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

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**INCOME TAX APPEAL NO.300/2011**

**Reserved on: 10<sup>th</sup> July, 2014**

**Date of decision: 18<sup>th</sup> July, 2014**

COMMISSIONER OF INCOME TAX ..... Appellant  
Through Mr. Kamal Sawhney, Sr.  
Standing Counsel with Mr. Sanjay Kumar, Jr.  
Standing Counsel.

versus

HEARTLAND DELHI TRANSCRIPTION SERVICES PVT LTD.  
..... Respondent  
Through Mr. P. Kapoor, Advocate with  
Mr. Anuj Dhir and Ms. Bina Gupta,  
Advocates.

**CORAM:**

**HON'BLE MR. JUSTICE SANJIV KHANNA**

**HON'BLE MR. JUSTICE V. KAMESWAR RAO**

**SANJIV KHANNA, J.:**

This appeal by the Revenue pertains to assessment year 2004-05 and relates to interpretation of Section 10B of the Income Tax Act, 1961 (Act, for short).

2. By order dated 11<sup>th</sup> May, 2011, the following substantial questions of law were framed:-

“(i) Whether ITAT was correct in law in allowing deduction u/s 10B of the Act to the assessee?”



(ii) Whether ITAT has correctly interpreted the provisions of Section 10B of the Act?”

2. The respondent is an assessee, who claims deduction/exemption under Section 10B of the Act in respect of an undertaking acquired from their sister concern M/s Heartland Information and Consultancy Services (P) Ltd. (HICS, for short). The said acquisition was made by the respondent-assessee from HICS in the period relevant to the assessment year 2002-03.

3. The Assessing Officer disallowed the claim for deduction under Section 10B observing that the assessee does not satisfy the requirement of sub-section (2) to Section 10B i.e. it was not formed by splitting up or reconstruction of business already in existence. Clause (iii) to Section 10B(2) was also relied upon to disallow the claim on the ground that the respondent assessee had not undertaken any new business and did not satisfy the requirement that the plant should not be used previously for any purpose. It was held that the respondent assessee had acquired computers from HICS, who had also claimed depreciation on the said asset before they were transferred to the respondent assessee. The assessment order mentions that for similar reasons, disallowance was made in the assessment years 2002-03 and 2003-04.

4. Commissioner of Income Tax (Appeals) reversed the opinion of



the Assessing Officer, following the first appellate order for t  
assessment year 2002-03. He observed that the undertaking eligible  
for deduction under Section 10B was setup by HICS after approval of  
Software Technology Park India (STPI) dated 8<sup>th</sup> July, 1999.  
Subsequently, this undertaking owned by HICS was transferred to the  
respondent assessee vide transfer agreement dated 14<sup>th</sup> February, 2001.  
The undertaking had not been setup by the respondent assessee, but  
was setup earlier by HICS and was transferred to the respondent  
assessee. In these circumstances, there was no violation of Section  
10B(2)(ii) or (iii) as the respondent assessee had entered into business  
transfer agreement dated 14<sup>th</sup> February, 2001 with HICS.  
Commissioner of Income Tax (Appeals) observed that there was no  
finding/observation that HICS had acquired or previously used  
machinery or equipments.

5. Revenue preferred appeals before the Income Tax Appellate  
Tribunal in respect of assessment years 2002-03 to 2004-05 as the  
respondent assessee had succeeded before the first appellate authority  
in the three years. The tribunal allowed the appeals of the Revenue in  
respect of assessment years 2002-03 and 2003-04 relying upon sub-  
section (9) to Section 10B. However, the appeal for the assessment  
year 2004-05 was dismissed observing that sub-section (9) to Section  
10B was omitted and was not applicable for the assessment year 2004-



05.

6. Before we examine the provisions of Section 10B of the Act, it would be relevant to note down the following admitted facts:-

(i) The respondent assessee was incorporated on 2<sup>nd</sup> August, 2000 and was engaged in “export” of digitised medical transcription.

(ii) The assessee had entered into an agreement dated 14<sup>th</sup> February, 2001 with HICS and purchased their entire business relating to medical transcription. HICS was a sister concern of the respondent assessee.

(iii) HICS had setup an undertaking on the basis of letter of intent issued by STPI in the assessment year 2000-01. The undertaking was setup/formed with new machinery and the undertaking when formed fulfilled the conditions and requirements of sub-section (2) to Section 10B.

(iii) It is not the case of the Revenue, nor was it pleaded or urged before the tribunal that the undertaking originally setup at the first instance by HICS, did not meet the eligibility norms or requirements of Section 10B(2).

7. Section 10B (1) and (2) of the Act as applicable, read:-

**“10B.** (1) Subject to the provisions of this section, a deduction of such profits and gains as are derived by a hundred per cent export-oriented undertaking from the export of articles or things or computer software for a period of ten consecutive assessment years beginning with the assessment year relevant to the previous year in which the undertaking begins to manufacture or produce articles or things or



computer software, as the case may be, shall be allowed from the total income of the assessee :

**Provided** that where in computing the total income of the undertaking for any assessment year, its profits and gains had not been included by application of the provisions of this section as it stood immediately before its substitution by the Finance Act, 2000, the undertaking shall be entitled to the deduction referred to in this sub-section only for the unexpired period of aforesaid ten consecutive assessment years :

[**Provided [further]** that for the assessment year beginning on the 1st day of April, 2003, the deduction under this sub-section shall be ninety per cent of the profits and gains derived by an undertaking from the export of such articles or things or computer software:]

**Provided also** that no deduction under this section shall be allowed to any undertaking for the assessment year beginning on the 1st day of April, [2012] and subsequent years :

**Provided also** that no deduction under this section shall be allowed to an assessee who does not furnish a return of his income on or before the due date specified under sub-section (1) of section 139.

(2) This section applies to any undertaking which fulfils all the following conditions, namely :—

- (i) it manufactures or produces any articles or things or computer software;
- (ii) it is not formed by the splitting up, or the reconstruction, of a business already in existence :

**Provided** that this condition shall not apply in respect of any undertaking which is formed as a result of the re-establishment, reconstruction or revival by the assessee of the business of any such undertaking as is referred to in section 33B, in the circumstances and within the period specified in that section ;

- (iii) it is not formed by the transfer to a new business of machinery or plant previously used for any purpose.

*Explanation.*—The provisions of *Explanation 1* and *Explanation 2* to sub-section (2) of section



80-I shall apply for the purposes of clause (iii) of this sub-section as they apply for the purposes of clause (ii) of that sub-section.

8. Sub-section (1) to Section 10B stipulates that deduction under the said section would be available in respect of profit and gains derived by a hundred per cent export-oriented undertaking for a period of 10 consecutive years, which will begin with the assessment year in which the undertaking begins to manufacture or produce articles, things or computer software. Profit and gains of the said undertaking shall be reduced or deducted from the total income of the assessee i.e. the income earned by the proprietor or owner of the eligible undertaking. Sub-section (2) to Section 10B stipulates that the undertaking must fulfil the requirements stipulated therein. Clause (ii) states that the undertaking should not be formed by splitting up or reconstruction of business already in existence. The proviso is also relevant and states that the condition in clause (ii) would not apply if the undertaking is formed as a result of re-establishment, reconstruction or revival of business by the assessee as stipulated in Section 33B in the circumstances and the period specified.

9. Clause (iii) to Section 10A is a negative covenant, which stipulates that undertaking should not be formed by transferring old plant and machinery i.e. plant and machinery, which is previously,



used to a new business, i.e., the undertaking which is formed. The said embargo or prohibition relates to the initial formation or setting up of the undertaking. Thus, the undertaking should not be formed by transfer of plant and machinery, which was previously used for any purpose. Explanation to sub-section (2) makes explanation (1) and (2) to sub-section (2) to Section 80I applicable to clause (iii). Explanation 1 to Section 80I(2) deals with plant and machinery, which was used outside India and the same is not to be regarded as plant and machinery previously used for any purpose, subject to stipulations. Explanation 2 to Section 80I (2) states that the total value of the old plant and machinery or the parts should not exceed 20% of the total value of the plant and machinery for the purpose of clause (ii) to Section 80I(2). The said stipulation will equally govern and is applicable to Section 10B. [For the purpose of present appeal, we need not decide the question whether the stipulation in explanation 2 to Section 80I(2) as applicable to Section 10B, would be applicable at the stage of initial formation or would be even applicable thereafter/subsequently and has to be examined in each assessment year. The said issue does not arise for consideration in the present appeal].

10. Sub-section (1) refers to deduction of profit and gains of an undertaking. The deduction is to be allowed for a period of 10 years from the year in which undertaking begins to manufacture, produce etc.



articles, things or computer software. The beginning and end point for claiming the deduction are stipulated. These have reference to the eligible undertaking. Sub-clause (ii) to Section 10B(2) incorporates a negative condition and states that the undertaking must not be formed by splitting up or reconstruction of business already in existence. Clause (ii) refers to the date on which the undertaking mentioned in sub-section (1) is created or formed. On the date of formation, the undertaking should not violate the condition stipulated in clause (ii) i.e. that it should not be created by splitting up or reconstruction of a business already in existence. Clause (ii) does not have any reference to the period of 10 years stipulated in sub-section (1) to Section 10B, after an undertaking is formed or created without violation of clause (ii) to Section 10B(2). Clause (ii) to Section 10B(2) does not apply to the period, post formation of the undertaking, covered under sub-section (1), when the undertaking which at the time of formation meets the requirements of clause (ii) to Section 10B(2). The undertaking, of course meet the requirements and fulfil the condition that it manufactures or produces articles, things or computer software during the assessment year. The proviso equally supports the said interpretation as it also refers to the date of formation of the undertaking, for seeking benefit under Section 10B(1). The requirements under clauses (ii) and (iii) in this manner do not relate to



the subsequent period, i.e. post or after formation.

11. We have already noted the factual position. It is an accepted and admitted fact that the undertaking was formed or created by HICS and there is no allegation or finding by the Assessing Officer that on the date of formation of the undertaking, there was violation of clause (ii) and (iii) to Section 10B(2). The undertaking, when it was formed, satisfied and duly fulfilled the requirements of the said clauses, as it was not formed by splitting up or reconstruction of a business already in existence. It was a new undertaking and there is no factual finding that at the time or establishment or formation of the undertaking, business already in existence was splitted or reconstructed. It is accepted that the plant and machinery procured at the time of formation was new.

12. The next question, which arises for consideration, is whether there is any bar or prohibition in Section 10B on transfer or sale of the undertaking by the assessee, who has formed or established the same, to another assessee and whether the purchaser/acquirer assessee can be denied benefit under Section 10B of the Act. Before we answer this question, one clarification is required. Sub-section (1) to Section 10B stipulates the tax holiday period as 10 years, which should be continuous/consecutive and begins from the assessment year relevant to the previous year in which the undertaking begins to manufacture or



produce articles, things or computer software. Thus, the period of years is with reference to the undertaking and transfer or change of undertaking will not alter or increase the tax holiday period of 10 years. The same is fixed with reference to the date on which the production or manufacture begins.

13. Sub-section (9) to Section 10B before it was deleted/omitted with effect from 1<sup>st</sup> April, 2004 by the Finance Act, 2003 used to read as under:-

“(9) Where during any previous year, the ownership or the beneficial interest in the undertaking is transferred by any means, the deduction under sub-section (1) shall not be allowed to the assessee for the assessment year relevant to such previous year and the subsequent years.”

14. Before we interpret the aforesaid section, the effect thereof and why and how it was omitted, we would also like to reproduce sub section (9A) to Section 10B, which was inserted by the Finance Act, 2002 with effect from 1<sup>st</sup> April, 2003, but was deleted/omitted by the Finance Act, 2003 with effect from 1<sup>st</sup> April, 2004. Sub-section (9A) used to read:-

“(9A) Notwithstanding anything contained in sub-section (9), where as a result of reorganisation of business, a firm or a sole proprietary concern is succeeded by a company and the ownership or beneficial interest in the undertaking of the firm or the sole proprietary concern is transferred to the company, the deduction under sub-section (1) in



respect of such undertaking shall be allowed to the company, as the same would have been allowed to such firm or sole proprietary concern, as the case may be, if the reorganisation had not taken place :

**Provided** that, –

(a) in the case of a firm, the aggregate of the shareholding in the company of the partners of the firm is not less than fifty-one per cent of the total voting power in the company and their shareholding continues to be as such for the period for which the company is eligible for deduction under this section ;

(b) in the case of a sole proprietary concern, the shareholding of the sole proprietor in the company is not less than fifty-one per cent of the total voting power in the company and his shareholding continues to remain as such for the period for which the company is eligible for deduction under this section.

15. Another important amendment made with effect from 1<sup>st</sup> April, 2004 to Section 10B was insertion of sub-section (7A) with effect from 1<sup>st</sup> April, 2004 and the same reads:-

“(7A) Where any undertaking of an Indian company which is entitled to the deduction under this section is transferred, before the expiry of the period specified in this section, to another Indian company in a scheme of amalgamation or demerger –

(a) no deduction shall be admissible under this section to the amalgamating or the demerged company for the previous year in which the amalgamation or the demerger takes place; and

(b) the provisions of this section shall, as far as may be, apply to the amalgamated or resulting company as they would have applied to the



amalgamating or the demerged company if the amalgamation or demerger had not taken place.”

16. Omission/deletion of sub-section (9) with effect from 1<sup>st</sup> April, 2004 has made important and significant change. It altered and the negative stipulation on transfer was withdrawn. The said sub-section was a part of the section originally enacted by the Finance Act, 2000. Sub-section 9 stipulated that where ownership or beneficial interest in the undertaking was transferred by any means, the deduction under sub-section (1) would not be allowed to the assessee in the assessment year relevant to the said previous year i.e. the year of transfer and subsequent years. In other words, if there was change of ownership of the undertaking by any mode, benefit under Section 10B would not be available to the seller or transfer in the year of transfer or the new owner/beneficial owner in that year or subsequent years. Deletion of the said sub-section had the consequence of removing the specific negative covenant. Thus, for accounting period after 1<sup>st</sup> April, 2003, the aforesaid prohibition or bar was no longer applicable and ceased to operate. When we examine sub-section (9A), which was inserted by the Finance Act, 2002 and omitted after one year by the Finance Act, 2003 with effect from 1<sup>st</sup> April, 2004, it would indicate that the Legislature had noticed the ill effect of the prohibition casted in sub-section 9 and had partly modified and removed the bar in



specific/particular cases by the Finance Act, 2002 with effect from April, 2003. Sub-section 9A operated as an exception to absolute bar/prohibition created by sub-section 9. However, there was no need for sub-section (9A) to exist and remain in the statute, once the bar and prohibition under sub-section (9) was removed by the Finance Act, 2003 with effect from 1<sup>st</sup> April, 2004. Accordingly, sub-section 9A was omitted along with Section 9 at the same time.

17. The submission on behalf of the Revenue that in spite of removal and omission of sub-section (9), the bar and prohibition should be read or implied in view of insertion of sub-section (7A) to Section 10B is misconceived. Sub-section (7A) is an enabling provision and not a disabling provision. It deals with cases of amalgamation or demerger and stipulates that benefit will be allowed for the un-expired period when there is a transfer as a result of amalgamation or demerger. In case, the Legislature wanted to retain the prohibition contained in sub-section (9), it would have retained the said sub-section clear and categorical, and not omitted it. Sub-section (7A) would then have been a proviso and explanation to the prohibition in sub-section (9) like '(9A)'. Sub-section (9) would have then, if it had not been omitted, continued to apply to all other transfers by any mode other than the modes specified in sub-section (9A) or (7A). This was not the intention of the Legislature because sub-section (9) and (9A) to



Section 10B were deleted/omitted by Finance Act, 2003 with effect from 1<sup>st</sup> April, 2004. Sub-section (9A) applied to different factual matrix and situations, which may not be covered by sub-section (7A). If the reading of the Revenue is accepted, then by incorporating sub-section (7A) and omitting (9A), the Legislature had withdrawn the benefit under the latter section. This was obviously not the purpose or intent behind omission of sub-sections 9 and 9A. Sub-section (7A) as stated above is only an enabling provision and not a disabling provision. The present case is not a case of transfer by way of amalgamation or demerger.

18. The ratio and the view which we have taken finds support from the judgment of the Madras High Court in *Commissioner of Income Tax-I, Coimbatore Vs. Heartland KG Information Ltd.* [2013] 359 ITR 1 (Madras) and of Bombay High Court in *Commissioner of Income Tax Vs. Sonata Software Ltd.* [2012] 21 TAXMAN 23 (Bom.)

19. *Heartland KG Information Ltd.* (supra) is a case of sister concern of the respondent-assessee and the facts are almost identical. The assessee in the said case was entitled to benefit under Section 10A and it was held that the transfer did not attract the *pari materia* restriction and negative covenant under clauses (ii) and (iii) to Section 10A(2) as it was not a case of splitting up or reconstruction. It was a case of transfer of entire business or the undertaking itself as a whole.



In Section 10A there was no specific prohibition and implied bar | inference to adduce that transfer of entire business would be treated as hit by clauses (ii) and (iii) of Section 10A(2). The Madras High Court had relied upon decision of the Supreme Court in *Textile Machinery Corporation Limited, Calcutta versus Commissioner of Income Tax, West Bengal* (1977) 2 SCC 368 and Bombay High Court in *Sonata Software Limited* (supra).

20. This decision of the Madras High Court was subsequently followed in *Commissioner of Income Tax, Chennai versus Sri Renuga Textile Mills Limited* (2012) 26 TAXMAN 108 (Madras). The subsequent decision refers to Section 10B(2), clauses (ii) and (iii). Reference was made to CBDT Circular dated 13<sup>th</sup> December, 1963 stating that benefit under Section 84 would be available to the successor for remaining years. We shall refer to this circular subsequently.

21. *Sonata Software Limited* (supra) is more direct though this decision also related to Section 10A as it existed in the Assessment Year 1998-99. The stipulations in the applicable sub-section (2) to Section 10A were identical. It was held as under:-

“8. The issue before the Court is whether the two requirements, cast in negative terms, have been fulfilled. Clause (ii) of Sub-section (1) of Section 10A stipulates that the industrial undertaking must not be formed by splitting up or reconstruction of a



business already in existence. In other words, the test in law is as to whether the undertaking is formed by splitting up or reconstruction of a business already in existence. In *CIT v. Gaekwar Foam and Rubber Company Ltd.* (Supra) a Division Bench of this Court construed the provisions of Section 15C of the Income Tax Act, 1922, Section 15C(2)(i) contained a similar provision that the section would apply to an industrial undertaking which is not formed by the splitting up or the reconstruction of a business already in existence or by the transfer to a new business of building, machinery or plant used in a business which was being carried on before 1 April 1948. In that case, there was a partnership firm and its assets and goodwill were taken over by the assessee for a stated consideration and against the allotment of shares to the three partners in the assessee company. The Assessing Officer had rejected the claim of exemption under Section 15C on the ground that the assessee was formed by the reconstruction of the business already in existence. The Appellate Commissioner took a different view which was affirmed by the Tribunal. The Division Bench of this Court held that the reconstruction of a business connotes that the original business is not to cease functioning and the undertaking must continue to carry on the same business in an altered form. On the other hand if the ownership of a business or an undertaking is transferred that would not constitute a reconstruction. The Division Bench held as follows:

“...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 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 alterations and changes are substantial, there would be little scope for describing what emerges as a reconstruction of the business. Thus for instance if the ownership of a business or an undertaking changes hands not ostensibly but in reality and effectively, that would not be reconstruction or if the very nature of the business is changed, that again would not be reconstruction. On the other hand, reorganization of the business on sounder lines or alterations in the mode or method or scope of the activities of the business or in its personnel or infusion of new blood in the management or control of the business which may even be by some changes in the constitution of persons interested in the undertaking would certainly be no more than reconstruction of the business if it is substantially the same business carried on by substantially the same persons.”

Reconstruction, the Division Bench held, means that substantially the same business is carried on and substantially the same persons carry it on:

“...The emphasis, it will be noticed, is on two things - when substantially the same business was carried on and substantially the same persons were carrying it on. It is also to be noticed that the learned Judge draws a clear distinction between a reconstruction and a sale of an undertaking. In the case of a sale, there can be no question of reconstruction. Now, in these matters, we have to look at the substance of the transaction and not the form. If looking at the substance of the transaction, it is a sale, then the concept of reconstruction must be ruled out for in such a case there is no scope for speaking about any reconstruction of an existing business....”

9. The judgment of the the Division Bench of this Court in *Gaekwar Foam* was approved by the Supreme Court in a judgment in *Textile Machinery*



*Corporation Ltd. v. Commissioner of Income Tax* (Supra). The Supreme Court in that case dealt with the issue as to whether within the meaning of Section 15C(2)(i) of the Income Tax Act, 1922, the industrial undertakings which consisted of a steel foundry division and jute mill division were not formed by the reconstruction of a business already in existence. The Supreme Court observed that in order to be entitled to the benefit of Section 15C the following facts would have to be established by the assessee:

- “(1) investment of substantial fresh capital in the industrial undertaking set up;
- (2) employment of requisite labour therein;
- (3) manufacture or production of articles in the said undertaking;
- (4) earning of profits clearly attributable to the said new undertaking and
- (5) above all, a separate and distinct identity of the industrial unit set up.”

10. The Supreme Court was of the view that the new undertaking must not be substantially the same old existing business. Even if a new business is carried on but by piercing the veil of the new business it is found that there is employment of the assets of the old business, the benefit will not be available. From this perspective the Court held that a substantial investment of new capital is imperative.

11. The Tribunal in the present case has come to the conclusion that where a running business is transferred lock, stock and barrel by one assessee to another assessee the principle of reconstruction, splitting up and transfer of plant and machinery cannot be applied. According to the Tribunal the benefit of Section 10A attaches to the undertaking and not to the assessee which owns the undertaking. The benefit of Section 10A was held to have attached itself to the STP unit of the software division which was owned by IOCL till 19 October 1994 and it was owned by the assessee



subsequent to that date. What is material, according to the Tribunal, is not who owns the undertaking but whether the undertaking is entitled to the benefit available under Section 10A. As regards the issue of transfer by IOCL to the assessee, the Tribunal noted that Section 10A(9) was substituted by the Finance Act 2000 with effect from 1 April 2002. Section 10A(9) provided that where during any previous year the ownership or beneficial interest in an undertaking of the business is transferred by any means, the deduction under sub-section (1) shall not be allowed to the assessee for the Assessment Year relevant to such previous year and the subsequent years. The Tribunal noted that if a transfer between IOCL and the assessee were to be effected after 1 April 2001, that would result in the undertaking being disentitled to the benefit under Section 10A. This was a pointer to the fact that prior to the substitution a transfer of ownership or beneficial interest in the undertaking would not disentitle an assessee to the benefit of Section 10A. (As a matter of fact it may also be noted that the provisions of Section 10A(9) were omitted by the Finance Act 2003 with effect from 1 April 2004).

12. The judgment of the Division Bench of this Court in *Gaekwar Foam* explains that the concept of a reconstruction of a business implies that the original business is not to cease functioning and its identity is not lost. Reconstruction is of a business already in existence and there must be a continuation of the activities and business of the same industrial undertaking. Where the ownership of a business or undertaking changes hands that would not be regarded as reconstruction. This judgment has specifically been approved by the Supreme Court in *Textile Machinery Corporation* (Supra). As regards the splitting up of a business, the relevant test is whether an undertaking is formed by splitting up of a business already in existence. Unless the formation of the undertaking takes place by the splitting up of a business already in existence, the negative



prohibition would not be attracted. In the present case, the entire business of the software undertaking was transferred to the Assessee. The undertaking of the Assessee was not formed by the splitting up of the business.”

22. The aforesaid judgment refers and interprets the term “reconstruction”. The said term has been explained by the Delhi High Court in *Commissioner of Income Tax versus Ganga Sagar Corporation Limited*, (1973) 92 ITR 173 (Delhi). Ratio of the said decision was approved by the Supreme Court in *Textile Machinery Corporation Limited* (supra).

23. However, for the reasons and the ratio expounded above with reference to the word/term “formed”, we would like to place reliance and emphasis on the reasoning elucidated and explained by the Supreme Court in *Bajaj Tempo Limited, Bombay versus Commissioner of Income Tax, Bombay City-III, Bombay* (1992) 3 SCC 78. In the said decision the word “formed” as used in Section 15C of the Income Tax Act, 1922, which also had a similar negative covenant that the industrial undertaking should not be formed by splitting up or reconstruction of business already in existence or transfer of a new building, machinery of plant, previously used in business, was set up for consideration and it was opined:-

“9. .... Sub-section (2) advances the objective of sub-section (1) by including in it every undertaking except if it is covered by clause (i) for which it is



necessary that it should not be formed by transfer of building or machinery. The restriction or denial of benefit arises not by transfer of building or material to the new company but that it should not be formed by such transfer. This is the key to the interpretation. The formation should not be by such transfer. The emphasis is on formation not on use. Therefore it is not transfer of building or material but the one which can be held to have resulted in formation of the undertaking.....

**10.** Reverting to the Bombay decision on which the High Court relied for answering the question against the assessee we would assume for purposes of this case that lease of the building amounted to transfer. Yet what is significant is that the High Court did not examine the impact of word 'formed'. It proceeded on basis that once lease amounted to transfer the assessee became ineligible from claiming any exemption. The Court further repelled the contention advanced on behalf of assessee on strength of Calcutta decision in *CIT v. Sainthia Rice & Oil Mills* [(1971) 82 ITR 778 (Cal)] that transfer of building to the new business to disentitle the undertaking should have been of the assessee himself. In our opinion this aspect of the Bombay decision was correctly decided and the tribunal was not justified in deciding in favour of assessee on this ground. We therefore endorse the view of Bombay High Court and Punjab and Haryana High Court in *Phagoo Mal Sant Ram v. CIT* [(1969) 74 ITR 734 (P&H HC)] to this extent that, 'previously used in any other business' cannot be construed so narrowly as to confine it to building of the assessee only. But we do not approve of the Bombay view that if a new undertaking is established in a premises taken on lease then it, always, amounts to formation of the undertaking by transfer of the building previously used as the decision was given without examining the scope of the word 'formed' which as we have indicated above, was construed by this Court in *Textile Machinery Corporation Ltd.* [(1977) 2 SCC 368 : 1977 SCC (Tax) 282 :



(1977) 107 ITR 195] which approved a decision of Delhi High Court in *CIT v. Ganga Sugar Corporation Ltd.* [(1973) 92 ITR 173 (Del)] ‘Form’ according to the dictionary has different meanings. In the context in which it has been used it was intended to connote that the body of the company or its shape did not come up in consequence of transfer of building, machinery or plant used previously for business purpose. Use of the negative before word ‘formed’ further strengthens it. In other words building, machinery or plant used previously in other business should not result in the undertaking being formed by it. The transfer to take out the new undertaking out of purview of sub-section (1) must be such that but for transfer the new undertaking could not have come into being. In our opinion, on facts found by the tribunal, the part played by taking the building on lease was not dominant in formation of the company. The High Court was therefore not justified in answering the question in favour of the revenue.”

(emphasis supplied)

24. For the purpose of the present statute, i.e., Income Tax Act, 1961 difference between an undertaking, and the owner thereof, i.e., the assessee is well recognised and too apparent to be ignored and, therefore, when the Legislature in sub-section (1) and other sub-sections used the term “undertaking” as distinct from its owner/proprietor, the assessee, the effect thereof must be given full play. Way back in 1963, Circular F.No. 15/15/63-IT(A1) was issued with reference to Section 84 of the Act stating that the Board, i.e., the Central Board of Direct Taxes had agreed that benefit of the said Section attaches itself to the undertaking and not to the owner thereof.



The successor would be entitled to benefit of the unexpired period five years provided the undertaking was taken over as a running concern. More specific is the support and affirmation from the circular issued by the Board after amendment was brought about by Finance Act 2002 to Sections 10A and 10B. The relevant portions of which read as under:-

**“19.5** Under the existing provisions of section 10A, the deduction is available for a maximum period of ten consecutive assessment years starting from the year of commencement of production. After the assessment year commencing on or after 1-4-2010, no deduction shall be available irrespective of the year of commencement of production. However, in respect of undertakings commencing operation in the notified Special Economic Zones (SEZs) on or after 1<sup>st</sup> April, 2002, the Finance Act, 2002 intends to provide a separate tax holiday for a total period of seven assessment years, comprising of a deduction of 100% of export profits for five years followed by deduction of 50% of export profits for subsequent two years. The proposal shall have the effect of extending the deduction under section 10A beyond the assessment year 2010 - 2011, in respect of undertakings operating from the notified Special Economic Zones (SEZs).

**19.6** Sub-section (9) of Section 10A and sub-section (9) of section 10B provide that no deduction under those sections shall be available where during any previous year the ownership or the beneficial interest in the undertaking is transferred by any means.

**19.7** The above provision was introduced by the Finance Act, 2000 to prevent trading in incentives by such companies formed only for that purpose. However, the above provision was not intended to bring within its purview cases of



genuine business reorganization while maintaining the major portion of ownership or beneficial interest with the same persons who were the owners of the business before such reorganization.

**19.8** Exceptions were made by the Finance Act, 2001 in the case of Private Ltd. companies becoming companies in which public are substantially interested as also disinvestment of equity shares by venture capital companies or funds. It was also clarified that cases of change in shareholding pattern in the case of public limited companies will also not affect the deduction.

**19.9** The Finance Act, 2002 has introduced sub-section (9A) to provide that in case of genuine reorganization of business whereby a proprietary concern or a partnership is succeeded by a company, the prohibition of sub-section (9) will not apply if the beneficial ownership of not less than 51% continues to be held by the original promoters. Since, undertakings can be owned by body corporate also, it is clarified that this will hold good even if the proprietor happens to be a body corporate.

**19.10** This is however, subject to the condition that, the aggregate of the shareholding in the company of the partners of the firm, or of the sole proprietor in case of a proprietorship concern, is not less than fifty-one per cent of the total voting power in the company and their shareholding continues to be as such for the period for which the deduction under this section is being claimed by the company in respect of the undertaking.”

25. However, as noted above, in the very next year substantial changes were made by Finance Act 2003, sub-sections (9) and 9A of Section 10B were both deleted. Similar changes were also made in Section 10A of the Act. Noticing the different views and interpretations being taken, CBDT has issued Circular No. 01/2013



dated 17<sup>th</sup> January, 2013 and in paragraph (iv) it has been observed:-

“(iv) WHETHER TAX BENEFITS UNDER SECTIONS 10A, 10AA AND 10B WOULD CONTINUE TO REMAIN AVAILABLE IN CASE OF A SLUMP-SALE OF A UNIT/UNDERTAKING.

The vital factor in determining the above issue would be facts such as how a slump-sale is made and what is its nature. It will also be important to ensure that the slump sale would not result into any splitting or reconstruction of existing business. These are factual issues requiring verification of facts. It is, however, clarified that on the sole ground of change in ownership of an undertaking, the claim of exemption cannot be denied to an otherwise eligible undertaking and the tax holiday can be availed of for the unexpired period at the rates as applicable for the remaining years, subject to fulfilment of prescribed conditions.”

(emphasis supplied)

26. Subsequently, instruction No. 17/2013 was issued by the Board as it was reported that the Assessing Officers were not following the clarificatory Circular No. 1/2013 issued by the Board dated 17<sup>th</sup> January, 2013. The field authorities were advised to follow the circular in letter and spirit and it was also advised that further appeals should not be filed where orders were passed prior to the issue of the circular as the issue/dispute was clarified. It is pursuant to the circular that for the Assessment Year 2005-06, the Assessing Officer in the case of respondent assessee did not file any appeal before the tribunal after the first appellate authority had allowed the deduction to the assessee



under Section 10A. Similarly, for the Assessment Year 2006-07, the Assessing Officer wanted to deny the deduction, but DRP issued directions to allow the said deduction. For Assessment Year 2007-08, the position is similar to Assessment Year 2005-06 and the Assessing Officer has not filed any appeal against the decision in favour of the respondent-assessee by the first appellate authority. For Assessment Years 2008-09 and 2009-10, the Assessing Officer himself allowed the claim under Section 10A.

27. In view of the aforesaid discussion, we answer the aforesaid questions of law in affirmative, i.e., in favour of the respondent-assessee and against the appellant-Revenue. The appeal is accordingly dismissed. Respondent will be entitled to costs as per Delhi High Court Rules.

-sd-

**(SANJIV KHANNA)**

**JUDGE**

-sd-

**(V. KAMESWAR RAO)**

**JUDGE**

**JULY 18, 2014**  
**NA/VKR**