

IN THE HIGH COURT OF JUDICATURE AT MADRAS

RESERVED ON : 11.04.2017
DELIVERED ON : 10.07.2017

Coram

The Honourable Mr. Justice RAJIV SHAKDHER
and
The Honourable Mr. Justice R. SURESH KUMAR

Tax Case (Appeal) Nos. 533 to 538 of 2010, 1217 to 1220 of 2010
and 787 and 788 of 2014

1. The Commissioner of Income tax
Pondicherry

.... Appellant in T.C.(A) Nos. 533 to
538 of 2010, 787 and 788 of 2014

Vs

1. M/s. Leo Fasteners
A-27A, Industrial Estate,
Thattanchavady,
Pondicherry - 9.

.... Respondent in T.C.(A) Nos. 533 to
538 of 2010, 787 and 788 of 2014
and Appellant in
T.C.(A) Nos. 1217 to 1220 of 2010

2. The Assistant Commissioner
of Income Tax
Circle I, Pondicherry

... Respondent in TCA 1217 to 1220/10

Prayer : Appeals filed under Section 260A of the Income Tax Act, 1961 against the orders dated 28.08.2009 and 12.11.2010 on the file of the Income Tax Appellate Tribunal, Chennai "B" Bench passed in I.T.A. Nos. 2057 to 2062/MDS/2008 and I.T.A. Nos. 171, 172, 749, 750, 1083, 1084/MDS/2010 respectively and appeal against the order of the Commissioner of Income Tax (appeals) in I.T.A. Nos. 174, 173, 616, 615, 172, 617/07-08 and I.T.A. Nos. 172/07-08 & 400/09-10 dated 31.07.2008 and I.T.A. Nos. 347, 397, 400/09-10 dated 29.04.2010 respectively and appeal against the order of the Additional Commissioner of Income Tax, Puducherry Range, Pondicherry (Circle I) made in P.N.No/G.I No AABFL06523/303-L/Assessment year 2000-2001 dated 29.12.2006, Assessment year 2001-2002 dated 29.12.2006, Assessment year 2002-2003 dated 31.12.2007, Assessment year 2003-2004 dated 31.12.2007, Assessment year 2004-2005 dated 29.12.2006, Assessment year 2005-2006 dated 31.12.2007, Assessment year 2004-2005 dated 29.12.2006, Assessment year 2005-2006 dated 31.12.2007, Assessment year 2006-2007 dated

29.12.2008, Assessment year 2007-2008 dated 18.12.2009 , Assessment year 2006-2007 dated 29.12.2008 and Assessment year 2007-2008 dated 18.12.2009 respectively.

For Appellant/Revenue : Mr.J.Narayanasamy

For Respondents/Assessee : Mr.K.Ravi for M/s.Rugan & Arya

C O M M O N J U D G M E N T

(Judgment of the Court was delivered by RAJIV SHAKDHER,J.)

1. The captioned matters concern twelve (12) appeals. Out of which, eight (8) appeals have been filed by the Revenue, i.e., T.C.(A)Nos.533 to 538 of 2010 and 787 and 788 of 2014, while the remaining four (4) appeals have been filed by the Assessee, i.e., T.C.(A)Nos.1217 to 1220 of 2010. Out of the eight (8) appeals filed by the Revenue, six (6) appeals assail the order of the Income Tax Appellate Tribunal (in short 'the Tribunal') dated 28.08.2009, while the remaining two (2) assail the order of the Tribunal dated 12.11.2010. Likewise, four (4) appeals, filed by the Assessee, assail the order of the Tribunal dated 12.11.2010.

2. The record shows that six (6) appeals have been disposed of by the one bench of the Tribunal, by a common order, while the other six (6) appeals have been disposed of by another bench of the Tribunal via another common order. As a matter of fact, one member of the Tribunal is common to both orders.

2.1. Counsel for parties are agreed that there is a common thread and rationale running through the impugned orders of the Tribunal, which has left both sides aggrieved.

2.2. In order to give a synoptic view of the various assessment orders and orders-in-appeal passed, albeit, qua different periods by the authorities below, we have set forth the details pertaining to the same, in the form of a table set out hereafter:

T.C. (A) Nos.	Filed by	Assessment year	Assessment Order	CIT (A) order	Order of the Tribunal
533/2010	Revenue	2000-01	29.12.2006	31.7.2008	28.08.2009
534/2010	Revenue	2001-02	29.12.2006	31.7.2008	28.08.2009
535/2010	Revenue	2002-03	31.12.2007	31.7.2008	28.08.2009
536/2010	Revenue	2003-04	31.12.2007	31.7.2008	28.08.2009

537/2010	Revenue	2004-05	29.12.2006	31.7.2008	28.08.2009
538/2010	Revenue	2005-06	31.12.2007	31.7.2008	28.08.2009
787/2014	Revenue	2006-07	29.12.2008	29.4.2010	12.11.2010
788/2014	Revenue	2007-08	18.12.2009	29.4.2010	12.11.2010
1217/2010	Assessee	2004-05	29.12.2006	31.7.2008	12.11.2010
1218/2010	Assessee	2005-06	31.12.2007	31.7.2008	12.11.2010
1219/2010	Assessee	2006-07	29.12.2008	29.4.2010	12.11.2010
1220/2010	Assessee	2007-08	18.12.2009	29.4.2010	12.11.2010

3. Given the aforesaid state of affairs, while, narrating the facts and discussing the issues, we would be describing the parties as Assessee and Revenue, as against Appellant and Respondent.

4. The appeals, mainly veer around two (2) aspects, though cumulatively, several questions of law have been framed. The first aspect concerns the claim of deduction made by the Assessee under Section 80IB of the Income Tax Act, 1961 (in short, 'the 1961 Act'). The Assessee, evidently, has two units, which were set up at two different points in time and, are ubiquitously referred to by the Authorities below as Unit-I and Unit-II. The Assessee claims separate deduction under Section 80IB of the 1961 Act at the prescribed rates qua both Unit-I and Unit-II, on the ground that each unit, by itself, is separate industrial undertaking. The Revenue's contention that the two units have emerged by a process of splitting and/or reconstruction of the existing undertaking, is vigorously contested by the Assessee.

4.1. Via the aforementioned assessment orders, the Assessee has declined the relief qua both Unit-I and Unit-II, broadly, on the ground that both Units were formed by splitting and reconstruction of existing undertakings.

4.2. The Commissioner of Income Tax (Appeals)s [in short CIT(A)s] have partly allowed the appeals. The order dated 31.07.2008, passed by, one CIT(A) has been followed in substance by the other CIT(A), which passed the order dated 29.04.2010. In doing so, the CIT(A)s have allowed the Assessee to claim deduction, as was sought for, at the rate of 25%, vis-a-vis profits generated qua Unit-I and, in so far as Unit-II is concerned, deduction claimed has been scaled down from 100% to 25%, based on the broad reasoning that it is not an independent

unit, which can exist on its own.

4.3. The Tribunal via the aforementioned impugned orders, has sustained the views taken by the CIT(A)s.

4.4. It is, on account of this, both the Assessee and the Revenue are aggrieved and, thus, have preferred the captioned appeals.

5. The second aspect, which arises for consideration, is embedded in T.C.(A)Nos.1219 and 1220 of 2010. As regards this aspect, the Assessee is aggrieved by the fact that the Tribunal has upheld the computation of deduction under Section 80IA, by allowing for squaring off loss incurred by, one, Unit, albeit, for earlier years. This, according to the Assessee, is contrary to the judgment of the Tribunal rendered in : Rangamma Steels and Malleables V. Assistant Commissioner of Income Tax.

6. Before we proceed further, it may be relevant to cull out the questions of law, which have been framed qua the captioned appeals:

T.C.(A)Nos. 533 to 538 of 2010:

(i). Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in law in holding that the Assessing Officer cannot reconsider the issue of granting the deduction under Section 80IB after the lapse of time, even if there is a survey in the premises of the assessee and findings of the survey shows that the assessee has manipulated his profits so as to get maximum deduction under Section 80IB of the Act ?

(ii). Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in ignoring the provisions of Section 80IA(10) read with 80IA(13) and give suitable direction to the Assessing Officer to reconsider the issue on the basis of the materials available on record ?

T.C.(A)Nos.1217 and 1218/2010:

(i). Whether on the facts and in the circumstances of the case, the Appellate Tribunal was right in upholding the denial of the benefit under Section 80 IB to Unit 2, when under identical circumstances deduction has been allowed to Unit 1, as well as other entities similarly placed ? and

(ii). Whether on the facts and circumstances of the case, the Tribunal was right in upholding denial of deduction under Section 80 IB when all the conditions laid down in the section have been met by the assessee, on the ground that there are transactions between inter connected undertakings and diversion of profits to the eligible undertaking, without first directing the assessing officer to exercise his

powers under Section 80IB(8) and 80 IA(10) and ascertain the quantum of inflated profits if any?

T.C.(A)Nos. 1219 and 1220/2010:

(i). Whether on the facts and in the circumstances of the case, the Appellate Tribunal was right in upholding the denial of the benefit under Section 80IB to Unit 2, when under identical circumstances deduction has been allowed to Unit 1, as well as other entities similarly placed? and

(ii). Whether on the facts and circumstances of the case, the Tribunal was right in upholding denial of deduction under Section 80 IB when all the conditions laid down in the section have been met by the assessee, on the ground that there are transactions between inter connected undertakings and diversion of profits to the eligible undertaking, without first directing the assessing officer to exercise his powers under Section 80IB(8) and 80 IA(10) and ascertain the quantum of inflated profits if any?"

(iii). Whether the Tribunal was right in upholding the computation of deduction under Section 80IA by reducing the losses of one unit for earlier years, contrary to the decisions of a co-ordinate bench in which the judicial member was common?

TCA 787 and 788 of 2014:

(i) Whether on the facts and in the circumstances of the case, the Tribunal was right in law in holding that deduction under Section 80IB is not proper?

7. Having regard to the above, and in order to adjudicate upon the captioned appeals, the following broad facts are required to be noticed. The facts, which we have been able to glean from the records placed before us, are as follows:

8. The Assessee, it appears, at the relevant point in time, was in the business of manufacturing High Tensile Precision Fasteners (in short Fasteners), which are also referred to as "nuts" in the market. These nuts are extensively used in the automobile industry.

8.1. It appears that the Assessee, which is a partnership firm, comprised of one Mr.L.M.Shah and his son Mr.A.L.Shah. The Assessee firm was constituted in March, 1998.

8.2. During the period relevant for Assessment year (A.Y.) 1998-99, the Assessee purchased two Nut former machines. This was followed by the Assessee purchasing in May, 2002, one more Nut Former machine, though, via the import route. For the next five (5) years, relevant for A.Ys.1998-99 and 2002-03, the Assessee claimed deduction at the rate of 100% of the profits derived by it for conducting the business of manufacturing fasteners/nuts.

8.3. The Assessee claims that it set up a second Unit and, started commercial production qua the said Unit on 23.10.2003. Since, the second unit was set up, the Assessee claimed deduction vis-a-vis this unit, which is referred to as Unit -II, by the Authorities below, at the rate of 100% of the profits derived in respect of the said unit, with effect from A.Y.2004-05.

8.4. The Assessing Officers, appear to have an objection to the Assessee claiming Section 80IB deduction vis-a-vis both units. According to the Assessing Officers, Unit -I and Unit -II were not, by themselves, "integrated units". By which, it appears, the Revenue meant independent industrial undertakings.

8.5. In other words, their view was that the units were formed by splitting and/or reconstructing existing business. In coming to this conclusion, the Assessing Officers traced the business carried out by the father and son, i.e., Mr.L.M.Shah and Mr.A.L.Shah (collectively referred to as Messrs Shah & Shah) to 1984, when, an entity in the form of private limited company, by the name, Fastenex Private Limited (in short 'FX'), was incorporated and set up by them.

8.6. The Assessing Officers noticed that, in the first instance, FX had imported a Nut Former Machine, in 1984, from a Taiwanese source, which was followed by two other machines, being imported, albeit, in 1994 and 1996.

8.7. The incorporation and setting up of FX was followed by, Mr.A.L.Shah, floating a proprietary concern, under the name and style of Formex (in short FOX). Resultantly, in the name of proprietary concern, between 1994 and 1996, four (4) Nut Former machines were purchased. FX, evidently, claimed deduction under Section 80IA of the 1961 Act between 1994-95 and 1999-2000, at the rate of 100%.

8.8. As alluded to above, in between the Assessee's first Unit, i.e., Unit-I was set up in March, 1998, whereby, deduction was claimed under Section 80IB of the 1961 Act, at the full rate of 100% for first five (5) years, i.e., periods relevant to A.Ys.1998-99 and 2002-2003.

9. Apart from the aforesaid entities, the Assessing Officers also noticed the incorporation and setting up of the following entities by Messrs.Shah & Shah.

- (i) Brightenex Pvt. Ltd. (in short BPL)
- (ii) Toolex Pvt. Ltd. (in short TPL)
- (iii) Auro Engineering.

10. The Assessing Officers, in order to show connection between aforementioned entities and, to demonstrate the untenability of Assessee's stand that Units I and II were independent undertakings, which would be eligible for deduction under Section 80IB, adverted, broadly, to stages/process

involved in the manufacture of fasteners/nuts. While alluding to the manufacturing process, an attempt was made to link each process to an entity or entities, as the case may be. In this behalf, the record discloses the following:

(i) Process of "wire rod pickling" and "phosphating" is carried on by BPL

(ii) The next stage, which involves, "forging" is carried out by FX, FOX and the Assessee, by using Nut Former Machines.

(iii) The third stage, which involves, "Nut Tapping" is also carried out by FX, FOX and the Assessee.

(iv) The last stage, which involves plating of the goods, is carried out by BPL.

10.1. Besides the above, certain secondary operations, such as, "cap cutting", "curling" and "drilling" is carried out by FX, FOX and the Assessee.

10.2. The tools and dyes required in the carrying out of operations, such as, nut forging and nut tapping were, apparently, supplied by TPL, apart from other services, which were rendered by it.

10.3. This information, it appears, was culled out by the Revenue from documents including loose sheets seized in a survey carried out under Section 133A of the 1961 Act, in respect of the aforementioned entities, which included the Assessee.

11. The record shows that the survey was carried out on 18.11.2004 and 19.11.2004. The survey, inter alia, revealed that the Assessee had understated scrap sales and investments made in a certain immovable properties.

11.1. The record also shows that in respect of the A.Y.2004-05, the Assessee filed a revised return on 14.05.2003, wherein, it admitted additional income of Rs.12,91,000/- qua sale of scrap. Furthermore, they also recomputed this deduction under Section 80IB of the 1961 Act.

12. Thus, based on the documents impounded, and their analysis, the Assessing Officers came to the conclusion that the Assessee manipulated inter-group transactions only for the purpose of claiming tax benefits. The Assessing Officers specifically concluded that TPL had been used as a conduit to transfer machinery and that the manipulation was done in a manner that the value of the transferred machines always remained below 20% of the total value of the plant and machinery installed in the recipient concern, i.e., in the instant case, the Assessee. In this behalf, the role of FX and FOX was also discussed by the Assessing Officer.

13. Based on these broad findings, the Assessing Officer rejected the claim of the Assessee for deduction under Section 80IB of the 1961 Act, both for Unit - I and Unit-II.

13.1. Thus, in effect, the entire claim made by the Assessee under Section 80IB of the 1961 Act was disallowed.

14. As regards the other aspect, that is, deduction claimed by the Assessee under Section 80IA of the 1961 Act was

concerned, which arises for consideration in T.C.(A)Nos.1219 and 1220 of 2010, the concerned Assessing Officer, in effect, adjusted the losses incurred by its one wind mill division, albeit, for earlier years, against profits of the A.Ys. in issue, while calculating the total taxable income.

14.1. The observations made in this regard by the concerned Assessing Officer via two separate orders, pertaining to A.Y.s.2006-07 and 2007-08 are extracted hereunder:

T.C.(A)No.1219 of 2010: (A.Y.2006-07)

"The provision of Sec.80IA (4)(iv) of the Income Tax Act clearly states that the "undertaking which is engaged in generation of Power" and hence, the profits have to be arrived for windmill division together as an undertaking and not as a individual division.

Further, the assessee had also got a loss of Rs.2,59,37,516/- on account of depreciation in the windmill business in the Asst. Year 2005-06. As per the provision of 80AB, the deduction shall be allowable only on the gross total income (i.e.,) after setting-off of the earlier losses. Accordingly, if the loss of the current Asst. Year (i.e.,) Asst. Year 2006-07 is adjusted (i.e., Rs.1,31,20,482 - Rs.33,85,137 = Rs.97,35,345/-), the balance of Rs.9,73,53,450/- is adjusted against the earlier years loss of Rs.2,59,37,516/-, there will be no profit left for deduction u/s 80IA of the Income Tax Act."

T.C.(A)No.1220 of 2010 (A.Y.2007-08):

"On the other hand, on perusal of records revealed that the assessee-firm has computed the amount eligible u/s 80-IA at Rs.1,44,07,087/- to Wind Power Division-I and Rs.86,93,342/- in Power Division-II.

The provision of 80IA(4)(iv) of the Income Tax Act clearly states that the "undertaking which is engaged in generation of Power" and hence, the profits have to be arrived for windmill division together as an undertaking and not as a individual division. Accordingly, the allowable deduction 80IA is restricted to Rs.68,98,260/- as against Rs.2,31,00,429/- claimed."

15. Being aggrieved, the Assessee preferred appeals before the CIT(A)s. As indicated, at the outset, the CIT(A)s partly allowed the appeal. The lead order is the order dated 31.07.2008. The other order dated 29.04.2010, passed by another CIT(A), substantially follows the order dated 31.07.2008, both in its reasoning and conclusion.

15.1. The conclusion reached by CIT(A)s, is that, while the Assessee would be entitled to deduction under Section 80IB qua

Unit-I, it would not be entitled deduction vis-a-vis Unit -II.

16. The Tribunal, in both the orders, which are dated 28.08.2009 and 12.11.2010, has accepted the view taken by CIT(A) in the orders referred to above in paragraph 2.2. Substantially, the Tribunal has approved the findings and the reasoning given by CIT(A), in the order dated 31.07.2008. This is reflected in the Tribunal's order dated 12.11.2010.

17. Therefore, for the purpose of disposal of the appeals, we propose to discuss and highlight the reasoning given by the Authorities below qua the Assessee, vis-a-vis, A.Y. 2004-05, which is also the course adopted by the Tribunal.

18. The relevant orders of the Authorities below, with respect to the said A.Y. will thus had taken into account by us. The Assessing Officer's order, which relates to A.Y.2004-05 is dated 29.12.2006. The order of the CIT(A), for the very same A.Y. is dated 31.07.2008, while, the related order of the Tribunal is dated 12.11.2010.

19. In order to appreciate the issues raised in the present appeals, both by the Assessee and the Revenue, one would, therefore, have to set down, as to what is the scope of Section 80IB of the 1961 Act, when, deduction is claimed by any Assessee and not just the Assessee in the instant matter. It must be noted that but for some minor changes, none of which are material over a period of time, the provisions of Section 80IB, have more or less remained the same.

20. Therefore, what is it that an Assessee is required to demonstrate to claim deduction under Section 80IB of the 1961 Act, to the extent it is relevant for the instant appeals, is, broadly, as follows.

20.1. The Assessee in order to claim deduction at the prescribed percentage qua profits and gains derived from an industrial undertaking, which is required to demonstrate that it fulfils the following negative and positive attributes as set out in sub-section (2) of Section 80IB.

(i) It is not formed by splitting up, or the reconstruction of a business already in existence;

(ii) It is not formed by the transfer to a new business of machinery or plant previously used for any purpose;

(iii) It manufactures or produces any article or thing, not being any article or thing specified in the list in the Eleventh Schedule or operates one or more cold storage plant or plants, in any part of India.

(iv) Where the industrial undertaking uses power, to aid in the manufacture or production of articles or things, it is required to employ 10 or more workers. In cases, where, manufacturing process is carried out without the aid of power, the number of workers employed should not be less than 20.

20.2. As would be evident, the first two attributes have negative connotations, while 3rd and 4th attributes are positive in nature.

20.3. Interestingly, in so far as the prohibition of forming

an industrial undertaking by a transfer of machinery and plant, previously used, for any purpose to a new business is concerned, Explanation 2 contained in Section 80IB(2) provides some latitude. The Explanation indicates that the negative condition will not get kicked-in, if, the value of machinery, or plant, or a part thereof, so transferred, does not exceed 20% of the total value of the machinery, or plant, used in the recipient business.

20.4. Thus, as long as the transfer of plant and machinery in the undertaking qua which deduction is sought, is less than the total value of plant and machinery installed in the industrial undertaking, that by, itself, will not disentitle the Assessee from claiming deduction under Section 80IB.

21. The objection, which has been, principally, propounded by the Revenue in its appeals is that, the Assessee, who is the owner of both Unit I and Unit II, had violated the first eligibility condition, which is that, both units had been formed by splitting and/or re-constructing the business.

21.1. The entire thrust of the Assessing Officers' finding has been that the business of manufacture of fasteners/nuts has been spread over various entities, only to derive a tax benefit under Section 80IB of the 1961 Act.

21.2. The CIT(A)s and the Tribunal, however, have not wholly subscribed to this view of the Assessing Officers. They have granted the relief to the Assessee, vis-a-vis Unit I. In doing so, they have come to the conclusion that unless, it could be shown that formation of the undertaking is predicated on the transfer of plant and machinery from an existing business, the Assessee cannot be declined the relief qua Unit I. In coming to the conclusion, both CIT(A)s and the Tribunal fortified their reasoning by adverting to the fact that between A.Ys.1998-99 and 2002-03, the Assessee had claimed, and was, granted the benefit of the provisions of Section 80IB.

21.3. The reasoning of the CIT(A), which has been approved by the Tribunal, in its orders, is reflected in the following observations, in the order dated 31.07.2008, passed qua A.Y.2004-05 (T.C.(A)No.1217 of 2010)

"4.11.4.3. As held by the Supreme Court unless the undertaking, Unit-I in the present appellant's case, is established to have been formed as a result of transfer of buildings, plant and machinery, etc., the benefit of deduction u/s80-IB cannot be denied. The mere fact that certain items of plant and machinery which were previously used in the business of the sister concerns were transferred, that too in the second year of its commencing the business will not disentitled the appellant firm to the benefits granted by law and to do so would amount to giving a very narrow interpretation which will go against the spirit behind the provision granting the relief.

4.11.5. In order to see whether the appellant firm had been formed as a result of transfer of assets in a substantial manner from the other two concerns, M/s.Fastenex Pvt. Ltd. or Formex, it is necessary to analyse the assets position as well as the manner of functioning and the net profit results of these concerns, year-wise. As already indicated, the capital of these concerns remained intact when the appellant firm was formed. It is only that certain second-hand machinery items - Tapping machines that were transferred to the firm through M/s.Toolex Pvt. Ltd. a quick glance of the profits of these two concerns for the accounting periods relevant for the assessment years 1999-2000 to 2005-06 will show that these concerns had been functioning in their own right independently.

4.11.5.1. On a study of the details furnished by the appellant's representative, it is seen that Fromex, the proprietary concern of Shri. A.L.Shah, is the only one that had been carrying on the activities of manufacturing nuts and it had been claiming deduction u/s 80-IB in respect of its profits. The year-wise break up details of sales/gross receipts/income and the net profits thereon, of this concern are furnished as under :

Accounting Period ended	Income		Expenditure	80-IB Claimed	New Profit
	Sales (Rs.)	Service Charge (Rs.)	Tooling & Service (Rs.)	(Rs.)	(Rs.)
31.3.1999	4,16,02,933.61	----	32,97,564.00	----	1,92,36,640.62
31.3.2000	3,57,66,717.59	----	33,39,132.00	21,76,142.00	1,13,00,073.37
31.3.2001	2,82,14,437.42	----	33,92,096.00	8,00,766.00	64,00,998.67
31.3.2002	----	57,13,610.00	30,23,570.00	94,353.00	46,22,385.98
31.3.2003	----	125,91,272.25	43,15,785.00	----	6,97,493.00
31.3.2004	1,64,904.06	1,66,74,654.52	48,07,823.81	1,04,788.98	32,48,696.00
31.3.2005	----	2,05,62,222.00	72,11,745.59	----	65,43,128.00

4.11.5.2.Two pints are clear from the above data.

(i) For the initial three accounting periods ending with 31.1.99, 31.3.2000 and 31.3.2001 Formex had been showing huge sales turnover in respect of which it had been claiming deduction u/s 80-IB also. The assessment year 2000-01 was the seventh year of claim.

(ii) But, however, for the subsequent accounting periods, that is, from the financial year 2001-02 to 2004-05, there had been no sale of nuts, but, this concern had been showing income by way of service charges only.

4.11.5.3.Which means that over a period of time, the appellant firm had taken over the entire manufacturing activities of nuts. But, that does not mean that the firm M/s.Leo Fasteners itself was formed by splitting up or reconstruction of the concern, Formex. And the mere fact that the appellant firm ultimately took over the entire activity of manufacturing nuts from Formex will not disentitle it to the benefit of deduction u/s 80-IB.

4.11.6.As far as the affairs of M/s.Fastenex Pvt. Ltd. are concerned, this is a limited company and it had been showing only service charges as income against which it had claimed huge expenditure by way of job work right through from the financial year 1999-2000 upto 2004-05. On a perusal of the profit and loss account statements of this company, it is seen that it had been showing income from the activity of generating power from wind mills also. And it had been claiming deduction u/s 80-IA/80-IB. The break-up details of service charges, expenditure and net profit for this concern are furnished in the table given below:

Financial Year	Service charges (Rs.)	Sales under sales Tax Act (Rs.)	New Profit (Rs.)
2004-05	1,80,12,180.22	----	44,84,865.96
2003-04	1,45,85,324.99	----	8,33,617.16
2002-03	1,52,46,764.62	8,49,957.80	5,36,238.68
2001-02	164,72,781.23	----	63,93,211.60
2000-01			4,52,989.33

4.11.7. Thus, even on an analysis of the affairs of the other concerns and in particular, the proprietary concern, Formex, nothing could be brought out in concrete terms to show that the formation of the appellant firm was by splitting up or by reconstruction of any of these connected concerns. The totality of the facts do indicate that there had been transactions between the connected concerned and the appellant firm in the sense that they had carried out certain processes involved in the manufacture of nuts and it is only the appellant firm which had taken credit for the entire sale of nuts ultimately over a period of years. But, still, going by the principles laid down by the Supreme Court in the cases of Textile Machinery Corporation Ltd. Vs. CIT and Bajaj Tempo Ltd. Vs. CIT, there is nothing in the affairs of the firm M/s. Leo Fasteners to indicate that it had been formed by splitting up or reconstruction of an already existing business, either in the first accounting period or later on. It was highlighted in the case of Textile Machinery Corporation Ltd. Vs. CIT, that the new undertaking must be an integrated unit by itself wherein articles are produced and at least a minimum number of persons had been employed as prescribed by law and this is precisely the situation in the present appellant's case. The facts brought out by the appellant's representative and as discussed in the above paragraphs will reveal that the totality of the facts prevailing in the formation and functioning of Unit-I of the appellant firm certainly conforms to the views expressed by the Apex Court and therefore, the Assessing Officer's views are not to be accepted as correct.

4.12. In view of the foregoing discussions, it is held that the Unit-I of the appellant firm cannot be said to have been formed by splitting up or reconstruction of an industrial undertaking that already existed and there had been no violation of any of the conditions as laid down in sec.8-IB in its formative years. In so far as the profits of Unit-I are concerned, it has to be that they will qualify for the deduction u/w 80-IB."

21.4. Since, the Assessing Officers had also denied the relief to the Assessee, inter alia, on the ground that most of the work involved in the manufacture of fasteners/nuts is carried out by its sister concerns, i.e., FX, FOX and BPL, and therefore, the Assessee could not be allowed deduction under Section 80IB of the 1961 Act, as it was not carrying out manufacturing activity; it was an aspect, which was also examined by the CIT(A) in the very same order. The CIT(A), after a detailed analysis, came to the conclusion that the Assessee was performing the most vital function, which was nut

tapping.

21.5. In this regard, the following observations and findings of fact returned by the CIT(A), need to be noticed.

"5. Now coming to the question as to whether the appellant firm had carried on any manufacturing activity at all in the light of the fact that certain processes were got done by the firm on job-work basis only, the salient features of the impugned order on this aspect of the issue had been narrated in paragraphs Nos.4.1(i) to 4.1(f) and 4.1(viii) above. It is because the appellant firm had got done certain processes through its connected concerns, viz., Fastenex, Formex and Brightenex, and the percentage of sales turnover were quite high when compared to the consumption of the raw materials for a number of accounting periods including the impugned year, the Assessing Officer was of the view that the appellant firm by itself had not carried on any manufacturing activities. He had observed as under in the impugned order :

"In addition, payments are also made to Toolex and Brightenex for Tools/Dies and pickling/phosphating & planting respectively. It is to be noted that M/s.Toolex and M/s.Brightenex are also exclusively operating for the business of the group and do not have any transactions with outsiders. Thus, in the whole process what the assessee would claim is that tapping of the nuts is done by them and also work relating to cap cutting etc. if any. But, as we have already seen, machinery belonging to other concerns has been transferred using the conduit of Toolex to create tapping capacity in this concern. This kind of manipulation is the reason for such high profit margins whereas all other sister concerns who have actually done most of the processes involved, hardly disclose any taxable incomes. Sri L.M.Shah and Sri A.L.Shah who are the persons behind the whole arrangement have thus shifted the profits from other concerns to LFA and then to LFA, Unit-II primarily to avail deduction u/s 80-IB."

"All the concerns are involved in the same business and are inter-related in the manufacturing process of nuts. As mentioned previously, M/s.Fastenex, M/s.FOX have been manufacturers of nuts and had already availed of the tax benefits u/s 80-IA. They are now being shown as job workers for production of nut blanks from the wire rod. As regards Brightenex and Toolex, they are also part of the manufacturing process of nuts. M/s.Brightenex provides pickling/phosphating and planting services. M/s.Toolex provides service towards tools and dies. Therefore, the Shah Group has been

shifting profits from one concern to another on the basis of mere book entries. Therefore, it is clear that LFA is not an independent production unit".

5.1.As against the above views, during the course of hearing of the appeal, the appellant's representative has made efforts to explain the different processes involved in the manufacture of nuts and he has also explained in clear terms as to what are the processes carried on by the appellant firm after getting the raw materials processed by its connected concerns upto a certain stage. It is necessary to understand the different processes involved in the manufacturing of nuts to begin with. The different processes involved are Forging, Pickling, Phosphating, Wire drawing, Plating and Nut Tapping. Certain secondary operations like assembly, welding, Curl cutting etc. are also carried out. The two main stages are producing Blanks and Tapping. Blanks are stated to be only semi-finished components which do not have a marketable value and 'forging' is the process of producing 'blanks' with the help of machinery called 'Nut Formers'. The various stages of processing as explained by the representative are briefly stated as under :

"Leo Fasteners procures raw materials/ components and processes them for manufacture of nuts. The raw materials (wore rods) procured are pickled, phosphated and then wire drawn using the services of sister concerns. Then such wire drawn rods are converted into blanks either by themselves or through outsourcing. Later, the main and vital process (nut tapping) which adds utility value for the nuts and makes the products usable is being performed by M/s.Leo Fasteners.

In case of certain special nuts, secondary operation like assembly, welding etc. is done which enhances the performance of the nuts and also creates greater value addition. These processes are also performed by the unit which effects the sale of nuts".

"Blanks" are only semi-finished components and are not readily marketable. Also, the blanks do not have any utility value. They can only be used as a component from which nuts can be manufactured. "Forging" is the process involving nut formers to produce blank nuts from the rods. This process is being carried out by Leo Fasteners (Both units), Fastenex P. Ltd. and Formex. This process can be considered crucial only from the investment/capacity angle.

Thus only when the blanks are processed (tapped) properly, duly meeting the requisite precision level do

they result in "NUTS" which are readily marketable. "Nut tapping" is the process involving tapping machines to produce "nuts" from the blanks. This clearly brings out the vitality of the tapping process vis-a-vis all other activities involved. This process had been carried on by Leo Fasteners wherever Leo fasteners had sold the nuts.

For some of the nuts, further processing through welding / assembly is carried out, based on the design requirement. These steps, by adding certain component to the basic nut, enhances their performance as well as adds to the reaslisable value.

To explain the insignificant nature of the other processes involved, such processes have been explained in detail hereunder also explaining the concerns involved in such non-core activities :

"Pickling" is the treatment of metallic surfaces in order to remove stains, rust or scale with a solution containing strong mineral acids, before subsequent processing. This process can by no stretch of imagination be termed as core as there is no transformation in the materials as such and this is being performed by M/s.Brightenex P. Ltd.

"Phosphating" is the method of protecting a steel surface from corrosion through the application of chemical phosphate conversion coating. This process also can never be termed as core as there is no transformation in the materials as such. This process is also being carried out by M/s.Brightenex P. Ltd.

"Wire drawing" is the process used to reduce or change the diameter of a wire or rod through a single or series of drawing die(s). This process also can never be termed as core as the diameter of the rods alone undergo a change during this process and rods (input) continue to be rods (output) even after the process. This process is also being carried out by M/s.Brightenex P. Ltd.

5.2. The explanation given as above will give a general idea of the various processes involved in bringing out the final product "nut" from the raw materials, wire rods. It is seen from a careful study of the submissions made that there are tow important stages in the various processes involved in the manufacture of nut - Nut Forging, which produces blanks and Tapping/Threading. It has been explained above that it is only the process called 'Nut Tapping' which bring about the vital change in the raw material to make the final product commercially and qualitatively different from the raw material. 'Nut Tapping' is

nothing but the act of threading the nuts. It was submitted that although upto the stage of producing nut blanks, the processes of pickling, phosphating and forging are done by the appellant firm with the help of the sister concerns on job work basis, the main activity of nut tapping/threading which is crucial to produce a nut, is being done only by the appellant firm. It was also highlighted that after the stage of "Nut tapping", the materials are subjected to further processes viz., crimping and welding which are carried out only by the appellant firm and further the process of plating the nuts are done by the connected concern, M/s.Brightenex Pvt. Ltd. But, however, all the nuts so manufactured are passed through quality control by the appellant firm only before they are brought out in the market."

(emphasis is ours)

21.6. Clearly, on both counts, CIT(A) held in favour of the Assessee, which is that, it not only was not formed by splitting or reconstruction of an existing business, and that, it did carry out manufacturing activity, contrary to what the Assessing Officers have held.

22. In so far as Unit II is concerned, the CIT(A), in the very same order, while noticing that certain secondary operations were carried out in Unit II, and that, the Assessee had endeavoured to set up Unit II, with the object of enhancing the quality of the final product, i.e., fasteners and nuts and, in that behalf, had imported five (5) brand new nut former machines, declined to grant the relief to the Assessee vis-a-vis Unit II.

22.1. This was, after the Assessee had given details of investments in fixed assets, which, mainly, comprise of both imported and indigenous machinery, amounting to Rs.3,23,18,377.14. Out of this amount, investment in imported machinery, i.e., nut formers, was Rs.2,44,53,489/-, while investment in indigenous machinery amounted to Rs.74,33,489.88. After making adjustment for Cenvat Credit and pre-operative expenses, the total investment in plant and machinery alone was Rs.3,14,05,120.38. The balance comprise of furniture, office equipment, electrification and testing equipments.

22.2. In addition to this, the CIT(A) also noticed that the Assessee had supplied new products to its customers, which were manufactured in Unit II. A list of 78 customers, to whom sale had been made during the financial year 2003-04 and another 40 customers to whom new products, manufactured by Unit II, had been sold during the very same period, were also mentioned. The details of 60 employees engaged in Unit II, for the year ending 31.03.2004, along with their P.F. account numbers were also given.

22.3. The record shows that Unit No.II has separate electricity connection, licence and is located in separate and identifiable premises.

23. In so far as the production process is concerned, the following information is found on record.

" (a) The processes of the wire rod pickling and phosphating and also wire drawing were done by M/s.Brightenex Pvt. Ltd. The next stage of processing called forging was done in a shared manner by three concerns, viz., M/s.Fastenex, Formex and M/s.Leo Fasteners by using nut former machines.

(b) The next processing of nut tapping work was also done by the above three concerns in a shared manner.

(c) The final plating of the nuts was done by M/s.Brightenex Pvt. Ltd.

(d) Certain secondary operations like cap-cutting, curling and drilling were also done by the three concerns, M/s.Fastenex, Formex and M/s.Leo Fasteners.

(e) The tools and dies required in the operation of nut forging and nut tapping were supplied by M/s.Toolex pvt. Ltd. and certain other services were also rendered by this concern.

(f) The appellant firm had also shown certain payments having been made to other concerns in the Group for getting components and services which would make it clear that it had not carried on all the processes involved in the manufacturing of nuts."

(emphasis is ours)

23.1. Furthermore, the Assessee relied upon its excise returns to establish that it was a new and separate undertaking involved in the manufacture of fasteners/nuts.

23.2. Despite the said record, the CIT(A) declined, as indicated above, to grant the benefit on the basis of the following rationale and reasoning.

".....6.2.13.Thus, it is the contention of the appellant that it is mainly because certain improvisation of the already existing product had been made in Unit-II and new improved quality nuts were also being manufactured and additionally new items of plant and machinery had been installed, it has to be taken that the products turned out by Unit-II are commercially distinct from the products manufactured by Unit-I and for all these purposes, fresh capital had been inducted in Unit-II, this unit must be considered as a "new industrial undertaking" entitled for deduction u/s 80-IB in respect of its profits at 100% and not at 25%.

6.3. On a careful consideration of the facts

brought out by the appellant's representative, it is clear that the formation of the Unit-II cannot be considered to be a "new industrial undertaking". Though there is a possibility of considering the new unit as an expansion of the firm, in the sense that the appellant firm went in for improvisation of the product it was already manufacturing and in order to improve the quality of the finished products it could have gone in for the improvisation of the plant and machinery by importing five new 'Nut Formers' with the latest technology, still the commercial product that is manufactured by both the units are one and the same. The fact that the nuts or fasteners turned out by Unit-II are qualitatively different from the nuts produced by Unit-I will not make any difference. The fact remains that the partners of the appellant firm had diverted their own funds as well as the loan funds as towards making investments in Unit-II which amounts to splitting of the funds of the appellant firm only for the purposes of investing in a new Unit-II to bring out perhaps qualitatively a different product though, fundamentally, this unit is also engaged in the manufacture of nuts or fasteners used in the automobile industry only. It may be a fact that the firm had invested by acquiring more items of machinery for making improvisation in the existing product. But, there is nothing brought on record to show that the new product is commercially different from the nuts or fasteners produced by Unit-I. No doubt, the appellant's representative had given certain information regarding the quality of the nuts that were turned out by the Unit-II and the additional processing to be done on the materials used to that there could be a better product qualitatively. It has been stated that the processing itself was different. But, still, Unit-II cannot be said to be having an independent status as a new industrial undertaking. And the introduction of certain techniques in the processing cannot amount to bringing about a different processing altogether. There is nothing to indicate that a nut could be manufactured by Unit -II by adopting totally a new process. In fact, as shown in the earlier paragraphs, upto the stage of producing Nut Blanks, the processing were done by other concerns in the group on job-work basis for both the units of the appellant firm. It is all the same processes.

6.3.1. As rightly observed by the Assessing officer, Unit-II was able to make a turnover of Rs.6.44 Crores by purchasing manufactured nut blanks from Unit-I to the extent of Rs.3.16 Crores. Apart from these purchases, Unit-II might be involved in

manufacturing nuts of different quality on its own and it could have been performing all the operations right from stage one. But, all the activities put together will only lead to the conclusion that Unit-II had also been manufacturing only nuts, but, perhaps, of a different quality used in the automobile industry. The commercial use of the products manufactured by both the units is one and the same. So, when there had been inter-unit transactions and also the products are the same, Unit-II not having an independent legal status, it cannot be said to be a 'new industrial undertaking' in its own right or it cannot be said to be a separate unit apart from Unit-I. Therefore, there is not enough merit in the plea of the appellant's representative that Unit-II must be treated as a 'new industrial undertaking'.

6.4. From the data furnished in the tables in paragraph No.6.2.9 and 6.2.9.3 above, the following points are clear :

- (i). In order to form Unit-II, the partners of the appellant firm had contributed funds in the form of capital as well as loans and the firm had also borrowed funds from State Bank of India, Siruthozhil Branch and HDFC.
- (ii). In the Statement of Affairs as on 31.03.05, the partner Shri A.L.Shah had also shown the investments made in Unit-II separately.
- (iii). The firm had made separate investments in Fixed Assets and to be more specific, in plant and machinery, by going in for the import of Nut Formers to the value of Rs.2,44,53,489/-. The total investments made in Fixed Assets as at 31.3.2004 stood at Rs.3,23,18,377/-.
- (iv). The investment included second-hand machinery items-Tapping Machines - purchased from M/s.Toolex Pvt. Ltd. to the tune of Rs.29,49,302/- and this constituted just 9.39% of the total value of Plant and Machinery as at 31.3.2004.
- (v). The total value of machinery further included Rs.12,35,000/- representing the value of second-hand machinery transferred from Unit-I. Even if these items are considered, the percentage of the total value of second-hand machinery items purchased by the firm for Unit-II would work out to less than 20% as at 31.3.2004.
- (vi). There seems to be no purchase of any second-hand machinery during the financial year 2005-05 for Unit-II.

6.4.1. All the above facts seemingly indicate that there are no irregularities in the formation of Unit-II and therefore, such formation conforms to the principles laid down by the Supreme Court as brought out in the earlier paragraphs of this appellate order and so, Unit-II must be given the status of a new industrial undertaking. But, as will be seen from the discussions to emerge in the following paragraphs, this view is incorrect, because, there are certain other vital facts viz., the transactions between Unit-I and Unit-II that are to be taken into consideration before forming any opinion.

6.5. The way in which the Unit-II had been formed is not similar to the way in which the firm itself was formed way-back in the year 1998. The subtle distinction that has to be made is that at that point of time, a new legal entity was formed as partnership between Shri L.M.Shah and Shri A.L.Shah and the firm enjoyed an independent legal status whereas, Unit-II of the firm is not so. The appellant firm M/s. Leo fasteners was started as an integrated unit by itself in which articles were being produced. Whereas, formative of Unit-II was not so and obviously, it had been formed through diversion of funds and stock of Unit-I.

6.6. As seen from the copy of the order in No.6346/99/B1/CTD dated 6.8.2003 of the Deputy Commercial Tax Officer, Puducherry, wherein the tax holiday period had been extended for a further period of 4 years from 18.3.2003 to 17.3.2007, there is no mention of the existence of two units in the appellant firm or the manufactured product being different commercially in Unit-II.

6.7. Whatever investments that had been made by the appellant firm during the financial year 2003-04 from the funds brought in in the form of capital contributions as well as loans from partners and banks etc. no doubt, can be said to have been made for expanding its business activity of manufacturing nuts which the firm had all along been carrying on. The partners had made investment in the firm M/s.Leo Fasteners only for expanding their business. But the investment had been split and had been diverted as towards Unit-II. The whole lot of investments made in Unit-II can be considered only as splitting up or reconstruction of the already existing unit of the firm. In fact, from the details of plant and machinery as on 31.3.2004 given in respect of Unit-I,

it is seen that the firm had scrapped machinery items to the value of Rs.18,42,240/- which it had purchased from M/s.Toolex Pvt. Ltd. and these machinery items were nothing but tapping machines. So, though the value of the machinery items scrapped may be small when compared to the total value of machinery items newly purchased, still, the main activity of tapping that was carried on by the firm was split and was shared by the newly formed so-called Unit-II also. Apart from this, the deployment of newly imported Nut Formers in a separate unit called Unit-II would amount to splitting the activities of the appellant firm. So, Unit-II cannot be considered as an integrated unit by itself as per the Supreme Court's decision cited supra.

6.7.1 The Unit-II cannot be considered to be an integrated unit by itself. This is further evidenced by the fact that there had been transfer of nut blanks from Unit-I to Unit-II during the impugned accounting period as well as in the next accounting period. there had been sale of nut blanks to the tune of Rs.3,14,26,875/- during the financial year 2003-04 and for Rs.8,98,39,763/- during the financial year 2004-05 to Unit-II. These transactions make it evident that the whole idea of forming Unit-II is to shift the activities of Unit-I to Unit-II in course of time so that the firm could keep claiming deduction u/s 80-IB continuously, that too, at a higher rate by shifting the profits of Unit- to Unit-II.

6.8. The facts brought out and the further discussions as in the above paragraphs will only lead us to the inference that though the appellant firm had tried to make it appear that the Unit-II is a new industrial undertaking by showing that fresh capital had been introduced, substantial investments had been made in fixed assets including buildings and plant and machinery, sufficiently new labour force had been deployed, etc., still, its activities cannot be viewed independently and it cannot be said to have an independent existence. What the partners of the appellant firm would have done under normal circumstances for expanding their business, had been done in the name of Unit-II and what the firm would have done to improve its already existing product had been done in the name of Unit-II. Above all, there had been transfer of stock- semi-furnished (nut blanks) from Unit-I to Unit-II, which is nothing but transfer of working capital. And by this process, the firm had tried to claim double advantage. The sale of nut blanks to Unit-II had been included in the computation of the profits of Unit-I for the purposes of claiming

deduction u/s 80-IB at 25% for the impugned accounting period. And also, in addition to the above, the profits arising on sale of the nuts which had been produced from the nut blanks of Unit-I were also included in the profits of Unit-II for the purpose of claiming higher deduction at 100% u/s 80-IB. This situation is not permissible in law.

6.8.1 In view of the foregoing discussion, it is held that Unit-II which is not an integrated unit by itself cannot be considered as a 'new industrial undertaking' whose profits would qualify for deduction u/s 80-IB at 100%.

6.9 To sum up, the following are the inferences to be drawn from the discussions in the above paragraphs:

- (i). Having accepted the stand that the firm M/s. Leo Fasteners is a valid partnership formed in the year 1998 and it had gone into commercial production of nuts in that year, the Assessing Officer was not correct in questioning or doubting its very formation while dealing with its claim for deduction u/s 80-IB for the assessment year 2004-05.
- (ii). Simply based on certain details gathered during the course of the survey operations regarding the transfer to the appellant firm of second-hand machinery items through the connected concern, M/s. Toolex Pvt. Ltd. the Assessing Officer was not correct in his inference that the machinery items were shifted just to show tapping capacity in the appellant firm and to shift the profits in order to claim deduction u/s 80-IB. In so long as the law permits acquisition of second-hand machinery items up to 20% of the total value of plant and machinery each year what the appellant firm had done cannot be viewed as illegal or as amounting to violation of or circumventing any provision of law.
- (iii). A device or a methodology adopted by the appellant firm intelligently in the course of its tax planning without violating any legal provision cannot be questioned.
- (iv). The transactions between the appellant firm and the other connected concerns whereby those concerns had performed certain processes on job-work basis will not come in the way of the appellant firm claiming the deduction u/s 80-IB as it had also performed certain vital processes - "nut tapping" which brings changes into the materials used or rather the 'nut blanks' to make them commercially different products - the

'nuts'. Without performing tapping, it will not be possible to bring out a nut.

(v).As far as Unit-II is concerned, it cannot be considered to be a new undertaking both in its formation as well as in its activities.

(vi).The formation of Unit-II by the appellant firm was with a view to divert its profits so that it could claim deduction u/s 80-IB not only at a higher rate but also for a longer period of time. That is, if Unit-II were to be accepted as a new industrial undertaking, then the appellant firm could have continued to claim the benefit of deduction u/s 80-IB for a further period of ten years which deserves to be discouraged. This cannot be considered to be an act of tax planning."

(emphasis is ours)

23.3. This rationale and reasoning was dittoed by the Tribunal.

23.4. The reasoning provided by CIT(A), which has been accepted by the Tribunal, for denying the relief to the Assessee to Unit II are as follows:

(i). Even, if, there was improvisation in the production of the final product, i.e., fasteners/nuts, it was not a commercially different product.

(ii). That Unit II could be considered as an expansion of Unit I. This improvisation on the product could have been brought about in Unit I. The fact that fasteners/nuts manufactured in Unit No.II were qualitatively different from those manufactured in Unit I, will not make any difference.

(iii). That Unit II, in the given period, was able to generate a turnover of Rs.6.44 crores by purchasing nut blanks from Unit I, to the extent of Rs.3.16 crores. The commercial use of the products manufactured by Units I and II are one and the same.

(iv). That the Deputy Commercial Tax Officer, Puducherry, who, vide order dated 06.08.2003 extended the tax holiday for a period of four (4) years, spanning between 18.03.2003 and 17.03.2007, made no mention of the existence of two units or, that, the product manufactured in Unit II was commercially different.

(v). The fact that partners had made investment in the form of capital and loan for expanding their business, would not help the cause of the Assessee as "investment had been split and had been diverted (sic as) towards Unit No.II". The whole investment made in Unit II "can be considered only as splitting

up or reconstruction of already existing unit of the firm". The deployment of imported nut formers in a separate unit, i.e., Unit II, would amount to splitting up of the activities by the Assessee. Hence, Unit II could not be considered as an integrated unit, by itself. There had been transfer of nut blanks to the tune of Rs.3,14,26,875/-, as indicated above, in the financial year, 2003-04 and also a transfer of nut blanks to the tune of Rs.8,98,39,763/- for the financial year 2004-05 to Unit II.

(vi). The whole idea being to shift the activities from Unit I to Unit II, so that, deduction under Section 80IB of the 1961 Act can be claimed at a higher rate.

23.5. Therefore, what comes through first and foremost is that, there is an acceptance of fact that the Assessee has, if, nothing else, expanded its business by taking the following steps:

(i). Had made investment in Unit II in the form of capital and loan given by the partners of the Assessee as well as amount accessed in the form of loan from Banks, such as, SBI and HDFC.

(ii) Had imported from Taiwan four (4) nut former machines.

(iii) There is no denial of the fact that it has engaged separate labour force.

(iv) It has operations in a separate and identifiable premises.

(v) It has a separate licence.

(vi) It has separate electricity connection.

23.6. Given these facts, one needs to determine is whether expansion, by itself, would make the Assessee eligible for deduction under Section 80IB of the 1961 Act.

24. The most frequently cited case in the context of Section 80IB is the judgment of the Supreme Court in the matter of Textile Machinery Corporation Limited, Calcutta V. The Commissioner of Income Tax West Bengal, Calcutta (1977) 2 SCC 368.

24.1. This was the decision, which was rendered under Section 15 C of the Income Tax Act, 1922. The provisions of Section 15C was somewhat similar to Section 80IB of the 1961 Act.

24.2. In that case, the Supreme Court was called upon to rule, whether the Assessee would be entitled to deduction in the background of the following facts.

24.3. The facts, broadly, which obtain in the said case, are as follows:

The Assessee was in the business of manufacture of boilers, machinery parts, wagons etc. The Assessee had established Steel Foundry Division and a Jute Division. These divisions produce goods, which were required by the Assessee. The Assessee also procured material from outside agencies. The Assessee had maintained separate accounts. In this case too, no old assets

were used in the aforementioned two divisions. The Tribunal, in the said case, had allowed the claim for deduction made by the Assessee under Section 15C, but, it had been reversed by the High Court on the ground that it involved reconstruction of the old business.

24.4. The Supreme Court, while dealing with the issue of, whether or not in the given facts, the Assessee was disentitled to deduction, made the following apposite observations :

Again, the new undertaking must not be substantially the same old existing business. The third excluded category mentioned above significant. Even if a new business is carried on but by piercing the veil of the new business it is found that there is employment of the assets of the old business, the benefit will be not available. From this it clearly follows that substantial investment of new capital is imperative. The words "the capital employed" in the principal clause of section 15C are significant, for fresh capital must be employed in the new undertaking claiming exemption. There must be a new undertaking where substantial investment of fresh capital must be made in order to enable earning of profits attributable to that new capital. The assessee continues to be the same for the purpose of assessment. It has its existing business already liable to tax. It produced in the two concerned undertakings commodities different from those which it has been manufacturing or producing in its existing business. Manufacture of production of articles yielding additional profit attributable to the new outlay of capital in a separate and distinct unit is the heart of the matter, to earn benefit from the exemption of tax liability under section 15C. Sub-section (6) of the section also points to the same effect, namely, production of articles. The answer, in every particular case depends upon the peculiar acts and conditions of the new industrial undertaking on account of which the assessee claims exemption under section 15C. No hard and fast rule can be laid down. Trade and industry do not run in earmarked channels and particularly so in view of manifold scientific and technological developments. There is great scope for expansion of trade and industry. The fact that an assessee by establishment of a new industrial undertaking expands his existing business, which he certainly does, would not, on that score, deprive him of the benefit under section 15C. Every new creation in business is some kind of expansion and advancement. The true test is not whether the new industrial undertaking connotes expansion of the existing business of the assessee but whether it is all the same a new and identifiable undertaking separate and distinct from the

existing business. No particular decision in one case can lay down an inexorable test to determine whether a given case comes under section 15C or not. In order that the new undertaking can be said to be not formed out of the already existing business, there must be a new emergence of a physically separate industrial unit which may exist on its own as a viable unit. An undertakings is formed out of the existing business if the physical identity with the old unit is preserved. This has not happened here in the case of the two undertakings which are separate and distinct.

It is clear that the principal business of the assessee is heavy engineering in the course of which it manufactures boilers, wagons, etc. If an industrial undertaking produce certain machines or parts which are, by themselves, identifiable units being marketable commodities and the undertaking can exist even after the cessation of the principal business of the assessee, it cannot be anything but a new and separate industrial undertaking to qualify for appropriate exemption under section 15C. The principal business of the assessee can be carried on even if the said two additional undertakings cease to function. Again, the converse is also true. The fact that the articles produced by the two undertakings are used by the Boiler Division of the assessee will not weigh against holding that these are new and separate undertakings. On the other hand the fact that a portion of the articles produced in these two new industrial undertakings had been sold in the open market to others is a circumstance in favour of the assessee that the new industrial units can function on their own. Use of the articles by the assessee is not decisive to deny the benefit of section 15C.

Section 15C partially exempts from tax a new industrial unit which is separate physically from the old one, the capital of which and the profits thereon are ascertainable. There is no difficulty to hold that section 15C is applicable to an absolutely new undertaking for the first time started by an assessee. The cases which give rise to controversy are those where the old business is being carried on by the assessee and a new activity is launched by him by establishing new plants and machinery by investing substantial funds. The new activity may produce the same commodities of the old business or it may produce some other distinct marketable products, even commodities which may feed the old business. These

products may be consumed by the assessee in his old business or may be sold in the open market. One thing is certain that the new undertaking must be an integrated unit by itself wherein articles are produced and at least a minimum of ten persons with the aid of power and a minimum of twenty persons without the aid of power have been employed. Such a new industrially recognisable unit of an assessee cannot be said to be reconstruction of his old business since there is no transfer of any assets of the old business to the new undertaking which takes place when there is reconstruction of the old business. For the purpose Of section 15C the industrial units set up must be new in the sense that new plants and machinery are erected for producing either the same commodities or some distinct commodities. In order to deny the benefit of section 15C the new undertaking must be formed by reconstruction of the old business. Now in the instant case there is no formation of any industrial undertaking out of the existing business since that can take place only when the assets of the old business are transferred substantially to the new undertaking. There is no such transfer of assets in the two cases with which we are concerned.

We will now deal with the question whether the two undertakings the assessee are formed by reconstruction of the existing business. The word 'reconstruction' is not defined in the Act but has received judicial interpretation. In *re South African Supply and Cold Storage Company, Wild v. Same Company*(1), Buckley, J. dealing with the meaning of the word 'reconstruction' in a company matter observed as follows :--

"What does 'reconstruction' mean ? To my mind it means this. An undertaking of some definite kind is being carried on, and the conclusion is arrived at that it is not desirable to kill that undertaking, but that it is desirable to preserve it in some form, and to do so, not by selling it to an outsider who shall carry it on--that would be a mere sale--but in some altered form to continue the undertaking in such a manner as that the persons now carrying it on will substantially continue to carry it on. It involves, I think, that substantially the same business shall be carried on and substantially the same persons shall carry it on. But it does not involve that all the assets shall pass to the new company or resuscitated company, or that all the shareholders of the old company shall be shareholders in the new company or resuscitated company. Substantially the business and the persons interested must be the same".

.....

The Delhi High Court also in Commissioner of Income-tax v. Gangs Sugar Corpora-

tion Ltd.(a), accepted the above concept of 'reconstruction' in the following passage :- "We have given the matter our earnest consideration and are of the view that in the reconstruction of business, as in the reconstruction of a company, there is an element of transfer of assets and of some change, however partial or restricted it may be, of ownership of the assets. The transfer, however, need not be of all the assets. It is none the less imperative that there should be continuity and preservation of the old undertaking though in an altered form.

(1) [1904] 2 Ch. 268. 35 I.T.R. 662.

(3) 92 I.T.R. 173.

The concept of reconstruction of business would not be attracted when a company which is already running one industrial unit sets up another industrial unit. The new industrial unit would not lose its separate and independent identity even though it has been set up by a company which is already running an industrial unit before the setting up of the new unit".

We endorse the above views with regard to reconstruction of business.

Reconstruction of business involves the idea of substantially the same persons carrying on substantially the same business. It is stated on behalf of the Revenue that the same company in the instant case continues to do the same business of heavy engineering---no matter certain spare parts necessary as components to completion of the end- product are now manufactured in the business itself. The fact that the assessee is carrying on the general business of heavy engineering will not prevent him from setting up new industrial undertakings and from claiming benefit under section-15C if that section is otherwise applicable. However, in order to be entitled to the benefit under' section 15C, the following facts have to be established by the assessee. subject always to the time-schedule in the section :--

(1) investment of substantial fresh capital in the industrial undertaking set up, (2) employment of requisite labour therein, (3) manufacture or production of articles in the said undertaking, (4) earning of profits clearly attributable to the said new

undertaking, and (5) above all, a separate and distinct identity of the industrial unit set up.

We may add that there is no bar to an assessee carrying on a particular business to set up a new industrial undertaking on account of which exemption of tax under section 15C may be claimed.

The legislature has advisedly refrained from inserting a definition of the word 'reconstruction' in the Act. Indeed, in the infinite variety of instances of restructuring of industry in the course of strides in technology and of other developments, the question has to be left for decision on the peculiar facts of each case.

If any undertaking is not formed by reconstruction of the old business that undertaking will not be denied the benefit of section 15C simply because it goes to expand the general business of the assessee on some directions. As in the instant case, once the new industrial undertakings are separate and independent production units' in the sense that the commodities produced or the results achieved are commercially tangible products and the undertakings can be carried on separately without complete absorption and losing their identity in the old business, they are not to be treated as being formed by reconstruction of the old business."

25. Therefore, having regard to the principles of law laid down by the Supreme Court, which, to summarize, are that, the fact that an existing unit has been substantially expanded, would not disentitle an Assessee for claiming deduction under Section 80IB of the 1961 Act.

26. In the instant case also, to examine whether there is an substantial expansion, one would have to look at the following indices:

(i) Is there an investment to substantiate fresh capital in the concerned industrial undertaking.

(ii) Is there employment of requisite labour.

(iii) Whether or not, the undertaking manufactures or produces articles or things.

(iv) Whether or not, it has profits, which are clearly attributable to the industrial undertaking qua which deduction is sought.

(v) Whether or not, it has the industrial undertaking qua which deduction is sought, has a separate or distinct identity.

26.1. When these tests are employed, it is quite clear that in so far as Unit II is concerned, the Assessee has employed a substantial amount of fresh capital.

26.2. In this behalf, the CIT(A)s have held that the investment made by the partners by way of capital contribution and loan has been split and/or diverted from Unit I.

26.3. To our minds, this objection loses sight of the fact that what is required to be examined is that separate and distinct investment has been made to expand or set up a new industrial undertaking. The fact that the source of investment, i.e., are common to Units I and II, by itself, would not disentitle the Assessee from claiming deduction qua Unit II on this score. Furthermore, CIT(A)s orders itself show that moneys have also been borrowed from banks, such as, SBI and HDFC, to fund Unit II.

26.4. Therefore, this objection, to our minds, is completely, misconceived.

26.5. Furthermore, the Assessee has engaged separate labour and is engaged in manufacture and production of articles.

26.6. The objection taken by the Authorities below, that the article produced and/or manufactured by the Assessee is commercially no different from what Unit I manufactured, according to us, is not a ground on which deduction claimed under Section 80 IB can be denied to the Assessee.

26.7. The only condition that the Assessee, in this behalf, is required to fulfill is that, they should manufacture and produce an article or thing. Sub-clause (iii) of sub-section (2) of Section 80IB of the 1961 Act does not require that, in order to claim deduction, the article or any manufacture must be commercially different from that which is manufactured under the aegis of the existing business.

26.8. Employing such a test would, in our view, result in altering the scope, and the effect of sub-clause (iii) of Section 80IB(2) of the 1961 Act and adding a condition, which is not provided for by the legislature.

27. In so far as the aspect of transfer of machinery is concerned qua Unit I, the CIT(A)s and the Tribunal have accepted the fact that the machinery, if transferred is below the permissible limit of 20% of the total value of plant and machinery, it cannot be viewed as violation of the conditions prescribed under Section 80IB of the 1961 Act for claiming deduction. However, when it came to putting to test the said proposition, vis-a-vis Unit II, the Authorities below construed such transfer as manipulation, only to claim deduction under Section 80IB of the 1961 Act, by keeping the value of the transferred machinery below the permissible limit of 20% of the total value of the plant and machinery of the recipient unit, i.e., Unit II.

27.1. According to us, this objection is without any basis. There is no discussion, either in the order of the Tribunal, or in the order of the CIT(A)s, as to how this would amount to manipulation, as long as the machinery transferred to Unit II was within the permissible limit of 20%, as set out in

Explanation 2 to sub-section (2) of Section 80IB. This could not, in our view, form the basis for declining the deduction claimed by the Assessee.

27.2. In raising this objection, the Authorities below have ignored the fact that the condition stipulated in sub-clause (ii) of sub-section (2) of Section 80IB disentitle the Assessee from claiming a deduction, only, if, the formation of the new business takes place via transfer of machinery and/or plant, previously used for any purpose. Therefore, it is not a mere transfer of plant and machinery, which is used previously for some purpose, but the fact that transfer is of such nature that it enables the formation of the undertaking qua which deduction is sought by an Assessee. It is not the Revenue's case that the transferred machinery enabled the formation of Unit II.

27.3. As indicated herein above, four (4) nut former machines were imported specifically for setting up Unit II. Furthermore, the record shows that the value of the transferred machines were below 20%. Therefore, we find no basis for declining the claim for deduction made by the Assessee under Section 80IB on the ground that it had manipulated the transfer of machinery in such a manner that its value was kept below 20% of the total value of the plant and machinery installed in Unit II.

28. This issue came up for consideration before the Supreme Court in the matter of: Bajaj Tempo Ltd. V. Commissioner of Income Tax (1992) 196 ITR 188.

28.1. This case was again decided under the provisions of Section 15C of the 1922 Act. Notably, Section 15C of the 1922 Act did not have appended to it a provision similar to Explanation 2 to Section 80IB(2) of the 1961 Act, despite which, the Supreme Court made the following apposite observations:

" Words of a statute are undoubtedly the best guide. But if their meaning gets clouded then the courts required to clear the haze. Sub-section (2) advances the objective of sub-section (1) by including in it every undertaking except if it is covered by clause (i) for which it is necessary that it should not be formed by transfer of building or machinery. The restriction or denial of benefit arises not by transfer of building or material to the new company but that it should not be formed by such transfer. This is the key to the interpretation. The formation should not be by such transfer. The emphasis is on formation not on use. Therefore it is not every transfer of building or material but the one which can be held to have resulted in formation of the undertaking. "

28.2. In this case, the Supreme Court was called upon to rule whether carrying on business by a new undertaking in a premises leased from another business would disentitle the

Assessee to claim deduction under Section 15 C of the 1922 Act. The Supreme Court, as indicated above, ruled in favour of the Assessee by stressing on the fact that it is not a mere transfer of machinery and plant, which was used, previously, for other purpose, that would deprive an Assessee from claiming deduction, but what would, in fact, disentitle the Assessee from claiming deduction, if, transfer enables the formation of new business qua which deduction is claimed. The Court held that the provisions of the like nature, which are incorporated in the Statute by the Legislature to give a fillip to industrialization, should, in case of doubt and/or ambiguity, be interpreted in a manner, which favours the Assessee. In other words, such provisions should liberally construed.

29. The second objection, which the Authorities below have taken qua Assessee vis-a-vis his claim for deduction in respect of Unit II is that, it had purchased nut blanks from Unit I. In this context, one may note that in respect of financial year 2003-04, nut blanks, worth Rs.3,14,26,875/- were purchased, while in financial year, 2004-05, nut blanks, worth Rs.8,98,39,763/- were purchased. Based on this, it was concluded by the CIT(A)s that the whole idea was, to shift the activities from Unit I to Unit II. However, it is not suggested by the Authorities below that Unit II had not purchased the nut blanks for a true value from Unit I.

29.1. Once again, in our opinion, the mere fact that nut blanks were purchased from Unit I cannot be a reason to deny deduction under Section 80IB, vis-a-vis Unit II. The deduction is made available to the Assessee, vis-a-vis Unit II, as it fits the attributes of an industrial undertaking and not to the Assessee per se. As long as the Assessee has invested a substantial amount in setting up an industrial undertaking, which is separate and distinct, it is entitled to claim the said deduction.

29.2. As indicated above, the substantial expansion of Unit I or even, if, Unit II is concerned as an expanded form of Unit I, which, for the reasons given above, is clearly substantial, it cannot be denied deduction under Section 80IB of the 1961 Act. The fact that it has used raw material, i.e., nut blanks, which have been supplied by Unit I, cannot come in the way of one reaching a conclusion that it is a separate and independent unit. This proposition can be better explained by the following illustration. Say for example, the Assessee had established Unit II, in another company or entity, would the Revenue, then, be able to deprive such an entity of exemption under Section 80IB of the 1961 Act. The distinction, separateness and independence of an industrial undertaking cannot be made dependent only on the attribute of ownership.

29.3. Therefore, for all these reasons, we are of the view that both CIT(A)s as well as the Tribunal were wrong in

concluding that the Assessee could not claim deduction under Section 80IB of the 1961 Act vis-a-vis Unit II.

30. At this stage, we must deal with one last argument advanced on behalf of the Revenue, which is that, the Tribunal ought to have directed the Assessing Officer to reconsider the issue, based on the material on record, as to whether or not, vis-a-vis Unit I, the Assessee ought to be given deduction as claimed.

30.1. In this regard, the provisions of Section 80IB(13) read with Section 80 IA(10) were relied upon by the Revenue. According to us, this course is not commended, as the material on record has been thoroughly appraised at each level, i.e., by the Assessing Officer, followed by CIT(A)s and the Tribunal, via its orders dated 28.08.2009 and 12.11.2010.

30.2. Therefore, no reconsideration of material was required, as suggested by the Revenue. Consequently, this contention of the Revenue is rejected based on the facts and circumstances emerging in this case.

31. This brings us to the discussion qua the other aspect of the matter, i.e., the computation made by the Assessing Officer in respect of deduction claimed by the Assessee under Section 80IA of the 1961 Act.

31.1. This issue arises, as indicated hereinabove, only in T.C.(A)Nos.1219 and 1220 of 2010.

31.2. The Assessee is aggrieved by the fact that in computing the deduction, which ought to have been made available to it, the provisions of Section 80IA(4)(iv) have been wrongly construed.

31.3. For this purpose, our attention has been drawn to that part of the Assessment Order dated 29.12.2008, which has been passed in respect of A.Y.2006-07, and Assessment Order dated 18.12.2009, which has been passed in respect of A.Y.2007-08. We have already extracted the relevant parts of the two Assessment Orders.

31.4. A careful perusal of the extracts, which are contained in Paragraph 14.1. would show that the Assessing Officer has done two things: firstly, it has treated two separate power divisions as one undertaking; and secondly, set off the losses of earlier years against profits of the years in issue.

31.5. The aforesaid two aspects are clearly evident, when, Assessment Order dated 29.12.2008 pertaining to A.Y.2006-07 is perused. A similar squaring off exercise vis-a-vis two separate power divisions has been carried out by the Assessing Officer vide his order dated 18.12.2009, passed vis-a-vis A.Y.2007-08.

31.6. As correctly submitted by the counsel for the Assessee, this methodology of computing deduction under Section 80IA of the 1961 Act has been proscribed by a Division Bench of this Court in the matter of : Velayudhaswamy Spinning Mills Pvt. Ltd. V. Assistant Commissioner of Income Tax (2012) 340 ITR 477 (Madras).

31.7. The Division Bench in this case held that the

provision does not allow the Revenue to look backwards and, then, adjust the losses of earlier years against income of the eligible industrial undertaking by notionally bringing them forward and setting them off, even though they have been already been set off against other income of the Assessee. In other words, once, set off losses has taken place against other income of the Assessee, they cannot be brought form and again squared off against his current income.

31.8. In coming to this conclusion, the Division Bench, inter alia, relied upon the judgment of the Supreme Court, in Liberty India V. CIT [2009] 317 ITR 218 (SC). The observations made in that behalf are extracted hereafter, for the sake of convenience.

Heading "C" is relevant for considering the issue in these appeals. The relevant provisions that are to be considered are sections 80-1, 80-IA and 80-IB. In the case of Liberty India v. CIT, [2009] 317 ITR 218 (SC); [2009] 225 CTR (SC) 233; [2009] 28 DTR (SC) 73, the apex court considered the scope of sections 80-1, 80-IA and also section 80-IB of the Act, wherein, it has been held that Chapter VI-A provides for incentives in the form of tax deductions essentially belong to the category of "profit-linked incentives". Therefore, when section 80-IA/80-IB refers to profits derived from eligible business, it is not the ownership of that business which attracts the incentives. Further, it has been held that sections 80-IB/80-IA are the code by themselves as they contain both substantive as well as procedural provisions. The Supreme Court further observed in the said judgment that sub-section (5) of section 80-IA provides for manner of computation of profits of an eligible business. Accordingly such profits are to be computed as if such eligible business is the only source of income of the assessee.

15. Section 80-IA reads as follows:

"80-IA. (1) Where the gross total income of an assessee includes any profits and gains derived by an undertaking or an enterprise from any business referred to in sub-section (4) (such business being hereinafter referred to as the eligible business) there shall, in accordance with and subject to the provisions of this section, be allowed in computing the total income of the assessee, a deduction of an amount equal to hundred per cent, of the profits and gains derived from such business for ten consecutive assessment years.

(2) The deduction specified in sub-section (1) may, at the option of the assessee, be claimed by him for any ten consecutive assessment years out of fifteen years beginning from the year in which the undertaking or the

enterprise develops and begins to operate any infrastructure facility or starts providing telecommunication service or develops an industrial park or develops a special economic zone referred to in clause (iii) of sub-section (4) or generates power or commences transmission or distribution of power or undertakes substantial renovation and modernisation of the existing transmission or distribution lines.

(4) This section applies to—

(i) any enterprise carrying on the business of (i) developing, or (ii) operating and maintaining, or (iii) developing, operating and maintaining any infrastructure facility which fulfils all the following conditions, namely:—

(a) it is owned by a company registered in India or by a consortium of such companies (or by an authority or a board or a corporation or any other body established or constituted under any Central or State Act);

(b) it has entered into an agreement with the Central Government or a State Government or a local authority or any other statutory body for (i) developing, or (ii) operating and maintaining, or (iii) developing, operating and maintaining a new infrastructure facility;

(c) it has started or starts operating and maintaining the infrastructure facility on or after the 1st April, 1995.

(5) Notwithstanding anything contained in any other provision of this Act, the profits and gains of an eligible business to which the provisions of sub-section (1) apply shall, for the purposes of determining the quantum of deduction under that sub-section for the assessment year immediately succeeding the initial assessment year or any subsequent assessment year, be computed as if such eligible business were the only source of income of the assessee during the previous year relevant to the initial assessment year and to every subsequent assessment year up to and including the assessment year for which the determination is to be made."

16. From a reading of sub-section (1), it is clear that it provides that where the gross total income of an assessee includes any profits and gains derived by an undertaking or an enterprise from any business referred to in subsection (4), i.e., referred to as the eligible business, there shall, in accordance with and subject

to the provisions of the section, be allowed, in computing the total income of the assessee, a deduction of an amount equal to 100 per cent, of the profits and gains derived from such business for ten consecutive assessment years. Deduction is given to eligible business and the same is defined in sub-section (4). Sub-section (2) provides option to the assessee to choose 10 consecutive assessment years out of 15 years. Option has to be exercised, if it is not exercised, the assessee will not be getting the benefit. Fifteen years is outer limit and the same is beginning from the year in which the undertaking or the enterprise develops and begins to operate any infrastructure activity, etc. Sub-section (5) deals with quantum of deduction for an eligible business. The words "initial assessment year" are used in sub-section (5) and the same is not defined under the provisions. It is to be noted that "initial assessment year" employed in sub-section (5) is different from the words "beginning from the year" referred to in sub-section (2). The important factors are to be noted in sub-section (5) and they are as under:

"(1) It starts with a non obstante clause which means it overrides all the provisions of the Act and other provisions are to be ignored;

(2) It is for the purpose of determining the quantum of deduction;

(3) For the assessment year immediately succeeding the initial assessment year;

(4) It is a deeming provision;

(5) Fiction created that the eligible business is the only source of income; and

(6) During the previous year relevant to the initial assessment year and every subsequent assessment year."

17. From a reading of the above, it is clear that the eligible business were the only source of income, during the previous year relevant to the initial assessment year and every subsequent assessment years. When the assessee exercises the option, the only losses of the years beginning from initial assessment year alone are to be brought forward and no losses of earlier years which were already set off against the income of the assessee. Looking forward to a period of ten years from the initial assessment is contemplated. It does not allow the Revenue to look backward and find out if there is any loss of earlier years and bring

forward notionally even though the same were set off against other income of the assessee and the set off against the current income of the eligible business. Once the set off is taken place in earlier year against the other income of the assessee, the Revenue cannot rework the set off amount and bring it notionally. A fiction created in sub-section does not contemplates to bring set off amount notionally. The fiction is created only for the limited purpose and the same cannot be extended beyond the purpose for which it is created."

(emphasis is ours)

31.9. As a matter of fact, this view has been followed by Madras High Court in a decision rendered on 12.01.2015 in a batch of Tax Case Appeals, the lead Appeal being: T.C.(A)No.408 of 2014, titled: Commissioner of Income Tax V. Eastman Exports Global Clothing Private Limited.

32. Therefore, following the the ratio of the judgments of the Division Bench of this Court, referred to above, it is quite clear, that if, once the Assessee has exercised the option of choosing the initial Assessment year, only losses of the years beginning from the initial Assessment Year can be brought forward. The Revenue cannot notionally bring forward losses of earlier years, which have been set off against other income of the Assessee.

32.1. Furthermore, having regard to the other aspect of the matter, which is, whether or not, the two power generating units should have been considered separately, one can once again, rely upon the judgment of the Division Bench in the matter of : Velayudhaswamy Spinning Mills Pvt. Ltd. V. Assistant Commissioner of Income Tax (2012) 340 ITR 477 (Madras), wherein, quite clearly, after analysing the provisions of Section 80IA (5), it has come to the conclusion that a fiction has been created to the effect that, the eligible business is required to be considered as the only source of income.

32.2. Therefore, the approach adopted by the Assessing Officer in the two Assessment Orders of treating two separate power generating divisions as a single undertaking is, according to us, not the right approach.

33. As a matter of fact, in the matter of Commissioner of Income Tax V. Dewan Kraft Systems Pvt. Ltd. dated 27.02.2007 in I.T.A.Nos.977 of 2005 and 186 of 2006, the Division Bench of the Delhi High Court, has dealt with some what similar circumstances.

33.1. The Assessee, in that case, was engaged in the business of fabrication and supply of equipments and technical items. The Assessee had business units, located at Kalamb in Himachal Pradesh, and also, business units in Delhi and Noida, in the State of Uttar Pradesh. The Assessee claimed deduction

under Section 80IA of the 1961 Act vis-a-vis Kalamb unit. In the case of Unit situated at Delhi, since, there was a loss, no deduction was claimed. The Assessing Officer, while examining the extent of deduction to be given under Section 80IA of the 1961 Act, vis-a-vis the Kalamb unit, adjusted the loss returned by the Assessee vis-a-vis the Delhi Unit.

33.2. This issue travelled to the Division Bench of the High Court. The Division Bench noted that sub-section (5) of Section 80IA of the 1961 Act opens with the non-obstante clause and that it created a deeming fiction, which provided for it a special method to enable computation of profits and gains qua eligible business.

33.3. In sum, the Division Bench disapproved the approach adopted by the Assessing Officer of squaring off losses of the Delhi Unit against the Kalamb Unit, located in Himachal Pradesh.

33.4. We are in respectful agreement with the approach adopted in the said matter, which is in line with the observations made by the Division Bench of this Court in the matter of : Velayudhaswamy Spinning Mills Pvt. Ltd. V. Assistant Commissioner of Income Tax (2012) 340 ITR 477 (Madras).

34. As a matter of fact, as correctly submitted by the counsel for the Assessee, the Tribunal in : Rangamma Steels & Malleables V. Assistant Commissioner of Income Tax [2010] 132 TTJ 365 has adopted the same approach.

34.1. Therefore, according to us, in computing the deduction claimed by the Assessee under Section 80 IA of the 1961 Act, the Assessing Officer ought to have treated the two power divisions as a separate undertakings and furthermore, desisted from setting off the losses of earlier years against the profits of the Assessment Years in issue, by bringing them forward notionally, despite the fact that they had already been set off, as claimed by the Assessee in the earlier years.

35. For the foregoing reasons, T.C.(A) Nos.533 to 538 of 2010, preferred by the Revenue are dismissed. The questions of law raised therein are answered against the Revenue and in favour of the Assessee.

36. Similarly, T.C.(A)Nos.787 and 788 of 2014, preferred by the Revenue, are also dismissed.

36.1. We must, however, indicate that the question of law was not, appropriately, framed, as indicated in our narration above.

36.2. The Tribunal vide its order dated 12.11.2010 has allowed the Assessee's claim for deduction under Section 80IB vis-a-vis Unit I, while disallowing the same in respect of Unit II. Therefore, the Revenue's grievance, if at all, could have been directed towards the Tribunal's view qua Unit I.

36.3. The question of law thus, according to us, if, re-formulated, should read as : whether in the facts and circumstances of the case, the Tribunal was right in sustaining deduction claimed under Section 80IB of the 1961 Act vis-a-vis Unit I.

37. For the reasons stated above, we have sustained the conclusion reached, both by the CIT(A) and the Tribunal in this behalf. The question of law, is, accordingly, answered in favour of the Assessee and against the Revenue.

38. This brings us to the appeals filed by the Assessee in T.C.(A)Nos.1217 to 1220 of 2010. These Appeals are allowed. The Assessee will, accordingly, be entitled to claim deduction under Section 80IB of the 1961 Act in respect of Unit II as well, apart from the claim for deduction in respect of Unit I, which, as noted above has been sustained by us.

38.1. Furthermore, we have also concluded in favour the Assessee that the computation of deduction, under Section 80IA of the 1961 Act, by the Assessing Officer, in respect of A.Ys.2006-07 and 2007-08 vide Assessment Orders dated 29.12.2008 and 18.12.2009, has to be carried out keeping in mind the legal principles set forth by the Division Bench of this Court in the matter of Velayudhaswamy Spinning Mills Pvt. Ltd. V. Assistant Commissioner of Income Tax (2012) 340 ITR 477 (Madras).

38.2. In this behalf, as noted above by us, the decision of the Delhi High Court in the matter of Dewan Kraft Systems Private Limited, with which, we have agreed, would also be applicable. Accordingly, these appeals are allowed. The questions of law raised therein are answered in favour of the Assessee and against the Revenue. However, the Assessing Officer is directed to re-compute the deduction claimed by the Assessee under Section 80IA of the 1961 Act, vis-a-vis A.Ys.2006-07 and 2007-08, keeping in mind the foregoing discussion.

39. In sum, while, T.C.(A)Nos.533 to 538 of 2010, 787 and 788 of 2014, preferred by the Revenue, are dismissed; T.C.(A) Nos.1217 to 1220 of 2010, preferred by the Assessee, are allowed. However, there will be no order as to costs.

s/d-

Assistant Registrar(CO)

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Sub-Assistant Registrar

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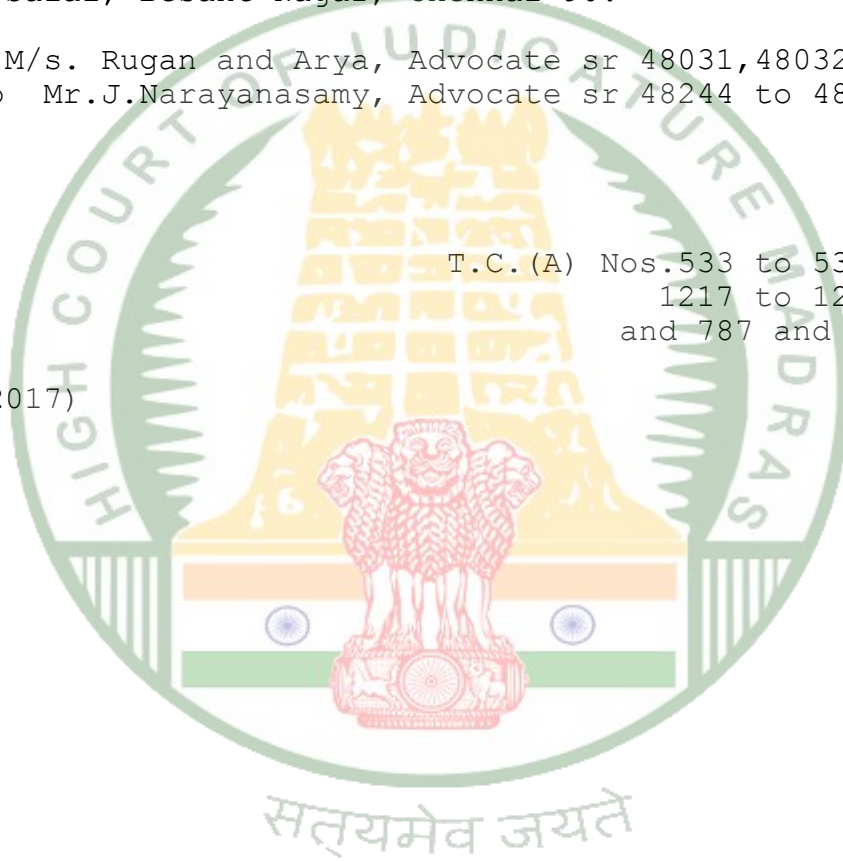
1. The Income Tax Appellate Tribunal, Chennai "B" Bench.
Chennai.
2. The Commissioner of Income Tax
Circle I, Pondichery.

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3. The Assistant Commissioner of Income Tax
Circle I, Pondichery.
 4. The Commissioner of Income Tax Appeals XII
121, Mahatma Gandhi Road, Nungampakkam, Chennai 34.
 5. The Additional Commissioner of Income Tax,
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Income Tax Appellate Tribunal,
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T.C.(A) Nos.533 to 538 of 2010,
1217 to 1220 of 2010
and 787 and 788 of 2014

SP(29/07/2017)



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