SUPREME COURT OF INDIA

Vijay Ship Breaking Corpn.

Vs.

Commnr. of Income Tax, Ahmedabad

C.A.Nos.6692-6723 of 2003

(S.H. Kapadia and B. Sudershan Reddy JJ.)

01.10.2008

ORDER

1. Leave granted in Special Leave Petitions.

2. Two questions, as stated hereinbelow, arise for determination in this batch of Civil Appeals:

> "(1) Whether appellant-assessee was entitled to deduction under Sections 80-HH and 80-I of the *Income Tax Act, 1961* in respect of ship breaking activity undertaken by it? (2) Whether 'usance interest' partakes of the character of purchase price and, therefore, not liable to deduction at source under Section 195(1) of the *Income Tax Act, 1961*?"

3. We may refer to C.A.Nos.6692-6723/2003 for deciding these appeals.

4. Answer to Question No.1:

> The Income Tax, 1961 Act does not define the expression 'industrial undertaking'. Section 80HH falls under Chapter VIA. Section 80HH falls under sub-Chapter C which deals with "deductions in case of certain incomes". Section 80HH deals with deduction in respect of profits and gains from newly established industrial undertakings. Under Section 80HH(1), it is, inter alia, provided that where gross total income of an assessee includes any profits and gains derived from an industrial undertaking to which the section applies, then, a deduction shall be allowed in computing the total income of the assessee for such profits and gains of an amount equal to 20% thereof. However, under Section 80HH(2), the deduction applies only to an industrial undertaking which fulfils certain conditions, namely, that the industrial undertaking must be involved in the activity of "manufacturing or producing articles". It is this expression in clause (i) of sub-section (2) of Section 80HH which arises for consideration before us in this case. reported in 204 ITR 412, a Division Bench of this Court held that the word 'production' has a wider connotation than the word

'manufacture'. It was further held that the word 'production' when used in juxtaposition with the word 'manufacture' takes in bringing into existence new goods by a process which may or may not amount to manufacture. It also takes in all the by-products, intermediate products and residual products which emerge in the course of manufacture of goods.

5. Learned counsel Shri Ranbir Chandra, appearing on behalf of the Department, emphasizes the words "new goods". In fact, the impugned judgment of the Gujarat High Court also proceeds on the basis that when a ship breaking activity is undertaken, the articles which emerged from the activity of ship breaking continued to be the part of the ship; that such parts do not constitute new goods and, consequently, in this case, the impugned judgment proceeds to hold that the assessee was not entitled to claim the benefit under Sections 80HH and 80I of the 1961 Act as there was neither production nor manufacture of new goods by the process of ship breaking.

6. We do not agree with the view taken by the Gujarat High Court in the impugned judgment for the following reasons: reported in 251 ITR 807, the Bombay High Court has analysed the entire ship breaking activity, the articles which emerged from that activity, the various steps which are required to be undertaken for ship breaking activity and, consequently, after placing reliance on the judgment of this Court in Budharaja's case (supra), it has held that the ship breaking activity resulted in production of articles which emerged when the ship breaking activity stood undertaken. In our view, the important test which distinguishes the word 'production' from 'manufacture' is that the word 'production' is wider than the word 'manufacture' as held in Budharaja's case. Further, it is true that in Budharaja's case, the Division Bench has used the word 'new article'. However, what the Division Bench meant was that a distinct article emerges when the process of ship breaking is undertaken. Further, the Legislature has used the words 'manufacture' or 'production'. Therefore, the word 'production' cannot derive its colour from the word 'manufacture'. Further, even according to the dictionary meaning of word 'production', the word 'produce' is defined as something which is brought forth or yielded either naturally or as a result of effort and work (see Webster's new international dictionary). It is important to note that the word 'new' is not used in the definition of the word 'produce'.

7. Secondly, the judgment of the Bombay High Court in the case of Ship Scrap Traders (supra) stands affirmed by the judgment of this Court in the case of case, the question arose before a Bench of three Judges of this Court was as to whether extraction and processing of mineral ore amounts to production within the meaning of the word in Section 32A(2)(b)(iii) of the 1961 Act? It was held that the word 'production' is wider than the word 'manufacture'. It was held that the word 'production' has a wider connotation than the word 'manufacture'. It was further held that the mined ore need not be a new product. In fact, the Department had raised an identical argument in that case stating that the mined ore was not a new product and, consequently, there was no production. This argument has been specifically rejected in Sesa Goa's case.

8. For the aforestated reasons, therefore, we are of the view that the Tribunal in the present case was right in allowing the deduction under Sections 80HH and 80I to the assessee holding that the ship breaking activity gave rise to the production of a distinct and different article. Accordingly, the said question is answered in favour of the assessee and against the Department.

Answer to Question No.2:

9. As regards the second question, we may state that in this case, the controversy which arose for determination was whether the assessee was bound to deduct TDS under Section 195(1) of the 1961 Act in respect of usance interest paid for purchase of the vessel for ship breaking? According to the Department, TDS was deductible under Section 195(1) whereas, according to the assessee, such interest partook of the character of the purchase price and, therefore, TDS was not deductible. Therefore, the key question which arose for determination was whether the assessee was in default for not deducting TDS under Section 195(1) of the 1961 Act? It may be mentioned that we are not required to examine this question in the light of the impugned judgment because after the impugned judgment which was delivered on March 20, 2003, the Income Tax Act was amended on 18th September, 2003 with effect from 1st April, 1983. By reason of said amendment, Explanation-2 was added to Section 10(15)(iv)(c), which reads as under:

> "Explanation 2---For the removal of doubts, it is hereby declared that the usance interest payable outside India by an undertaking engaged in the business of ship-breaking in respect of purchase of a ship from outside India shall be deemed to be the interest payable on a debt incurred in a foreign country in respect of the purchase outside India."

10. On reading that Explanation, it is clear that usance interest is exempt from payment of income tax if paid in respect of ship breaking activity. This amendment came into force only after the impugned judgment. It was not there when the impugned judgment was delivered.

11. For the aforestated reasons, question No.2 as to whether the assessee was bound to deduct TDS under Section 195(1) is answered in favour of the assessee and against the Department. The assessee was not bound to deduct tax at source once Explanation-2 to Section 10(15)(iv)(c) stood inserted as TDS arises only if the tax is assessable in India. Since tax was not assessable in India, there was no question of TDS being deducted by the assessee. Therefore, question No.2 is answered in favour of the assessee and against the Department.

12. Accordingly, Civil Appeals filed by the assessee(s) are allowed and Civil Appeal filed by the Department is dismissed, with no order as to costs.