Jammu & Kashmir High Court
Commissioner Of Income-Tax vs Abdul Ahad Najar on 17 November, 2000
Equivalent citations: 2001 248 ITR 744 J K
Author: B Saraf
Bench: B Saraf, S Bashir-Ud-Din
JUDGMENT B.P. Saraf, C.J.

1. By this reference under Section 256(1) of the Income-tax Act, 1961 (the "Act"), the Income-tax Appellate Tribunal, Amritsar Bench, Amritsar (the "Tribunal"), has referred the following two questions of law to this court for opinion at the instance of the Revenue :

"1. Whether, on the facts and in the circumstances of the case, the Appellate Tribunal has erred in taking the view that the letter dated December 2, 1974, from the Central Board of Direct Taxes addressed to the Vice-President, Jammu Forest Lessees' Association, constituted an instruction so as to be binding on the Income-tax Officer ?

2. Whether, on the facts and in the circumstances of the case, the Appellate Tribunal is right in law in holding that the undertaking of the assessee constituted an industrial undertaking within the meaning of Section 80J(4) and that it is entitled to claim deduction admissible under Section 80J of the Income-tax Act, 1961, in respect of the income from this undertaking ?"

2. The controversy in this reference pertains to the assessment year 1975-76. The material facts giving rise to this reference are as follows. The asses-see, who is a forest lessee, was engaged in the business of forest exploitation. For the assessment year 1975-76, the assessee submitted a revised return and claimed deduction of Rs. 33,060, being the sum equal to six per cent, of the capital employed, as deduction under Section 80J of the Act. In the covering letter attached to the revised return, the assessee claimed that the assessee fulfilled all the conditions of a newly established industrial undertaking within the meaning of Section 80J of the Act since it was engaged in the manufacture and production of articles. The case of the assessee was that the planks sawn out of logs and articles produced therefrom were different in shape from logs. The assessee relied upon the order of the Appellate Assistant Commissioner, Jullundur, where he had held that the assessee in that case, who derived income from forest exploitation, was an industrial undertaking engaged in the manufacture and pro duction of articles and was entitled to deduction under Section 80J. The Income-tax Officer did not accept the above contention of the assessee. According to him, the assessee did not fulfil one of the pre-requisites of grant of relief under Section 80J that the industrial undertaking should manufacture or produce articles because he had effected substantial sales in the form of logs, as out of total sales of Rs. 40,42,169 sale of log's amounted to Rs. 16,75,653 which was about 40 per cent, of the total turnover of the assessee. The Income-tax Officer held that the process of converting trees into log's did not involve much sawing operations as after felling the trees it had been cut into logs and sold as such. The Income-tax Officer observed that no planks were sawn out of the logs and, therefore, the log's produced were not at all different in content from the trees and the sale of logs did not involve any manufacturing operations. The Income-tax Officer further observed that the process of sawing of logs into planks also did not involve any manufacture of articles because, according to him, planks could not be considered to be articles as those could not

be put to any use, but could be put to use only after they were further processed by carpenters. The Income-tax Officer also observed that the assessee had not put up any machinery such as sawing machines for sawing of planks but the entire work of sawing was entrusted to other sawing machine owners who had been paid huge amounts as sawing charges. According to the Income-tax Officer, the assessee having not employed any machinery of his own for sawing operations, he could not be considered as having carried out manufacturing operations. The Income-tax Officer did not accept the contention of the assessee that even wages paid for getting timber sawn would involve manufacturing operations whether it was carried out by the assessee himself or with the help of other sawing machine owners. According to the Income-tax Officer, relief under Section 80J of the Act would be available only if the assessee carries on the manufacturing operations with the aid of its own machinery. As no sawing machines had been deployed by the assessee, he held that the assessee could not be said to be an industrial undertaking. The Income-tax Officer also held that the manufacturing process could not be carried on by bare hands and until and unless machinery was employed in the business, there would be no manufacturing operations. As the assessee had not employed any machinery for sawing planks, according to the Income-tax Officer, he could not be said to have fulfilled the conditions of Section 80J and, as such, he was not entitled to relief under that section. Aggrieved by the order of the Income-tax Officer, the assessee appealed to the Appellate Assistant Commissioner of Income-tax. The contention of the assessee before the Appellate Assistant Commissioner was that the forest operations carried on by him amounted to manufacturing process. In support of this contention, he relied upon a letter dated December 2, 1974, of the Central Board of Direct Taxes addressed to Shri J. L. Kuthiala, Vice President, Jammu Forest Lessees Association, confirming that the provisions of Clauses (xxxi) and (xxxii) of Sub-section (1) of Section 5 of the Wealth-tax Act, 1957, would be applicable to such of the undertakings of the forest lessees as are engaged in the business of extraction of wood from forests, i.e., felling, roping, lopping, removing the bark of trees, cutting logs and trees into required lengths of sleepers, sawing the same by manual labour or by sawing machines into sleepers, transporting the same by dry slides, wet slides, ropeways and ultimately launching into stream and river. The Appellate Assistant Commissioner held that the use of machinery was not indispensable to a manufacturing process and even for the conversion of the standing trees into logs, labour was required as something is converted into something else, viz., logs. He was of the opinion that logs could be said to be a new product emerging out of manufacturing process. He, therefore, held that the assessee was entitled to relief under Section 80J of the Act. The Revenue appealed to the Tribunal. The Tribunal did not find any reason to interfere with the order of the Appellate Assistant Commissioner and dismissed the appeal. While doing so, the Tribunal referred to the letter of the Under Secretary, Central Board of Direct Taxes, addressed to Shri J. L. Kuthiala, Vice President, Jammu Forest Lessees Association, cited above, wherein it was stated that the forest lessees who were engaged in the business of extraction of wood, felling, roping, lopping, removing the bark of trees and cutting logs into required length of sleepers and from the trees and sawing the same by manual labour or by sawing machines into sleepers and transporting the same by dry slide, wet slide, ropeways and ultimately launching into stream and river would be treated as an industrial undertaking and observed that the instructions or circulars of the Central Board of Direct Taxes were binding on the income-tax authorities and that they were required to give effect to such instructions if they were for the benefit of the assessees. Since the instructions in question were for the benefit of the assessee, the Tribunal held that the Income-tax Officer was not justified in not

giving effect to the same and rejecting the claim of the assessee for relief under Section 80J of the Act. The Tribunal confirmed the order of the Appellate Assistant Commissioner holding that the assessee fulfilled all the conditions laid down under Section 80J(4) of the Act and that it was entitled to the statutory deduction thereunder. Aggrieved by the order of the Tribunal, the Revenue applied for reference of the questions of law arising out of the order of the Tribunal to this court for opinion under Section 256(1) of the Act, which the Tribunal allowed. Hence, this reference.

3. We have heard Mr. Anil Bhan, learned counsel for the Revenue and perused the order of the Tribunal. The controversy in this ease is about the entitlement of the assessee to deduction under Section 80J of the Act. Section 80J, as it stood at the material time, provides for deduction out of profits and gains derived by a newly established industrial undertaking which manufactures or produces articles. Sub-section (4) of Section 80J provides that the Section would apply only to those industrial undertakings which fulfil all the conditions set out therein. These conditions are :

"(i) it is not formed by the 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) if manufactures or produces articles, or operates one or more cold storage plant or plants, in any part of India, and has begun or begins to manufacture or produce articles or to operate such plant or plants, at any time within the period of thirty-three years next following the 1st day of April, 1948, or such further period as the Central Government may, by notification in the Official Gazette, specify with reference to any particular industrial undertaking ;

(iv) in a case where the industrial undertaking manufactures or produces articles, the undertaking employs ten or more workers in a manufacturing process carried on with the aid of power, or employs twenty or more workers in a manufacturing process carried on without the aid of power."

4. It is evident from the above provision that in order to claim relief under Section 80J of the Act, the industrial undertaking must manufacture or produce articles. It is a condition precedent. The manufacturing process mentioned in Clause (iv) of Sub-section (4) of Section 80J refers to the process undertaken to manufacture or produce articles. The question that arises for consideration in the instant case is whether the assessee, a forest lessee in the State of Jammu and Kashmir, who was engaged in the extraction of timber and other forest produce from the forest, was entitled to deduction under Section 80J. The answer will depend upon the answer to the question whether extraction of timber from forest by cutting standing trees would amount to manufacture or production of articles. Admittedly, the assessee cut trees in the forest converted them not only into logs but also into planks and other articles for the purpose of sale. The production of planks and other articles during the year constituted 60 per cent, of the total production of the assessee. There can be no dispute about the fact that the logs and planks are articles. The only question that may require consideration' is whether those articles were manufactured or produced by the assessee. The uncontroverted factual position is that the assessee did not "purchase" logs and planks, etc. As a forest lessee, his business was to cut standing' trees and to extract timber and convert the same in

the form of logs, planks, etc., for the purpose of sale. Logs and planks are never known as trees. They are undoubtedly different from standing trees. A common man who likes to purchase logs or planks would not purchase a standing tree. A standing tree as such is not a commodity, which a common man in need of timber would purchase. The most primary form in which timber is sold in the market is in the form of logs and planks. Cutting of trees and conversion of timber obtained therefrom into logs and planks can be done by manual labour or mechanical process. However, by whichever method it is done, the process of conversion of the felled tree into log's, planks, etc., would amount to a manufacturing process. Section 80J does not require that in order to get deduction, manufacture should be carried on only with the aid of power. On the other hand, it clearly postulates that manufacturing process can be carried on manually without the aid of power. That is evident from the fourth condition set out in Sub-section (4) of Section 80J which provides that in a case where the industrial undertaking manufactures or produces articles, it should employ ten or more workers in a manufacturing process carried on with the aid of power and "employ twenty or more workers in a manufacturing process carried on without the aid of power". It is, therefore, not correct to say that the process of manufacturing articles can be regarded as manufacturing process for the purposes of Section 80J only if it is carried on with the aid of machines or power. Manufacturing process carried on manually would also be manufacturing process. It is clear from the above that the activity of the forest lessees of extraction of timber from the forest and conversion of the same into logs, planks, etc., is a manufacturing process.

5. in fact, the question whether the forest lessees of Jammu and Kashmir were entitled to the benefit of Section 80J of the Act came up for consideration of the Central Board of Direct Taxes (the Board) as for back as in the year 1982. The Board, after obtaining legal opinion from the Ministry of Law, Government of India, issued the following circular on February 22, 1982 (see [1982] 135 ITR (St.) 7) :

"Deductions under Section 80HH and 80J of ihe Income-tax Act in the case afforest lessees-Clarification regarding.--A reference was made to the Board as to whether undertaking's engaged in extraction of timber and other forest produce by leasing out forests would be entitled to deductions under sections 80HH and 80J of the Income-tax Act, 1961.

2. The matter was considered by the Board in consultation with the Ministry of Law which had given an opinion (copy enclosed) that the answer to the question posed would depend on the nature of the activity of the forest lessees ; however, if the process involved is not merely conversion of standing trees into fire-wood but also manufacture of new saleable commodities, the benefit of deduction under sections 80J and 80HH would be available.

3. These instructions may please be brought to the notice of all officers working in your charge."

[Circular No. 329, dated February 22, 1982]

6. The opinion of the Ministry of Law, referred to in the above circular, reads as below (see (1982] 155 ITR (St.) 7) :

"We have gone through the order passed by the Income-tax Appellate Tribunal on October 21, 1981, in the appeal filed by the forest lessees of Jammu and Kashmir. Before the Tribunal, the assessee advanced arguments on the basis of a letter written by the Minister of State for Finance to a Member of Parliament wherein it is stated that if the process involved in the business of the members of the Jammu Forest Lessees Association is not merely conversion of standing trees into fire-wood but also manufacture of new commodity saleable as such, the benefit of Section 80J/80HH of the Income-tax Act, 1961, will be available.

2. The Tribunal observed that it cannot be held that the assessee is manufacturing any new commodity as such.

3. If the process involved is merely conversion of standing trees into fire-wood or similar articles, it cannot be said that a new commodity saleable as such has come into existence. As pointed out in our previous opinion dated November 25, 1974, the transformation of wood into sleepers could be considered to be a change in the sense of a manufacture, since a new commodity saleable as such, namely, sleepers, is brought into existence by such process.

4. In other words, it is not merely the cutting of trees and selling of fire-wood that would amount to manufacture. The process should involve the making of a different commodity having distinctive name, character or use. In the case of trees, the making of sleepers would amount to such a process as would amount to manufacture.

5. The result is that to the extent the Jammu Forest lessees convert standing trees into sleepers, they would be entitled to the benefit of Section 80J/80HH of the Income-tax Act."

7. There is also an earlier communication on December 2, 1974, from the Central Board of Direct Taxes addressed to Shri J. L. Kuthiala, Vice President, Jammu Forest Lessees Association, Jammu, whereby the Board confirmed to the Association as under :

"I am directed to refer to your letter dated April 3, 1974, addressed to the Finance Minister and to confirm that the provisions of Clauses (xxxi) and (xxxii) of Sub-section (1) of Section 5 of the Wealth-tax Act, 1957, would be applicable to such of the undertakings of the forest lessees as are engaged in the business of extraction of wood from the forest, i.e., felling, roping, lopping, removing the bark of the trees and cutting logs into required lengths of sleepers and from the trees and sawing" the same by manual labour or by sawing machine into sleepers and transport the same by dry slide, wet slide, rope-ways and ultimately launching into stream and river."

8. The Tribunal has also placed reliance on the above communication of the Board in support of its finding that the assessee was engaged in manufacture of articles. The question which was referred to the Board was whether the forest lessees of Jammu and Kashmir could be said to be engaged in the business of manufacture of goods and entitled to the benefit of exemption from wealth-tax under Clauses (xxxa), (xxxi) and (xxxii) of the Wealth-tax Act. At the material time, the benefit of exemption in respect of the assets of an industrial undertaking under the aforesaid Clauses was available only to industrial undertakings which were engaged in the business, inter alia, of

manufacture and processing of goods. It is in that context that this clarificalion was issued by the Board and it was informed that forest lessees of Jammu and Kashmir, who were engaged in the manufacture and production of logs and planks and other articles of timber, were entitled to relief under Section 80J of the Act.

9. Otherwise also, it is clear that the activity undertaken by the assessee clearly amounts to manufacture and production of articles. The expressions "manufacture" and "produce" have not been defined in the Income-tax Act. The dictionary meaning of "manufacture" is "transform or fashion new materials into a changed form for use". In common parlance, manufacture means production of articles from raw or prepared materials by giving these materials new forms, qualities, properties or combinations, whether by hand labour or by machinery. In other words, it means making of articles or materials commercially different from the basic components by physical labour or mechanical process. In its ordinary connotation, manufacture signifies emergence of new and different goods as understood in relevant commercial circles. So far as the meaning of the word "produce" is concerned, though the word "produce" has a wider connotation than the word manufacture, when used in juxtaposition with the word "manufacture", it takes in bringing into existence new goods by a process which may not amount to manufacture. The activity of extraction of wood by the assessee from the forest by felling the trees and converting the same into logs, planks, sleepers and other articles, undoubtedly, falls within the definition of "manufacture".

10. Moreover, in the instant case, the controversy whether the activity of the assessee-forest lessee amounts to manufacture of articles also stands concluded by the circulars of the Board set out above. Section 119(1) of the Act in clear terms provides that all authorities employed in the execution of the Act are duty bound to observe and follow the orders, instructions and directions of the Board. It is well settled that the circulars issued by the Board are binding on the officers and persons employed in the execution of the Act, more so the circulars beneficial to the assessee which tone down the rigour of the law. The benefit of such circulars is available to the assessee even though the circulars might have deviated from the strict tenor of the statutory provision and mitigated the rigour of the law. In view of the binding nature of the circulars, it is not open to the Revenue to raise a contention which is contrary to the circulars and instructions issued by the Board. In that view of the matter also, the assessee in the present case is entitled to relief under Section 80J of the Act.

11. In the premises, we are of the clear opinion that the Tribunal was justified in taking the view that the letter dated December 2, 1974, of the Central Board of Direct Taxes constituted instruction binding on the Income-tax Officer. On the merits of the claim of the assessee under Section 80J of the Act also, we are of the opinion that the Tribunal was right in law in holding that the undertaking of the assessee constituted an industrial undertaking within the meaning of Section 80J(4) of the Act and that the assessee was entitled to claim deduction under Section 80J of the Act in respect of the income from that undertaking.

12. Accordingly, we answer question No. 1 in the negative, i.e., in favour of the assessee and against the Revenue. Question No. 2 is answered in the affirmative and in favour of the assessee and against the Revenue.

13. This reference is disposed of accordingly with no order as to costs.