

IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI 'A' BENCH, MUMBAI.

Before Shri B.R. Baskaran (AM) & Smt. Kavitha Rajagopal (JM)

I.T.A. No. 1920/Mum/2020 (A.Y. 2009-10)
C.O. No. 129/Mum/2021 (A.Y. 2009-10)

M/s. Lupin Limited 7 th Floor, Kalpataru Inspire Off. Western Express Highway, Santacruz East Mumbai-400 055.	Vs.	DCIT, Circle-3(4) 29 th Floor Center 1, World Trade Centre Cuffee Parade Mumbai-400 005.
(Appellant)		(Respondent)

I.T.A. No. 395/Mum/2021 (A.Y. 2009-10)

ACIT, Circle-3(4) 29 th Floor Center 1, World Trade Centre Cuffee Parade Mumbai-400 005.	Vs.	M/s. Lupin Limited 7 th Floor, Kalpataru Inspire Off. Western Express Highway, Santacruz East Mumbai-400 055.
(Appellant)		(Respondent)

PAN : AAACL1069K

Assessee by	Shri Rajan Vora & Hemen Chandaria
Department by	Smt Shailja Rai & Shri Salil Mishra
Date of Hearing	10.11.2022
Date of Pronouncement	03.02.2023

ORDER

Per B.R.Baskaran (AM) :-

The cross appeals filed by the parties and the cross objection filed by the assessee are directed against the order dated 22-09-2020 passed by Ld CIT(A)-57, Mumbai and they relate to the assessment year 2009-10.

2. The assessee is engaged in the business of manufacture and sale of pharmaceuticals products. The assessee filed its return of income for the year under consideration u/s 139(1) of the Act on 30-09-2009 declaring total income of Rs.77.29 crores under normal provisions of the Act and declaring book profit of Rs.459.47 crores u/s 115JB of the Act. The return of income filed by the assessee was processed u/s 143(1) of the Act on 31-03-2011. Subsequently, it was selected for scrutiny by issuing notice u/s 143(2) of the Act on 13.06.2011. When the assessment was pending, search action took place in the hands of the assessee on 15.3.2012. Consequent thereto, the proceedings u/s 153A of the Act was initiated by issuing notice on 18-01-2013 and the present assessment order came to be passed.

3. During the course of search proceedings, a statement u/s 132(4) of the Act was recorded from

- (a) Shri Mahesh R Sanur, the cashier of the assessee company.
- (b) Shri Kamal Kishore Sharma, Managing Director of M/s Lupin Ltd.

During the course of operation of prohibitory order u/s 132(3) of the Act, a Statement was recorded u/s 132(4) from Shri Ramesh Swaminathan, President (Finance & Planning) also. Post search, a statement was recorded from Shri Ramesh Kumar Khaitan, Vice President (Taxation) u/s 131 of the Act on 10-05-2012. We are making reference to all these statements recorded, since the AO has placed reliance upon them.

4. Shri Mahesh R. Sanur, the cashier of the assessee company admitted in his statement that the company has given cheque payments to a commission agent named M/s Versatile Vintrade P Ltd and received cash back from the above said person, i.e., the assessee has been booking bogus expenses in the form commission expenses. He further admitted that an aggregate amount of Rs.37.43 crores represents total of unaccounted cash receipts for the period from 1.4.2009 to 31.12.2010. The Statement so given by Shri Mahesh R Sanur was confronted with the Managing Director Shri Kamal Kishore

Sharma. He confirmed the statement given by Shri Mahesh R Sanur and agreed to surrender a sum of Rs.37.43 crores for the period from 1.4.2009 to 31.12.2010. He also stated that the above said disclosure/surrender has been made after consultation with Shri K R Gupta, Director, Corporate Affairs of the assessee company. The Managing Director also admitted that the company has made transaction by way of mere book entries in other years also. Accordingly, he agreed to offer Rs.60.33 crores in aggregate in various financial years starting from F.Y 2004-05 to 2011-12. He also submitted that the above said sum of Rs.60.33 crores has been expended for various miscellaneous purposes. In this back ground, the AO completed the assessment by making various additions. The Ld CIT(A) granted partial relief and hence both the parties have filed appeals assailing the order passed by Ld CIT(A) on the issues decided against each of them.

5. We shall first take up the appeal filed by the assessee. On certain issues, both the parties are in cross appeals. Hence those common issues are adjudicated together, by pointing out the same.

6. The first issue urged by the assessee relates to the disallowance of unverified expenses. In the statement recorded u/s 132(4) of the Act, the assessee had admitted that it has claimed bogus commission expenses of Rs.4,76,34,543/- in Ay 2009-10. In the return of income filed for AY 2009-10 u/s 153A of the Act, the assessee has, however, admitted a sum of Rs.4,27,45,491/- only, being the commission payments made to M/s Agnes Bruno Limited and M/s Apsara Vanijya Limited amounting to Rs.3.12 crores and Rs.1.16 crores respectively. The assessee did not offer the payments made to following persons as its income:-

Sr. No.	Vendor Name	TIN No.	Amount (Rs.)
1	Chem Tech Associates	24220201320V	25,866
2	Paras Sales Corporation	24211400462V	8,94,204
3	Chemtech Automation Pvt. Ltd.	27030181564V	11,17,998

4	Apsara Power Laundry	N.A..	1,014
5	Pravin Electricals Pvt Ltd	27080276548V	5,07,620
6	Amar Enterprises	242U400713V	5,02,401
7	Paras Vijay	08752706343	14,35,218
8	Paras Ice Factory	23223605480V	3,19,196
9	Parasnath Agencies	23804102092V	85,535
	Grand Total		48,89,052

When questioned, the assessee submitted that it had booked bogus expenses by way of commission payments only and such commission payments have been duly offered in the return of income filed u/s 153A of the Act. It was submitted that the above said expenses aggregating to Rs.48,89,052/- are in the nature of actual expenses incurred under various heads and these expenses are not bogus in nature. It was submitted that these expenses have been wrongly taken as commission expenses at the time of search proceedings. It was submitted that these expenses are of general nature like consumables, laundry charges, spares, capital expenses etc. Accordingly, it was submitted that there was no requirement of surrendering Rs.48,89,052/- as the income of the assessee. The assessee contended that non-disclosure of Rs.48,89,052/- amounts to retraction from the statements given u/s 132(4) of the Act.

6.1 The AO did not accept the explanations given by the assessee. He noticed that the assessee has not filed any letter specifically retracting the statement given u/s 132(4) of the Act prior to filing of return of income. The AO, by placing reliance on the decision rendered by Mumbai bench of ITAT in the case of Urmila & Co Ltd (35 Taxmann.com 589) and held that the disclosure given in the sworn statements recorded u/s 132(4) of the Act cannot be ignored. Accordingly, the AO held that the amount of Rs.48,89,052/- is liable to be taxed. The AO noticed that the above said amount included capital expenses of Rs.9,86,470/-. Accordingly, he added difference amount of Rs.39,02,582/- (Rs.48,89,052/- (-) Rs.9,86,470/-) to the total income. The Ld CIT(A) also confirmed the same.

6.2 We heard the parties on this issue and perused the record. We notice that the main submission of the assessee is that it has booked bogus expenses in the form of commission payments only, i.e., there is no admission as regard to other expenses. It is the submission of the assessee that the expenses to the tune of Rs.48,89,052/- were also wrongly included in the commission expenses by the search team. These expenses are of general nature like consumables, laundry charges, spares, capital expenses etc. Before the AO, it has been clarified that the above said amount was not offered to tax as these are not bogus in nature. In support of these contentions, the assessee has furnished screen shot material statement and delivery challans on samples in respect of three vendors, viz., M/s Paras Sales Corporation, M/s Chemtech Automation P Ltd and M/s Paras Vijay.

6.3 The assessee also took a contention that it has retracted from the statement by not disallowing these expenses while computing total income at the time of filing return of income. We noticed that the search took place in the hands of the assessee on 15-03-2012 and the return of income was filed u/s 153A of the Act on 18.02.2013, i.e., almost after expiry of 11 months. The assessee did not submit any specific retraction letter. Hence the return of income filed by the assessee could be described as only deemed retraction.

6.4 In our view, we may leave aside the issue as to whether the said retraction is valid or not, since the assessee is supporting its stand for not disallowing these expenses on merits. In our view, the stand of the assessee, in the facts and circumstances of the case, merits acceptance. First of all, there is no dispute that the amount of Rs.48,89,052/- is not in the nature of commission expenses, i.e., the assessee has admitted that it has booked bogus expenses by way of commission payments only. Secondly, it has furnished the details of materials purchased through these bills, delivery challans etc., to prove receipt of materials. The assessee has also explained the reason as to why these expenses were not added to the total income while computing total income. We notice that the tax authorities have ignored all

these aspects on merits, but placed their reliance on the statement made u/s 132(4) of the Act. The provisions of sec.132(4) enables the assessing officer to presume that the admission made in the statement “may be” used in the assessment proceedings. It is well settled proposition of law that it is a rebuttable presumption, meaning thereby, the deponent could show that the admission made by him in the statement was wrong. In the instant case, in our view, the assessee has rebutted the admission by furnishing evidences in support of the expenses. The very same fact that a sum of Rs.9,86,470/- out of the above said expenditure amount of Rs.48,89,052/- represents Capital expenditure (which fact has also been accepted by the AO) would show that there is merit in the submission of the assessee. For booking bogus expenses, it is unlikely that anyone will account for bogus capital expenses. Accordingly, we are of the view that the explanation given by the assessee on this aspect merits acceptance. Accordingly, we set aside the order passed by Ld CIT(A) on this issue and direct the AO to delete the addition of Rs.39,02,582/-. Accordingly, we hold that the consequential disallowance of depreciation on the capital expenditure amount of Rs.9,86,470/- is also not warranted and we direct the AO accordingly.

7. The next issue urged by the assessee relates to the disallowance of bogus purchases of Rs.7,90,83,655/-. During the course of search proceedings, the assessee admitted in the statement recorded u/s 132(4) of the Act that it has accounted for bogus purchases to the tune of Rs.10,00,88,095/-. The party-wise details of the same are given by the AO in pages 12 and 13 of the assessment order. However, in the return of income filed u/s 153A of the Act, the assessee offered a sum of Rs.23,66,548/- only.

7.1 When questioned about the same, the assessee submitted that:-

(a) it has never admitted that the purchase transactions are bogus.

(b) It had offered/surrendered “input VAT credit” under protest u/s 48 and Rules 51-55 of Maharashtra Value Added Tax Act (MVAT) on technical reasons, i.e., the assessee may not be eligible for input VAT

credit, if the supplier has not paid VAT tax. Hence revised sales tax returns were filed before the MVAT authorities.

(c) On the basis of the revised sales tax returns only, the assessee surrendered the above said amount of Rs.10.00 crores at the time of search proceedings.

(d) Thereafter, the assessee carried out detailed analysis and found that most of the vendors name did not find place in the list of suspicious dealers disclosed by the MVAT department in its website. Accordingly, it filed "re-revised Sales tax returns" for the financial years 2006-07 to 2010-11. The above said re-revised sales tax returns were accepted by the MVAT authorities to the maximum extent, i.e., the genuineness of purchases were proved to the extent of Rs.9,77,21,547/-. The assessee could not reconcile the balance amount of Rs.23,66,548/- for want of certain details. Hence the same was offered to tax in the return of income filed u/s 153A of the Act.

7.2 The AO did not accept the contentions of the assessee for the following reasons:-

(a) The Investigation wing of department had investigated the transactions carried on by a person named Sri Naresh Kantilal Shah through various concerns in his name and in the name of his associates. He admitted in the statement recorded on 7.9.2021 that he has provided only accommodation entries through these concerns. It was noticed that the assessee herein has purchased materials from the concerns belonging to above said person to the tune of Rs.2.17 crores during the period from March, 2010 to February, 2011.

(b) During the course of search operations, the assessee (Managing Director of the assessee) has offered Rs.58.80 crores towards bogus purchases made during the period from AY 2005-06 to 2012-13. This was also confirmed by the President (finance & planning). During the post search enquiries, the Vice President (Taxation) offered additional income of Rs.1,17,92,093/- in respect of purchases made from four parties belonging to Global Impex Group.

(c) Placing reliance on the decision rendered by co-ordinate bench in the case of Urmila & Co Ltd vs. DCIT (35 taxmann.com 589), the AO held that the assessee has made bogus purchases to the tune of Rs.9,77,21,547/-. However, he noticed that this amount included certain capital expenses, DEPB purchases not debited to Profit and loss account. The AO held that the depreciation on capitalized amount is not allowable. Accordingly, the AO computed disallowable amount at Rs.7,90,83,655/- as under:-

Total amount of disclosure not offered to tax	-	9,77,21,547
Less:- Amounts capitalized	-	2,13,85,644
Less:- Purchase of DEPB licenses not debited to P & L Account	-	67,15,759
Add:- Depreciation disallowable		88,43,539
Add:- Additional amount offered by the assessee, Vide its letter dated 05.03.2014	-	6,19,972
Net amount of disallowance	-	7,90,83,655

The Ld CIT(A) has confirmed the above said disallowance.

7.3 We heard the parties on this issue and perused the record. We notice that the assessee has submitted that it has revised VAT returns under protest on 8th July, 2011, after Sales tax survey, since it would not get input VAT credit on the alleged bogus purchases. It is stated that on the basis of revised sales tax returns, it has agreed to surrender Rs.58.80 crores during the course of search towards bogus purchases in various years, which included Rs.10.00 crores pertaining to the year under consideration. However, it is stated that the assessee has noticed that the most of the vendors were not included in the final list of suspicious dealers published by MVAT authorities in its website. Hence, the assessee has re-revised its VAT returns after verification on 26th June, 2012, i.e., subsequent to the date of search. According to the assessee, the re-revised VAT returns has since been accepted by the VAT authorities. Accordingly, it was submitted that the surrender of income towards alleged bogus purchases was made on the basis of incomplete information and further on the reasons that the assessee was not able to prove the genuineness of purchases at that point of time.

7.4 With regard to the statement given by one of the vendors Shri Naresh Kantilal Shah, which was referred to by the AO, the assessee submitted that it has not made any purchases from the concerns belonging to the above said person during the year under consideration. On legal aspects, the assessee

has contended that the addition could not be made merely on the basis of statement given on oath.

7.5 The Id D.R, on the contrary, supported the orders passed by tax authorities on this issue.

7.6 We notice that the assessing officer has entirely placed his reliance on the statement given by the employees and directors of the assessee u/s 132(4) of the Act. Besides the above, the AO has also placed reliance on the statement given by Shri Naresh Kantilal Shah, one of the accommodation entry providers and also the statement given by the Vice President (Taxation). However, we notice that the surrender made by him was not added by the AO. We notice that the assessing officer did not examine the explanations of the assessee as to why it was constrained to make surrender towards alleged bogus purchases. Though there was no specific retraction of the surrender so made, yet we have noticed earlier that the surrender made in the statement recorded u/s 132(4) of the Act can be rebutted by producing evidences against the surrender. In the instant case, the additional evidences relied upon by the assessee to rebut the surrender are:-

- (a) Re-revised VAT returns.
- (b) VAT orders passed by the VAT authorities accepting the re-revised VAT returns,

The question of suspicious dealers came to fore only on the reason that these dealers did not deposit VAT tax after issuing accommodation bills. If the assessee could get VAT credit against these bills, then it may be possible to presume that the suppliers are genuine. Under these set of facts, it is claimed by the assessee that the surrender towards bogus purchases was made on the technical reason that the said suppliers have not paid VAT amount, which would disentitle the assessee to claim VAT credit and hence the assessee cannot effectively prove the genuineness of purchases. If the re-revised VAT returns have been accepted by the VAT authorities and the assessee got the credit of VAT amount, it is submitted that the entire

foundation on which the surrender was made got demolished. It is also submitted that these suppliers are not included in the list of suspicious dealers by MVAT authorities.

7.7 Under these set of facts, we are of the view that the assessee may be provided with one more opportunity to prove the genuineness of purchases. Accordingly, this issue requires fresh examination at the end of the AO, since the AO has not examined these factual aspects. In order to prove the genuineness the assessee may also furnish documents/details, on sample basis, to show that the relevant goods have been received and used by it. Accordingly, we set aside the order passed by Ld CIT(A) on this issue and restore the same to the file of AO for examining it afresh in the light of discussions made supra.

8. The next issue urged by the assessee relates to the claim for deduction expenses classified as "Prior Period Expenses" in the financial statements amounting to Rs.4,91,608/-. The details of Prior period expenses are given below:-

Parekh Cargo Logistics P Ltd (Agency charges, Parcel charges, Certification charges, licence Registration charges)	-	36,608
Khimji Kunverji & Co. (Internal audit fee)	-	4,25,000
Cirrus Media Research (Retainership charges)	-	30,000

		4,91,608
		=====

The assessee did not claim the above said expenses while computing return of income, but claimed the same before the AO. It was submitted that though the expenses were related to the earlier year, yet the liability has accrued and crystallized during the current year. Accordingly, it was claimed as deduction during the year under consideration. Since it was a new claim made without filing revised return of income, the AO rejected the same by

following the decision rendered by Hon'ble Supreme Court in the case of Goetze (India) Ltd vs. CIT (284 ITR 323)(SC).

8.1 We notice that the assessee did not contest the decision of AO rendered on this issue before Ld CIT(A). Even though this claim has been made without filing revised return of income, the Hon'ble Supreme Court has held in the very same case of Goetze (India) Ltd (supra) that its decision will not impinge the power of the Tribunal to admit additional ground. Since all the facts relating to this issue are available on record, we admit this ground and proceed to dispose of the same.

8.2 A perusal of the three expenses would show that they are in the nature of payment towards professional fees, meaning thereby, the corresponding professional services would have been availed by the assessee before the end of the relevant financial year. Hence, under the mercantile system of accounting, the assessee should have created provision for the expenses as at the yearend for all known expenses, even if the relevant bills have not been received by that point of time. The principle that the "liability accrued and crystallized during the year" would apply only to those cases, where the liability itself is in dispute and got finally settled in the subsequent years. Best example would be the dispute relating to "Wage increment", i.e., in the case of increase in wages, the liability to pay increment could be known only after settlement of dispute and hence it could be claimed only in the year in which the dispute is settled, i.e., an uncertainty should surround the liability itself in order to apply this principle. In the instant case, there is no uncertainty with regard to all the three items of expenses listed above. Hence, in our view, this principle will not apply. Accordingly, we are of the view that these expenses do not relate to the year under consideration and hence the claim of the assessee is liable to be rejected.

8.3 The assessee has made an alternative claim that the Tribunal may direct the AO to allow these expenses in the year to which it pertains to. In our view, the Tribunal does not have power to issue direction to the AO for a year, which is not before it. However, the assessee may move appropriate petition before the AO for making the additional claim in the year to which these expenses pertain to in accordance with law and the said petition may be considered in a liberal manner by the AO.

9. The next issue contested by the assessee as well as revenue relates to the disallowance made u/s 14A of the Act. This is a common issue in the appeals filed by both the parties. The facts relating to this issue are that the assessee earned exempt dividend income of Rs.19,57,249/- during the year under consideration. In the return of income, it disallowed a sum of Rs.89.79 lakhs u/s 14A of the Act consisting of interest disallowance of Rs.65.04 lakhs and expenditure disallowance of Rs.24.75 lakhs. However, during the course of assessment proceedings, the assessee claimed before the AO that it did not incur any expenditure in earning exempt dividend income and accordingly contended that no disallowance u/s 14A should be made. The AO refused to entertain a new claim in view of the decision rendered by Hon'ble Supreme Court in the case of Goetze (India) Ltd (supra).

9.1 Before Ld CIT(A), the assessee reiterated its contentions. The Ld CIT(A) directed the AO to restrict the disallowance u/s 14A of the Act to the amount of exempt income. Both the parties are aggrieved by the decision so rendered by Ld CIT(A) on this issue.

9.2 We heard the parties on this issue and perused the record. Even though the assessee has voluntarily disallowed higher amount of expenditure u/s 14A of the Act, in our view, the same may be amended, if the disallowance made by the assessee is not in accordance with the mandate of law under the principle that there is no estoppels against the law. It is the

submission of the assessee, the law relating to disallowance u/s 14A of the Act was at nascent stage and it has made disallowance as per its understanding at the relevant point of time. When the law on sec. 14A developed later, the assessee has sought correction of amount disallowed by it, as per the subsequent development of law. We find merit in the said claim of the assessee.

9.3 We notice that the assessee was having own funds of Rs.1124.62 crores and Rs.1421.23 crores as on 1.4.2008 and 31.3.2009 respectively. The value of investments stood at Rs.292.49 crores and Rs.473.87 crores as at the beginning and end of the year. Besides the above, the assessee has purchased and sold units of various mutual funds to the tune of Rs.133 crores. Thus, it can be seen that the own funds available with the assessee was more than the value of investments and hence it shall be presumed that the investments have been made out of own funds and in that case, there is no requirement of making any disallowance out of interest expenses as held by Hon'ble Bombay High Court in the case of HDFC Bank Ltd (2014)(366 ITR 505). Hence the interest disallowance made by the assessee is liable to be deleted.

9.4 With regard to the expenses, the contention of the Ld A.R is that the dividends were received directly into its bank account and hence no expense has been incurred in earning dividend income. However, we notice that the value of investments held by the assessee has increased by about 180 crores during the year under consideration. Besides the above, the assessee has purchased and sold mutual funds to the tune of Rs.133 crores. Hence it cannot be said that it did not use various resources of its business for the purpose of carrying above said activities. It is the submission of the assessee that the increase in investments is due to increase in shares of foreign subsidiaries, whose dividend income is taxable, meaning thereby the exempt income has been earned mainly from units of mutual fund. Considering the

investments in mutual funds and earning dividend income from them, we are of the view that the provisions of Rule 8D(2)(iii) should not be applied. Accordingly, in the facts and circumstances of the case, we are of the view that the disallowance to be made u/s 14A may be estimated. Accordingly, we direct the AO to disallow 15% of the exempt income and in our view, the same would meet the requirements of sec. 14A of the Act. We order accordingly.

10. The next ground urged by the assessee relates to the claim for deduction of "Provision for bad and doubtful debts" from the Net profit while computing book profit u/s 115JB of the Act. The facts relating thereto are that the assessee had created "Provision for bad and doubtful debts" of Rs.23.50 million in the Profit and loss account. While filing return of income, the assessee computed "book profit" as required u/s 115JB of the Act and the said provision mandates that any "Provision created for diminution in the value of assets" should be added to the Net Profit, if it is debited to the Profit and Loss account. Accordingly, the assessee added the above said amount of Rs.23.50 million to the Net profit as per the above said provision.

10.1 Before the AO, the assessee took a different stand and contended that the "Provision for bad and doubtful debts" should not be added to the Net profit. Since a new claim was made without filing revised return of income, the AO rejected the same, following the decision rendered by Hon'ble Supreme Court in the case of Goetz (India) Ltd (supra). In the appellate proceedings, the Ld CIT(A) held that there is a specific provision in clause (i) to Explanation (1) to sec. 115JB of the Act to add back "any amount set aside as provision for diminution in the value of any assets", i.e., it is the view of the Ld CIT(A) that the "Provision for bad and doubtful debts" would fall under this category and hence, the assessee has rightly added the above said amount while computing book profit at the time of filing of return of income.

Since the assessee has taken a different stand before the tax authorities, the Ld CIT(A) rejected the claim of the assessee.

10.2 It is the contention of the assessee that the “Provision for bad and doubtful debts” debited to the Profit and loss account has been reduced from “Sundry debtors” balance and the net amount of ‘Sundry debtors balance’ was only shown in the “assets side” of Balance Sheet. Relying upon following decisions rendered by Hon’ble High Courts, the ld A.R contended that the provision for bad and doubtful is not required to be added to net profit, if it is reduced from the amount of Sundry debtors, as it has been interpreted by Hon’ble High Courts that such kind of treatment would amount to write off and such kind of actual write off would not be hit by clause (i) of the explanation to sec. 115JB of the Act.

- (a) CIT vs. Vodafone Essar Gujarat Ltd (2017)(397 ITR 55)(Guj)
- (b) ACC Ltd (2019)(112 taxmann.com 402)(Bom)
- (c) Sun Pharmaceuticals Ltd (2017)(87 taxmann.com 215)(Guj)
- (d) Yokogawa Ltd (2012)(204 Taxman 305)(Kar)

10.3 The Ld DR, on the contrary, submitted that there is vast difference between “actual write off of debts” and “Provision created for bad and doubtful debts”. The ld D.R submitted that Hon’ble Gujarat High Court has taken the view that the reduction of “Provision for bad and doubtful debts” from ‘Sundry Debtors’ balance shown in the Assets side of Balance sheet resulted in obliterating such provision from its accounts. The Ld D.R submitted that the meaning of the term “obliterate” has been defined in Cambridge dictionary as “to remove all signs of something, either by destroying it or by covering it so that it cannot be seen”. The Ld CIT-DR submitted that, in the instant case, the Provision for bad and doubtful debts does not obliterate the corresponding debt merely for the reason that the same is reduced from the Sundry debtors balance in the Balance Sheet, i.e., it was only a method of presenting the accounts. In the books of accounts,

the Provision for bad and doubtful debts account have been maintained separately and no part of debts got obliterated in the books of accounts. Inviting our attention to the Schedule of Sundry debtors given in Schedule 8 of the Annual report, the Ld D.R submitted that the amount reduced towards “provision for doubtful debts” was shown as 30 million as on 31.3.2008 and it has increased to 53.50 million as on 31.3.2009, i.e, by the amount of Rs.23.50 million created towards “Provision for doubtful debts” during the current year. This fact amply clears that the assessee is keeping “Provision for bad and doubtful debts” separately and it did not obliterate the corresponding debt at all in its books of account. Accordingly, the Ld CIT-DR contended that the “Provision for bad and doubtful debts” squarely falls under the category of “Provision for diminution in the value of assets” and hence the same was rightly added by the assessee itself in its return of income and by the tax authorities also.

10.4 We heard rival contentions and perused the record. There should not be any dispute that the “total income” is computed in accordance with the provisions of Income tax Act and for computing “total income”, the entries made in the books of accounts are not relevant. For computing “book profit” u/s 115JB of the Act, the annual accounts are required to be prepared as per the Companies Act, which require preparation of annual accounts as per established accounting policies, accounting standards. It is well settled that, under the accounting principles, the expression “Provision for bad and doubtful debts” and “write off of bad debts” connote two different meaning. The expression “write off of bad debts” represents actually writing of debts as bad in the books of account, meaning thereby, the debt itself is removed permanently from the accounts of the assessee. On the contrary, the expression “Provision for bad and doubtful debts” represents expected loss in realization of debts. Under the accounting concept of “Prudence”, it is required to make provision for all known expenses and losses, even if has not been actually paid. Even if the actual amount is not known, it is necessary to

make provision on estimated basis in order to make the accounts true and fair. All the companies make “Provision for bad and doubtful debts” under Prudence principle, since it is quite natural that some portion of debt could not be realized.

10.5 While preparing financial statements, two methods of presentation are followed while preparing Balance Sheet. First method is to show “Provision for bad and doubtful debts” in the liability side of Balance Sheet as part of “Provisions and liabilities”. The other method is to reduce the “provision for bad and doubtful debts” from Sundry debtors balance in the Assets side of Balance Sheet.

10.6 Clause (i) of Explanation 1 to sec. 115JB states that “the amount or amounts set aside as provision for diminution in the value of any asset” should be added to the Net profit while computing book profit. The case of the revenue is that the “Provision for bad and doubtful debts” falls under this category, since it only represents a provision created for diminution in the value of “sundry debtors”. As per the accounting principles, the contentions of the revenue is correct, since “actual write off bad debts” and “provision for bad and doubtful debts” are different, having two different meanings under the Accounting Principles.

10.7 But the question that arises in the context of Income tax Act is whether the meaning or character of “Provision for bad and doubtful debts” would undergo a change, merely a different method of presentation of accounts is made while preparing Balance Sheet, i.e., if it was shown as reduction from the value of “sundry debtors balance” in the assets side of Balance Sheet instead of showing the same in the liability side of Balance Sheet as part of “Provision and liabilities”? We should keep in mind that all the assessee usually maintain separate ledger account for “Provision for bad and doubtful debts account” in its books of account. In the instant case

also, the Provision for bad and doubtful debts account was having opening balance of Rs.30 million and the new provision created during the year amounting to Rs.23.50 million was added to it and the closing balance was shown at Rs.53.50 million. Hence, in this case also, the assessee has kept separate ledger account for "Provision for bad and doubtful debts" and the same is carried forward year after year.

10.8 We notice that the Hon'ble Gujarat High Court in the case of CIT vs. Vodafone Essar Gujarat Ltd (supra) and the Hon'ble Karnataka High Court, in the case of Yokogawa Ltd (supra) has expressed the view that the "Provision for bad and doubtful debts", if reduced from the amount of "Sundry debtors balance" in the assets side of Balance Sheet would amount to actual write off of bad debts and accordingly, it would not be hit by clause (i) of Explanation 1 to sec.115JB of the Act. Both the High Courts have followed the decision rendered by Hon'ble Supreme Court in the case of Vijaya Bank (323 ITR 166)(SC). The Hon'ble Apex Court was considering the provisions of sec.36(1)(vii) r.w.s 36(2) of the Act in the context of a banking company. Under the provisions of sec.36(1)(vii) of the Act, an assessee is eligible to claim deduction of "amount of any bad debt or part thereof which is **written off as irrecoverable** in the accounts of the assessee". Explanation 1 to sec. 36(1)(vii) reads as under:-

"Explanation 1:- For the purposes of this clause, any bad debt or part thereof written off as irrecoverable in the accounts of the assessee shall not include any provision for bad and doubtful debts made in the accounts of the assessee".

The above said explanation recognized the distinction between "actual write off bad debts" and "Provision for bad and doubtful debts". The Hon'ble Supreme Court, in the case of Vijaya Bank and after considering Explanation 1 to sec. 36(1)(vii), has held that the reduction of "Provision for bad and doubtful debts" from the "Loans and Advances" account would meet the requirements of sec. 36(1)(iii), viz., "written off as irrecoverable".

10.9 We noticed earlier that the total income is computed in accordance with the provision of Income tax Act and “Book profit” is computed on the basis of financial statements prepared in accordance with the accounting principles and accounting standards. Even though the decision in the case of Vijaya Bank (supra) was rendered by Hon’ble Supreme Court in the context of sec. 36(1)(vii) of the Act relating to computation of income, the Hon’ble High Courts have chosen to extend the said principle laid down by Hon’ble Supreme Court to computation of “book profit” u/s 115JB of the Act, wherein the accounting principles and accounting standards acquire prime importance. Following the decision rendered by High courts (referred supra), we hold that the amount of “Provision for bad and doubtful debts”, if reduced from the amount of “Sundry debtors balance” in the assets side of Balance Sheet, the same would not be hit by clause (i) of Explanation 1 to sec.115JB of the Act. Accordingly, we set aside the order passed by Ld CIT(A) on this issue and direct the AO not to add the amount of Provision for bad and doubtful debts to net profit, while computing book profit u/s 115JB of the Act.

11. The next issue, which is common in the appeal of the assessee and revenue, is the disallowance of commission expenses paid to M/s Tuticorin Trexim P Ltd. During the course of search proceedings, the AO received information from DGIT (Inv), Mumbai in respect of commission of Rs.152.26 lakhs paid to M/s Tuticorin Trexim P Ltd, which was considered to be an accommodation entry. When questioned, the assessee submitted that it has paid a sum of Rs.143.50 lakhs only to the above said concern during the financial year 2008-09 relevant to the year under consideration. The assessee further submitted that the above said amount has been offered to tax by it in the succeeding assessment year 2010-11. It was also submitted that there is no requirement to make disallowance again, since the tax has been charged in both the years upon the assessee only on book profits computed u/s 115JB of the Act. The AO did not accept the contentions of

the assessee and accordingly added a sum of Rs.152.26 lakhs to the total income. The Ld CIT(A) directed the AO to restrict the disallowance to Rs.143.50 lakhs and rejected the claim of the assessee that the very same amount offered in AY 2010-11 should be excluded. Both the parties are aggrieved.

11.1 We heard the parties and perused the record. There should not be any dispute that the amount of disallowance cannot exceed the amount debited to the Profit and Loss account. During the year under consideration, the assessee has claimed a sum of Rs.143.50 lakhs as commission expenses. Hence the Ld CIT(A) was justified in holding that the disallowance should be restricted to Rs.143.50 lakhs. At the same, it is the claim of the assessee that the above said amount of Rs.143.50 lakhs has been inadvertently offered as income in AY 2010-11. If that is the case, there is merit in the submission of the assessee that it would result in double taxation of same item of income, which is not permitted under the law.

11.2 It is settled principle that each year is different and the income of one year cannot be taxed in another year. Since the commission amount of Rs.143.50 lakhs has been claimed in AY 2009-10 and since the assessee itself has accepted the same to be bogus, the disallowance of above said expense has been rightly made in AY 2009-10 only. It cannot be shifted to any other year. However, if the very same amount has been offered voluntarily by the assessee as its income in the succeeding AY 2010-11, the assessee may move appropriate petition before tax authorities in accordance with law seeking exclusion of Rs.143.50 lakhs in that year.

12 The assessee has raised an additional ground with regard to the claim for deduction u/s 10B of the Act. In this ground, it is contended that the deduction u/s 10B of the Act should be computed with reference to Profits and gains derived by 100% Export Oriented Units (Pril, Oral and Goa) from

exports without deducting allowances under the Income tax Act, i.e., the claim of the assessee is that the deduction should be allowed on commercial profits. In this regard, the assessee has placed its reliance on the decision rendered by co-ordinate bench of Tribunal in the case of Reliance Industries Ltd (ITA No.7299 & 136/Mum/2017 dated 10th November, 2020). The Ld D.R submitted that the above said issue is a new ground taken by the assessee before the Tribunal. Inviting our attention to sec.10B(6) of the Act, the ld D.R submitted that this sub-section contemplates that the depreciation and other allowances should be allowed and even if the assessee did not claim deduction u/s 10B in any of the year, then the depreciation and other allowances are deemed to have been allowed. Accordingly, the Ld D.R submitted that the intention of the legislature is that the depreciation and other allowances are to be deducted from the profits and the deduction shall be allowed thereon. Accordingly, the ld D.R submitted that this issue may be restored to the file of AO for examining it.

12.1 We heard the parties on this issue and perused the record. Since the assessee is raising an altogether new issue, which has not been examined by the tax authorities, the ld D.R submitted that this claim of the assessee requires examination at the end of AO. We agree with the submission made by Ld D.R. Accordingly, we restore this issue to the file of AO for examining this claim of the assessee.

13. We shall now take up the appeal filed by the revenue. The first issue contested by the revenue relates to the disallowance of mark to market loss of Rs.3,39,71,181/- made by the AO and deleted by Ld CIT(A). The assessee is supporting the decision rendered by Ld CIT(A) on this issue in the cross objections filed by it. The assessee had revalued the derivative contracts outstanding as at the yearend in respect of foreign exchange receivables. The same resulted in a loss of Rs.3.39 crores and it was claimed by the assessee has deduction. The AO disallowed the claim by placing reliance on CBDT

Instruction no.3/2010 and holding it as notional loss. The Ld CIT(A) noticed that an identical disallowance made by the AO in AY 2008-09 has been deleted by the Tribunal in ITA No.7513 & 7274/Mum/2014 and the same has been affirmed by the Hon'ble Bombay High Court in ITA No.1532 of 2017 dated 2nd April, 2019. Accordingly, the Ld CIT(A) deleted this disallowance. The revenue is aggrieved.

13.1 We heard the parties on this issue and perused the record. It is the submission of the assessee that the forward contracts have been entered to cover future export receivables. The break-up details of above said loss are given as under by the assessee:-

M to M Loss in relation to effective portion of Forward Contract outstanding on 31.3.09	-	42,53,527
M to M Loss in relation to ineffective portion of Option contract outstanding on 31.3.09	-	39,97,341
M to M Loss in relation to derivative asset w/off relating to Option Contract	-	2,66,20,000

		3,48,70,868
Less:- Reversal of M to M Loss in relation to Ineffective portion of Option contract		8,99,687

Net amount of claim		3,39,71,181
		=====

13.2 The Ld A.R submitted that an identical issue has been examined by the Tribunal in the assessee's own case in AY 2008-09 and it has been decided in favour of the assessee following the decision rendered by Hon'ble jurisdictional Bombay High Court in the case of CIT vs. M/s D Chetan & Co (ITA No.278 of 2014 dated 01-10-2016)([2016] 75 taxmann.com 300 (Bombay)). We also notice that the decision rendered by the Tribunal in the assessee's own case has since been upheld by Hon'ble Bombay High Court, vide its order dated 2nd April, 2019 in ITA No.1532 of 2017. In the case of M/s D Chetan & Co. (supra), the Hon'ble Bombay High Court held as under:-

“5. Being aggrieved, the Revenue preferred an appeal to the Tribunal. The impugned order of the Tribunal upheld the finding of the CIT (Appeals) that the loss incurred by the Respondent Assessee was a revenue loss and not connected with any speculation activities. **The Tribunal found that the transaction of forward contract had been entered into for the purpose of hedging in the course of its normal business activities of import and export of diamonds.** Thus, the Revenue's appeal was dismissed by the impugned order of the Tribunal.

6. Mr. Malhotra, learned Counsel appearing for the Revenue submits that this appeal had to be admitted as the impugned order has ignored its order in the case of S. Vinodkumar Diamonds (P.) Ltd. v. Addl. CIT [\[2013\] 59 SOT 124/35 taxmann.com 337 \(Mum. - Trib.\)](#) rendered on 3 May 2013 which on similar facts is in favour of the Revenue. He further submits that the impugned order of the Tribunal is suspect because it accepts the Respondent assessee's claim without calling upon it to prove that the same was not speculative. Lastly, he sought to place reliance upon Accounting Standard-11 to claim that such a loss is not allowable thereunder.

7. The impugned order of the Tribunal has, while upholding the finding of the CIT (Appeals), independently come to the conclusion that the transaction entered into by the Respondent assessee is not in the nature of speculative activities. **Further the hedging transactions were entered into so as to cover variation in foreign exchange rate which would impact its business of import and export of diamonds.** These concurrent finding of facts are not shown to be perverse in any manner. In fact, the Assessing Officer also in the Assessment Order does not find that the transaction entered into by the Respondent assessee was speculative in nature. It further holds that at no point of time did Revenue challenge the assertion of the Respondent assessee that the activity of entering into forward contract was in the regular course of its business only to safeguard against the loss on account of foreign exchange variation. Even before the Tribunal, we find that there was no submission recorded on behalf of the Revenue that the Respondent assessee should be called upon to explain the nature of its transactions. Thus, the submission now being made is without any foundation as the stand of the assessee on facts was never disputed. So far as the reliance on Accounting Standard-11 is concerned, it would not by itself determine whether the activity was a part of the Respondent-assessee's regular business transaction or it was a speculative transaction. On present facts, it was never the Revenue's contention that the transaction was speculative but only disallowed on the ground that it was notional. Lastly, the reliance placed on the decision in S. Vinodkumar Diamonds (P.) Ltd. (supra) in the Revenue's favour would not by itself govern the issues arising herein. This is so as every decision is rendered in the context of the facts which arise before the authority for adjudication. Mere conclusion in favour of the Revenue in another case by itself would not entitle a party to have an identical relief in this case. In fact, if the Revenue was of the view that the facts in S. Vinodkumar (supra) are identical/similar to the present facts, then

reliance would have been placed by the Revenue upon it at the hearing before the Tribunal. The impugned order does not indicate any such reliance. It appears that in S. Vinodkumar Diamonds (P.) Ltd. (supra), the Tribunal held the forward contract on facts before it to be speculative in nature in view of Section 43(5) of the Act. However, it appears that the decision of this court in CIT v. Badridas Gauridu (P.) Ltd. [\[2003\] 261 ITR 256/\[2004\] 134 Taxman 376 \(Mum.\)](#) was not brought to the notice of the Tribunal when it rendered its decision in S. Vinodkumar Diamonds (P.) Ltd. (supra). **In the above case, this court has held that forward contract in foreign exchange when incidental to carrying on business of cotton exporter and done to cover up losses on account of differences in foreign exchange valuations, would not be speculative activity but a business activity.**

8. In the above view, the question of law, as formulated by the Revenue, does not give rise to any substantial of law. Thus, not entertained.”

The Ld CIT(A) has followed the decision rendered by Hon’ble jurisdictional High Court and has decided this issue in favour of the assessee.

13.3 We notice from the break-up details of the claim extracted above, the M to M loss on “forward contracts” was Rs.42.53 lakhs. The other two items relate to “ineffective Option Contracts” and “Derivative asset w/off relating to option contracts”. The nature of these items is not clear and we notice that no tax authority has examined these items. If these transactions have been entered in the course of carrying on of regular business activities and the underlying assets are trading items, the loss arising on their revaluation at the year end is allowable as deduction. It is to be seen that the underlying assets having foreign currency exposure is also revalued as at the year end. Accordingly, for the limited purpose of verifying these factual aspects, we restore this issue to the file of the AO for examining this issue in the light of principles laid down by Hon’ble jurisdictional Bombay High Court in the case of D Chetan & Co (supra).

14. The second issue contested by the revenue relates to the disallowance of claim made u/s 35(2AB) of the Act. The assessee had incurred expenses amounting to Rs.42.58 crores on Clinical trials, Analytical charges and Bio

Analysis and Bio Equivalence studies outside its in-house approved/recognised R&D facility. The assessee did not claim this amount as deduction u/s 35(2AB) of the Act in the return of income filed by it, but only appended a note explaining the details. Before the AO, during the course of assessment proceedings, the assessee claimed that the above said expenditure is eligible for weighted deduction u/s 35(2AB) of the Act. The AO noticed that the above said expenditure has not been approved by DSIR in Form No.3CL dated 11.7.2012 issued by it. Further, the assessee has put up this new claim without filing a revised return of income, which is against the decision rendered by Hon'ble Supreme Court in the case of Goetze (India) Ltd (supra). Accordingly, the AO rejected the claim of the assessee.

14.1 The Ld CIT(A) noticed that the Ahmedabad bench of Tribunal in the cases of Cadila Pharmaceuticals vs. ACIT (2012)(25 taxmann.com 519) and the Hon'ble Gujarat High Court in CIT vs. Cardila Healthcare Ltd (2013)(31 taxmann.com 300) has held that the term "in-house" research used in section 35(2AB) must be viewed in the context in which it has been used by the Legislature. If research is conducted within the organization through utilization of external use of resources or staff, it can be stated to fall within the meaning of in-house research. The ld CIT(A) also noticed that similar views have been expressed in the following cases:-

- (a) ACIT vs. Torrent Pharmaceuticals (ITA No.3569/Ahd/2004)(Ahd)
- (b) Sun Pharmaceuticals Industries Ltd (111 taxmann.com 218)(Ahd)
- (c) DCIT vs. Aurobindo Pharma Ltd (ITA No.1604 & 1605/Hyd/2016)(Hyd).

Accordingly the Ld CIT(A) held that the expenditure spent outside the facility, but necessarily incurred for the purpose of 'in-house' research is allowable u/s 35(2AB) of the Act. Accordingly, he directed the AO to allow weighted deduction.

14.2 The Ld D.R submitted that the deduction u/s 35(2AB) is allowable only in respect of expenditure incurred in-house only. It has been held so by the Tribunal in the following cases:-

- (a) Concept Pharmaceuticals Ltd vs. ACIT (2011)(43 SOT 423)(Mum)
- (b) MAHLE Behr India (P) Ltd vs. DCIT (130 taxmann.com 7)(Pune)

The Ld D.R further submitted that the expenses incurred outside the in-house facility has not been certified by DSIR in Form no.3CL. The Ld CIT-DR further submitted that the assessee has furnished the details of approval granted by DSIR in Form 3CM to various research facilities created by the assessee, which are placed at pages 817 to 820 of the paper book. She submitted that many research facilities have not been approved for the year under consideration. Accordingly, the Ld DR submitted that, on these counts also, the assessee is not eligible for deduction u/s 35(2AB) of the Act.

14.3 We heard the rival contentions and perused the record. In our view, following questions arises on this issue in respect of the claim u/s 35(2AB) of the Act made by the assessee:-

- (a) Whether expenditure incurred on clinical trials, bioequivalence studies *outside the in-house facility* is eligible for weighted deduction u/s 35(2AB) of the Act?
- (b) Whether the weighted deduction u/s 35(2AB) could be allowed during the year under consideration, even if the expenditure has not been certified by DSIR in Form no.3CL?
- (c) Whether expenditure incurred prior to the date of approval could be allowed as deduction?
- (d) Whether the deduction u/s 35(2AB) could be allowed in the absence of approval of scientific research in-house facility by DSIR?

14.4 With regard to the first question, conflicting views have been expressed by different benches of the Tribunal. However, Hon'ble Gujarat

High Court has considered this issue as under in its decision reported in the case of Cadila Healthcare Ltd (2013)(31 taxmann.com 300)(Guj) as under:-

“11.Revenue has also suggested following question :

"D. Whether the Appellate Tribunal has substantially erred in holding that the expenses incurred outside the approved R&D facility would also get weighted deduction based on the word under "on in house" interpreting contradictorily to the finding of coordinate bench in *Concept Pharmaceuticals Ltd. v. ACIT* (ITAT, Mum) reported at [43 SOT 423?](#)"

12. We may record that question 'E' in the appeal memo is an additional question which has an element of above noted question. We have, therefore, not separately reproduced the same in this order. The issue is whether the assessee who has incurred expenditure for scientific research, which was not in the in-house facility, could be covered for deduction under section 35(2AB) of the Income Tax Act, 1961.

13. More or less, facts are not in dispute. The assessee carried out scientific research in its facility approved by the prescribed authority. It incurred various expenditure including on clinical trials for developing its pharmaceutical products. These clinical trials were conducted outside the approved laboratory facility. The Revenue holds a belief that such expenditure not having been incurred in the approved facility cannot form part of the deduction provided under section 35(2AB) of the Act. The Tribunal observed that the term 'in-house' used in section 35(2AB) of the Act must be viewed in the context of which it has been used. If by utilizing the staff or resources of an organization, research is conducted within the organization rather than through utilization of external use of resources or staff, it can be stated to be an in-house research. On such basis, the Tribunal rejected the Revenue's contention that merely because an expenditure which was not incurred in the in-house facility cannot be discarded for the weighted deduction under section 35(2AB) of the Act. Learned counsel for the Revenue, however, strongly relied on the certificate issued by the Prescribed Authority, which segregated the expenditure in two parts, that incurred in in-house facility and that incurred outside.

14. In our opinion, the Tribunal committed no error. Section 35(2AB) of the Act provides for deduction to a company engaged in business of biotechnology or the business of manufacture or production of any article or thing notified by the Board towards expenditure of scientific research development facility approved by the prescribed authority. Such deduction at the relevant time was one-and-a-half times expenditure which has now been increased to twice the eligible expenditure. We may notice that explanation to section 35(2AB)(1) which was introduced by the Finance Act 2001 with effect from 1.4.2002 reads as under:

"Explanation - For the purposes of this clause, "expenditure on scientific research" in relation to drugs and pharmaceuticals, shall include expenditure incurred on clinical drug trial, obtaining approval from any regulatory authority under any Central, State or Provincial Act and filing an application for a patent under the Patents Act, 1970 (39 of 1970)."

15. Such explanation thus provides that for the purpose of said clause, i.e. clause (1) of section 35(2AB), expenditure on scientific research in relation to drugs and pharmaceuticals shall include expenditure incurred on clinical drug trial, obtaining approval from any regulatory authority under the Central, State or Provincial Act and filing an application for a patent under the Patents Act, 1970.

16. The whole idea thus appears to be to give encouragement to scientific research. By the very nature of things, clinical trials may not always be possible to be conducted in closed laboratory or in similar in-house facility provided by the assessee and approved by the prescribed authority. Before a pharmaceutical drug could be put in the market, the regulatory authorities would insist on strict tests and research on all possible aspects, such as possible reactions, effect of the drug and so on. Extensive clinical trials, therefore, would be an intrinsic part of development of any such new pharmaceutical drug. It cannot be imagined that such clinical trial can be carried out only in the laboratory of the pharmaceutical company. If we give such restricted meaning to the term expenditure incurred on in-house research and development facility, we would on one hand be completely diluting the deduction envisaged under sub-section (2AB) of section 35 and on the other, making the explanation noted above quite meaningless. We have noticed that for the purpose of the said clause in relation to drug and pharmaceuticals, the expenditure on scientific research has to include the expenditure incurred on clinical trials in obtaining approvals from any regulatory authority or in filing an application for grant of patent. The activities of obtaining approval of the authority and filing of an application for patent necessarily shall have to be outside the in-house research facility. Thus the restricted meaning suggested by the Revenue would completely make the explanation quite meaningless. For the scientific research in relation to drugs and pharmaceuticals made for its own peculiar requirements, the Legislature appears to have added such an explanation.

17. In the case *Dy. CIT v. Mastek Ltd.* [\[2012\] 210 Taxman 432/25 taxmann.com 133 \(Guj.\)](#) and connected matters, a Division Bench of this Court had touched on the aspect of what can be termed as scientific research. In the context, certain observations made by the Bench may be of some relevance.

"25. It can thus be seen that the term scientific research in the context of the deduction allowable under section 35(1) of the Act would include wide variety of activities. It can also be appreciated that every scientific research need not necessarily result into the ultimate goal with which it may have been undertaken. Often times

in the field of research and invention, the efforts undertaken may or may not yield fruitful results. What is to be ascertained is whether any scientific research was undertaken and not whether such scientific research resulted into the ultimate aim for which such research was undertaken. It can be easily envisaged that the scientific research undertaken often times would completely fail to achieve desired results. That by itself does not mean that no scientific research was undertaken. What the Legislature desired to encourage by granting deduction under section 35(1) of the Act was a scientific research and not necessarily only the successful scientific research undertaken by an assessee."

18. We are, therefore, of the opinion that the Tribunal committed no error. Merely because the prescribed authority segregated the expenditure into two parts, namely, those incurred within the in-house facility and those can were incurred outside, in our opinion, by itself would not be sufficient to deny the benefit to the assessee under section 35(2AB) of the Act. It is not as if that the said authority was addressing the issue for deduction under section 35(2AB) of the Act in relation to the question on hand. The certificate issued was only for the purpose of listing the total expenditure under the Rules. Therefore, no question of law arises."

It can be noticed that the Hon'ble Gujarat High Court, after making extensive discussion on the issue and after holding that the Tribunal has committed no error, refused to admit the issue by observing no question of law arises. The revenue has challenged before Hon'ble Supreme Court the decision of Hon'ble Gujarat High Court in holding that no question of law arises. The Hon'ble Apex Court, vide its order dated 14th October, 2015 passed in SLP (c) No.770/2015 has directed the Hon'ble Gujarat High Court to admit the question of law and hear the revenue. However, no other order, if any, passed by Hon'ble Gujarat High Court was brought to our notice on the issue under our consideration in pursuance of the directions given by Hon'ble Supreme Court. In this connection, we may gainfully refer to the decision rendered by co-ordinate bench of Hyderabad in the case of DCIT vs. Aurobindo Pharma Limited (supra), wherein the effect of direction given by Hon'ble Supreme Court was examined and it was observed as under:-

"..... As seen from the order of the Supreme Court in Special Leave to Appeal (C) No.770/2015, dated 13.10.2015, the grievance of Revenue with reference to non-framing of three questions were considered by the Hon'ble Supreme Court as those three questions are considered to 'substantial question of law' and referred to the Hon'ble High Court to hear

the aforesaid three questions of law. However, the judgement already passed by the Gujarat High Court has not been set-aside....”

The Hyderabad bench of Tribunal also distinguished the decision rendered by the Mumbai bench of Tribunal in the case of Concept Pharmaceuticals Ltd (supra) by observing as under:-

“We have considered rival contentions and perused the case law placed on record. In the decision of Concept Pharmaceuticals Ltd (supra) the Coordinate bench did not allow the expenditure spent outside the R & D unit but the Bench has not considered the explanation introduced with reference to ‘Clinical Trials’. By very nature, the Clinical Trials cannot alone be done within research facility as they require cooperation from the Medical Doctors, Hospitals, Volunteers and patients, therefore such expenditure has to be necessarily spent outside the facility, but for the purpose of ‘in-house’ research. This issue was examined by the Coordinate Bench which was subject matter of appeal before the Gujarat High Court and Gujarat High Court has approved the same.....”

Accordingly, following the decision of Hon’ble Gujarat High Court, we hold that the amount spent by the assessee on clinical trials outside the approved in-house facility is eligible for weighted deduction u/s 35(2AB) of the Act.

14.5 The next question is Whether the weighted deduction u/s 35(2AB) could be allowed during the year under consideration, even if the expenditure has not been certified by DSIR in Form no.3CL?. The ld D.R placed her reliance on the decision rendered by Hon’ble Karnataka High Court in the case of Tejas Network Ltd (2015)(60 taxmann.com 309)(Kar), wherein it was held that the AO cannot sit in judgment over the report submitted by prescribed authority. Accordingly, the Ld D.R submitted that the AO has to necessarily follow the report given by the prescribed authority. The Ld D.R submitted that, in the instant case, the DSIR (Prescribed authority) has not certified the expenses incurred outside the in-house facility and the AO could not sit in judgment over the said report. Accordingly, the Ld D.R submitted that the unapproved expenses cannot be allowed deduction u/s 35(2AB) of the Act.

14.6 The next question is whether expenditure incurred prior to the date of approval could be allowed as deduction? Both these questions are answered together.

14.7 The legal sanctity of Form no.3CL was examined by the Pune bench of ITAT in the case of Cummins Ltd vs. DCIT (ITA No.309/Pun/2014 dated 15.5.2018 relating to AY 2009-10). It was held as under:-

"45. The issue which is raised in the present appeal is that whether where the facility has been recognized and necessary certification is issued by the prescribed authority, the assessee can avail the deduction in respect of expenditure incurred on in-house R&D facility, for which the adjudicating authority is the Assessing Officer and whether the prescribed authority is to approve expenditure in form No. 3CL from year to year. Looking into the provisions of rules, it stipulates the filing of audit report before the prescribed authority by the persons availing the deduction under section 35(2AB) of the Act but the provisions of the Act do not prescribe any methodology of approval to be granted by the prescribed authority *vis-à-vis* expenditure from year to year. **The amendment brought in by the IT (Tenth Amendment) Rules w.e.f. 1-7-2016, wherein separate part has been inserted for certifying the amount of expenditure from year to year and the amended form No. 3CL thus, lays down the procedure to be followed by the prescribed authority. Prior to the aforesaid amendment in 2016, no such procedure/methodology was prescribed. In the absence of the same, there is no merit in the order of Assessing Officer in curtailing the expenditure and consequent weighted deduction claim under section 35(2AB) of the Act on the surmise that prescribed authority has only approved part of expenditure in form No. 3CL. We find no merit in the said order of authorities below.**

46. The Courts have held that for deduction under section 35(2AB) of the Act, first step was the recognition of facility by the prescribed authority and entering an agreement between the facility and the prescribed authority. Once such an agreement has been executed, under which recognition has been given to the facility, then thereafter the role of Assessing Officer is to look into and allow the expenditure incurred on in-house R&D facility as weighted deduction under section 35(2AB) of the Act. Accordingly, we hold so. Thus, we reverse the order of Assessing Officer in curtailing the deduction claimed under section 35(2AB) of the Act by Rs. 6,75,000/-. Thus, grounds of appeal No.10.1, 10.2 and 10.3 are allowed."

14.8 The question of allowing deduction u/s.35(2AB) of the Act was considered by the Hon'ble Delhi High Court in the case of *CIT v. Sadan Vikas (India) Ltd.* [\[2011\] 335 ITR 117 \(Del\)](#) where AO refused to accord the benefit of

the weighted deduction to the assessee under s. 35(2AB) on the ground that recognition and approval was given by the DSIR in February/September, 2006, *i.e.*, in the next assessment year and, therefore, the weighted deduction cannot be allowed. In this case, the CIT(A) confirmed the order of the AO. The Tribunal held that the assessee would be entitled to weighted deductions of the aforesaid expenditure incurred by the assessee in terms of the s. 35(2AB) of the Act and in coming to this conclusion, the Tribunal relied upon the judgment of Gujarat High Court in *CIT v. Claris Lifesciences Ltd.* [326 ITR 251 \(Guj\)](#). In its decision the Hon'ble Gujarat High Court had held that the cut-off date mentioned in the certificate issued by the DSIR would be of no relevance. What is to be seen is that the assessee was indulging in R&D activity and had incurred the expenditure thereupon. Once a certificate by DSIR is issued, that would be sufficient to hold that the assessee fulfils the conditions laid down in the aforesaid provisions. The Hon'ble Delhi High Court followed the decision of the Hon'ble Gujarat High Court and upheld the decision of the Tribunal. The Hon'ble Delhi High Court quoted the following observations of the Hon'ble Gujarat High Court and agreed with the said view:

"7. ... The lower authorities are reading more than what is provided by law. A plain and simple reading of the Act provides that on approval of the research and development facility, expenditure so incurred is eligible for weighted deduction.

8. The Tribunal has considered the submissions made on behalf of the assessee and took the view that section speaks of : (i) development of facility; (ii) incurring of expenditure by the assessee for development of such facility; (iii) approval of the facility by the prescribed authority, which is DSIR; and (iv) allowance of weighted deduction on the expenditure so incurred by the assessee.

9. The provisions nowhere suggest or imply that research and development facility is to be approved from a particular date and, in other words, it is nowhere suggested that date of approval only will be cut-off date for eligibility of weighted deduction on the expenses incurred from that date onwards. A plain reading clearly manifests that the assessee has to develop facility, which presupposes incurring expenditure in this behalf, application to prescribed authority, who after following proper procedure will approve the facility or otherwise and the assessee will be entitled to weighted deduction of any and all expenditure so incurred. The Tribunal

has, therefore, come to the conclusion that on plain reading of s. itself, the assessee is entitled to weighted deduction on expenditure so incurred by the assessee for development of facility. The Tribunal has also considered r. 6(5A) and Form No. 3CM and come to the conclusion that a plain and harmonious reading of rule and Form clearly suggests that once facility is approved, the entire expenditure so incurred on development of R&D facility has to be allowed for weighted deduction as provided by s. 35(2AB). The Tribunal has also considered the legislative intention behind above enactment and observed that to boost up research and development facility in India, the legislature has provided this provision to encourage the development of the facility by providing deduction of weighted expenditure. Since what is stated to be promoted was development of facility, intention of the legislature by making above amendment is very clear that the entire expenditure incurred by the assessee on development of facility, if approved, has to be allowed for the purpose of weighted deduction."

From the above discussion it is clear that prior to 1-7-2016 Form 3CL had no legal sanctity and it is only w.e.f 1-7-2016 with the amendment to Rule 6(7A)(b) of the Rules, that the quantification of the weighted deduction u/s.35(2AB) of the Act has significance. Further, the date of approval shall not be cut off date for allowing scientific research expenditure u/s 35(2AB) of the Act.

14.9 The next question is whether the deduction u/s 35(2AB) could be allowed in the absence of approval of scientific research in-house facility by DSIR? Under the provisions of sec.35(2AB) approval of in-house research facility is a mandatory condition for allowing deduction under that section. Accordingly, if no approval of scientific research facility is available, then the deduction u/s 35(2AB) is not allowable.

14.10 In the instant case, the Ld D.R took us to the copy of approvals placed in the paper book and submitted that approval of some of the research facilities are not available. Further, the assessee has not furnished the break-up details of scientific research expenses incurred in each of the research facility centre. Accordingly, we are of the view that these factual aspects require verification at the end of AO. Accordingly, we are restoring

this issue to the file of AO for the limited purpose of obtaining the details of scientific research expenses incurred in each of the approved in-house facility and then examine the issue in the light of discussions made supra.

15. The next issue urged by the revenue relates to the claim for deduction of ESOP expenses. The assessee had floated ESOP scheme titled as "Lupin Employee Stock Option Plan 2003" and Lupin Employee Stock Option Plan 2005. During the year under consideration, certain employees have exercised the option and the value of fringe benefit was computed at Rs.5,74,85,065/-, being the difference between fair market value of equity shares on the date of vesting of option and amount recovered from or paid by the employee on exercising of option. The assessee paid Fringe benefit tax on the above said amount. Before the AO, the assessee claimed deduction of above said amount of Rs.5.74 crores even though it is not debited to the Profit and Loss account. The AO noticed that the CBDT, in its Circular No.9 of 2007, has clarified that this fringe benefit is not allowable as deduction. Further, the assessee has also made new claim without filing revised return of income, which is not in accordance with the procedure prescribed by Hon'ble Supreme Court in the case of Goetz (India) Ltd. Accordingly, the AO rejected the claim of the assessee.

15.1 The Ld CIT(A) allowed the claim of the assessee following the decision rendered by Special bench of Bangalore ITAT in the case of Biocon Ltd vs. DCIT (144 ITD 21). It is pertinent to mention that the decision rendered by the Special bench has since been upheld by the Hon'ble Karnataka High Court in 430 ITR 151.

15.2 The Ld D.R submitted that the Circular no. 9 of 2007 issued by CBDT has not been considered by the Special bench or by the Hon'ble High Court of Karnataka.

15.3 We heard Ld A.R and perused the record. It is well settled proposition that the Circular issued by CBDT is binding only on tax authorities and it will not bind on the Courts. The Hon'ble Karnataka High Court has dealt with this issue as under in the case of Biocon Ltd (supra) as under:-

“9. In the instant case, the ESOPs vest in an employee over a period of four years *i.e.*, at the rate of 25%, which means at the end of first year, the employee has a definite right to 25% of the shares and the assessee is bound to allow the vesting of 25% of the options. It is well settled in law that if a business liability has arisen in the accounting year, the same is permissible as deduction, even though, liability may have to quantify and discharged at a future date. On exercise of option by an employee, the actual amount of benefit has to be determined is only a quantification of liability, which takes place at a future date. The tribunal has therefore, rightly placed reliance on decisions of the Supreme Court in Bharat Movers *supra* and Rotork Controls India P. Ltd., *supra* and has recorded a finding that discount on issue of ESOPs is not a contingent liability but is an ascertained liability.

10. From perusal of section 37(1), which has been referred to *supra*, it is evident that an assessee is entitled to claim deduction under the aforesaid provision if the expenditure has been incurred. The expression 'expenditure' will also include a loss and therefore, issuance of shares at a discount where the assessee absorbs the difference between the price at which it is issued and the market value of the shares would also be expenditure incurred for the purposes of section 37(1) of the Act. The primary object of the aforesaid exercise is not to waste capital but to earn profits by securing consistent services of the employees and therefore, the same cannot be construed as short receipt of capital. The tribunal therefore, in paragraphs 9.2.7 and 9.2.8 has rightly held that incurring of the expenditure by the assessee entitles him for deduction under section 37(1) of the Act subject to fulfillment of the condition.

11. The deduction of discount on ESOP over the vesting period is in accordance with the accounting in the books of account, which has been prepared in accordance with Securities and Exchange Board of India (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999.”

15.4 The Special bench has expressed the view that the assessee is entitled for deduction of ESOP expenses when the rights are “vested” in the hands of the assessee and the said view has since been upheld by the Hon’ble Karnataka High Court. Hence the deduction should be allowed in the year in which the rights are vested in the hands of the assessee. For this purpose, the actual exercise of option by the employee is not relevant.

15.5 In the instant case, it is not clear as to whether the year under consideration, i.e., FY 2008-09 is the “vesting period” for the amount of Rs.5,74,85,066/- claimed by the assessee. In the written submission, it is stated by the assessee that the above said amount represents value of fringe benefit of “ESOP exercised by the employees” during the year under consideration. Hence, it is required to be examined, in the instant case, as to whether the period of vesting and period of exercising of option is one and the same by examining two ESOP schemes referred above. Further, the assessee has stated before the AO that it has not debited above said amount in its books of account. However, before Ld CIT(A), it has been claimed that the discount was amortised over the vesting period. The question that arises is whether the assessee is required to account for the discount amount in the books of account. In the decision rendered by Hon’ble Karnataka High Court, the High Court has observed as under:-

“11. The deduction of discount on ESOP over the vesting period is in accordance with the accounting in the books of account, which has been prepared in accordance with Securities and Exchange Board of India (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999.”

Even though, under the Income tax Act, entries whether made or not in the books of account are not relevant, in our view, it is required to be examined as to whether there is mandatory statutory requirement to account for discount or not and further its impact on computation of income. In our view, all these factual aspects require verification at the end of AO. Accordingly, we set aside the order passed by the Ld CIT(A) on this issue and

restore the same to the file of AO to examine the above said factual aspects and decide the issue in the light of discussions made supra.

16. In the result, the appeal filed by the assessee and the revenue are treated as partly allowed. The cross objection filed by the assessee is allowed.

Pronounced in the open court on 03.02.2023.

Sd/-
(KAVITHA RAJAGOPAL)
Judicial Member

Sd/-
(B.R. BASAKARAN)
Accountant Member

Mumbai; Dated : 03/02/2023

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent
3. The CIT(A)
4. CIT
5. DR, ITAT, Mumbai
6. Guard File.

//True Copy//

BY ORDER,

(Assistant Registrar)
ITAT, Mumbai

PS