
(1983) 12 MAD CK 0016

In the Madras High Court

Case No : Tax Case No. 669 of 1978 (Reference No. 403 of 1978)

Commissioner of Income Tax (Central), Madras

APPELLANT

Vs

S.S.M. Sizing Centre

RESPONDENT

Date of Decision : 05-12-1983

Acts Referred:

Income Tax Act, 1961 — Section 33, 33(1)(B)

Citation : (1985) 155 ITR 782

Hon'ble Judges : V. Ratnam, J; G. Ramanujam, J

Bench : Division Bench

Advocate : J. Jayaraman and Nalini Chidambaram, for the Appellant; G. Sarangan, for the Respondent

Judgement

Ramanujam, J.—The following questions of law have been referred to this court by the Income Tax Appellate Tribunal at the instance of the

Revenue as arising out of its order dated December 12, 1975, in I.T.A. Nos. 1916 of 1973-74 and 304 of 1974-75, relating to the assessment

years 1970-71 and 1971-72 :

(1) Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the assessee was entitled to the higher rate of

development rebate as provided in section 33(1)(b)(B)(i) in respect of machinery used by it in its business ?

(2) Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the operations carried on by the assessee

would amount to manufacture of textiles as specified in item 32 of the Fifth Schedule ?

2. The assessee in this case is a registered firm engaged in the business of warping, sizing and bleaching of cotton yarn. The company had incurred

certain expenditure amounting to Rs. 11,678 between April 1, 1969, and November 16, 1969, the date of commencement of its operations. The

company claimed this amount as a revenue expenditure or in the alternative as a pre-production expenditure to be capitalised and allocated to

depreciable asset. Development rebate was also claimed in case it is capitalised. The said expenditure consisted of factory wages, interest,

travelling, advertisement, etc. The ITO disallowed these items and also did not allow these to be capitalised and allocated for purposes of

development rebate and depreciation. The company had also incurred expenditure in the earlier years amounting to Rs. 27,467. This consisted of

mortgage deed expenses, interest, salary, guarantee commission, etc. This has been allocated between building and plant and machinery at Rs.

9,156 and Rs. 18,312. The company also claimed enhanced development rebate under s. 33(1)(b)(B)(i) in respect of the machinery on the ground

that they have been used for the manufacture of textiles. This claim was negated by the ITO.

3. The assessee took the matters in appeal to the AAC but without success. Thereafter, the matters were taken to the Tribunal. The Tribunal

following the decision of the Supreme Court in Challapalli Sugar Ltd. Vs. The Commissioner of Income Tax, A.P., Hyderabad, , held that so far as

items other than interest, the matter is governed by the decision of this court in Commissioner of Income Tax Vs. L.G. Balakrishnan and Bros. (P.)

Ltd., and in that view, the Tribunal directed the AAC to determine the items of expenditure allowable in the light of the said two decisions. As

regards the appeal relating to the assessment year 1971-72, the Tribunal held that the assessee is entitled to have the written down value reworked

for determining the cost for purpose of depreciation as has been done in the year 1970-71. As regards the assessee's claim for enhanced

development rebate under s. 33(1)(b)(B)(i) of the Act, the Tribunal held that since the assessee is engaged in warping, sizing and bleaching of

cotton yarn, the operations will fall under item 32 of the Fifth Schedule. According to the Tribunal, the word "textiles" occurring in item 32 of the

Fifth Schedule will amount to manufacture of textiles and, therefore, the assessee is entitled to development rebate in accordance with s. 33(1)(b)

(B)(i). Aggrieved by the said view of the Tribunal, the Revenue has sought and obtained a reference on the questions set out above.

4. In this reference, we are not concerned with the other items of dispute between the parties before the Tribunal. The dispute between the parties in this reference is confined to the assessee's claim for higher rate of development rebate provided for in s. 33(1)(b)(B)(i) read with item 32 of the Fifth Schedule. The Tribunal has actually found these facts : The assessee buys grey cotton yarn and with the aid of kier machine boils them with chemicals, then washes and bleaches with bleach liquor or with dye vats. Then, it is further loaded into a machine, squeezed, dried and bundled. Then the yarn is sized and warped in machinery with the aid of electrical hoist and at the same time starch and other chemicals are cooked and pumped inside the sizing machine. The yarn is then processed as sized yarn. The Tribunal has taken the view that these operations carried on by the assessee will attract item 32, that item 32 would cover not only woven fabric, but also anything which is capable of being woven and, therefore, the assessee is entitled to claim a higher development rebate provided for in s. 33(1)(b)(B)(i) of the Act. The Tribunal rejected the contention put forward on behalf of the Revenue that the expression ""textiles"" occurring in item 32 will cover only manufacture of cloth from raw material and will not take note of any intermediary process. The question is whether the view taken by the Tribunal is correct.

5. Item 32 of the Fifth Schedule to the I.T. Act is as follows :

Textiles (including those dyed, printed or otherwise processed) made wholly or mainly of cotton, including cotton yarn, hosiery and rope.

6. The scope of the item was considered by Division Bench of this court in an unreported decision an T.C. No. 151 of 1977 Commissioner of

Income Tax, Tamil Nadu-III Vs. North Arcot District Co-operative Spinning Mills Ltd., ., to which one of us was a party. In that case also the

Tribunal upheld the assessee's claim on the ground that cotton yarn will fall within the expression ""textiles"" On a reference, this court considered

the scope of s. 33(1)(b)(B)(i)(a) and held that the purpose of Schedule V is to specify the articles or things which will be covered by s. 33(1)(b)

(B)(i) and item 32 actually specifies textiles, cotton yarn, hosiery and rope. This court specifically refused to retract the scope of the expression

textiles"" to textiles made wholly or mainly of cotton but expressed the view that cotton yarn, hosiery and rope have been treated in the definition as

independent items of textiles. It was ultimately held in that case that the assessee who is a manufacturer of cotton yarn should be taken as a manufacturer of an item specified in entry 32 of the Fifth Schedule and that machinery and plant in respect of which development rebate has been claimed having admittedly been used in the manufacture of cotton yarn, a specified item in entry 32, the assessee is entitled to claim the benefit of the provisions in s. 33(1)(b)(B)(i). Reference has also been made in that case to an earlier decision of this court in Premier Mills Ltd. Vs.

Commissioner of Income Tax, , wherein entry 32 of the Fifth Schedule has been held to refer to textiles, cotton yarn, hosiery and rope for the purpose of s. 33. It cannot be disputed that for claiming benefit of s. 33(1)(b)(B)(i), the assessee must show that the machinery in respect of which a higher development rebate is claimed must be shown to have been used in the manufacture of textiles specified as item 32 in the Fifth Schedule, that is, textiles made wholly or mainly of cotton, cotton yarn, hosiery and rope. Therefore, the assessee who claims benefit of s. 33 must show that the machinery in respect of which development rebate is claimed had been used for the manufacture of either textiles made wholly or mainly of cotton or cotton yarn, hosiery and rope.

7. According to the assessee, the operations carried on by it such as warping, sizing and bleaching of cotton yarn amounts to a manufacturing activity and, therefore, the concerned machinery should be taken to have been used in the manufacture of cotton yarn. Thus, the question arises as to whether the activities carried on by the assessee can be taken to amount to manufacture of cotton yarn so as to attract s. 33(1)(b)(B)(i).

References has been made by the learned counsel for the Revenue to the following decisions in support of its stand that the activity carried on by the Assessee is not manufacture. South Bihar Sugar Mills Ltd., etc. Vs. Union of India (UOI) and Others, , is a case where the Supreme Court, while constructing the scope of item 14H of Schedule I to the Central Excises and Salt Act, 1944, held that the Central Excises and Salt Act charges duty on manufacture of goods, that the word "manufacture" implies a change but every change in raw material is not manufacture, that there must be such a transformation that a new different article must emerge having a distinctive name, character or use and that the gas generated

by the parties in that case was kiln gas and not carbon dioxide as known to the trade and, therefore, the kiln gas generated is neither carbon dioxide nor compressed carbon dioxide known as such to the commercial community and hence cannot attract item 14H in the First Schedule. In that case, the court was concerned with the question whether the gas generated did not amount to manufacture of gas so as to make the gas generated as excisable. Therefore, that decision cannot be taken to throw any light on the issue before us. In *Mcnicol v. Pinch* [1906] 2 KB 352, the court was constructing the scope of the expression "manufacture of saccharin" occurring in the Finance Act of 1901 and the Revenue Act of 1903, and the expression was construed as meaning "bringing into being saccharin". We do not see how this decision also helps the assessee. If the interpretation placed in that decision on the statutory expression is taken as a guide in this case, then manufacture of yarn can only refer to the activity of bringing into being an article called "cotton yarn". Therefore, the process of converting cotton into yarn can alone be termed as manufacture of cotton yarn and the manufacture of cotton yarn will not include any of the activities carried on by the assessee after it purchases cotton yarn. In *P.C. Cheriyan Vs. Mst. Barfi Devi*, , the expression "manufacturing purposes" occurring in s. 106 of the Transfer of Property Act was held not to include a business of retreading of tyres. In that case, it was held that a broad test for determining whether a process is a manufacturing process is whether it brings about a complete transformation of the old components so as to produce a commercially different article or commodity and that retreading of old tyre does not bring into being a commercially distinct or different commodity, that the old tyre retains its original character or identity as tyre, that retreading does not completely transform it into another commercial article although it improves its performance and serviceability as a tyre and that no new or distinct article emerges from retreading of old tyres. This decision of the Supreme Court helps the Revenue in this case. Admittedly, in the instant case, cotton yarn is purchased by the assessee and not manufactured by it. After the purchase of the cotton yarn, the assessee carries on operations like wrapping, sizing and bleaching of yarn produced by or purchased from someone else. The application of sizing materials and bleaching agent on the yarn purchased by the assessee does not and cannot amount to manufacture

or production of cotton yarn. The yarn even after the treatment given to it by the operations such as wrapping, sizing and bleaching is not

transformed into any other commercial article, though the operations carried on by the assessee improves its performance, the cotton yarn treated

by the assessee with the above operations retaining its basic structure and identity and after the treatment, it does not cease to be cotton yarn. Even

after the process of wrapping, sizing and bleaching, it continues to be cotton yarn and no new commercial product comes into existence.

Therefore, the assessee cannot be taken to have used the machinery for the manufacture of cotton yarn as such. In *The Deputy Commissioner of*

Sales Tax (Law), Board of Revenue (Taxes) Vs. O. Sadasivan, the question arose as to whether dyed and coloured cotton yarn falls under entry

4(ii) of the Second Schedule to the Kerala General Sales Tax Act, 1963. The court held that despite the process of dyeing and colouring, cotton

yarn would remain cotton yarn and it does not undergo a process of transformation so as to make sales tax exigible separately on that

commodity after the process of dyeing and colouring. In that case, the Revenue contended that after dyeing and colouring, the cotton yarn has

become a commercially different product and, therefore, separate sales tax is exigible on the dyed and coloured cotton yarn but that contention

was rejected by the court and held that even after dyeing and colouring, the cotton yarn continues to be the same article. In *Commissioner of Sales*

Tax v. Harbilas Rai & Sons [1968] 21 STC 17, the Supreme Court had occasion to construe the word "manufacture", occurring in Explanation

II(ii) to s.2(h) of the UP Sales Tax Act, 1948. The Supreme Court held that the word "manufacture" has various shades of meaning, and in the

context of sales tax legislation, if the goods to which some labour is applied remain essentially the same commercial article, it cannot be said that

the final product is the result of manufacture. In that case, the assessees who were dealers in pig bristles, bought bristles plucked by Kanjars from

pigs, boiled them, washed them with soap and other chemicals, sorted them out according to their sizes and colours, tied them in separate bundles

of different sizes and dispatched them to foreign countries for sale. The question arose whether the bristles so sent were manufactured goods within

the meaning of Explanation II(ii) to s. 2(h) of the said Act. The court held that the bristles dispatched by the assessee were not taxable as they are

not manufactured goods. A Division Bench of this court in Writ Appeal No. 325 of 1977 (S.S.M. Finishing Centre v. Secretary to Government),

to which one of us was a party, has actually dealt with these operations such as those carried on by the assessee and held that it is not a

manufacturing process. In that case, the question arose as to whether the appellants were manufacturing or producing any principal product so as

to fall within the notification issued by the Government in G.O. Ms. No. 2072, Public Works Department, dated November 19, 1969, which

exempted from payment of electricity charges, if electricity is used in the process of manufacturing or producing a principal product. The operations

carried on in that case were bleaching, sizing and colouring of cotton yarn and cotton fabrics which the appellants therein purchased from others.

The court was clearly of the opinion that having regard to the very process employed by the appellants, namely, bleaching, sizing and colouring

cotton yarn or cotton fabrics which were purchased from others, there is no question of the appellants manufacturing or producing any product in

their undertaking. The view expressed in that decision clearly applies to the facts of this case.

8. The learned counsel for the assessee relies on the decision of a Bench of this court in Commissioner of Income Tax, Tamil Nadu-I Vs. Simpson

and Company Ltd., , as supporting his stand that the activities carried on by the assessee in this case amount to manufacturing activity for the

manufacture or production of cotton yarn which comes within the expression ""textiles"" occurring in item 32 of the Fifth Schedule. In that case, the

assessee engaged in the construction of bodies for buses, motor-trucks, etc., on chassis supplied by the customers, purchased various items of

new machinery and installed the same in its plant. The assessee's claim for grant of development rebate at a higher percentage under s. 33(1)(b)

(B)(i) of the I.T. Act, 1961, was rejected by the ITO but it was allowed by the Tribunal and that was upheld by this court holding that a bus body

can be regarded either as an automobile ancillary or the end result of the construction, on the very skeleton of a chassis, the body of a motor-truck

or bus and hence the items of machinery engaged in this kind of process would be entitled to higher development rebate. The Tribunal found that

the machinery will fall under items 5, 10 and 20 of the Fifth Schedule. Item 5 refers to internal combustion engines, item 10 refers to the machinery

engaged in the construction, production or manufacture of motor-trucks and buses, and item 20 refers to automobile ancillaries. The court, while upholding the order of the Tribunal, observed that the assessee was engaged in the construction of bus bodies, motor-trucks and other vehicles, that the process by which the assessee makes a mere chassis into a full-fledged motor bus or a truck is a manufacturing process and the machinery used for that manufacturing process should be taken to be entitled to the benefit of higher development rebate. Therefore, that decision cannot be of any help to the assessee. In Commissioner of Income Tax, Andhra Pradesh Vs. Vijaya Spinning Mills Ltd., , a Division Bench of the Andhra Pradesh High Court held that concerns manufacturing cotton yarn are also entitled to the higher development rebate on their plant and machinery under s. 33(1)(b)(B)(i) read with entry 32 of Schedule v, like industries manufacturing textiles. This decision is in quite accord with the view taken by this court in T.C. No. 151 of 1977 Commissioner of Income Tax, Tamil Nadu-III Vs. North Arcot District Co-operative Spinning Mills Ltd., , and it does not lay down any different principle. It does not touch on the question as to whether warping, sizing and bleaching amount to manufacture. Therefore, this decision also cannot support the assessee's stand at all. The learned counsel then refers to the decision of the Supreme Court in Idandas v. Anant Ramchandra, AIR 1982 SC 127, where the conversion of wheat into flour has been taken as a manufacturing process. But there, wheat and flour are treated as different commercial products and when wheat is converted into flour by applying a process and as that process brings into existence a new commercial product apart from wheat, it will definitely be a manufacturing process. Therefore, that decision also is not of any help to the assessee.

9. It is seen that the view taken in Deputy Commissioner of Sales Tax v. Sadasivan [1978] 42 STC 201, holding that even after the process of dyeing and colouring of cotton yarn, it continues to remain as cotton yarn has been accepted and followed by the Gujarat High Court in Nerol Abendaly v. Union of India [1979] ELT 181, and of the Bombay High Court in Shreemowas Cotton Mills Ltd. v. Union of India [1981] ELT 867 and of the Delhi High Court in J.K. Cotton Spinning and Weaving Mills Co. Ltd. v. Union of India [1981] ELT 887. In view of the fact that the

order of the Tribunal holding that the process employed by the assessee such as warping, sizing and bleaching amount to manufacture of textiles

without giving any reason for coming to such a conclusion is not legally tenable, we have to, therefore, answer both the questions in the negative

and against the assessee. The assessee will pay the costs of the Revenue. Counsel's fee Rs. 500.