

Ciba India (P) Ltd. Vs. Ito

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Court : Income Tax Appellate Tribunal ITAT Mumbai

Decided On : Aug-22-2007

Reported in : (2008)116TTJ(Mum.)945

Judge : S K Yadav, R Panda

Appellant : Ciba India (P) Ltd.

Respondent : ito

Judgement :

1. This appeal by the assessee is preferred against the order of the Commissioner (Appeals) on following grounds: (i) The Commissioner (Appeals)-IX, Mumbai (hereinafter referred to as the 'Commissioner (Appeals)') erred in upholding the disallowance of expenditure on scientific research of Rs. 96,99,624 claimed under Section 35(1)(iv) of the Income Tax Act, 1961.

(ii) The Commissioner (Appeals) ought to have directed the assessing officer to recompute the interest under Section 234B on giving effect to the appellate order.

2. We have heard the rival submissions and carefully perused the order of the authorities below and documents placed on record.

3. With regard to ground. No. 1, it is noticed that the assessee has claimed deduction under Section 35(1)(v) a sum of Rs. 96,99,624. The assessee has stated that it is engaged in 'research business' and investment, in joint ventures. The Principal objective of the company is engaging in specialised research

activities and to enter into joint ventures with Indian companies to undertake the manufacture of chemicals. The assessee was asked to justify the claim in this regard.

In response thereto it was stated that the assessee was engaged in the business of carrying out specialised research activities for two persons namely 'CIBA Speciality Chemicals Ltd.' of Switzerland and Chiron Diagnostic of USA and also stated that expenditure of a capital nature on scientific research related to the business of the assessee would therefore be allowable as a deduction. The assessing officer was not convinced with this explanation of the assessee and he disallowed the expenditure on scientific research on the ground that it is not laid out in scientific research related to the business. The assessing officer has also observed that Section 43(4)(nz) directly defines scientific research and also emphasises the aspect that it has to be 'related to a business'. In the same definition, it also refers to extension of that business. He further observed that Income Tax Act pre-supposes the existence of some business for the research to be carried out.

4. The assessee preferred an appeal before the Commissioner (Appeals) and placed heavy reliance upon the order of the Allahabad Bench of the Tribunal in the case of CIT v. U.P. Electronic Corporation Ltd. (2005) 276 ITR 451 (All) and also of the Bombay Bench of the Tribunal in the case of Veekers Spray v. CIT [IT Appeal Nos. 2035 & 2036 (Bom.) of 1977-78], but did not find favour with him.

5. Now the assessee is before us with the submissions that the assessee's main business is to provide consultancy services on the basis of specialised research activities and from this activity it has earned an income of Rs. 5,68,07,297. Whatever scientific research activities are undertaken by the assessee, it was with the objectives to prepare a scientific and analytical report or to provide the consultancy service to the desired person. It has already stated before the assessing officer that he has engaged in the business of carrying out specialised research activities for two persons namely CIBA Speciality Chemicals Ltd. of Switzerland and Chiron Diagnostic of USA and whatever data or information were collected on the basis of scientific research, it were furnished to these

companies and the income earned in lieu of that was offered to tax. He has also invited our attention to the judgment of Allahabad High Court in the case of U.P. Electronic Corpn. Ltd. (supra) in which Their Lordships have held that the term business is to be given a wide meaning and with the rapid advancement and growth in the field of science and technology even consultancy services offered would be covered under the term business.

For providing consultancy services, the expenditure from scientific research under Section 35 of the Income Tax Act, is allowable as it was laid out or expended or related to the business.

6. The learned Departmental Representative on the other hand has submitted that the expenditure of capital nature on scientific research can be allowed to be deducted if it is related to the business carried on by the assessee. Since the assessee was not doing any other business except the scientific research, the capital expense incurred thereon cannot be allowed under Section 35(1)(iv) of the Income Tax Act.

7. We have heard the rival submissions and carefully perused the orders of the authorities below and the judgment referred to the assessee.

Undisputedly, assessee was engaged only in the scientific research activities but the datas collected in the scientific research were utilised by two companies namely CIBA Specialty Chemicals Ltd. of Switzerland and Chiron Diagnostic of USA and on account of furnishing the information developed on the basis of scientific research activities, the assessee has earned substantial income. Now the question arises whether the expense of capital nature incurred on scientific research are eligible for deduction under Section 35 of the Act; where the assessee is engaged in specialised scientific research activities and providing the specialised consultancy on datas collected in scientific research to other companies? It is also to be seen whether providing of consultancy services or providing datas, collected on scientific research, amounts to business activity of the assessee These questions were examined by the Allahabad High Court in the case of U.P. Electronic Corpn. Ltd. (supra). The facts of this case are that the assessee is a Government undertaking and had been set up with the basic object

of promoting and developing electronic industries in the State of U.P. In the beginning it set up a factory to manufacture black and white T.V. sets with effect from 1-4-1987. The State Government created certain separate corporations. The factories owned by the assessee were transferred to the different corporations set up by the State Government namely, Uptron, Uptron Digital Systems, Uptron Communications etc. These corporations were wholly owned subsidiaries of the assessee. After the transfer of the factories, the respondent-assessee was engaged mainly in the work of research and development. The results of such research and development were used by the factories which were wholly owned subsidiaries. Besides research work, the assessee was engaged in providing consultancy services for which during the year under consideration it received a sum of Rs. 6,72,992 as fee. It had also received Rs. 3,03,000 from the State Government for preparing feasibility reports. Apart from it, it had also received a sum of Rs. 6,46,300 from the promotion and development of electronic industry in the State. It claimed deduction of Rs. 19,23,250 under Section 35 of the Act which related to the expenditure on scientific research. The Tribunal held that subsidiary companies have not made any claim of deduction under Section 35 of the Act on the expenditure incurred by the assessee on scientific research. It was further found that the objects for which the assessee was established would promote and develop electronic industry to establish the companies associations, etc. The Tribunal has also observed that the assessee's main income was from consultancy charges and preparation of feasibility reports for setting up electronic industries.

8. While dealing with the issue, their Lordships have observed that the expenditure on scientific research under Section 35 of the Act is allowable only when such expenditure is laid out or expended or related to the business. The term 'business' is to be given a wide meaning and with the rapid advancement and growth in the field of science and technology even the consultancy services offered would be covered under the term business. Their Lordships further observed that providing consultancy is the major source of revenue and it is not at all required to confine the term 'business' to mean only the sale and purchase of merchandise or manufacturing activities. Having observed that the assessee had derived income from consultancy services, preparation of feasibility report and other connected

activities, their Lordships have held that it had carried on business during the assessment year in question and was entitled for allowance of the expenditure incurred on scientific research which was related to its business.

9. From the perusal of these judgments, we are of the view that scientific research must be performed for or relating to the business of the assessee. The business may be of consultancy services or preparation of feasibility report. But expenditure of capital nature on scientific research can only be allowed to be deducted under Section 35 if it is related to the business of assessee. No doubt, these days there are various facet of business/ activities including rendering consultancy services of any nature, preparation of feasibility report on the basis of datas collected on survey or scientific research and its meaning cannot be restricted to the sale and purchase of merchandise or manufacturing activities. In the case of U.P.Electronics, the assessee was engaged in the consultancy service's and preparation of feasibility report and their Lordships have held that the assessee was engaged in a business independent to scientific research activities.

10. Turning to the facts of the case in hand, we find that the assessee was wholly engaged in scientific research activities and whatever results and datas were obtained and that were utilised by the two persons namely CIBA Speciality Chemicals Ltd. of Switzerland and Chiron Diagnostic of USA only. Meaning thereby, the assessee can only be called to be an extended unit of these two concerns in India, who is engaged in the specialised scientific research activity. The assessee was not doing any other business independent to research activities whereas according to Section 35(1)(iv) the expenditure of capital nature on scientific research can only be allowed to be deducted if it is related to the business carried on by the assessee. Since assessee was not engaged in any sort of business except the scientific research activity, expenditure incurred thereon cannot be called to have incurred a scientific research in relation of any business of the assessee. The language of relevant provision is quite unambiguous and clear and according to it deduction under this section can only be allowed if any expenditure of capital nature on scientific research is related to the business carried on by the assessee. For the sake of reference we reproduce the relevant provision as under: Section 35(1)(iv): In respect of expenditure on scientific

research, the following deductions shall be allowed (iv) in respect of any expenditure of a capital nature on scientific research related to the business carried on by the assessee, such deduction as may be admissible under the provisions of Sub-section (2).

11. Having carefully perused the above provision, we are of the view that without establishing the fact that the assessee is engaged any business activity, the expenditure of a capital nature on scientific research relating to such business cannot be allowed. We, therefore of the view that the judgment of Allahabad High Court was rendered on different set of facts and no assistance can be drawn in favour of the assessee.

12. In the instant case, the assessee is engaged in Scientific Research activities and whatever results of scientific research and the data as collected thereon were provided only to foreign based companies, i.e., CIBA Speciality Chemicals Ltd. of Switzerland and Chiron Diagnostic of USA. The assessee has not provided any consultancy services or any informations on the basis of data collected on scientific research to any other persons. As such the assessee can only be called to be an extended research unit of these two foreign based companies. Since assessee was not engaged in any other activities except scientific research for the above said two foreign based companies, it cannot be called that the scientific research undertaken by the assessee was related to the business of the assessee to make him eligible for deduction under Section 35 of the Income Tax Act. We, therefore, hold that the assessee is not entitled for deduction under Section 35 of the Act of the capital expenditure incurred on scientific research.

Accordingly, the order of the Commissioner (Appeals) stands confirmed.

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