

M/S. CHILLIES EXPORTS HOUSE LTD.

v.

COMMISSIONER OF INCOME TAX

APRIL 22, 1997

[S.C. AGRAWAL AND K.S. PARIPOORNAN, JJ.]

Finance Acts of 74-75, 76-77 & 77-78—S. 2(8)(c) of 74, S. 2(7)(c) of 76 and S. 2(6)(c) of 77, respectively—The term 'processing of goods' in relation to an 'Industrial Company'—Refers to the cumulative effect of all the activities carried out to make the goods marketable/exportable, and it is immaterial even if some part of that activity is done by an outside agency.

The short question raised in these Appeals was whether the Appellant was entitled to the concessional tax as applicable under S. 2(8)(c) of the Finance Act 74-75 based on a finding of whether there was 'processing of goods'. The High Court rejected the Appellant's case earlier *inter alia* on the ground that the Appellant only sorted, graded clipped and stemmed the chillies but did not do the fumigation which was done by another agency. The same reasoning was followed in the later cases as well.

The Appellant, relying on the judgment of the Supreme Court in *Chowgule & Co. v. Union of India*, 47 STC 124 pleaded that there was 'processing of goods' and hence was entitled to be taxed at 55% only. The Revenue contested by submitting that the *Chowgule* case was restricted in scope and referred to another decision of this Court in *Delhi Cold Storage P. Ltd. v. CIT*, (191 ITR 656).

Allowing the Appeal, this Court

HELD : 1. The entire matter requires a second look. A better investigation into the different activities carried on by the assessee which resulted in the making of the goods fit for export and how far the cumulative effect of those activities will amount to 'the processing of goods' should be arrived at in the light of the various decisions referred to hereinabove. Since such indepth investigation and analysis of the matter has not been made, the decision in the three instant appeals solely based on the earliest decision of the High Court of Madras, rendered in 115 ITR 73, when such materials were not available, cannot stand. The impugned judgments are

A set aside and the matters remitted to the High Court for a *denovo* consideration according to law. [918-D-F]

B 2. It is evident that the various aspects highlighted in the decisions adverted as also the circular of the Central Board of Direct Taxes were not available to the Madras High Court when it rendered its main decision in 1977 (115 ITR 73). The ultimate conclusion as to whether the assessee was carrying on the business of processing of goods would depend upon the consideration of all relevant materials available in the case. [917-E-F]

C 3. The Madras High Court has eschewed from consideration one important activity carried on in the matter, namely, the activity relating to fumigation by the treatment with methyl bromide on the ground that it was done by another (M/S. Mysodet Pvt. Ltd., Bangalore) on behalf of the assessee. That is an irrelevant or immaterial factor. The sole question is whether on a consideration of the totality of the activities including the one relating to the fumigation by the treatment with methyl bromide which enables the goods to be exported as a marketable commodity, amounted to the business of processing of goods. The High Court has omitted to consider the matter in that perspective. [917-F-G]

E 4. It also does not stand to reason to state that the dictum laid down by the three member bench in *Chowgule* case has been departed from in the later decision rendered by another coordinate Bench in the *New Delhi Cold Storage P. Ltd. v. Commissioner of Income Tax*, (191 ITR 656). It appears that since in the cold storage there was only an act of preservation- without any positive action this Court was inclined to take the view that the company running cold storage is not an industrial company and no process is involved. Fumigation requires positive action. The dictionary meaning of the said word is "to treat (something contaminated or infected) with fumes or smoke". The meaning for the word, "fumigate" is to subject to smoke or fumes, as for disinfection". Archaic-to perfume. Whether "refrigeration" "fumigation" are of the same or similar import, or whether there is any difference, is a matter which requires a close look. It appears that though the goods purchased by the assessee were chillies, it had to undergo a series of activities in order to make it marketable in the export market-a sensitive market. These and other consideration require proper evaluation and an indepth analysis and assistance from technical persons

H may be required to ascertain how far and to what extent the various

activities on, by the assessee to render the chillies purchased locally as one of export quality can be termed as "carrying on the business of processing of goods." [917-H; 918-A-D] A

Chowgule & Co. v. Union of India, 47 STC 124; *Delhi Cold Storage P. Ltd. v. Commissioner of Income Tax*, 191 ITR 656; *Commissioner of Income Tax, Gujarat-I v. Lakhtar Cotton Press Co. (Pvt.) Ltd.*, 142 ITR 503; *Commissioner of Income Tax v. Datacons (P) Ltd.*, 155 ITR 66; *Commissioner of Wealth Tax v. Syed Amjad Ali*, 202 ITR 19; *Shree Mulchand Co. Ltd. v. Commissioner of Income Tax*, 162 ITR 764; *Commissioner of Income Tax v. Rajmohan Cashews (P) Ltd.*, 185 ITR 472, Referred to. B

Collins English Dictionary and Webster's Comprehensive Dictionary referred to. C

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 3637 of 1983.

From the Judgment and Order dated 18.12.81 of the Madras High Court in T.C. No. 469 of 1978. D

T.A. Ramachandran, K.R. Ramamani and Mrs. Janaki Ramachandran for the Appellant.

J. Ramamurthy, Tara Chandra Sharma, B.K. Prasad and C. Radha Krishnan for the Respondent. E

The Judgment of the Court was delivered by

PARIPOORNAN, J. An identical question of law arises for consideration in this batch of three appeals. The appellant is the same firm in all the three appeals. The appellant-assessee is a public limited company carrying on *inter alia* the business of exporting chillies to United States of America, USSR and Ceylon. The only question that arises for consideration is "whether the appellant is an 'industrial company' as defined in the respective Finance Acts and can therefore be taxed only at 55%? The revenue is the respondent in all the appeals. F G

2. Civil Appeal No. 3637 of 1983 is filed against the judgment of the Madras High Court dated 18.12.1981 in Tax Case No. 469 of 1978 (Reference No. 289 of 1978) and relates to the assessment year 1974-75. Civil Appeal No. 8017 of 1995 is preferred against the judgment of the same H

Rates of income -tax

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I. In the case of a *domestic company*, --

(1) Where the company is a company in which the public are substantially interested, -

(i) in a case where the total income does not exceed Rs. 1,00,000 45 per cent, of the total income;

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(ii) in a case where the total income exceeds Rs 1,00,000 55 per cent, of the total income;

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(2) *Where the company* is not a company in which the public are substantially interested, --

(i) in the *case of an industrial company* --

(a) on so much of the total income as does not exceed Rs. 2,00,000 55 per cent.;"

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(emphasis supplied)

4. The basic facts relevant to all the three appeals are not in dispute. The question that arises for consideration is whether the appellant-assessee is an "industrial company" within the meaning of the Finance Act aforesaid (hereinafter referred to as the Act) and the tax should be levied at the concessional rate of 55% only. The assessee, a public limited company, is carrying on the business of sale and purchase of chillies. Chillies are exported to USSR, USA and Ceylon. The chillies purchased by the assessee company are sorted and graded as per Agmark specifications. *Better quality chillies are picked up and sorted out for export and before export they are clipped and stemmed and subjected to fumigation under expert technical hands in order to prevent deterioration and with a view to give better polish and appearance and during that process they are treated with methyl bromide.* A substantial part of the goods are exported. According to the assessee, it is engaged in the "business of processing of goods" and so entitled to the concessional rate of income tax as per the Finance Act. The revenue disputes this claim. According to it, no processing is involved and the goods purchased and exported are chillies and the assessee cannot be considered

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A to be an "industrial company" carrying on the business of processing of goods. The identical matter came up for consideration before the Madras High Court relating to the same assessee-appellant for the assessment year 1971-72 and the Court held that the assessee is not an industrial company coming within the meaning of section 2(6)(c) of the Finance Act No. 2 of 1971. The said decision is reported in 115 ITR 73. When the matter came up for consideration in subsequent years 1974-75, 1976-77 and 1977-78, the earlier decision rendered for the assessment year 1971-72 (115 ITR 73) was followed without discussion. In this batch of appeals, the appellant assails the reasoning and conclusion of the High Court contained in its judgment dated 8.12.1977 relating to the assessment year 1971-72 (115 ITR 73) as incorrect and unsustainable.

5. We heard counsel. Appellant's counsel vehemently contended that the decision of the High Court rendered for the assessment year 1971-72 (115 ITR 73) did not consider in an appropriate perspective the requirement of relevant provisions of the Finance Act or the meaning to be given to the word "processing of goods". As stated, the assessee-appellant purchased chillies. They were sorted and graded as per Agmark specifications. *Better quality chillies were picked up and sorted out for export and before export they were clipped and stemmed and subjected to fumigation under expert technical hands in order to prevent deterioration and with a view to give better polish and appearance and during that process they were treated with methyl bromide.* It is common ground that the appellant got the chillies fumigated by M/s. Mysodet Pvt. Ltd. Bangalore by paying charges therefor under a contract. On the basis of these facts, the High Court in the earlier decision (115 ITR 73) concluded that the relevant section of the Finance Act -- section 2(6)(c) -- suggests that the *appellant company itself* should engage in the entire activity which leads to the final processing of the goods. In the said decision, the High Court took the view that the appellant-assessee is concerned only with the activity of sorting and grading of chillies as per Agmark specifications and making them fit for export and before exporting clipping and stemming of chillies. The activity relating to fumigation by the treatment with methyl bromide was done by M/s. Mysodet Pvt. Ltd. and the assessee did not engage in this treatment of preservation and cannot claim the benefit of the concession specified in the Finance Act.

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6. We were referred to a few decisions by both the sides to understand the scope of the word "processing" contained in the respective Finance Acts and also as to how it was understood by the Board of Direct Taxes. We shall refer to them in brief. (These decisions were not available when the Madras High Court rendered the earlier decision reported in 115 ITR 73 dated 8.12.1977). Construing the word "processing" occurring in section 8(3)(b) of the Central Sales Tax Act and (Registration and Turnover) Rules, 1957, to decide whether the ore blended in the course of loading through the mechanical ore handling plant can be said to undergo processing when it is blended, a three Member Bench of this Court in *Chowgule & Co. v. Union of India*, (47 STC 124 at pp. 130-131) stated thus ;

"whether the ore blended in the course of loading through the mechanical ore handling plant can be said to undergo processing when it is blended. The answer to this question depends upon what is the true meaning and connotation of the word "processing" in section 8(3)(b) and rule 13. This word has not been defined in the Act and it must therefore be interpreted according to its natural meaning. Webster's Dictionary gives the following meaning of the word "process", "to subject to some special process or treatment, to subject (especially raw material) to a process of manufacture, development or preparation for the market, etc., to convert into marketable form as livestock by slaughtering, grain by milling, cotton by spinning, milk by pasteurising, fruits and vegetables by sorting and repacking." Where therefore any commodity is subjected to a process or treatment with a view to its "development or preparation for the market", as for example, by sorting and repacking fruits and vegetables, it would amount to processing of the commodity within the meaning of section 8(3)(b) and rule 13. The nature and extent of processing may vary from case to case; in one case the processing may be slight and in another it may be extensive; but with each process suffered, the commodity would experience a change. Wherever a commodity undergoes a change as a result of some operation performed on it or in regard to it, such operation would amount to processing of the commodity. The nature and extent of the change is not material. It may be that camphor powder may just be compressed into camphor cubes by application of mechanical force or pressure without addition or

A *admixture of any other material and yet the operation would amount to processing of camphor powder as held by the Calcutta High Court in Shri Om Prakas Gupta v. Commissioner of Commercial Taxes, (1995) 16 STC 935. What is necessary in order to characterise an operation as "processing" is that the commodity must, as a result of the operation, experience some change.*

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(emphasis supplied)

The above decision was followed by different High Courts in giving effect to similar provisions in Finance Acts in different contexts. In *Commissioner of Income-Tax, Gujarat- I v. Lakhtar Cotton Press Co. (Pvt.) Ltd.*, 142 ITR 503 the Gujarat High Court held that when the assessee was carrying on the business of ginning and pressing of cotton, and cotton received in bulk was mechanically pressed into small units and packed in commercial acceptable bales, it is an operation which results in the change of commodity and amounts processing of goods and the company engaged in such an activity is an industrial company entitled to concessional rate of tax since it is engaged in the processing of goods. In *Commissioner of Income-Tax v. Datacons (P.) Ltd.*, 155 ITR 66 the Karnataka High Court held that conversion of data furnished by customers into balance sheets, stock account, etc., amounts to processing of goods within the meaning of term contained in the Finance Act and so, the assessee is entitled to concessional rate of tax. The Allahabad High Court in *Commissioner of Wealth-Tax v. Syed Amjad Ali*, 202 ITR 19 held that the activity of crushing of tobacco leaves and separating stems and dust therefrom amounts to processing within the meaning of the relevant expression that occurred in Wealth Tax Act. The Bombay High Court in *Shree Mulchand Co. Ltd. v. Commissioner of Income- Tax*, 162 ITR 764 held that when a company purchases wool, sorts out the same in different qualities and colours and staple lengths, and then hand-washed to eliminate dirt, etc., and dried it in sun and blended uniformly for sale and export, a new commercial commodity is brought into existence and the operation carried on amounts to processing of goods and the assessee is an industrial company, entitled to concessional rate of tax under Finance Act 2 of 1971. The Kerala High Court in *Commissioner of Income-Tax v. Rajmohan Cashews (P.) Ltd.*, 185 ITR 472 held that when the assessee company was engaged in processing raw cashew nuts and the major operation of processing work was done by outside agencies on behalf

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of the assessee and charges, therefor, were paid by the assessee, the assessee was engaged in manufacture and processing of the goods and was an industrial company within the meaning of section 2(6)(c) of the Finance Act, 1972. The Court held that the fact the processing was not done in the factory of the assessee but in the factory of someone else would not necessarily mean that the assessee is not mainly engaged in the processing of the goods provided there is material to show that the processing was done by the outside agency for and on behalf of the assessee and the charges incurred therefor were paid by the assessee directly. Reference may also be made, in this connection, to circular No. 347 dated 7th July, 1982, issued by the Central Board of Direct Taxes, printed at 137 ITR (Statutes) p. 14, which is to the following effect :

"Circular No. 347, dated 7th July, 1982.

To

All Commissioners of Income-tax

Sir,

Subject : Book publishing - whether industrial companies.

The Board has received representations that companies engaged in publishing of books should be treated as industrial companies for the purpose of section 104 of the Income-tax Act, 1961. Reference has been made in this connection to the decisions of the Madras and Calcutta High Courts in the cases of *CIT, Madras v. Commercial Laws of India Pvt. Ltd.*, (1977) 107 ITR 822, and *Addl. CIT, West Bengal-II v. A. Mukherjee & Co. (P.) Ltd.*, (1978) 113 ITR 718, respectively. In the Madras decision it has been held that folding and stitching the printed sheets and converting them into parts or books, as the case may be, constituted processing of goods, In the Calcutta decision, it was held that it is wholly unnecessary for a publisher of books to be *an owner of a printing press or to be himself a book binder to be a manufacturer of books. A publisher may get the books printed from any printer, but the printer is a mere contractor and the publisher carries on the business of manufacturing and processing of goods.*

A 2. The Board has been advised to accept these decisions. In view thereof, book publishing *companies even though they may themselves not be engaged in the printing or binding of books qualify to be treated as industrial companies* for the purpose of section 104 as well as for the concessional tax treatment given to industrial companies.

B 3. The contents of the circular may kindly be brought to the notice of all officers working under your charge."

(emphasis supplied)

C On the basis of the above materials, counsel for the appellant vehemently contends that the entire approach made by the High Court and the conclusion reached by it is unsustainable and the above materials were not available to the Madras High Court when it rendered the parent decision in (1977) 115 ITR 73. It was contended that main reasoning in the said decision 115 ITR 73 is to the effect that the activity done by the assessee, namely, sorting and grading of chillies as per Agmark specifications and making them fit for export and before export clipping stemming of chillies were alone done by them but the activity relating to fumigation by the treatment of methyl bromide was done by another on its behalf, and so the assessee cannot claim the benefit and the totality of the activities cannot be considered as having been done by the assessee and it is on this basis of reasoning, it was held that in this view it cannot be said that the assessee was engaged in the processing of goods within the meaning of Finance Act No. 2 of 1971. The plea urged before us is that the word "processing" has been understood in a very wide sense by the three member Bench of this Court in *Chowgule* case (supra) and by various High Courts referred to hereinabove and, even if one or more of such activities in the series are entrusted to any other person like a contractor, to enable the assessee to complete the task, it will not disable or disentitle the assessee to claim the concessional rate of tax.

G 7. On the other hand, counsel for the Revenue submitted that the decision in *Chowgule* case (supra) rendered by a three member Bench of this Court has been given a restricted scope in a later three member decision of this Court in *Delhi Cold Storage P. Ltd. v. Commissioner of Income-Tax*, 191 ITR 656. In that case a private limited company was running a cold storate. It was held that the articles stored in cold storage

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did not undergo any process. The question was posed as to whether the cold storage company can be held to have been engaged in the processing of goods. A three member Bench of this Court, after quoting the passage subsequent to the one quoted by us hereinabove - *Chowgule* case 47 STC 124 at 131 held that the word "processing" is of wider amplitude, and has various aspects and meaning and observed at p. 660, "the judgment indicates that processing involves bringing into existence a different substance from what the material was at the commencement of the process". Counsel contended that in this case the goods purchased and exported are the same, namely, chillies. And so, it cannot be stated that by processing a different substance was brought into existence. It was further stated that the activity of fumigation in the present appeals is similar to preservation by refrigeration. It was further argued that the activity carried on by the assessee is only marginal or minimal and so the assessee cannot be said to be carrying on the business of processing of goods. Reference was also made to the decisions of Karnataka High Court in *Hind Nippon Rural Industries Pvt. Ltd. (No. 1) v. Commissioner of Income-Tax*, 201 ITR 581 and *Hind Nippon Rural Industries Pvt. Ltd. (No. 2) v. Commissioner of Income-Tax*, 201 ITR 588.

8. On hearing the rival pleas urged before us, it is evident that the various aspects highlighted in the decisions adverted to hereinabove as also the Circular of the Central Board of Direct Taxes were not available to the Madras High Court when it rendered its main decision in (1977) 115 ITR 73. The ultimate conclusion as to whether the assessee was carrying on the business of processing of goods would depend upon the consideration of all relevant materials available in the case. The Madras High Court has eschewed from consideration one important activity carried on in the matter, namely, the activity relating to the fumigation by the treatment with methyl bromide on the ground that it was done by another (M/s. Mysodet Pvt. Ltd., Bangalore) on behalf of the assessee. That is an irrelevant or immaterial factor. The sole question is, whether on a consideration of the totality of the activities including the one relating to the fumigation by the treatment with methyl bromide which enables the goods to be exported as a marketable commodity, amounted to the business of processing of goods. The High Court had omitted to consider the matter in that perspective. It also does not stand to reason to state that the dictum laid down by the three member Bench in *Chowgule* case (supra) has been departed from in the later decision rendered by another coordinate Bench in *New Delhi Cold*

A *Storage P. Ltd. v. Commissioner of Income-Tax*, 191 ITR 656. It appears that since in cold storage there was only an act of preservation -- without any positive action -- this Court was inclined to take the view that the company running cold storage is not an industrial company and no process is involved. Fumigation requires positive action. The dictionary meaning of the said word is, "to treat (something contaminated or infected) with fumes or smoke" (Collins English Dictionary). Webster's Comprehensive Dictionary - International Edition - p. 512, gives the meaning for word, "fumigate" thus, "To subject to smoke or fumes, as for disinfection". Archaic -- to perfume. Whether "refrigeration" and "fumigation" are of the same or similar import, or whether there is any difference, is a matter which

B requires a close look. It appears that though the goods purchased by the assessee were chillies, it had to undergo a series of activities in order to make it marketable or more marketable in the export market -- a sensitive market. These and other considerations require proper evaluation and an indepth analysis and assistance from technical persons may be required to ascertain how far and to what extent the various activities carried on, by

C the assessee to render the chillies purchased locally as one of export quality can be termed as "carrying on the business of processing of goods". The entire matter requires a second look. A better investigation into the different activities carried on by the assessee which resulted in making the goods fit for export and how far the cumulative effect of those activities

D will amount to "the processing of goods" should be arrived at in the light of the various decisions referred to hereinabove. Since such an indepth investigation and analysis of the matter has not been made, we are of the view that the decision in the three instant appeals solely based on the earlier decision of the High Court of Madras, rendered in 115 ITR 73,

E when such materials were not available, cannot stand. We, therefore, set aside the judgments in all the appeals and order a remit of the matters to the High Court for a denovo consideration according to law.

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9. The appeals are, therefore, allowed. There shall be no order as to costs.

G I.M.A.

Appeals allowed.