(2012) 06 GUJ CK 0018

In the Gujarat High Court

Case No : Tax Appeal No. 96 of 2000

Jhaveri Coaters (P) Ltd.	APPELLANT
Vs	
Asstt. CIT	RESPONDENT

Date of Decision : 19-06-2012

Acts Referred:
Income Tax Act, 1961 — Section 33B, 80HH, 80I, 80IA

Citation : (2012) 06 GUJ CK 0018

Hon'ble Judges : Harsha Devani, J;Akil Abdul Hamid Kureshi, J

Bench : Division Bench

Advocate : J.P. Shah with Manish Shah, for the Appellant; K.M. Parikh, for the Respondent

Final Decision : Allowed

Judgement

1. This appeal filed by the assessee calls in question legality of judgment of the Tribunal dt. 10-3-2000. While admitting the appeal on 18-9-2000, Division Bench of this court raised following substantial question of law :

Whether, the appellant was manufacturing an article or thing and therefore, was entitled to section 80IA relief?

Issue involved is with respect to claim of the assessee of deduction u/s 80IA of the Income Tax Act, 1962, (the Act for short) which was disallowed by the respondent authorities on the ground that the assessee cannot be stated to be manufacturing an article or thing. We are concerned with the assessment year 1995-96. For the said assessment year, the assessee filed its return of income on 30-11-1995 declaring a total income of Rs. 3,06,127. Assessee had claimed deduction u/s 80IA as it stood at the relevant time. Return was taken in scrutiny. AO called upon the assessee to justify its claim for deduction. Before the AO, the assessee submitted that assessee was a small scale industrial undertaking located in backward area and was engaged in the manufacturing of laminated sacks. Assessee pointed out that the assessee undertakes the process of laminating woven sacks. Such process is undertaken industrially with the use of various chemicals. At the end of such process, a new product comes into existence. It was pointed out that such end product namely, laminated HDPE bags can be used in chemical industry for storing fertilizer, etc. On the other hand, woven sack (without lamination) cannot be used for storing chemicals and fertilizers.

In support of their stand, the assessee also produced the experts opinion with respect to the process undertaken on the woven sack to convert them into laminated HDPE bags. The assessee pointed out that its manufacturing unit is registered with respective Government bodies as an industry. Necessary licenses also have been issued by such Government authorities. Assessee is a registered small scale industrial unit. The assessee contended that the provisions of section 80IA being beneficial in nature, the same should be liberally construed and the benefit of deduction should be made available to the assessee. Assessee further contended that it is manufacturing and producing laminated bags fit for use of fertilizer and chemical industry which use it could not have been put to without the process undertaken by the assessee. The assessee relied on several decisions on the issue to contend that the process undertaken by it amounts to manufacturing.

2. The AO however, did not accept the contentions of the assessee. He held that the assessee is not engaged in manufacture or production of an article or thing. He was of the opinion that raw material purchased by the assessee does not undergo any change in identity or character. He observed that there was no substantial value addition between the raw material and final product.

3. The assessee carried the issue in appeal before CIT(A) who however, confirmed the view of the AO by giving brief reasons.

4. The assessee thereupon approached the Tribunal and placed reliance on the material placed before the AO as well as experts opinion produced on record. The assessee also relied on large number of authorities of different High Courts as well as the Apex Court. The Tribunal however, without referring to such decisions observing that many of these cases have been decided by the Courts with reference to particular business activity involved in the case on hand, proceeded to independently ascertain for itself whether activities undertaken by the assessee can be stated to be manufacturing of an article or a thing. The Tribunal recorded that the assessee was admittedly processing semi-finished HDPE woven bags by undertaking process of lamination by coating by chemical process. The Tribunal however, was of the opinion that in the process the only change brought about was that bags get laminated. Even though such laminated bags are of higher quality and may fetch a higher price than the semi finished bags, the assessee was not manufacturing any new product which was commercially different from what was purchased for processing. In short, the Tribunal was of the opinion that before and after the process undertaken by the assessee, the bags remained as such and that such process therefore, cannot amount to

manufacture or production of an article or thing.

5. Learned counsel Shri J.P. Shah for the appellant vehemently contended that the respondent authorities and Tribunal erred in holding that the assessee did not manufacture an article or thing. Drawing our attention to the process undertaken by the assessee, as pointed out to the AO as well as basing heavy reliance on opinion of Shri K.S. Thakker, chartered engineer/professional engineer dt. 18-10-1999, counsel submitted that the process undertaken by the assessee would amount to manufacturing an article or thing. He submitted that the assessee admittedly purchased semi-finished HDPE bags. After subjecting such raw materials to chemical process in the unit of the assessee, laminated HDPE bags were manufactured. He pointed out that the cost of semi'' finished HDPE bags was Rs. 4 to Rs. 5 per kilogram whereas laminated HDPE bags would cost Rs. 9 per kilogram. Counsel further submitted that semi-finished HDPE bags could be put to entirely different use than what a laminated HDPE bag could be. Semi-finished HDPE bags are highly porous and that therefore, cannot be used for fertilizer and chemical industry which the laminated HDPE bags could be. In short, counsel would contend that entirely new article comes into existence through such process. Such new product is meant for entirely different set of uses as compared to semi-finished product. Counsel relied on the following decisions :

(1) India Cine Agencies Vs. Commissioner of Income Tax, Madras, , wherein the apex Court in relation to claim of assessee for deduction under sections 80HH and 80I of the Act had the occasion to interprete the terms production and manufacture.

(2) Titanor Components Ltd. Vs. Commissioner of Income Tax and Another, , wherein the Delhi High Court held that coating of noble rentals with oxides would bring about a change in its character and use making it fit for use in the production of chlorine and caustic soda. Process would therefore, amount to manufacturing of an article or thing.

(3) Commissioner of Income Tax, Mumbai Vs. Emptee Poly-Yarn Pvt. Ltd., , wherein the Apex Court applied the test of structural change to hold that twisting and texturising partially oriented yarn through thermo mechanical process would bring about a structural change in the yarn.

(4) The Commissioner of Income Tax Vs. Jamal Photo Industries (I) Pvt. Ltd., , wherein the Madras High Court observed that though expression "manufacture" involves the concept of changes effected to a basic raw material resulting in the emergence of, or transformation into, a new commercial commodity, it is not necessary that the original article or material should have lost its identity completely. All that is required is to find out whether as a result of the operation in question, a totally different commodity had been produced having its own name, identity, character or end use.

(5) Commissioner of Income Tax Vs. Darshak Ltd., , wherein in context of

deduction u/s 80I of the Act, the Division Bench of Karnataka High Court observed that the word manufacture is to be understood in a wide sense. The court held that transforming the plain glassware into decorative glassware with a process which was irreversible amounted to manufacturing activity.

(6) Commissioner of Income Tax Vs. Kashiram Textile Mills (P.) Ltd., , wherein Division Bench of this court held that dyeing and printing of grey cloth amounted to manufacture.

(7) The Commissioner of Income Tax Vs. Alfa Lamination, , wherein the Division Bench of this court observed that whether a particular activity amounts to manufacture or not would always be a question dependent upon the facts and evidence on record and would be based on the facts of each case. The only issue which would call for an inquiry is as to whether correct tests have been applied after finding the facts on record. It was observed that broadly, the requirement is that the raw material must be, in the first instance, subjected to a process of such a nature that it cannot be termed to be the same as the end-product after the raw material undergoes the process of manufacture. The article produced must be regarded by the trade as a new and distinct article having an identity of its own, an independent market after the commodity is subjected to the process of manufacture. It was observed that the nature and extent of the process would vary from case to case.

6. On the other hand, learned counsel Shri Parikh, for the Revenue opposed the appeal contending that the Revenue authorities as well as the Tribunal have correctly applied the tests laid down in various decisions of this Court as well as the Apex Court. He contended that the assessee is not undertaking any process which amounts to manufacturing. All that the assessee did was to laminate semi-finished HDPE bags. Nevertheless, the product remained the same. No new product distinctly marketable came into existence. Drawing our attention to the observations made by the Apex Court and by the Tribunal in the impugned orders, he contended that no interference is called for. Heavy reliance was placed on decision of the Apex Court in case of Commissioner of Income Tax, Orissa and Others Vs. N.C. Budharaja and Company and Others, , wherein the Apex Court had the occasion to interprete the terms manufacture and production. It was observed that while every manufacture can be characterised as production, every production need not amount to manufacture. We may however, record that such observations were made in context of claim of the assessee for deduction u/s 80HH of the Act with respect to their activities of construction of dam. It was in this context the Apex Court held that construction of dam cannot be stated to be a manufacture of article or thing. The assessee was therefore, not entitled to deduction u/s 80HH of the Act.

7. Having thus heard learned counsel for the parties and having perused the documents on record, we may examine the facts little more closely. The assessee, a small scale industrial unit undertakes the: process of converting semi finished HDPE bags into laminated HDPE bags through chemical process. The

semi-finished bags tend to be porous and are therefore, not used for the purpose of chemicals and fertilizer industries. Laminated HDPE bags on the other hand could be put to more sophisticated use. The assessee had pointed out to the respondent authorities that semi-finished bags can be used only for use such as storage of cement, etc. whereas the laminated bags could be used for more sophisticated use such as for fertilizer and chemical industry.

8. Further, it was pointed out that the semi-finished bags were available @ Rs. 4 to Rs. 5 per kilogram whereas laminated HDPE bags would fetch close to Rs. 9 per kilogram in market. Thus, there is a vast difference in prices between semi-finished and finished product. The very process which the assessee undertakes was outlined by its chartered engineer in his report dt. 18-10-1999 which suggests that the assessee undertakes the task of laminating a thin film of laminated HDPE on a HDPE woven cloth which after such process becomes laminated HDPE woven cloth of higher commercial value with no porosity. HDPE woven cloth which is raw material for this purpose is a porous material due to which HDPE woven cloth bags without lamination are used for packing low cost material such as cement. On the other hand, laminated HDPE bags are used for high cost material like fertilizer and chemicals etc. for which uses, non-laminated HDPE bags cannot be used due to porosity which would result into considerable wastage of materials and also adverse atmospheric effect. The process undertaken by the assessee was described in the following manner :

The process of manufacturing laminated HDPE woven cloth, is described in an enclosed line diagram, where, initially woven HDPE cloth (fabric) roll is taken on unwinder-machine, which feeds the cloth (fabric) to hot goodet for preheating, from hot goodet, cloth (fabric) is taken on webalgner which does the function of aligning and setting the needed tension on fabric. From Webalgner, cloth (fabric) is taken to lamination machine where lamination film is fed from film producing machine, which in turn is fed by learned PE extrusion machine. And thus a film coating takes place on one side during forward motion of fabric.

The one side film coated cloth is brought to cold good get, which does the function of cooling.

The cloth is then fed to the film-slitter, to reversing mechanism which reverses the side of fabric for other side coating. Thereafter, reversed fabric is taken once again to hot-goddet and then whole cycle of operation is repeated. After coating on the reverse side, fabric duly coated on both side, is brought to winder-mechanism to form a roll of laminated fabric.

9. From the above noted facts, it clearly emerges that the two products before and after the process undertaken by the assessee are entirely distinct and different. They have different uses and different identity under the market. There is considerable difference in price between the two products. In fact, laminated HDPE bags would cost per kilogram double than what the raw HDPE bags would. Their uses are also vastly different. This is so firstly because the non-laminated

HDPE bags tend to be porous and therefore, the stored material is likely to suffer greater loss. Such porous material also permits greater atmospheric effect on the stored material. On the other hand, lamination insulates the stored materials from both such adverse effects. On account of considerable difference in cost and on account of difference in quality, both sets of bags are likely to be used for entirely different purposes.

10. We may note that Apex Court in case of India Cine Agencies (supra), observed that manufacture is a transformation of an article, which is commercially different from the one, which is converted. The essence of manufacture is the change of one object to another for the purpose of making it marketable. The essential point thus is that in manufacture something is brought into existence, which is different from that which originally existed.

11. In case of Emptee Poly-Yarn (P) Ltd. (supra), the Apex Court noted with approval observations of an earlier decision in case of Commissioner of Income Tax-V, New Delhi Vs. Oracle Software India Ltd., wherein it was observed that if an operation/process renders a commodity or article fit for use for which it is otherwise not fit, the operation/process falls within the meaning of the word manufacture. In the said decision the Apex Court, as already noted, applied the test of structural change and held that twisting and text rising partially oriented yarn through thermo mechanical process brings about a structural change in yarn and thus makes process manufacture.

12. In the present case also, the process undertaken by the assessee brings about a structural change in semi-finished HDPE bags and brings into existence laminated HDPE bags which are put to entirely different kind of use.

13. This court in case of Alfa Lamination (supra) had emphasized that the new article which comes into existence through the process undertaken by them must be regarded by trade as a new and distinct article having an identity of its own, an independent market after the commodity is subjected process of manufacture. Surely, in the present case, a purchaser would certainly not bracket both the products together namely, semi-finished HDPE bags and laminated HDPE. Because of the very difference in the nature of two bags, their utility arid cost, both would be put to entirely different use.

14. As held by Madras High Court in case of Jamal Photo Industries (I) (P) Ltd. (supra), though expression manufacture involves the concept of changes in the first product, it is not necessary that original article or material could have lost its identity completely.

15. We may note that this question whether the assessee was involved in manufacturing of article or thing is germane since deduction under s. 80-IA of the Act was claimed by the assessee on the premise that its total income included profit and gain derived from business of industrial undertaking;" Term "industrial undertaking" is defined in clause (b) of sub-section (12) of section 80IA to carry the same meaning assigned to it in the explanation to section 33B.

Such Explanation of 33B reads as under :

Explanation : In this section, industrial undertaking means any undertaking which is mainly engaged in the business of generation or distribution of electricity or any other form of power or in the construction of ships or in the manufacture or processing of goods or in mining.

16. It was in this background necessary to ascertain whether the assessee was an industrial undertaking engaged in the manufacture of article or thing. The sum total of above discussion is that in our view, Revenue authorities as well as the Tribunal committed an error in holding that the process undertaken by the assessee did not amount to manufacture of an article or thing. We answer the question in the affirmative i.e. in favour of the assessee and against the Revenue. Orders under challenge are get aside. Tax appeal is allowed and disposed of.

