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TCA No. 1049 & 1050 of 2008

IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED : 13.12.2021

CORAM

THE HON'BLE MR. JUSTICE R. MAHADEVAN
and
THE HON'BLE MR. JUSTICE MOHAMMED SHAFFIQ

Tax Case Appeal Nos. 1049 & 1050 of 2008

M/s. Carborundum Universal Limited
“Parry House”
43, Moore Street
Chennai – 600 001

.. Appellant in both
the appeals

Versus

The Assistant Commissioner of Income Tax
Company Circle I (3)
Chennai

.. Respondent in both
the appeals

Tax Case Appeals filed under Section 260A of the Income Tax Act, 1961 against the orders dated 28.12.2007 passed by the Income Tax Appellate Tribunal, “A” Bench, Chennai in I.T.A.Nos.1102/(Mds)/2006 and 1103/(Mds)/2006 respectively.

For Appellant : Mr. R. Venkatanarayanan
in both the appeals

For Respondent : Mr.T.Ravikumar
Senior Standing Counsel
in both the appeals



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COMMON JUDGMENT

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These tax case appeals have been filed by the appellant / assessee, calling in question the correctness of the common order dated 28.12.2007 passed by the Income Tax Appellate Tribunal, 'A' Bench, Chennai, in I.T.A.Nos. 1102/Mds/2006 and 1103/Mds/2006 relating to the assessment years 2000-01 and 2002-03 respectively.

2. According to the appellant / assessee, they are engaged in the business of manufacturing and sale of abrasives, industrial ceramics and electro minerals. For the assessment years in question, they filed return of income, which were processed under Section 143(1)(a) of the Income-tax Act, 1961 (hereinafter referred to as “the Act”). The Assessing Officer issued notice under Section 148 for the purpose of scrutiny assessment and the assessment was completed under Section 143(3) read with Section 147 of the Act. While so, the Assessing Officer restricted the relief under Section 80HHC and Section 80 I and disallowed depreciation claimed on the merged entity and on Technical know-how fee paid and added the notional profit arising on valuation of closing inventory on account of mandatory adoption of Accounting Standard (AS 2) issued by ICAI. Further, the Assessing Officer included the



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sale of scrap in the total turnover and excluded 90% of gross interest income while computing deduction under 80HHC.

3.Challenging the orders of assessment, the assessee filed appeals before the Commissioner of Income-tax (Appeals)-III, Chennai, who partly allowed the appeals, by common order dated 28.02.2006. Aggrieved over the same, both the assessee and the Revenue went on further appeals before the Income Tax Appellate Tribunal. By order dated 28.12.2007, the Tribunal partly allowed the appeals filed by the assessee as well as the Revenue. Therefore, the present tax case appeals by the assessee alone.

4.By order dated 30.07.2008, TCA No.1049 of 2008 was admitted on the following substantial questions of law :-

“1. Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that scrap should be included in the total turnover while computing deduction under Section 80HHC?

2. Whether on the facts and circumstances of the case, the Tribunal was right in confirming the disallowance of depreciation claimed under Section 32 on the technical know how fee paid and holding that only relief under Section 35AB is to be allowed on such payment?



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3. *Whether on the facts and in the circumstances of the case, the Tribunal was right in confirming the disallowance of depreciation claimed under section 32 on the assets acquired through amalgamation?*

4. *Whether on the facts and in the circumstances of the case, the Tribunal was right in confirming the additional of notional profit arising on account of the inventory valuation due to mandatory application of AS-2?"*

5. By another order dated 30.07.2008, TCA No.1050 of 2008 was admitted by this court on the substantial question of law Nos.1 to 3 as were raised in TCA No.1049 of 2008, as stated above.

6. Heard both sides and perused the materials placed before this court.

7.1 As regards the first question of law, whether the sale of scrap should be included in the total turnover for the purpose of deduction under Section 80HHC of the Act, the same is covered by the decision of the Hon'ble Supreme Court in the case of *Commissioner of Income Tax vs. Punjab Stainless Steel Industries [(2015) 229 Taxman 0423 (SC)]*, wherein it was held that “the proceeds generated from the sale of scrap would not be included in the ‘total turnover’, for computation of deduction under Section 80HHC”.

The relevant paragraphs of the said decision are usefully extracted below:



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“22. So far as the scrap is concerned, the sale proceeds from the scrap may either be shown separately in the Profit and Loss Account or may be deducted from the amount spent by the manufacturing unit on the raw material, which is steel in the case of the respondent-assessee, as the respondent-assessee is using stainless steel as raw material, from which utensils are manufactured. The raw material, which is not capable of being used for manufacturing utensils will have to be either sold as scrap or might have to be re-cycled in the form of sheets of stainless steel, if the manufacturing unit is also having its re-rolling plant. If it is not having such a plant, the manufacturer would dispose of the scrap of steel to someone who would re-cycle the said scrap into steel so that the said steel can be re-used.

23. When such scrap is sold, in our opinion, the sale proceeds of the scrap cannot be included in the term ‘turnover’ for the reason that the respondent-unit is engaged primarily in the manufacturing and selling of steel utensils and not scrap of steel. Therefore, the proceeds of such scrap would not be included in ‘sales’ in the Profit and Loss Account of the respondent-assessee.

....

28. The intention behind enactment of [Section 80HHC](#) of the Act was to encourage export so as to earn more foreign exchange. For the said purpose the Government wanted to encourage businessmen, traders and manufacturers to increase the export so as to bring more foreign exchange in our country. If the purpose is to bring more foreign exchange and to encourage export, we are of the view that the legislature would surely like to give more benefit to persons who are making an effort to help our nation in the process of bringing more foreign exchange. If a trader or a manufacturer is trying his best to increase his exports, even at the cost of his business in a local market, we are sure that the Government would like to encourage such a person. In our opinion, once the Government decides to give some benefit to someone who is helping the nation in bringing foreign exchange, the Revenue should also make all possible efforts to encourage such traders or manufacturers by giving such business units more benefits as contemplated under the provisions of law.

29. For the aforesaid reasons, we are of the view that the view expressed by the High Court is in conformity with the normal



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accounting practice followed by the traders, including the respondent-assessee and it was justified in coming to a conclusion that the proceeds generated from the sale of scrap would not be included in the 'total turnover'.

7.2 Following the aforesaid decision, we are inclined to interfere with the finding of the Tribunal and this issue is answered against the Revenue and in favour of the assessee.

8. With regard to second question of law relating to the expenditure incurred by the assessee for the purpose of getting technical know-how on manufacture and process of goods, they are entitled to depreciation or deduction under Section 35AB, the same is covered by the decision of this court in *Carborundum Universal Ltd vs. The Joint Commissioner of Income Tax [(2012) TIOL 790 HC Mad IT]*, wherein it was held that “the assessee is entitled to deduction under section 35AB and not entitled to depreciation under section 32”. In view of the same, we answer this issue against the appellant/assessee and in favour of the revenue/respondent.

9.1 Regarding the third question of law, in the decision reported in the case of *Commissioner of Income Tax vs. Silical Metallurgic Ltd [324 CTR 29(Madras)]*, this Court concluded that “the amalgamation of one company



with the other company cannot be regarded as a splitting up or reconstruction or by a transfer of a new business of the plant and machinery of the old business. Thus, the amalgamation cannot be regarded as a splitting up of the company for the purpose of negating the claim of deduction under Section 80HH and 80-I, which has been statutorily conferred on the company, if such companies fulfil the conditions stipulated therein. Similar view was expressed by this court in another decision reported in the case of *EID Parry (India) Limited v. Deputy Commissioner of Income Tax [256 CTR 104 (Madras)]*, in which, it was held that “the accumulated loss and unabsorbed depreciation of the amalgamating company is deemed to be the loss or the allowance of depreciation to the amalgamated company for the previous year in which the amalgamation is effected”. The relevant paragraph of the said decision is reproduced below:

“23.As far as the present case is concerned, it is no doubt true that Explanation 2 is not similarly worded as Explanation 2A, which was considered by the Bombay High Court. The provisions contained in Explanation 2, applicable to the present case, in fact, brings out the intention better and is crisp in its language, as is evident from a reading of explanation 2. As per explanation 2, the actual cost of the block of assets at the hands of the amalgamated company is “the written down value of the block assets” as in the case of transferor company or the amalgamating company for the immediately preceding previous year as reduced by the amount of depreciation actually allowed in relation to the said immediately preceding previous year. The use of the phrase “for the



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immediately preceding previous year” with reference to the written down value at the hands of transferor company in understanding what should be the cost of the block of assets at the hands of amalgamated company.”

9.2 In view of the above decision, we are inclined to answer this issue in favour of the assessee and against the Revenue and is accordingly, answered.

10. As regards the fourth substantial question of law in TCA No.1049 of 2008, in the decision in the case of *Commissioner of Income Tax vs. George Oakes reported in [75 CCH 357 (Mad)]*, this Court was of the view that “the assessee having valued its inventory as per AS-2 prescribed by the ICAI, such a change was bonafide and was mandatory by the ICAI and the discrepancy in profitability arising in the year of change, cannot be forced to be taxed”. Similar view was upheld by the Hon'ble supreme court in the decision reported in the case of *VKJ Builders and Contractors (P) Ltd v. Commissioner of Income Tax in [318 ITR 204 (SC)]*, wherein it was held that “the closing stock of earlier year has to be treated as opening stock of current year and therefore where the opening stock of current year shows a lower value than the value of closing stock of earlier year as finally determined by the Assessing Officer, the same is amenable to rectification under Section 154 of the Act”. In view of the said decisions, this issue is answered in favour of the assessee.

<https://www.mhc.tn.gov.in/judis> 11. In the result, both the tax case appeals filed by the assessee are partly



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allowed to the extent as indicated above. No costs.

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J.]

[R.M.D,J.]

[M.S.Q,

13.12.2021

Internet : Yes

Index : Yes / No

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To

1. The Income Tax Appellate Tribunal,
Madras “A” Bench.
2. The Assistant Commissioner of Income Tax
Company Circle I (3)
Chennai



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