

BDO TAX UPDATE

1. **CIT v. Nestor Pharmaceutical Limited [2010-TIOL-124-HC-DEL-IT]**

Initial assessment year commences from the year in which commercial production starts, and not from the year of trial run production. Single sale transaction during trial run production tantamounts to commercial production for the purpose of section 80-IA of the Act.

Background:

Delhi High Court in its remarkable judgement has held that for the purpose of section 80-IA of the Income-tax Act ("the Act"), initial assessment year commences from the year in which commercial production starts, and not from the year of trial run production.

The High Court further observed that a single commercial transaction during the trial run period tantamounts to commercial production for the purpose of section 80-IA of the Act.

Facts:

Nestor Pharmaceutical Limited ("the assessee") was engaged in the business of manufacturing of pharmaceuticals formulations. The assessee carried out trial run production from 20th March 1998 and sold one water cooler and one air-conditioner in same year.

Issues for consideration:

1. Whether production of article during trial runs tantamounts to commercial production for the purpose of section 80 IA of the Act?
2. Whether sale of one water cooler and one air-conditioner for the purpose of obtaining registration of excise and sales tax shall be treated as "manufacturing" within the meaning of provision of section 80-IA of the Act?

Assessing Officer's contention:

The Assessing Officer ("the AO") contended that the assessee started commercial production in A.Y. 1998-1999. To support his argument, the AO pointed out that the assessee has showed closing stock as on 31st March 1998. The AO further contended that the assessee undertook commercial transaction (i.e. sale of one air-cooler and one air-conditioner) during A.Y.1998-1999. In view of above, the AO concluded that the for the purpose of section 80IA of the Act initial assessment year commences from A.Y. 1998-1999 and expires in A.Y. 2002-03.

Assessee's contention:

The assessee submitted that trial run production should not be regarded as commercial production for the purpose of section 80-IA of the Act. According to the assessee, the commercial production commenced only in A.Y. 1999-2000. Therefore, initial year commenced from A.Y 1999-2000 and not from A.Y.1998-1999 as contemplated by the AO. The assessee, to substantiate its claim, furnished a copy of no objection certificate from local authority and approval for release of HT power granted in the month of April 1998.

The Commissioner of Income tax (Appeals) ("CIT(A)") confirmed the order of the AO. Aggrieved with the order of CIT(A), the assessee preferred an appeal before the Tribunal.

Finding of the Tribunal:

The Tribunal observed that for the purpose of section 80-IA of the Act, there should be commercial production and not the trial production. In this regard reliance was

placed in the case of Metropolitan Spring Pvt. Ltd v. Commissioner of Income tax (CIT)¹ and CIT v. Himalyan Magnesite Limited². It further observed that merely having closing stock as on 31.3.1998 cannot lead to conclusion that there was commercial production for the purpose of section 80-IA of the Act.

With regard to sale of water cooler and air-conditioner, the Tribunal observed that once goods are sold from the trial run production, it could not be pleaded that sale is merely a trial run production and not commercial production of an article or a thing. The assessee has crossed the stage of trial production, with the sale of cooler and air-conditioner. It further ruled that quantum of sale is not deciding factor as to whether there is commercial production or not.

In view of this, the Tribunal held that initial assessment year for the purpose of section 80-IA of the Act, commences from A.Y. 1998-1999.

Aggrieved with the order of the Tribunal, the assessee preferred an appeal before the Hon'ble High Court.

Findings of the High Court:

The High Court confirmed the order of the Tribunal and held that trial run production cannot be regarded as commercial production. In this regard, reliance was placed in case of CIT vs. Hindustan Antibiotics Ltd³ and CIT v. Food Specialities Ltd⁴.

The High Court further observed that on sale of one water cooler and one air conditioner during the trial run production, the assessee crossed the stage of trial run period. Accordingly, the High Court held that initial assessment year for the purpose of section 80-IA commences from A.Y. 1998-1999 and not from A.Y.1999-2000, as contemplated by the assessee.

¹132 ITR 893 (Bom.)

²276 ITR 56 (All.)

³93 ITR 548 (Bom.)

⁴156 ITR 790

Contact Us

Head Office

42, Free Press House, 215, Nariman Point, Mumbai - 400 021.
Tel: +91 (22) 6639 1101-04 Fax: +91 (22) 2285 6237
tas@bdoindia.co.in

Ahmedabad

511-512, Span Trade Center, Opp. Kocharab, Ashram, Paldi, Ahmedabad - 380 007.
Tel: +91 (79) 2657 8900
Fax: +91 (79) 2658 1906

Bengaluru

No. 45, First Floor, 2nd Main, Sankey Road, (Above Indian Bank) Lower Palace Orchards, Bengaluru - 560 003.
Tel: +91 (80) 6454 2545/6454 2546
Fax: + 91 (80) 6454 2547

Hyderabad

Room No. 417 & 418, 4th Floor, Model House, Dwarkapuri Colony, Panjagutta, Hyderabad - 500 082.
Tel: +91 (40) 3062 1888
Fax: +91 (40) 6662 0277

Jaipur

Manish Mansion, Plot No. 247, Frontier Colony, Adarsh Nagar, Raja Park, Jaipur - 302 004.
Tel: +91 (141) 2604 743

Kolkata

Geetanjali Apartments, Suite 7G, 7th Floor, 8B, Middleton Street, Kolkata - 700 071.
Tel: +91 (33) 2229 8936/2229 6758
Fax: + 91 (33) 2226 4140

Mumbai

701 Leela Business Park, Andheri-Kurla Road, Andheri (E), Mumbai - 400 059.
Tel: +91 (22) 6672 9999
Fax: +91 (22) 6672 9777

New Delhi

3rd Floor, 52-B, Okhla Industrial Area, Phase III, New Delhi - 110 020.
Tel: +91 (11) 4711 9999
Fax: + 91 (11) 4711 9998

Pune

'Samanvaya', C.T.S. No. 425/36 Tilak Vidyapeeth Colony, Gultekdi, Pune - 411 037.
Telefax: + 91 (20) 2426 2372/2426 2543

Vadodara (Baroda)

301, 302, 303, 3rd Floor, Vidhi Complex, Opp. BPC, 68 Sampatrao Colony, Alkapuri, Vadodara - 390 005.
Tel: +91 (265) 6455 152-3
Fax: + 91 (265) 2343 233

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