IN THE HIGH COURT OF MADRAS

TC(A) No.188 of 2005

S MUTHURAJAN

Vs

DEPUTY COMMISSIONER OF INCOME TAX

Chitra Venkataraman and M Jaichandren, JJ

Dated: August 10, 2011

Appellant Rep by: R Vijayaraghavan
Respondent Rep by: K Subramanian

JUDGEMENT

Per: Chitra Venkataraman:

The following substantial questions of law raised by the assessee in this Tax Case Appeal against the order of the Tribunal relating to assessment year 1993-94.

"1. Whether on the facts and in the circumstances of the case, the Tribunal is wrong in disregarding the scope of Section 50 of the Income Tax Act for the purpose of computing the capital gains under the Income Tax Act?

2. Whether on the facts and in the circumstances of the case, the Tribunal is wrong in justifying ignoring the total additions made during the accounting year which is very relevant for the purpose of computing capital gains under Section 50 of the Income Tax Act and addition is much more than the sale consideration?

3. Whether on the facts and in the circumstances of the case, the Tribunal is wrong in computing the capital gains under sub section 2 of Section 50 without applying its mind?"

2. The assessee is an individual engaged in the business of rig operation, transportation of LPG gas, marbles etc. The assessee had an export oriented unit run under the name and style of 'GTP Granites'. On the expiry of the term of the benefit available to 100% export oriented unit under Section 10B of the Income Tax Act, 1996, during the year relevant to the assessment year 1993-94, on 2.7.1992, the assessee transferred the said unit to the closely held company called 'GTP Granites (P) Limited'. On a comparison of the value of the assets, as per the balance sheet as on 2.7.1992 and the value of the assets adopted by the closely held company, the Officer found that there was different in value of the assets to the extent of Rs.71,42,904/-. The Assessing Officer completed the assessment treating the difference as short term capital gains, the assets being block of assets transferred by the assessee.

3. Aggrieved by the same, the assessee went on appeal before the Commissioner of Income Tax (Appeals), who held that the assessee's business numbering seven have to be treated as a composite business, hence, it would be incorrect to segregate this for the purpose of

calculating the depreciation. Applying the concept of block of assets for the purpose of determining depreciation, the Commissioner of Income Tax (Appeals) held that the view of the Officer in determining the short term capital gains as arising out of the transfer of the assets from export oriented unit was not correct. The Commissioner of Income Tax (Appeals) further held that when the business of the assessee was taken as a whole and the adjustments due to transfer and addition made during the year had to be taken into account, the assessment made treating it as short term capital gain was incorrect. Thus, he allowed the assessee's appeal.

4. Aggrieved by the same, the Revenue went on appeal before the Income Tax Appellate Tribunal. The Tribunal pointed out that admittedly the assessee had sold the assets for a value more than what was shown as WDV in the balance sheet as on the date of transfer on 2.7.1992, whereas, the value adopted by the transferee company was more than the value adopted by the transferor company, which revealed the difference in value to the tune of Rs.71,42,904/-. When the assessee's business was taken over as a whole, the adjustment due to the transfer and the addition made during the year clearly revealed surplus attracting short term capital gains as per Section 50(2). In the circumstances, the Tribunal confirmed the view of the Assessing Officer to hold that the surplus amount resulting from that transfer of capital assets was liable to be assessed as short term capital gains under Section 50(2) of the Income Tax Act. Aggrieved by the said order, the assessee is on appeal before this Court.

5. Learned counsel appearing for the assessee placed reliance on the definition of 'block of assets' as given under Section 2(11) as well as to the scheme of Section 10B and submitted that given the fact that the relief under Section 10B is of on limited duration, on the expiry of said period, when the assessee transferred the said assets to one of his sister concerns, which is also in the same line of business, the investments made in the purchase of machines during the relevant assessment year has to take note of depreciation value as given to the block of assets. Hence, the benefit under Section 50(2) of the Act has to be given in favour of the assessee. He pointed out that there is no dispute on the side of the Revenue that the assets transferred and the asset purchased carry the same percentage of depreciation as given under the Rule to form 'block of assets'. That being so, when the assets in the block are transferred during the previous year, the cost of the assets have to be taken as written down value of the block of assets at the beginning of the previous year, as increased by the actual cost of assets which are purchased or acquired by the assessee during the previous year. The only requirement is that they fall within the meaning of 'block of assets'. Thus, going by sub section (2) of Section 50, the Assessing Officer should have considered the depreciation available in respect of the block of assets transferred and the assets purchased forming part of the same block of assets was much more than the sale consideration attributable to the assets transferred from the block on 2.7.1992. He further pointed out to Section 10B, sub section (4), sub clause (iv) and submitted that the scheme under sub section (4) of Section 10B, recognises that the assessee would be entitled to what would otherwise in the normal circumstances be applicable as regards various allowances available under the provisions of the Act. However, going by the restricted number of years of tax holiday, the benefit as contemplated under sub section have to be treated as exhausted there itself during that period covered under Section 10B of the Act. The allowances and the written down value of the assets used for the purpose of business of the 100% export undertaking has to be computed as if the assessee had claimed and had been actually allowed deduction in respect of depreciation for each of the relevant assessment years. Thus, he submitted that on the expiry of the term, the assessee reverted back to the regular assessment procedure. The concept of block of assets as originally stood would continue to be there available to the assessee in the matter of working out the relief under Section 50 of the Income Tax Act.

6. Per contra, learned standing counsel appearing for the Revenue submitted that given the fact that the 100% Export Oriented Unit is treated as an independent unit of business, the assets covered in the said business have to be treated independently and the definition of block of assets as given under Section 2(11) has to be viewed only in the limited manner restricted to that particular undertaking alone.

7. Referring to the depreciation Rules available for the relevant assessment year under consideration, he pointed out that the rate of depreciation given therein is industry specific. Thus, when 100% Export Oriented Unit is a separate undertaking of the business, the benefit of adjustment would be available only for the said unit of business and not be extended to other business.

8. Heard learned counsel for the assessee as well as learned Standing counsel for the Revenue and perused the materials on records.

9. Section 2(11) of the Income Tax Act defines 'block of assets' which reads as follows:-

"'block of assets' means a group of assets falling within a class of assets, being buildings, machinery, plant or furniture, in respect of which the same percentage of depreciation is prescribed."

10. Section 50(2) speaks about the computation of the capital gains in the case of depreciable assets, which read as follows:-

"where any block of assets ceases to exist as such, for the reason that all the assets in that block are transferred during the previous year, the cost of acquisition of the block of assets shall be the written down value of the block of assets at the beginning of the previous year, as increased by the actual cost of any asset falling within that block of assets, acquired by the assessee during the previous year and the income received or accruing as a result of such transfer or transfers shall be deemed to be the capital gains arising from the transfer of short term capital assets."

11. The only controversy raised in this Tax Case Appeal is as regards the computation of short term capital gains in terms of Section 50 of the Act. It is admitted by the assessee as well as by the Revenue that the assessee had 100% Export Oriented Unit under the name and style of GTP granites. It is also admitted by the Revenue that apart from 100% export oriented unit in the name of GTP granites, the assessee had other business too, which are as follows:-

"1. GRP Granites

2. Share income from Gounder Finance Corporation

3. Sabari Finance

4. GTP Transport Company

5. GTP Drilling Contractors

6. GTP Marbles & Granites

7. GTP Marbles."

12. The assessee does not dispute as a matter of fact that prior to the relevant assessment year viz., 1993-94, the assessee had the benefit of Section 10B in respect of the business transacted by GTP Granites. The assessee transferred the said unit to GTP Granites(Private) Limited on 2.7.1992. On the working of the capital gains arising on the transfer of plant and machinery, the assessee took the WDV on the block of assets of plant and machinery as on 2.7.1992 to be set off against the purchase of Poclain. The Revenue took the plea that there could not be set off of WDV on the block of assets sold as against the purchase of Poclain or some other business; hence, the excess value was to be treated as consideration received by the assessee. Taking the view that the above omission had resulted in the non assessment of short term capital gains, the assessment was sought to be reopened under Section 148 of the Income Tax Act.

13. In this connection, the submission of the learned Standing Counsel making reference to Section 10B, as well as to definition of 'block of assets' on the question of treating the transferred machinery as a block of assets for the purpose of working out the capital gains under Section 50(2) needs to be seen in terms of Section 10B of the Act. Section 10B is a special provision introduced with effect from 1.4.1989 for the purpose of granting benefits to newly established 100% export oriented undertaking. The section, as it originally stood, contemplated tax holiday by excluding the profits and gains derived by the assessee from 100% export oriented undertaking in the total income of the assessee subject to certain conditions given in the said Section. The exemption available by way of excluding this income was available only for five consecutive assessment years, falling within a period of eight years, beginning with the assessment year relevant to the previous year in which undertaking begins to manufacture or produce articles. The specification of the period is left to the option of the assessee.

14. Since the section contemplates exclusion of the income referrable to the 100% export unit, sub section (4) of Section 10B deals with the manner of availing various allowances available under the Act, particularly, with reference to Sections 32, 32A, 33, 36(1)(ix), 72(1), 74(1) and (3) of the Act. Thus, even though for the purpose of Section 10B, the export is referred to as the business of the undertaking, which must satisfy the requirement under Section 10B(2) to qualify for exemption and the income is excluded from the total income of the assessee, the assets of the undertaking are subject to the working of depreciation as per Section 32, that the WDV of any asset used for the purpose of the business of the undertaking is taken as if the claim on depreciation was actually allowed under each of the relevant assessment years. Thus, going by sub Section (4) of Section 10B, the various benefits under the Act available under the normal procedure has to be worked on the machineries and plant as if the claim had been considered and granted in spite of the fact that the income of the 100% Export Undertaking is exempted from tax.

15. As seen from the section, even though the assessee might have been engaged in 100% export, on the expiry of the term specified therein, the undertaking comes in automatically for regular assessment that the income chargeable has to be computed to tax in accordance with the provisions contained therein. When that being the case, the question is on the expiry of tax holiday, what would be the depreciation and other benefits that the assessee would be entitled to as regards the assets of the business undertaking engaged in 100% export oriented unit.

16. As already pointed out, Section 50 is a special provision for computation of capital gains in the case of depreciable assets. The said provision states that where the capital assets is

an asset forming part of a block of assets, then the computation of the capital gains has to be done in accordance with Section 50 of the Act. Under sub section (2) of Section 50, where any block of assets are transferred, the cost of depreciation at the hands of the transferee shall be written down value of the block of assets at the beginning of the previous year, as increased by the actual cost of any asset falling within that block of assets, acquired by the assessee during the previous year. The income thus received or accruing as a result of such transfer or transfer is deemed to be the capital gains arising from the transfer of short term capital assets. Given the fact that block of assets is identified by the percentage of depreciation granted, on going through the various heads under the schedule, we find that the depreciation percentage fixed is more of machinery specific rather than industry specific. Thus on going through the various clauses in the schedule, we find, if the asset transferred and the asset purchased fall for consideration under the self same percentage of depreciation, then the asset qualified for being termed as falling under a block of assets. Thus, if the assets transferred from the 100% Export Oriented Unit and the assets purchased come for same percentage of depreciation as prescribed in the table, the assessee would be justified in seeking adjustment in the matter of working out the capital gains.

17. The assessee carried on same line of business, both as an export undertaking as well as on domestic trade. In this case, apart from export business in granites, the assessee also had local business in selling granites. As far as the present case is concerned, as pointed out by the assessee, the assessee made an addition of 25% in the block of assets, viz., plant and machinery, during the previous year. Given the fact that the depreciation in respect of the asset transferred and purchased carry the same rate of depreciation, hence fall under 'block of assets', we find that the assessee is justified in its claim on capital gains, that with the cost of the new machinery added to the written down value of the machinery and the sale of the machinery during the relevant previous year, the Commissioner of Income Tax (Appeals) rightly considered the said aspect and granted relief to the assessee. Going by the provisions under Section 10B, we do not think the Revenue would be justified in treating the assets of an Export Oriented Unit in isolation on the expiry of the tax holiday period, particularly when Section 10B(4)(iv) recognised the deemed granting of the depreciation allowance during the currency of tax holiday, which means at the expiry of the period of five years, the WDV on the plant and machinery continued to be available for the business of the assessee which goes for normal assessment under various provisions of the Act. To hold that on the expiry of tax holiday period, the business of the assessee comes to a close would only mean the statutory closing of the business, thereby causing violence to the provisions under Section 10B(4). We are at a loss to understand how any such view could be projected by the Revenue. Learned Standing Counsel pointed out that Section 10B specifically uses the phrase 'business of the export undertaking'. Hence, on the expiry of the period of tax holiday, the business cannot be treated as though it was available thereafter for further tax treatment under the normal provisions. Except for mere plea on words, we do not find any logic in the said reasoning. The use of the phrase 'business of export undertaking' in Section 10B is meant to identify industry or undertaking which qualifies for tax holiday exemption. Thus going by the above, on the expiry of the period mentioned under Section 10B, the block of assets viz., plant and machineries, of the industry, are available for working out the relief under Section 50(2). So long as the assets are found to fall under the same depreciation, they fit in into the concept of block of assets for the purpose of Section 50(2) of the Act. On the mere score that the assessee was once 100% export undertaking, the assessee could not be denied of the benefit otherwise available to the assessee on the block of assets on the expiry of tax holiday period for the purpose of the working of capital gains under Section 50(2).

18. Thus on facts, contrary to the assertion of the learned standing counsel that eventhough the export unit has to be treated as an independent unit for the purpose of Section 10B, when the export unit formed part of the business of the assessee, on the expiry of tax holiday period, we do not find any logic in treating the assets as independent of business of the assessee that they do not form part of block of assets for the purpose of working out the relief on capital gains.

19. In the light of the above, we set aside the order of the Tribunal, thereby allowed the Tax Case Appeal and restore the order of the Commissioner of Income Tax (Appeals). No costs.