

**IN THE INCOME TAX APPELLATE TRIBUNAL  
MUMBAI BENCH “C”, MUMBAI  
BEFORE SHRI OM PRAKASH KANT, ACCOUNTANT MEMBER  
AND  
SHRI RAJ KUMAR CHAUHAN, JUDICIAL MEMBER  
ITA NO. 2243/MUM/2024 (A.Y: 2018-19)**

<b>ACIT, Kalyan,</b> 1 <sup>st</sup> floor, Mohan Plaza wayle Nagar, Khadakpada, Kalyan West, Maharashtra - 421301	<b>Vs. Omkar</b>	<b>Speciality</b> <b>Chemicals Ltd,</b> B-34 MIDC, Badlapur, Thane, Maharashtra - 421503 <b>PAN: AAACO7311D</b>
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**(Appellant)**

**(Respondent)**

<b>Assessee Represented by</b>	<b>:</b>	<b>None</b>
<b>Department Represented by</b>	<b>:</b>	<b>Shri Krishna Kumar, Ld. AR</b>
<b>Date of conclusion of Hearing</b>	<b>:</b>	<b>29.11.2024</b>
<b>Date of Pronouncement</b>	<b>:</b>	<b>10.12.2024</b>

**ORDER**

**PER RAJ KUMAR CHAUHAN (J.M.):**

1. This appeal is filed by the revenue against the order of Learned Commissioner of Income Tax (Appeals) – 52, Mumbai /National Faceless Appeal Centre (NFAC), Delhi [hereinafter referred to as the “CIT(A)”], passed under section 250 of the Income Tax Act, 1961 [hereinafter referred



to as “*the Act*”] dated 28.01.2024 for the A.Y. 2018-19 wherein revenue is aggrieved by the order of Ld. CIT(A) in not considering an amount of Rs. 52,58,54,632/- as revenue expenditure on account of write off of R & D expenses without furnishing the mandatory form 3CLA by the assessee. The gist of grounds taken in the appeal is that Ld. CIT(A) has wrongly set aside the order of AO.

2. The facts in brief are that, the assessee company is doing the business of manufacturing and selling of specialty chemicals and also engaged in research and development of new molecules, etc. Assessee has e-filed his return of income for the year under consideration on 24.10.2018 declaring total loss of (-) Rs.136,49,83,608/- and claiming refund of Rs. 5,60,000/-. The case was selected for scrutiny and the notice u/s 143(2) of the Act was issued on 22.09.2019 which was duly served on the assessee. The matter was assigned to NFAC and notice u/s 142(1) of the Act was issued alongwith questionnaire issued on 01.12.20, 04.12.20 and 23.12.20. In response, the assessee furnished the relevant details and documents through its Chartered Account which was duly examined by the AO. It was noticed by the AO that in response to the show cause notice issued, the assessee has not filed the audited report in Form 3CLA. It was also noticed by the AO



that assessee's claim for deduction u/s 35(2AB) of the Act was disallowed even in AY 2017-18 vide assessment order dated 29.12.2019 passed u/s 143(3) of the Act because the assessee has failed to furnish the requisite audit report in Form 3CLA. It was also observed that Sub section 4 of section 35(2AB) of the Act read with Rule 6 of the Income Tax Rules 1962 mandates to furnish the audit report in such manner as prescribed in Form 3CLA. Since the assessee has failed to furnish the information in Form 3CLA, the AO made addition of Rs. 54,38,79,787/- and added to the total income of the assessee treated as disallowance of inadmissible claim of deduction u/s 35(2AB) of the Act.

3. Aggrieved by the order of AO, the assessee filed the appeal before the Ld. CIT (A) and Ld. CIT(A) after considering the submissions of the assessee referred the contents of para 10 of AO's order as under:-

*10. With the above remarks, and from the data made available, total income of the assessee is determined as under: -*

<i>BUSINESS INCOME: -</i>	<i>(Rs.)</i>
<i>Business Loss, as per intimation u/s 143(1)(a)...</i>	<i>(-) 136,48,07,192/-</i>
<i>Additions/Disallowables discussed above :-</i>	
<i>1. Duty Draw back - Para 5</i>	<i>29,18,614/-</i>



2. Disallowance u/s. 35(2AB)..Para.7 54,38,79,787/-

Disallowance u/s. 40(a)(ia) :-

3.1 On account of TDS details 7,63,812/-

not furnished... Para-8.1. to 8.3.

3.2. On account of TDS defaults on 11,96,408/- 54,87,58,621/-

'Professional charges /consultancy fee' Para- 8.4.

Business Loss..(-) 81,60,48,571/-

**INCOME FROM OTHER SOURCES:-**

4. Addition on account of difference in 'Professional charges / consultancy fee' reported by Auditor in Form 3CD w.r.to expenses claimed in ITR... added u/s 69C Para-9. 59,15,402/-

11. This assessment order is passed u/s 143(3) r.w.s 144B of the Income Tax Act, 1961. Penalty proceedings u/s.270A of the Act initiated separately.

4. The submission of the assessee before the Ld. CIT(A) against the above addition and adjudication /findings of the same are in para no. 7.1.2 to 7.1.3 which are extracted below:-

*7.1.2 Appellants Submission as per SoF:*

*Disallowance of expense of Rs. 52,58,54,632 u/s 35(2AB)-*

*Expenditures of Rs.52.58 crores were incurred for achieving following objectives-*

*i. To develop new molecules for emerging markets and customers.*



- ii. *To improve on quality and consumption norms on existing products*
- iii. *To develop green chemistry*
- iv. *To find new processes which would reduce the cost and help gain edge over the competition.*

*The products and processes that were being developed were already in line of business of the assessee. The main intention of these development was to remain competitive in the market. To achieve the above objectives assessee had to procure various raw materials for development. Since these raw materials were used for development of new products/ processes, the same were being treated as part of capital work in progress. Also, these products/processes were in the line of business of assessee.*

*During the period, the capital work in progress could not be completed due to following reasons:*

- a. *Capital work in progress was not yielding expected results. Also, product/ process under development was not able to pass quality checks.*
- b. *Decreasing margins and increasing cost to further develop the product and processes,*
- c. *Increasing cost of complying with environmental regulations and standards.*
- d. *Non availability of working capital to further develop the product*

*Due to the above issues further development of the product was not feasible. Also, the product/ process under development were not yielding expected results. The expenditure incurred on development of these new product/ process were not claimed earlier as revenue expenditure because it was of capital nature entitled to depreciation after completion and commencement of its use for business. But since that stage was not reached, no asset came into existence. There would have been no occasion to claim the exceptional expense if the capital work-in-progress had completed its course. Since the development was abandoned, the capital work-in- progress did not proceed any further. The decision to abandon the*



*project was the cause for claiming the exceptional expenses, which was taken in the relevant year.*

*2. Application of patents cannot be the reason for capitalization of expenditure. If the expenditure for which the patent is applied is not eligible for being capitalized, then there is no reason for the assessee to wait for approval of related patents.*

*3. As per IND AS 36 (Impairment of Asset), An entity shall assess at the end of each reporting period whether there is any indication that an asset may be impaired. If any such indication exists, the entity shall estimate the recoverable amount of the asset. If the recoverable amount of an asset is less than its carrying amount, the carrying amount of the asset shall be reduced to its recoverable amount. That reduction is an impairment loss. An impairment loss shall be recognised immediately in profit or loss. We draw your attention to following judgements*

- a. Indo Rama Synthetics Ltd. vs. Commissioner of Income Tax*
- b. Binani Cement vs. Commissioner of Income Tax*
- c. Asia Power Projects P Ltd. vs. DCIT*

*In above cases it was held that that if there is no creation of new asset, then the expenditure incurred would be revenue in nature. However, if the new asset comes into existence, which is of enduring benefit, then such expenditure would be capital in nature.*

*From the above we would like to summarize as under:*

- 1. Assessee was already in business of development of the said products/ processes.*
- 2. Since the product/ processes under development had no commercial market and viability, the same was never completed and abandoned during capital work in progress stage.*
- 3. No new asset was created from the development of these products/ processes.*



*Taking the above points and earlier judgements into consideration we would like to state that expenditure of Rs.52,58,54,632/- was in nature of revenue and should be allowed as deduction during the year.*

*7.1.3 Adjudication: I have perused the order, grounds of appeal and the statement of facts. The disallowance consists of the following claims:*

*(i) Amount of deduction in excess of the amount debited to the profit and loss account: Rs. 1,80,25,155*

*(ii) Amount debited to profit and loss account as exceptional expenses: Rs.52,58,54,632*

*In relation to the claim of exceptional expenses, the assessee's submission is that this expenditure was incurred by way of the cost of research and development expenses for a number of products developed and for which patents were applied. However, only 6 patents were granted. On the contrary the AO has held that it is premature on the part of the assessee to have written off the entire expenditure incurred for the development of products for the reason stated by the assessee as reproduced above as part of the assessment order. The reasons for valuing the patents as zero value was also questioned by the AO. I have perused the rival contentions of the AO and the appellant. The genuineness of the expenditure not being in dispute and has been accumulated under the head 'Capital Work In Progress' without debiting the same to the profit and loss account. It is the \*prerogative of the management to resort to value the patent on the basis of the commercial principles. The management has valued the products for which patents were granted and in relation to other products for which patents were not granted under one basket and has valued the entire basket at zero and has accordingly shown this as an exceptional item as well. In the absence of any evidence to the contrary, the attempt on the part of the AO not to allow this claim may go against the principles of commercial prudence in which the appellant has the absolute say. Since the reasons assigned by the AO for not allowing the claim do not persuade me to accept the contentions of the AO. This disallowance by the*



*AO is not correct. Reliance is also placed on the decisions relied upon by the appellant. Hence, the appellant's ground on this score is 'allowed.'*

*Regarding the other disallowance of Rs 1,80,25,155 the reason given by the AO was in line with the stand taken for the earlier Asst Year namely 2017-18, The failure on the part of the appellant to furnish the requisite audit report in Form 3CLA was the reason for disallowance in the earlier Asst Year. For this Asst Year also, the AO recorded that despite specifically, repeatedly requested for the report in Form 3CLA was not submitted. For these reasons, the deduction was not allowable. During the appellate proceedings also, the appellant did not file Form 3CLA where it is a prerequisite for allowance of weighted deduction. This disallowance is confirmed on account of the continued failure on the part of the appellant. Therefore, on this ground the appellant partially succeeds to the extent of Rs.52.58 crores and fails to the extent of 1.80 crores. In the result, this ground is Partly Allowed.*

5. We have heard Ld. DR as well as Ld. AR on behalf of the parties. Ld. DR has argued that the order of Ld. CIT(A) is not reasoned order with respect to deletion of Rs. 52,58,54,632/- which was disallowed by the Assessing Officer. He further argued that the Rule 6 of Income Tax Rules 1962 mandates the filing of Form 3CLA for claiming deduction on account of research and development u/s 35(2AB) of the Act. It is therefore submitted that the Ld. CIT(A) has committed illegalities in setting aside the order of AO with respect to disallowance of Rs. 52,58,54,632/- .



6. On the other hand, Ld. AR on behalf of the assessee relied on the order of Ld. CIT (A) stating that there is no illegality or perversity in setting aside the order of AO where the disallowance is made wrongly.

7. We have considered the rival submissions and perused the orders of lower authorities. On perusal of the impugned orders and contents extracted above, it becomes evident that Ld. CIT(A) has not mentioned in his conclusion of adjudication about non submission of Form 3CLA by the assessee for claiming deduction u/s 35(2AB) of the Act. The Rule 6 (7A) (c) of Income Tax Rules 1962 are extracted below:-

***Rule 6(7A) in Income Tax Rules, 1962***

*(7A) Approval of expenditure incurred on in-house research and development facility by a company under sub-section (2AB) of section 35 shall be subject to the following conditions, namely :-*

*a) xxxx*

*b) xxxx*

*(c) The company shall maintain a separate account for each approved facility; which shall be audited annually and a report of audit in Form No.3CLA shall be furnished electronically to the Secretary, Department of Scientific and Industrial Research on or before the due date specified in Explanation 2 to sub-section (1) of section 139 of the Act for furnishing the return of income, for each succeeding year.*



*Explanation. - For the purposes of this sub-rule the expression "audited" means the audit of accounts by an accountant, as defined in the Explanation below sub-section (2) of section 288 of the Income-tax Act, 1961;*

*d) xxxx*

8. It is evident from the above rules that submission of audit report in Form 3CLA is precondition for claiming the benefit of section 35(2AB) of the Act. It is an admitted fact that Form 3CLA has not been furnished for the year under consideration. On perusal of the findings of the Ld. CIT(A), it is noticed that the finding is based on mere academic discussion than the factual and legal discussion on the issue and for these reasons, the impugned order with respect to setting aside disallowance of exceptional expenses of Rs. 52,58,54,632/- need to be set aside for fulfilling necessary requirement of Rule 6(7A)(c) of Income Tax Rules 1962.

9. From the above discussion, we are of the considered opinion that the matter needs to be considered and decided afresh by the Ld. CIT(A) after giving proper opportunity to the assessee to fulfill the necessary requirement of claim u/s 35(2AB) of the Act and Ld. CIT (A) shall decide the matter afresh with respect to claim of exceptional expenses as deduction u/s 35(2AB) of the Act by the assessee. Accordingly, the matter is



restored to the file of Ld. CIT(A) for deciding these grounds afresh as mentioned above.

10. In the result, appeal filed by the revenue is **allowed in above terms for statistical purposes.**

**Order pronounced in the open court on 10.12.2024**

**Sd/-**  
**(OM PRAKASH KANT)**  
**(ACCOUNTANT MEMBER)**

Mumbai / Dated 10.12.2024  
*Dhananjay, Sr.PS*

**Sd/-**  
**(RAJ KUMAR CHAUHAN)**  
**(JUDICIAL MEMBER)**

**Copy of the Order forwarded to:**

1. The Appellant
2. The Respondent.
3. CIT
4. DR, ITAT, Mumbai
5. Guard file.  
//True Copy//

BY ORDER

(Asstt. Registrar)  
**ITAT, Mumbai**