* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

\+ **I.T.A. Nos.740, 741, 755, 759 and 915/2007**

Date of Hearing: 13.08.2009

% Date of Decision: 8 .09.2009

The Commissioner of Income Tax
Delhi-IXI .....Appellant

Through: Ms. Prem Lala Bansal

Versus

J.D. Farms .....Respondents

Through Dr. Rakesh Gupta with
Ms.Aarti Saini

CORAM :-
THE HON'BLE MR.JUSTICE A.K.SIKRI
THE HON'BLE MR. JUSTICE VALMIKI J. MEHTA

1. Whether Reporters of Local papers may be allowed to see the Judgment?
2. To be referred to the Reporter or not?
3. Whether the judgment should be reported in the Digest?

A.K. SIKRI, J.

1. In all these appeals the respondent/assessee is same, namely, M/s. J.D. Farms. It is in the business of poultry farming and the question is as to whether the business activity can be treated as manufacturing activity thereby giving the benefit of deductions under Section 80 HHA and 80-I of the Income Tax Act (in short 'the Act') to the assessee. For the sake

of convenience we shall take note of the facts from ITA No.740/2007. The assessee had filed return declaring income at Rs.3,80,234/- for the assessment year 1998-99. This return was filed on 30.10.1998 in which the assessee had also claimed deduction under Section 80 HHA and 80-I of the Act claiming itself to be an industrial undertaking. Assessment was made. However, thereafter action under Section 147 of the Act was initiated against the assessee with reasons recorded vide order-sheet entry dated 17.4.2002. The basic reason was that the assessee was not an industrial undertaking as it was not having any manufacturing unit and was, thus, not entitled to deductions under Sections 80 HHA and 80-I of the Act.

2. As per the Assessing Officer, the deduction under Section 80 HHA is allowed only to the newly established small scale industrial undertakings which are engaged in the manufacturing and production of articles in rural areas. The deduction under Section 80-I on the other hand is allowed to newly established industrial undertakings. One of the necessary conditions to be fulfilled by the assessee in order to become eligible for deductions under Section 80 HHA and 80-I is that it should produce or manufacture any article or thing. In the reasons recorded for initiating action under Section 147 of the Act,

recorded vide order sheet entry dated 17.4.2002, it was recorded that "In the returns filed by the assessee for the assessment year 1996-97 to 2000-01, it has claimed deduction under Section 80 HHA and 80-I, thus, claiming to be an industrial undertaking. However, in the case of ***Indian Poultry*** **v.** ***CIT,*** (1998) 230 ITR 909, 911 (MP), the High Court held that the business of rearing chicks to broilers did not amount to manufacturing, even though the assessee used scientific methods in the process of rearing chicks. Hence, the assessee, carrying on the business of rearing chicks, is not entitled to any deduction under Section 80-I and 80HHA. Accordingly, noticed dated 22.4.2002 under Section 148 of the Act was served upon the assessee followed by detailed questionnaire dated 14.8.2002 along with notice dated 142(1) dated 14.8.2002.

3. The assessee claimed that business of poultry farming carried by the assessee amounted to manufacturing activity. The Assessing Officer did not agree with this argument of the assessee and passed detailed assessment order disallowing the deductions of Rs.1,38,267/- claimed under Section 80HHA and Rs.1,72,833/- claimed under Section 80-I and added these amounts to the returned income. The assessee filed appeal against the aforesaid orders of the Assessing Officer. This

appeal was dismissed by the CIT(A) vide orders dated 19.3.2004. Still dissatisfied, the assessee approached the Income-Tax Appellate Tribunal (in short the 'ITAT') against the aforesaid orders of the CIT(A). Similar issue raised in the other appeals, the ITAT consolidated all these appeals and have passed orders dated 17.11.2006 allowing these appeals partly. It is the department who feels aggrieved and has approached this Court under Section 260A of the Act by means of these appeals.

4. In this backdrop, the following question of law has arisen for consideration in the present appeal:-

> "Whether the ITAT was correct in law in allowing deduction under Section 80 HHA and 80-I of the Act to the assessee holding that the activity carried on by the assessee amounted to producing or manufacturing of an Article or thing?

5. In order to determine as to whether the business activity of the assessee amounts to manufacturing activity or not, it would be apposite to find out the exact nature of the activity. It is claimed by the assessee, which is found factually correct, that the activity of the assessee is not limited to the poultry farming. The eggs are hatched, chickens are fed and reared and then chickens are being slaughtered

by using sophisticated machinery and undertaking several processes. Various meat products are produced such as edible chicken meat and meat products like boneless chickens, full legs, drumsticks, wings as well as Giblets like chicken liver and Gizzards also commonly known as Offal. According to the assessee, to increase the shelf life of these products, tenderness and moisture retention, chicken is treated with salt and polyphosphates during chilling. On this basis the assessee claimed that it does not simply cut dead chicken into several parts and sell the cut parts. This process involves hard labour and scientific measures. Dressing, rearing, de-feathering, de-veining and de-boning is a human art and labour which makes the product consumable after preserving and packing it with the aid of machines. The question is whether the aforesaid process would make it a manufacturing process.

6. In the case of hatcheries itself, the question has come up for consideration before the Supreme Court and other Courts on number of occasions. We would, therefore, like to take note of those cases which would throw light on the principles to be applied in the instant case. The basic judgment is that of Supreme Court in the case of ***CIT*** v. ***Venkateshwara Hatcheries (P) Ltd. and other***, 237 ITR 174. In that case the question was as to whether the business of hatcheries run by

the assessee comes within the meaning of expression "manufacturing or produce articles or things" occurring in Sections 32A(2)(iii) or 80J(4)(iii) of the Act and consequently, whether the assessee was an "industrial undertaking". The Revenue had taken four arguments, namely:-

> "The first contention on behalf of the Revenue is that chicks, being animate creatures, cannot be termed as articles or things within the meaning of section 32A(2)(iii) or section 80J4(iii) of the Act. The second contention is that even if a chick could be construed as a article or thing it cannot be said that the assessee is producing chicks, that being a natural process of the development of the eggs. The third contention is that if the dictionary meaning of the word "articles or things" conveys different meaning, in that event the said words have to be interpreted in the context of the provisions of the Act, and regard must also be had to the legislative history of the provisions of the Act and the scheme of the Act and the fourth submission is that the assessee is not an industrial undertaking."

7. On the other hand, argument of the assessee was that hatching of eggs comes within the meaning of expression "production of an article or thing". It was emphasized that chickens were produced by mechanical process and therefore, the assessee was producing articles or things. Argument was also raised that better and larger numbers of chickens

are not possible by conventional method and therefore, for the larger growth of eggs and chicks, which was necessary for incubation, had to be mechanical as the broody hens are now virtually unobtainable from the commercial world. The Supreme Court refused to accept the aforesaid contentions of the assessee holding that the process did not amount to production of any article or manufacturing process. The relevant portion of the judgment of the Supreme Court reads as under:-

> "From a perusal of the self-stated steps taken by the assessee for the alleged production of chicks it is clear that the assessee does not contribute to the formation of chicks. The formation of chicks is a natural and biological process over which the assessee has no hand or control. In fact, what the assessee is doing is to help the natural or biological process of giving birth to chicks. The chicks otherwise can also be produced by conventional or natural method and in that process also, the same time is taken when the chicks come out from the eggs. What the assessee by application of mechanical process does in the hatchery is to preserve and protect the eggs at a particular temperature. But the coming out of chicks from the eggs is an event of nature. The only difference seems to be that, by application of mechanical methods, the mortality rate of chicks is less and the assessee may get chicks more in number. This, however, would not mean that the assessee produces chicks and that chicks are "articles or things." We are, therefore, of the opinion that the assessee is neither an industrial undertaking nor does the business of hatchery carried out by the assessee fall within the meaning of section 32A and section 80J of the

Act."

8. On an earlier occasion similar view was taken by the Madhya Pradesh High Court in ***Indian Poultry* v. *Commissioner of Income-Tax***, 230 ITR 909. The assessee company in that case was carrying on business of rearing chicks to broiler by applying scientific process and technology. It claimed deductions under Section 80HH and 80-I of the Act. The question was answered in the following manner holding that the aforesaid process did not amount to manufacture:-

> "Suffice it to say that the process which is involved in development of chicks into broilers is nothing but basically the chicks remain chicks only. There is no substantial change so as to acquire new commercial identity. Chicks are smaller ones and when they are reared for some time, they develop suitably for table purposes. Therefore, there is no change of the substance.
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> In this connection, two decisions of the Supreme Court of America may be referred to: (1) *East Texas Motor Freight Lines* v. *Frozen Food Express* (100 L. Ed. 917) and (2) *Anheuser Busch Brewing Association* v. *United States* (52 L. Ed. 336-338). Both these decisions of the Supreme Court of America have been approved by the Supreme Court of India also.
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> It is true that even if the chicks which develop into broilers and they are dressed and sold in the market, they still continue to be chicks only. Therefore, there is no substantial change in the matter. "Manufacture" implies a change, but

every change is not manufacture and yet every change in an article is the result of treatment, labour and manipulation and does not necessarily mean that on account of certain treatment and manipulation, a new identity has come to be acquired.

It the present case, the chicks are only reared for a few days and they are developed; thereafter they become broilers. Therefore, even after rearing, they remain chicks only."

9. This judgment was affirmed by the Supreme Court in ***Indian Poultry* v. *Commissioner of Income-Tax***, 250 ITR 664. By that time view had already been taken by the Supreme Court in ***Venkateshwara Hatcheries (P) Ltd.*** (supra) and the Court held that the matter was covered by the said judgment as is clear from the following:-

> "It is not in dispute that the case is covered against the assessee by the judgment of this court in *CIT* v. *Venkateswara Hacheries P. Ltd.* [1999] 237 ITR 174. The further point that was made by the assessee was that it not only reared the chicken but also dressed them for sale in the market and, therefore, a process of manufacture was carried out. But, it appears that there was no material laid before the Tribunal in this behalf. It is, therefore, not possible to conclude in the present matter that the dressing of poultry is tantamount to manufacture."

10. Another judgment which would of relevance and was strongly relied upon by the learned counsel for the Revenue is again the judgment of

the Supreme Court in ***Commissioner of Income-Tax*** **v.** ***Relish Foods***, 237 ITR 59. In that case the activity of the assessee therein included buying shrimps, peeling them and freezing them. The Supreme Court held that it did not involve any production or manufacture. We may, however, hasten to add that while doing so the Supreme Court had commented that there was no other material on record which could indicate a to what was done by the assessee and how it was done and in the absence of such material the aforesaid view was taken. However, at the same time the Court took note of its judgment in *Sterling Foods* v. *State of Karnataka*, [1986] 63 STC 239, wherein also it was held that process of frozen shrimps and prawns would not amount to manufacturing activity. Following portion of that judgment, in this behalf, is worthy of reproduction:-

> "Apart therefrom, there is the judgment of this court in *Sterling Foods* v. *State of Karnataka* [1986] 63 STC 239, where it has been held that the processed or frozen shrimps and prawns are commercially regarded as the same commodity as raw shrimps and prawns. When raw shrimps and prawns are subjected to the process of cutting of heads and tails, peeling, deveining, cleaning and freezing they do not cease to be shrimps and difference between raw shrimps and prawns and processed or frozen shrimps and prawns. In common parlance they remain known as shrimps and prawns. This judgment in *Sterling Food's* case [1986] 63 STC 239 (SC), has been

rightly applied by the Bombay High Court, in the case of *CIT* v. *Sterling Foods (Goa)* [1995] 213 ITR 851, to a claim under section 80HH of the Income-tax Act and it has been held that the activity of processing of prawns is not an activity of manufacture or production."

11. It is clear from the aforesaid judgments that in cases where the business concerns the livestock (chicks or prawns or shrimps etc.) normal rule is that the process of treating these livestock by itself would not be treated as manufacturing activity or production of an article. By applying mechanical process the mortality rate of such livestock is diminished or the biological process is smoothened, but that would not mean that some different articles or things have been produced. For this reason only, hatching of eggs by the application of mechanical methods is not treated as manufacturing activity. Likewise, development of chicks into broilers is also not treated as manufacturing activity as basically the chicks remain chicks only. It is for this reason even when the shrimps are processed or frozen to add commercial value thereto, it is not regarded as an activity of manufacturing or production. So much so even when this process includes cutting of heads and tails, peeling, deveining, cleaning and freezing, that would not make any difference as shrimps or prawns "do

not cease to be shrimps or prawns and become other distinct commodity."

12. Notwithstanding above principle laid down by the Supreme Court in the judgments noted above, learned counsel for the assessee tried to argue that the assessee is producing various meat products such as edible chicken meat and meat products like boneless chicks, full legs, drumsticks, wings as well as giblets like chicken liver and gizzards and therefore, it should not be treated as manufacturing process. According to him, process involves hard labour and scientific measure inasmuch as dressing, rearing, defeathering, deveining and deboning is a human art and labour which makes the product consumable after preserving and packing it with the aid of machines.

13. In so far as process of dressing, rearing, defeathering, deboning etc., is concerned, it would not make any difference in view of what is held by the Supreme Court in ***Relish Foods*** (supra) following its earlier judgment in ***Sterling Foods*** (supra). The only other difference is that the assessee is selling chickens in different forms, namely, boneless chickens or drumsticks or wings etc. That only means cutting the chicks into different parts and then selling those parts. However, if one is to keep in mind the ratio of the aforesaid judgments, even then the

answer has to be that it remains chicken and only different parts of the chicken are sold.

14. We are, therefore, of the opinion that the process undertaken by the assessee would not come within the meaning of expression "production of an article or thing." The Income-Tax Appellate Tribunal wrongly distinguished the judgment of the Supreme Court in ***Venkateshwara Hatcheries (P) Ltd.*** (supra). Thus, we answer the question in favour of the Revenue and against the assessee. This appeal is accordingly allowed and setting aside the orders of the Tribunal we restore the assessment order passed by the AO in this behalf. There shall be no orders as to costs.

(A.K. SIKRI)
JUDGE

(VALMIKI J. MEHTA)
JUDGE

September 8, 2009
hp.

- Review Petition 469/09 against order dt. 8.9.09