in any other business. In support of this

contention reliance was placed by him a decision of this court in the case of Capsulation Services Pvt. Ltd. Vs. Commissioner of Income Tax,

Bombay City-I, , where this court has taken the view that section 15C(2)(i) applies to an industrial undertaking which is not formed by the transfer

to a new business of building used in any other business. He pointed out that this court has taken the view that essential for the formation of an

industrial undertaking. In view of this the industrial undertaking can never be formed unless it has a building for its factory or establishment. and

though in that case the assessee had acquired an area of 2,000sq. ft. at a monthly rent of Rs. 1500 for the purpose of establishing its factory, since

that building and the portion thereof which business it had been previously used in ny other business before it had been acquired by the assessee,

the assessee was not entitled to the relief contemplated by section 15C of the Act. By parity of reasoning it was urged by Mr. Joshi before us that

since in the instant case the Tribunal has recorded a finding that the reconditioned machinery formed an important part of the company"s block, it

should be held that formation of an industrial undertaking without which the assessee-company would not have been in a position to manufacture its

products and for similar reasons the assessee-company should be disqualified from getting the benefit or relief u/s 15C of the Act, It is not possible

for us accept this contention of Mr. Joshi for the reasons which we shall presently indicate.

5. In the first place, what Mr. Joshi has relied upon is a part of the finding recorded by the Tribunal and not the whole of it. The entire finding

recorded by the Tribunal is to the effect that though the reconditioned machinery formed an important part of the company''s block, it was not the

nucleus around which the new undertaking was formed, that the preponderance of entirely new machinery continued year after year and even in the

year of account relevant to the assessment year 1961-62, reconditioned machinery formed a smaller part of the total block. In other the finding of

fact that has been recorded by the Tribunal has been that the reconditioned machinery, though it formed an important part of the company''s block,

was not the nucleus around which a new undertaking was formed. In fact, from the reconciliation statement which was filed before the Tribunal,

certain figures became very eloquent. In the year in which the assessee-company commenced manufacturing its finished products its total block

was worth Rs. 23,33,733 out of which buildings and lands accounted for Rs. 14,46,530. The plant and machinery which were admittedly not used

in any other business previously were of the value of Rs.8,69,627,During the next two years the ratio of entirely new machinery purchased was

a;ways higher than the value of the reconditioned machinery that was purchased in the year of account relevant to the assessment year 1961-62,

the total value of the new machinery which had been used previously was of the value of Rs. 17,2,682 while the reconditioned machinery figures

which were available from the reconciliation statement that the Tribunal has recorded a finding that the reconditioned machinery was not the

nucleus around which an undertaking was formed and that in all the relevant years there was preponderance of entirely new machinery. In other

words, from the valuation point of view substantial part of machinery which went to form the nucleus was the new machinery and not the

reconditioned machinery. None of the taxing authorities below nor the Tribunal has gone into the question whether from the production point of

view. Which was more important, the reconditioned machinery was important or newly purchase machinery was important nor was any argument

on that aspect of the matter ever before the taxing authorities as well as before the Tribunal. It may be pointed out that even the order passed by

the Income Tax Officer who had accorded relief to the assessee u/s 15C was prejudicial to the interest of the revenue principally on the basis of

valuation for, according to him, the assessee-company had installed second-hand machinery worth Rs. 19,31,582 as against the new machinery

worth Rs. 12,09,771. In other words, all the lower taxing authorities as well as the Tribunal proceeded on the basis of valuation of the respective

types of machinery installed by the assessee-company in the manufacture of its products and looking at the question from the valuation point of

view it seems to us that the finding recorded by the Tribunal will have to bee accepted that the reconditioned machinery, though it formed an

important part of the company''s block, would not be the nucleus around which a new undertaking was formed, and if that be so, it will be difficult

to accept Mr. Joshi''s contention that the company should be regarded as an undertaking formed by transfer, to a new business, of plant or

machinery previously used in any other business.

6. Mr. Joshi then sought support for his contention by relying upon the provisions of section 80J of the Income Tax Act, 1961, where, qua the

valuation aspect, certain percentage has been laid down by the legislature. He pointed out that under sub-section (4) of section 80J it has been

provided that the section applies to any industrial undertaking which fulfils all the specified conditions and condition No.2 mentioned in sub-section

(4) is in pari material the same as is to be found in the old section 15C(2)(i), namely , the section applies to any industrial undertaking when ""it is

not formed by the transfer to a new business of a building (not being a building taken on rent or lease), machinery or plant previously used for any

purpose"" and under the Explanation it has been provided thus : ""Explanation. - Where -

(a) in the case of an industrial undertaking, any building, machinery or plant, or any part thereof previously used for any purpose, or

(b) in the case of the business of a hotel, or any part thereof, previously used as a hotel, or any machinery or plant, or any part thereof, previously

used for any purpose,

is, in either case, transferred to a new business, and the total value of the building, machinery or plant or part so transferred does not exceed

twenty per cent. of the total value of the building, machinery or plant used in the business, then for the purposes of clause (ii) of sub-section (4) and

clause (a) of sub section (6), the condition specified therein shall be deemed to have been complied with and the total value of the building,

machinery or plant or part so transferred shall not be taken into account computing the capital employed in the industrial undertaking or the

business of the hotel.

7. The contention of Mr. Joshi was, having regard to this percentage which has been fixed of valuation of plant or machinery which has been so

transferred as compared to the total value of the entire block, similar aspect should be taken into consideration in the instant case, for even

according to the assessee''s own showing such recondition machinery formed 13% of the total block in the first year, 20% in the third year, being

the relevant assessment year 1961-62. He, therefore, urged that the assessee-company should be regarded as an undertaking formed by the

transfer, to a new business, of machinery or plant previously used in any other business. It is not possible to accept this contention of Mr. Joshi for

other business. It is not possible to accept this contention of Mr. Joshi for the obvious reason that the Explanation containing a provision for fixing

certain percentage of valuation of such used machinery in the old provision, viz., section 15C(2)(i) of the Indian Income Tax Act, 192. In the

absence of any to such provision being found in the old section 15C(2)(i) it will not be possible to decide the question by reference to certain

percentage has been fixed in the Explanation which has been incorporated for the first time and has been brought on the statue book for the first

time and has been brought on the statue book for the first time in the 1961 Act. The question will have to be considered generally as to whether the

reconditioned machinery or previously used machinery could be regarded as a substantial part of the machinery with which the undertaking has

been formed or not and from that aspect of the mater the figures which become clear from the recondition statement filed before the Tribunal are

very eloquent for, according to that statement, at the end of accounting period relevant to the assessment year 1961-62, the machinery which was

admittedly not used not previously was of the value of Rs. 17,22,682 while the reconditioned machinery was of the value of Rs. 14,95,715.

Substantially, therefore. it cannot be said that the reconditioned machinery wen to form an industrial undertaking in question even during the

accounting period relevant to the assessment year 1961-62. Such a view has been taken by the Punjab and Haryana High Court in the case of

Commissioner of Income Tax Vs. Hindustan Milk Food Manufacturers Ltd., In that case the court was concerned with a similar question arising

u/s 15C of the Indian Income Tax Act, 19. The Tribunal had granted the relief to the asessee u/s 15C on the basis that substantial part of the

machinery was new as it was common ground that 80% of that machinery was absolutely new and 20% of the machinery was reconditioned. The

relevant observations of the Punjab and Haryana High Court are at page 232, which run as follows :

The main ground on which the Tribunal proceeded was that as the substantial part of the machinery is new, it is immaterial whether 20per cent. of

the machinery is old. According to the Tribunal for all intents and purposes the entire machinery should be treated as new. We see no fundamental

fallacy in this approach. Such a contention did find favour with the Madras High Court in Commissioner of Income Tax Vs. Fenner Cockill Ltd., .

Mr. Awasthy contends that the basis of percentage is not the basis can be taken into account under the 1922 Act. It is undoubtedly true. We have

not taken that as the basis. We have only used the proportion to illustrate the point. The basis for our view is the same as that adopted by the

Madras High Court in Commissioner of Income Tax Vs. Fenner Cockill Ltd., . Therefore, whether way the matter is examined, we are of the

opinion that the Tribunal was right in allowing the benefit of section 15C of the Act to the assessee.

8. It will appear from the above observations that reference to percentage was made by the Tribunal in its order and the same was approved by

the High Court. A court contention was raised on behalf of the department that such percentage would not be relevant under the old Act. But the

High Court has pointed out that percentage was not referred to for the purpose of making it the basis of its decision but the same had been used

for the purpose of illustrating the point and the court took the view that there was no fallacy in the approach of the Tribunal. By parity of reasoning

it may be stated that in the instant case also the reconditioned machinery formed only 20% of the entire block and having which had not been

previously used and the reconditioned machinery which was employed by the assessee-company in the manufacture of its products during the

accounting period relevant for the assessment year 1961-62, it would be correct to say that substantial part of the machinery that was used in the

manufacture of it products in the assessee-company in the relevant assessment year was new and not the reconditioned machinery. Having regard

to the above discussion it will not be possible to accept Mr. Joshi''s contention which he put forward on the basis of the conditions that are to be

found in the Explanation which has been added to section 80J of the 1961 Act.

9. Coming to the interpretation of the relevant expression that is to be found in section 15C(2)(i), it would be desirable to set out the material

provision. Under the main provision of section 15C exemption from tax has been grated to newly established industrial undertakings and sub-

section (2) goes on to indicate the type of industrial undertakings to which the section would apply and sub-section (2)(i) of section 15C runs as

follows :

(2) This section applies to any industrial undertaking which -

(i) is not formed by the splitting up, or the reconstruction of, business already in existence or by the transfer to a new business of building,

machinery or plant used in a business which was being carried on before the 1st day of April, 1948.

10. We are not concerned with the first part of the aforesaid provision but we are concerned with the latter part according to which the section

would apply to an industrial undertaking which is not formed by the transfer, to a new business, of building machinery or plant used in a business

which was being carried on before the 1st day of April, 1948. In other words, the relief or exemption granted by the main provision would not be

available if an industrial undertaking is formed by the transfer to a new business of machinery or plant used in a business. Unquestionably, in the

instant case, part of the machinery has been purchased anew by the industrial undertaking for its production and part of the machinery, which has

been called ""reconditioned machinery"", has been import by the assessee-company from the U.K. and according to the statement of reconciliation

at the end of the accounting period relevant to the assessment year 1961-62, the machinery which was not used previously was of the value of Rs.

17,22,682 while the reconditioned machinery was of the value of Rs. 14,95,715. The question is whether the industrial undertaking of the

assessee-company could be said to have been ""formed by the transfer, to a new business, of machinery or plant used in a business"". A two-fold

contention was raised before us by Mr. Kaka appearing for the assessee-company. In the first place, he urged that the reconditioned machinery

should not be equated with second-hand machinery or machinery which has been previously used but should be regarded as a new machinery.

Secondly, he urged that there was no evidence on record to show that this reconditioned machinery which had been imported by the assessee-

company from the U.K. had been used previously either in the U.K. from where it was imported or in India after it was imported but before it was

installed in the assessee''s factory : and in any case he urged that this reconditioned machinery was never previously used in India. Having regarded

to the view which we are taking on the latter part of the contentions urged before us, it would be unnecessary for us to decided the first contention

urged by him in support of his case. In support of the latter contention strong reliance was placed by him upon the decision of the Punjab and

Haryana High Court in Commissioner of Income Tax Vs. Hindustan Milk Food Manufacturers Ltd., A specific question as to whether on the facts

ad circumstances which obtain in the case before it, the assessee''s industrial undertaking was not formed by the transfer to its business of

machinery or plant previously used in any other business within the meaning of section 15C(2)(i) of the Indian Income Tax Act, 1922, for the

purpose of tax exemption in accordance with section 15C(1) of the said Act had been referred to the High Court. The facts were that the

assessee, which was a public company limited company and was engaged in the production of milk had for its establishment imported machineries

from the U.K. it was common ground that 80% of that machinery was absolutely new and 20% of the machinery was reconditioned. There was no

evidence that the reconditioned machinery was used in England, after reconditioning before it was sent out to India. A finding had been recorded

that the said machinery had the benefit of tax exemption u/s 15C in the United Kingdom. The assessee claimed tax exemption u/s 15C of the

Indian Income Tax Act, 1922, on the ground that the total capital invested in acquiring and installing the machinery had been expended for

purposes of this industry. The Income Tax Officer repelled the claim of the assessee and held that in order to get the benefit of section 15C, the

machinery must be totally new, and since, in his opinion, as part of the machinery was used previously in another business he refused to great the

benefit of the aforesaid provision. The Appellate Assistant Commissioner confirmed this decision of the Income Tax Officer while the Appellate

Tribunal reversed that decision and granted the assessee the benefit of section 15C. The department sought the reference to the High Court for

decision of the aforesaid question. In answering the question in favour of the assessee the Punjab and Haryana High Court observed thus-see

Commissioner of Income Tax Vs. Hindustan Milk Food Manufacturers Ltd.,

In our opinion the correct approach is that the machinery must have been in use in any other business in India and not in any business anywhere

else in the world. This view ample support from the phraseology used in the provision. The use of the word ''building'', in relation to transfer, clearly

indicates that the transfer is of a thing existing in India, whether that is building or machinery or plant, otherwise the legislature would not have

clubbed the word ''building'' along with ''machinery'' or ''plant''. In the very context of the provision, the machinery can be new or old and all that

would have to be seen is whether in the case of old machinery it had been used in a business in India or not. The object of this provision seems to

be that the benefit of section 15C is not available qua the same item twice. We are, therefore, clearly of the view that the contention of the learned

counsel to the contrary cannot be accepted."" It could appear clear from the aforesaid decision and the relevant observation which we have quoted

above that the expression ""machinery or plant used in any business"" occurring in sub-section in sub-section 2(i) of section 15C have been

interpreted by the Punjab and Haryana High Court in Commissioner of Income Tax Vs. Hindustan Milk Food Manufacturers Ltd., to mean

machinery or plant used in a business in India"" and not ""machinery or plant used in a business anywhere else in the world"". It is true that the words

in India"" do not occur in the relevant provision but such interpretation has been put on the relevant expression by the Punjab and Haryana High

Court on the two factors : first, that the provision also refers to a building the transfer of which is contemplated and such transfer contemplated is of

a thing existing in India and since the word ""building"" has been clubbed together with the words ""machinery and plant"", the machinery and plant, the

transfer of which is contemplated, must be machinery or plant which has been used in India; secondly, the object of the provision appears to be

that the benefit of section 15C should not be made available qua same item twice. It was having regard to these two factors that the Punjab and

Haryana High Court has put a particular interpretation on the relevant expression ""machinery or plant in business"". Since the very same expression

has come up for our interpretation in the present reference before us, we would adopt the same interpretation as it is highly desirable that while

interpreting all-India fiscal statues uniformity should be maintained.

11. Apart from interpretation aspect, on the facts in the instant case before us, it was not dispute by Mr. Joshi appearing for the revenue that there

was no material on record to show that this reconditioned machinery which had been used in the manufacture of its products by the assessee-

company during the accounting period relevant for the assessment year 1961-62 had been previously used either in the U.K. in its reconditioned

form or in India after its import into India by the assessee and before its installation in the assessee''s factory. This was a case where the

Commissioner of Income Tax had sought to revise the order of the Income Tax Officer who had initially granted the relief to the assessee and,

therefore, it was up to the revising authority to find material on record on the basis of which an inference could be drawn that the reconditioned

machinery which had been imported by the assessee-company had been previously used either in the U.K. or in India in any business. In the

absence of any such material on record, it will be difficult to came to the conclusion that the condition indicated in section 15C(2)(i) had been

satisfied or fulfilled so as to disentitle or disqualify the assessee-company from getting the relief conferred under the main provision of section 15C.

In our view, therefore, since it has not been established by material on record that the reconditioned machinery which had been imported by the

assessee-company from the U.K. had been previously used in any business either in the U.K. or in India prior to its installation in the assessee''s it

is not possible to accept the contention of Mr. Joshi that the assessee-company has disentitled itself to get the benefit of section 15C of the Act.

12. Having regard to the above discussion, we are of the view that the question referred to us needs to be answered in the affirmative and in favour

of the assessee. Department will pay the cost of the reference to the assessee.