

**IN THE INCOME TAX APPELLATE TRIBUNAL  
'C' BENCH, BENGALURU**

**BEFORE SHRI INTURI RAMA RAO, ACCOUNTANT MEMBER  
and  
SHRI LALIET KUMAR, JUDICIAL MEMBER**

ITA No.1607/Bang/2017  
(Assessment year : 2013-14)

M/s.Gemini Graphics Pvt. Ltd.  
No.7, Mathrukrupa, I Floor, Temple Road,  
Malleswaram,  
Bengaluru-560003. ... Appellant  
*PAN:AAACG 5250 F*

Vs.

Deputy Commissioner of Income-tax,  
Circle 3(1)(2),  
Bengaluru. ... Respondent

Appellant by : Shri H.V.Gowthama, CA.  
Respondent by : Shri R.K.Jha, CIT(DR)

Date of hearing : 08/11/2017  
Date of pronouncement : 26/12/2017

**ORDER**

**Per INTURI RAMA RAO, AM :**

This is an appeal filed by the assessee directed against the order of the Commissioner of Income Tax (Appeals)-3, Bengaluru, [CIT(A)] dated 31/05/2017 for the assessment year 2013-14.

2. The assessee-appellant raised the following grounds of appeal:

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1. The learned Commissioner of Income Tax(Appeals) erred in upholding the order of learned Assessing Officer in disallowing the claim u/s.35(1)(iv) of Income Tax Act in respect of Capital Expenditure made by the Appellant for Research & Development unit.
2. The learned Commissioner of Income Tax (Appeals) should have appreciated the fact that all the machineries & other capital assets installed were used only in respect of Research & Development Wing, which was also proved that new products were manufactured by the Appellant company. Evidence in respect of new products sale were also produced both before Hon'ble CIT(A) and learned Assessing Officer.
3. The learned Commissioner of Income Tax(Appeals) was wrong to state that the new products manufactured by the Appellant in the R&D Unit were only an extension of the existing products and hence it cannot be said that the Appellant has carried out any "Scientific Research".
4. The learned Commissioner of Income Tax(Appeals) was wrong in mentioning that the activities carried out by the Appellant by using new Plant & Machinery were its regular manufacturing activities i.e. manufacturing of paper.
5. The learned Commissioner of Income Tax was wrong in concluding that Scientific Research requires a different type of activities to make the Appellant eligible for R & D expenditure u/s.35(1)(iv).

For the above & any other grounds that may be advanced at the time of hearing, the Appellant prays that the R&D expenses be allowed in full.

3. Briefly facts of the case as under: The assessee is a company duly incorporated under the provisions of the Companies Act 1956. It is engaged in the business of manufacture of printing of paper. Return of income for the assessment year 2013-14 was filed on 30/09/2013 declaring total income of Rs.3,49,71,770/-. Against said return of income, the assessment was completed by the Deputy Commissioner of Income-tax, Circle 3(1)(2), Bangalore, [hereinafter referred to as the AO] vide order dated 30/03/2016 passed u/s 143(3) of the Income Tax Act 1961 [ 'the Act' for short]. The AO, while completing the assessment denied the claim made u/s 35(1)(iv) of the Act. The assessee made a claim for deduction of Rs.3,54,00,000/- under the provisions of section 35(1)(iv) claiming to be capital expenditure incurred on R&D. During the course of assessment proceedings, the AO denied the claim holding that the assessee had failed to furnish details of research carried on.

4. The facts set out by the AO on this issue are as follows:

6. The Assessee's claim of capital expenditure on R&D cannot be accepted for the following reasons:

6.1. Assessee's claimed that the products manufactured such as Abrasive Base Kraft Paper. Brown & White crepe filter paper & seed germination paper are manufactured first time in India and same is not available elsewhere. Subsequent submission of assessee's own submissions shows these papers were manufactured by other entities detailed as under:

6.1.1. White Crepe filter Paper is being manufactured by the entities viz., Senapathy Whitelly, Bangalore ; Shri. Radha Madhav.Fibers, Muzaffar Nagar and S.S. Filters Navi. Mumbai and Three AAR, Sonapat.

6.1.2. Similarly seed germination paper is being manufacturing by S.S. Filters , Navi Mumbai, Bangalore paper & pulp mills, Bangalore three AAR Sonipat, Haryana and absence Kraft Paper & Burnal mills, Raipur.

6.1.3. Kraft paper were manufactured has Raman Boards Ltd, Mysore, ITC Tribeni Tissues Kolkata, Puchumjee pulp and paper , pune, Aura Papers Hyderabad, Shree. Krishna Paper mill industries Jaipur.

6.2. Hence assessee claim that there papers were not known to India cannot be accepted. Considering the fact that products which were available in the market produced by other manufacturers in India cannot be considered as a products which as emerged out of research of the assessee is not acceptable.

6.3. Assessee claimed that it had existing customers Saint Gobain, Bangalore/ Grindwell Norton, Carbo randim unicersal. (CUMI), Chennai & other customers in Delhi. However on perusal of the sales made by the assessee from unit III. Where R&D activities alleged to have been taken place not even a single sales made to the above referred parties. Thus assessee's claim that its continued R & D activity from the previous years has not resulted in any manufacturing/sales to any of the claims.

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7.0. Further, sales register of unit III shows substantial sales were done to its printing unit (unit-I) products were sold were parchment paper, creame woven paper other sales were made are majority of them are papers used from cheque printing (MLCR) with or without water mark of the banks like, Dena Bank, Indian Overseas Bank, Citi Bank etc. The assessee claim of indigenious papers invented and manufactured in its R&D unit cannot to accepted.

8.0. Considering the fact that assessee has not applied for any patent also shows that there were no such researched products made by the assessee. It is pertinent to note that no prudent businessman will not reap the benefits of R & D.

9.0. Assessee did not furnish any details about the researchers or skilled manpower employed for R&D work. Further, no expenditure on manpower is quantified for R & D work. Thus, it is evident assessee has not carried on any R & D work.

10.0. Assessee has not substantiated in whatsoever manner regarding how different is the machineries purchased are different from other paper manufacturing machines

11.0. Assessee's turnover has shown substantial increase from the last year's products it is evident from the director's report that the incurred in sales usually attributable to security paper (Cheque prints paper for the boulevards) which was manufactured in unit III. Such spurt in manufacturing/sales would not have been possible without engaging additional machinery. Thereby it is amply clear that

alleged machinery claimed to have been used for R& D work has been put to use for its regular paper manufacturing work.

12.0. In view of the above, assessee claim of Research & development cannot be acceptable, accordingly claim of capital expenditure u/s. 35(i)(iv) is disallowed and treated as normal capital expenditure and sum of Rs. 3,54,33,770/- has been added to the total income of the assessee.

5. Being aggrieved by the above addition, an appeal was preferred before the CIT(A) who confirmed the addition holding that the assessee had failed to establish that the machinery was used to carry out any kind of scientific research. The relevant findings of the CIT(A) are as under:

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7.2 In the present case it is very much apparent that the appellant has only installed a new Machine for the purpose of its regular manufacturing activities. Although by using the impugned machine the appellant has manufactured new products such as Abrasive papers, Kraft Paper, Brown & White Crepe Filter Paper, etc., it is also evident that the same machine has been primarily used in the normal manufacturing activities for producing other products which were manufactured by the appellant in the normal course of its business. In fact the AO has made a specific finding that consequent to the installation of the new machine the volume of business of the appellant company has increased substantially, which clearly indicate that the new machine was installed only for the purpose of increasing the manufacturing capacity of the appellant company. Therefore considering these facts and specifically in the absence of any evidence to show that the appellant had actually carried out any kind of scientific research activities which are in the nature of 'Systematic Investigation for increasing the knowledge base' it cannot be said that the new machine was utilized for the purpose of scientific research. Section 35(1)(iv) refers to expenditure of a capital nature on 'Scientific Research' related to the business carried on by the assessee. In the present case the appellant has completely failed to establish that the new machine was used to carry out any kind of 'Scientific Research'. Therefore the contention of the appellant cannot be accepted.

6. Being aggrieved, the assessee is in appeal before us. The learned AR of the assessee submitted that the assessee has carried on R&D activity relevant to the business of printing of security paper which is the business of the assessee. He also submitted that the machinery which was claimed to be used in the research and development activity was exclusively used by Research and activity development activity. On the direction from the bench, the learned AR of the assessee also furnished details of the personnel employed in R&D activity and the nature of work carried out by them and also the details of amount spent on plant and machinery employed in R&D activity etc. He further submitted that by reason of this activity, appellant-company has developed processing of manufacturing paper and also in the process of developing special paper like wet strength abrasive paper (contact) wet strength abrasive paper (unquotal), lab. Grade Filter paper and Gemman Ashless paper.

On the other hand, the learned Id.CIT(DR) placed reliance on the orders of the lower authorities.

7. We heard rival submissions and perused material on record. In this case, the assessee made a claim for deduction of Rs.3,54,00,000/- under

the provisions of clause (iv) of sub-section (1) of section 35 of the Act. The relevant provisions read as under:

***“Expenditure on scientific research.***

**35. (1)** *In respect of expenditure on scientific research, the following deductions shall be allowed—*

*(iv) in respect of any expenditure of a capital nature on scientific research related to the business carried on by the assessee, such deduction as may be admissible under the provisions of sub-section (2):*

***Provided*** *that the research association, university, college or other institution referred to in clause (ii) or clause (iii) shall make an application in the prescribed form and manner to the Central Government] for the purpose of grant of approval, or continuance thereof, under clause (ii) or, as the case may be, clause (iii) :*

***Provided further*** *that the Central Government] may, before granting approval under clause (ii) or clause (iii), call for such documents (including audited annual accounts) or information from the research association, university, college or other institution as it thinks necessary in order to satisfy itself about the genuineness of the activities of the research association], university, college or other institution and that Government may also make such inquiries as it may deem necessary in this behalf :*

***Provided also*** *that any notification issued, by the Central Government under clause (ii) or clause (iii), before the date on which the Taxation Laws (Amendment) Bill, 2006 receives the assent of the President†, shall, at any one time, have effect for such assessment year or years, not exceeding three assessment years] (including an assessment year or years commencing before the date on which such notification is issued) as may be specified in the notification:*

***Provided also*** *that where an application under the first proviso is made on or after the date on which the Taxation Laws (Amendment) Bill, 2006 receives the assent of the President†, every notification under clause (ii) or clause (iii) shall be issued or an order rejecting the application shall be passed within the period of twelve months from the end of the month in which such application was received by the Central Government.”*

The requirement of clause (iv) is that assessee should carry on scientific research relating to business carried on by the assessee and any capital expenditure incurred in carrying out such research shall be allowed as deduction under provisions of sub-section (2) of section 35. In the present case, AO denied the claim on account of failure of the assessee to

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produce details regarding nature of scientific research activity carried on by the assessee. Even in the proceedings before the CIT(A), assessee had failed to do so. But the AO had not brought any material on record rebutting the claim of the assessee. Further he had not even referred to any material to say that the assessee-company had not carried on any R&D activity which is relevant for the business carried on by the assessee-company. Therefore, in the interest of justice, we remand this issue back to the file of the AO to decide the issue in accordance with law after giving due opportunity of being heard to the appellant-company.

8. In the result, the appeal filed by the assessee is treated as partly allowed for statistical purposes.

*Order pronounced in the open court on 26<sup>th</sup> December , 2017*

Sd/-  
**(LALIET KUMAR)**  
**JUDICIAL MEMBER**

Place : Bengaluru  
D a t e d : 26/12/2017  
*srinivasulu, sps*

**Copy to :**

- 1 Appellant
- 2 Respondent
- 3 CIT(A)
- 4 CIT
- 5 DR, ITAT, Bangalore.
- 6 Guard file

sd/-  
**(INTURI RAMA RAO)**  
**ACCOUNTANT MEMBER**

By order

Senior Private Secretary  
Income-tax Appellate Tribunal  
Bengaluru