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

\+ **ITA No.531/2011**

**Date of Order: 08.08.2011**

**The Commissioner of Income Tax …… Appellant**

Through: Ms. Rashmi Chopra, Advocate

Versus

**Tata Communications Internet Services Ltd. …… Respondent**

Through: Mr.Prakash Kumar with Mr. Vikas Dhawan, Advocates

**CORAM:**
**HON'BLE MR. JUSTICE A.K. SIKRI**
**HON'BLE MR. JUSTICE M.L. MEHTA**

**M.L. MEHTA, J. (Oral)**

1. Admit on the following substantial questions of law:

*"(a) Whether on the facts and in the circumstances of the case, the ITAT erred in law and on merits in holding that the assesse was entitled to deduction under Section 801A of the Income Tax Act, 1961 on income from internet services and internet telephon?*

*(b)Whether the ITAT erred in law and on merits in holding that deduction under Section 80IA of the Income Tax Act, 1961 cannot be denied after having been granted in the 1st year of claim?"*

2. With the consent of the counsel of parties, we have heard the matter finally.

3. This is an appeal preferred by Commissioner of Income Tax (CIT) against the order dated 26.2.2010 passed by learned Income Tax Appellate Tribunal ("the Tribunal" for short) whereby the Tribunal set aside the decision of CIT(A) and allowed the appeal of the Assessee allowing deductions under Section 80 IA of the Income Tax Act ("the Act" for short) for the assessment year 2006-07 holding inter alia that the Revenue cannot decline deduction for subsequent year for alleged violation of Section 80 IA(3) of the Act. Claiming of deduction under Section 80IA of the Act can only be considered for the year of formulation of business. The Tribunal also held that the provisions of Section 80IA (4) (i) to Section 80IA (3) of the Act will not apply to the business of the assessee which was formulated and/or commenced prior to the assessment year 2004-05.

4. The Assessee company which was incorporated under the name of C.G. Graphnet Pvt. Limited which was engaged in the business of providing telecommunication services and on 15.11.1996, its name was changed to CG Fax Mail Ltd and the company was converted into a public limited company on 23.09.1997. The Company was acquired by Direct Internet Limited in August, 2000 and its name was changed to Primus Telecommunications Limited with effect from 27.9.2000. The company was stated to be in the business of providing fax mail services. The Department of Telecommunication granted license to the assessee company on 5.01.1999 for carrying of business activities for Internet Services and Internet Telephony

Services from October, 2000. As per the license issued on 5.1.1999, with effect from October, 2000, the company started two new services viz. Internet Services and Internet Telephony Services. Thereafter, this license was updated as the internet services and internet telephony services provider from 2002. The business of Fax and Email services which were being carried out earlier were discontinued and in the financial year 2003-04 the company was solely carrying on the business of internet service provider and internet telephony services. The assessee had claimed that since the first invoice was cut on 17.10.2000 and it filed income tax regularly and as per the provisions of Section 80IA(4) of the Act, it was entitled to deduction right from the assessment year 2001-02. It was claimed that as per the provisions of 80IA(2), the assessee could claim deduction under Section 80IA(4) for 10 years out of 15 years starting from the year in which the assessee started its business being assessment year 2001-02. Since the assessee had not claimed deduction under Section 80IA (4) of the Act for the assessment year 2001-02, 2002-03 and 2003-04 and the first year of claim under section 80IA (4) was 2004-05 and as it had been granted deduction under Sections 80IA(4) of the Act for the assessment year 2004-05 and 2005-06, it was entitled to deduction for the relevant assessment year i.e. 2006-07.

5. The AO has rejected the claim of assessee for deduction of Rs.11,12,41,929/- under Section 80IA of the Act. While rejecting the claim for deduction, the AO has reasoned as under:

> *"7.The perusal of the record reveals that originally the license agreement was granted initially for a period of 15 years to M/s CG Faxmail Limited. Another license agreement was executed*

*on 19 April, 2002 which was issued in the name of Primus Telecommunication India Limited which was already in existence. There was only change of name of company from M/s CG Faxmail Limited to Telecommunication India Limited on 27.9.2000 as per certificate of the ROC. It clearly establishes that a company was already in existence in 1999 also. Therefore, it is not a new business but has been formed by continuing the business- the old business with the old assets. According to Section 80IA (3) such undertaking should not be formed by splitting up, or the reconstruction of business already in existence (ii) it should not be formed by a transfer to a new business of machinery or plant previously used for any purposes. The balance sheet for the assessment years 2003-04 and the details furnished in respect of fixed assets, I is evident that old machinery has been used meaning thereby that all the old machinery which was used by the assessee previously has been carried forward. In view of these facts, the assessee has not fulfilled the conditions laid down in section 80IA (3), hence the claim of the assessee under section 80IA is denied.*

*8. The assessee also claims that the deduction under Section 80IA was allowed in the earlier asstt years. So it should be allowed for the asstt year under consideration, is not tenable. I have perused the asstt record for the asstt year 2005-06. Nothing has been discussed in the said order about merit of the claim regarding deduction u/s 80IA. Simply deduction u/s 80IA has been allowed in computation of income. It appears that deduction u/s 80IA was allowed without examining the factual aspects as well as the legal requirements stipulated in section 80IA.* ***It is settled law that if an issue legal or factual is not examined and no quasi judicial adjudication is made thereon, it cannot be said that the same creates a precedent to be followed for all time to come on the fallacious ground of consistency. The law of consistency as elucidated by the Apex Court in Radha Soami Satsang vs. Commissioner of Income Tax 193 ITR 0321 clearly underlines that though each assessment year being a unit an what was decided in one year might not apply in the following year but "where a***

***fundamental aspect permeating through the different assessment years has been found as a fact one way or the other and parties have allowed that position to be sustained by not challenging the order, it would not be at all appropriate to allow the position to be changed in a subsequent year".***

*9. What emerges from the above legal proposition is that to apply the rule of consistency, the issue must have been* ***"found as a fact one way or other".*** *But where no enquiry is conducted into the veracity of a contention, and an assessment order is framed without going into the various aspects- legal or factual- on the basis, it cannot be said the issue "has been found as a fact" so as to invoke the law of consistency. Thus, the contention of the assessee that the issue of deduction u/s 80IA stands duly examined and allowed in earlier asstt years is not tenable. I reject the same accordingly.*

*9.1 Coming to the legal requirements, it may be appreciated that deduction u/s 80IA is available only to an undertaking i.e. an undertaking which is not formed by splitting up or the reconstruction of a business already in existence.*

*Accordingly, it is held that the deduction u/s 80IA claimed by the assessee is hit by the mischief of provisions of section 80IA(3) (ii)."*

6. The assessee went in appeal before the CIT(A) which dismissed the appeal holding that the assessee had violated the restrictive condition as laid down under Section 80IA(3) of the Act. The CIT(A) also rejected the contentions of the assessee that since it was a providing telecommunication services it was eligible for deduction under Section 80IA; the provisions of section 80IA(3) are not applicable since the business of telecommunication services was commenced prior to 1.4.2004; the change of ownership does not affect the claim of relief under Section 80IA and the assessee was entitled to

deduction on the principle of rule of consistency for having been allowed deduction for the assessment year 2004-05 and 2005-06 under Section 143(3).

7. The matter was taken in appeal by the assessee to the Tribunal which allowed the appeal and allowed the deductions as claimed by the assessee. The department is in appeal against the impugned order of the Tribunal.

8. It was submitted before us by the learned counsel for the assessee that section 80IA(3) was not applicable inasmuch as the case of the assessee falls within the ambit of section 80IA(4)(ii) of the Act. In this regard, it was submitted that the provisions of section 80IA(3) had been amended with effect from 1.4.2005 by the Finance Act (I)) of 2004 whereby Clause(ii) of sub section (4) of the Act had been brought within the ambit of Section 80-IA. In other words, the claim was that till 1.4.2005 the provisions of Section 80IA(3) of the Act did not apply to the provisions of Section 80IA (4)(ii) of the Act. In this regard reliance was also placed upon the Circular No.5 of 2005 dated 15.7.2005 of CBDT wherein it was clearly mentioned that if an undertaking is formed by transfer of old plants and machinery or asking for reconstruction of existing business, but has started providing telecommunication services prior to 1.4.2004, it would continue to get tax benefit under Section 80IA of the Act and that the amendment takes effect from 1.4.2005 as applied in relation to assessment year 2005-06 and subsequent assessment years. Referring to the agreement dated 5.1.1999 and dated 19.4.2002, the learned counsel for the assessee submitted that the agreement dated 19.4.2002 did not result into new business being started. He also drew our attention to the copy of the notice issued by the AO for

assessment year 2005-06 dated 25.9.2007 for the purpose of assessment under Section 143(3) wherein in Clause 19 of the said notice, the assessee had been asked to substantiate with documentary evidence its claim of deduction under Section 80IA and also reply of the assessee dated 5.12.2007 wherein this issue had been clarified. It was urged that the assessee had started its new business of fax and email right from the financial year 2003-04 and had incurred expenditure of Rs. 2.65 crores in relation to its business of internet services and internet telephony.

9. On the other hand, it was submitted by learned counsel for the revenue that the company was incorporated in 1994 and the assessee had itself in the case of assessment for the year 2003-04 confirmed that the business of the assessee was started in 1997. He submitted that the assessee had been originally in the business of fax and email services and in October 2000 it had ventured into the new business of internet services by entering into the agreement with DOT on 5.1.1999. It was submitted that vide an agreement dated 19.4.2002, the assessee had started another business of internet telephony and accordingly it had three lines of business being fax and email started in 1997, internet services started in 2000 and telephony services were started in 2002. Based on this, it was submitted that the internet and telephony services being a new business were formed on splitting up and reconstruction of business of fax and email already being done by the assessee and the plant and machinery of the whole business was used by it for the new business. Based on this premise, it was submitted that the provisions of Section 80IA (3) of the Act were applicable and consequently the assessee was not entitled to the benefit of deduction under Section 80IA. With regard to the plea of

consistency based on the assessment year 2004-05 and 2005-06 whereby all such deductions were allowed, it was submitted that the AO had not considered different incomes from the fax and email and from internet services and internet telephony for the assessment year 2004-05 and 2005-06 and that cannot be utilized for all time deductions under Section 80IA.

10. There is no dispute with regard to the fact that Clause (ii) of the Section 80IA (4) was inserted in Section 80IA (3) by the Finance Act II of 2004 with effect from 1.4.2005 and that this was not with retrospective effect. It became applicable only after its insertion with effect from 1.4.2005. The Circular issued by DBDT explaining the provisions of Finance Act II of 2004 testifies the fact that this insertion took effect from 1.4.2005 and is to apply in relation to the assessment year 2005-06 and subsequent years. The first claim of the assessee for deduction under Section 80IA indisputably was for assessment year 2004-05. The Tribunal has rightly recorded that the business of fax and email has been started by the assessee in 1997 and the business of providing internet services during the year 2000 being from 17.10.2000, the relevant assessment year 2001-02. The question for consideration would be as to whether there was any violation of provisions in the claim of deduction under Section 80IA(4) (ii) of the Act for assessment year 2001-02 or at the maximum for the first year of deduction under Section 80IA being the assessment year 2004-05. Admittedly, the assessee was granted deduction under Section 80IA for the assessment year 2004-05. The Tribunal was right in holding that the revenue could not pick up the assessment year granting claim holding that there was violation of provisions of Section 80IA(3) on the ground that the business was formed by splitting up and reconstruction of

business already in existence or that it was formed by transfer of plants and machinery to the new business. The bar as provided under Section 80IA(3) is to be considered only for the first year of claim for deduction under Section 80IA. Once the assessee is able to show that it has used new plants and machinery which has not been previously used for any purpose and the new undertaking is not formed by splitting up or reconstruction of business already in existence, it is entitled to the deduction under Section 80IA for subsequent years. Since the assessee had been granted claim of deduction right from the assessment year 2004-05 under Section 80IA, consequently it cannot be denied deduction for the subsequent years inasmuch as restrain of Section 80IA(3) cannot be considered for every year of claim of deduction, but can be considered only in the year of formation of the business.

11. Be that as it may, Clause (ii) of Section 4 of Section 80IA was inserted in sub clause 3 of Section 80IA with effect from 1.4.2005 and the business of the assessee had been formed and started much prior to that. The restriction placed by Section 80IA(3) to the provisions of 80IA(4) (ii) would not bar the assessee for continuing its claim of deduction under Section 80IA. Since the provisions of 80IA(3) are not applicable to the present assessee, it having commenced its business much prior to 1.4.2005, Section 80IA(3) would not disentitle it from claiming deduction under Section 80IA on its income from internet services and internet telephony services.

12. In our view, the Tribunal was right in holding that the assessee could not be said to have been formed by splitting up or reconstruction of the business already in existence as its business had commenced after 1.4.1995

and before 31.3.2005 and the assessee had started its business of fax and email services right from the financial year 2003 and 2005 and it continued to carry on the business of internet telephony.

13. Insofar as the objection of the revenue that there had been change in the name of pattern of shareholding it does not make any difference as it is a well settled rule of law that benefit under Section 80IA of the Act is available to an undertaking and not to the assessee since the undertaking continues to carrying on its business without any reconstruction of business already in existence.

14. Even otherwise, on merits the conditions under Section 80IA(3) of the Act are seen to be fully met by the assessee and on this ground also the assessee is entitled for deduction under Section 80IA of the Act. The first contention is that section 80IA(3) of the Act provides that the eligible business is not formed by splitting up or reconstruction of the business already in existence. Based on the facts discussed above, it may be noticed that the assessee started its new business in the existing company and the said business could not be said to have been formed either by splitting up or reconstruction of the existing business. It is to be noted herein that the business of providing internet services was awarded by the government to the assessee in the year 1999. The second contention of applicability of section 80IA (3) regarding use of old plants and machinery is also not relevant in the case of the present assessee as the business of assessee had not come into existence or formed by transfer of any old plants and machinery. The license was granted to the assessee on 5.1.1999 and it purchased new plants and

machinery worth Rs. 5.65 crore during the financial year 2000-01 for this telecommunication business.

15. Reliance is placed on the case of ***The Commissioner of Income Tax*** **v** ***Mahaan Foods Ltd.*** [(2008)216 CTR (Del) 148 of this Court wherein this Court observed as under:

> *"10. The term "**splitting up of the business already in existence**" indicates a case where the integrity of a business earlier in existence is broken up and different sections of the activities previously conducted are carried on independently. [**CIT v. Hindustan General Industries Ltd. [1982] 137 ITR 851 (Delhi**)].*
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> *11. As observed by Supreme Court in **Textile Machinery v. CIT [1997] 107 ITR 19(SC), "**The term **'reconstruction'** implies that the identity of the business should not be lost, and substantially the same business should be carried on by substantially the same person. 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".*
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> *12. As per findings of fact recorded by the Tribunal, it has been stated that "in the present case the old undertaking no longer existed and remained identifiable. It was completely submerged in the new industrial undertaking of the*

*assessee. The provisions of Section 80IA of the Act with reference to Explanation 2, do not require that new industrial undertaking should be raised on separate plot of land leaving the earlier undertaking totally untouched. We find that the processes for which the Assessee entered into technological collaborations with M/s Rotacom Industries, B.V., Netherlands and M/s Seppo Ralli OY, Finland were the key processes of the Assessee"s industrial undertaking and other processes such as storage of milk in stainless steel storage tanks, pre-warming, pre-heating, pasteurization were only of preparatory nature for the manufacturing of the product of the Assessee. The Assessee appears to have introduced almost entirely new manufacturing technology and processes."*

*13. The reconstruction of a business or an industrial undertaking must necessarily involve the concept that the original business or undertaking is not to cease functioning, and its identity is not to be set to be lost or abandoned. The concept essentially rests on changes but the changes must be constructive and not destructive. There must be something positive about the whole matter as opposed to negative. The underlying idea of a reconstruction evidently must be - and this is brought out by the section itself - of a 'business already in existence'. There must be a continuation of the activities and business of the same*

*industrial undertaking. The undertaking must continue to carry on the same business though in some altered or varied form. If the alteration and changes are substantial, there would be little scope for describing what emerges as a reconstruction of the business.* ***(See CIT v. Gaekwar Foam and Rubber Co. Ltd. [1959] 35 ITR 662 [Bom.]***

*14. From the perusal of Section 80-IA of the Act it is clear that the statute itself has envisaged and approved of a situation in which an old existing smaller industrial undertaking is absorbed by a new much bigger industrial undertaking."*

16. In view of our above discussion, we answer both the questions in negative i.e. in favour of the assessee and against the revenue. The appeal deserves no merit and is hereby dismissed.

**M.L. MEHTA**
**(JUDGE)**

**A.K. SIKRI**
**(JUDGE)**

August 08, 2011
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