

IN THE HIGH COURT OF KARNATAKA AT BENGALURU

DATED THIS THE 24th DAY OF APRIL, 2015

BEFORE

THE HON'BLE MR.JUSTICE ARAVIND KUMAR

WRIT PETITION NO.7004/2014 (T-IT)

BETWEEN:

M/S TEJAS NETWORKS LIMITED
A COMPANY INCORPORATED UNDER
THE COMPANIES ACT, 1956
HAVING ITS OFFICE AT:
PLOT NO.25, 5TH CROSS,
J.P. SOFTWARE PARK
ELECTRONIC CITY,
PHASE-1, HOSUR ROAD,
BENGALURU-560 100
REPRESENTED BY ITS
MANAGING DIRECTOR
MR. SANJAY NAYAK
S/O SRI. SHANKAR NAYAK
AGED ABOUT 49 YEARS.

... PETITIONER

(BY SRI N VENKATARAMAN, Sr.COUNSEL A/W
SRI K.R.VASUDEVAN & SRI. HARISH ADVOCATES)

AND:

1. THE DEPUTY COMMISSIONER OF
INCOME TAX, CIRCLE 12(4),
BENGALURU
RASHTROTHANA PARISHAD BHAVAN
(4TH FLOOR) NO.14/3A,
NRUPATHUNGA ROAD
BENGALURU-560 001.
2. THE DISPUTE RESOLUTION PANEL,
BENGALURU,

RASHTROTHANA PARISHAD BHAVAN
(6TH FLOOR) NO.14/3A,
NRUPATHUNGA ROAD
BENGALURU-560 001.

.....RESPONDENTS

(BY SRI K.V.ARAVIND, SR.PANEL COUNSEL)

THIS WRIT PETITION IS FILED UNDER ARTICLE 226 AND 227 OF THE CONSTITUTION OF INDIA, PRAYING TO QUASH THE IMPUGNED ORDER ISSUED BY THE R-1, PASSED U/S. 143(3) OF THE ACT, DATED 31.1.2013 FOR THE ASSESSMENT YEAR 2009-10 VIDE ANNEUXRE-R & THE CONSEQUENTIAL DEMAND NOTICE ISSUED BY THE R-1, DATED 31.01.2014 FOR THE ASSESSMENT YEAR 2009-10 THAT IS VIDE ANNEXURE R-1.

THIS PETITION COMING ON FOR DICTATING ORDERS THIS DAY, THE COURT MADE THE FOLLOWING:

ORDER

Petitioner is seeking for quashing of the assessment order passed by first respondent under 143(3) r/w Section 144C(13) of the Income Tax Act, 1961 (for short 'Act') dated 31.01.2013 - Annexure-R and consequential demand notice dated 31.01.2014 at Annexure-R1 issued by first respondent. By consent of learned Advocates appearing for parties matter is taken up for final hearing.

FACTUAL MATRIX:

2. Petitioner is an assessee under the Act and is engaged in the business of software development, manufacturing and trading of networking equipments. Return of income for the assessment year 2009-10 came to be filed on 29.09.2009 declaring nil income and claiming loss of ₹7,75,95,922/- On said return being selected for scrutiny, notice came to be issued and draft assessment order came to be framed on 27.03.2013 under Section 144C(1) of the Act whereunder income of petitioner was revised after making certain adjustments. On receipt of the draft assessment order, assessee filed its objection before the Dispute Resolution Panel ('DRP' for short) and after affording opportunity of hearing to the assessee, DRP issued a direction to the jurisdictional assessing Officer on 30.12.2013. The DRP held that where the express provisions of the Act excludes certain expenditure from the purview of Section 35 of the Act, such expenditure cannot be allowed and as such, the report of the prescribed

authority cannot be considered as far as such excluded expenditure is concerned. It was also held by DRP that certificate issued by the prescribed authority cannot over rule the express provision of the Act and accordingly directions came to be issued to assessing Officer after considering the directions issued by the DRP, framed assessment order on 31.01.2013 – Annexure-R framed assessment order whereunder as against the deduction claimed by the assessee under Section 35(2AB) in respect of Research and Development expenditure in a sum of ₹ 89,35,48,193/-, a sum of ₹ 48,41,82,071/- was disallowed and same came to be added to the income of assessee-company. Further, a sum of ₹2,63,68,301/- claimed by the assessee as 100% deduction under Section 35(1)(i) also came to be disallowed. Said order of assessment dated 31.01.2013 is impugned in the present writ petition.

3. I have heard the arguments of Sriyuths N Venkataraman, learned Senior counsel appearing on

behalf of Sri K.R.Vasudevan, for petitioner, Sri K.V.Aravind, learned Senior panel counsel appearing for respondents.

CONTENTIONS ON BEHALF OF ASSESSEE:

4. It is the contention of Sri Venkataraman, learned Sr.counsel appearing on behalf of petitioner that order of first respondent is arbitrary, without application of mind and it is without jurisdiction and has been passed without following due process of law. He would elaborate his submission by contending there are no foundational facts on the basis of which the first respondent could have ignored the certificate issued by the prescribed authority – Department of Scientific and Industrial Research (for short 'DSIR') which is the prescribed authority under Rule 6(1) of the Income Tax Rules, 1961 empowered to issue certificate to the assessee who claims allowance of expenditure under Section 35(2AB) or 35(1)(i) of the Act. It is contended that petitioner is engaged in developing and selling

optical network products to its worldwide customers and as such carry out product development activities in developing optical transmission telecommunication equipment which is a continuous process and as such, petitioner is entitled to claim deduction of sum equal to two times of the expenditure incurred on 'scientific research' as permitted under Section 35(2AB) of the Act. It is contended that petitioner accordingly has obtained approval in form No.3CL after audit came to be conducted by DSIR and a report has been submitted by the said prescribed authority by its report dated 10.04.2013 duly communicated to the Director General of Income Tax (Exemptions) whereunder expenditure to the tune of ₹ 46.03 Crores as against claim of ₹59.57 Crores of the petitioner came to be approved. It is the grievance of the petitioner that once such certificate is issued, it is deemed that the petitioner has complied the conditions prescribed under Section 35(2AB) and consequently, it would be eligible to claim the deduction permissible under the said Section. He would draw the

attention of the Court to the impugned order whereunder at paragraph 4.9 the approval granted by DSIR came to be considered and held that it cannot be considered as the only condition for claiming deduction under Section 35(2AB) on the premise that sub-section (2) Section 43(4) enables the Assessing Officer to exclude the expenditure incurred by an assessee in the acquisition of rights, in or arising out of scientific research and held that expenditure recorded as product development expenditure by the assessee cannot be accepted as research and development expenditure being eligible for deduction under Section 35(2AB) and Section 35(1)(i) r/w Section 43(4)(ii) of the Act and accordingly disallowance of the claim is without jurisdiction and it would amount to sitting in judgment over the certificate issued by the prescribed authority and same is impermissible.

5. He would further elaborate his submission by contending that if an Assessing officer were to

entertain a doubt with regard to certificate issued by prescribed authority, the course left open to such assessing officer is to forward the same to the Central Board of Direct Taxes (for short 'CBDT') and the Board in turn is required to refer the question to the prescribed authority whose decision would be final and the technical aspects being involved with regard to scientific research, the prescribed authority being a specialized authority, it would be in a better position to examine the issue and as such, this task of certifying or disallowing the claims made in this regard having been outsourced by the Revenue under the Act, assessing Officer cannot sit in judgment over such certificate issued and hence, in the instant case, the assessing officer committed a jurisdictional error in rejecting the claim on the ground that he would be empowered to disallow such claim made by the assessee though duly certified by the prescribed authority by taking recourse to the later portion of sub-clause (ii) of sub-section (4) of Section 43 of the Act. He would summarise his

submissions by contending the definition of 'scientific research' found in Section 43(4) has been imported to Section 35(2AB) and 35(3) and the assessing authority while examining the claim for deduction under Section 35(2AB) will have to necessarily accept the certificate or the report issued by the prescribed authority and once such report is furnished, assessing Officer has no jurisdiction to examine the correctness or otherwise of such expenditure certified by the prescribed authority and the only option left to the assessing officer when disagreeing with the report is to seek for clarification from the prescribed authority through Board. Hence, he would contend that assessing Officer could not have gone into merits of the certificate issued by prescribed authority and as such impugned order is bad and erroneous in law.

6. In support of his submissions, he has relied upon the following judgments.

- (1) **(2008) 174 Taxman 113 (Guj.)**
CIT vs. Claris Lifesciences Ltd.,

- (2) **(2012) 207 Taxman 216 (Delhi)**
CIT vs. Sandan Vikas (India) Ltd.,
- (3) **(1976) 105 ITR 864 (All)**
J K Synthetics vs. ITO
- (4) **(2012) 210 Taxman 432 (Guj.)**
Deputy Commissioner of Income-tax (Asstt.)
vs. Mastek Ltd.,
- (5) **(1973) 87 ITR 539 (SC)**
Raza Textiles Ltd., vs. Income Tax Officer,
Rampur
- (6) **(2003) 128 Taxman 190**
Hemalatha Gargya vs. CIT
- (7) **(2013) 40 taxman.com 545**
Vodafone India Ltd., vs. Union of India
- (8) **(1961) 41 ITR 191 (SC)**
Calcutta Discount Co. Ltd., vs. Income Tax
Officer
- (9) **(2003) 264 ITR 566 (SC)**
Commissioner of Income-tax vs. Foramer
France
- (10) **(2007) 001 CLR 0067 (SC)**
Union of India and Another vs. Kunisetty
Satyanarayana
- (11) **(AA) (2009) 236 ELT 425 (SC)**
M/s Godrej Sara Lee Ltd., vs. Asst.
Commissioner
- (12) **(2010) 254 ELT 6 (SC)**
Asst. Commissioner, Commercial Tax
Department vs. Shukla & Brother

CONTENTIONS ON BEHALF OF REVENUE:

7. Per contra, Sri K.V.Aravind, learned Panel counsel appearing for respondents would submit that petitioner without exhausting the alternate remedy of appeal namely, approaching the jurisdictional Income Tax Appellate Tribunal, has invoked the extraordinary jurisdiction of this Court and the same being impermissible, petition is liable to be dismissed on this ground alone. In support of this proposition, he has relied upon the judgment of Hon'ble Apex Court in the case of **CIT vs CHABILDAS** reported in **(2013)357 ITR 357(SC)**.

8. It is the contention of Sri K.V.Aravind, learned panel counsel appearing for respondent-Revenue that present writ petition is liable to be dismissed on the ground that petitioner not having availed alternate remedy and contends that order impugned in the present writ petition has been passed by the jurisdictional Assessing Officer under Section

143(3) read with Section 144C(13) of the Income Tax Act, 1961 or in other words, draft assessment order having been issued to the petitioner was subject to objections and as such assessee objected to said order before the Dispute Resolution Panel which comprises of Three Principal Commissioners or Commissioners of Income Tax constituted by the Board and they in turn have recorded a finding on the claim of allowability sought for by the petitioner under Section 35(2AB) of the Act by rejecting the contention of assessee. He would further contend that only course that was left open to the assessing Officer on receipt of approval of draft assessment order by DRP, was to accept the said findings of DRP and as such assessing Officer has passed an order which is appealable under Section 253 of the Act before Income Tax Appellate Tribunal. On account of non availment of the alternate remedy, he prays for dismissal of the writ petition.

9. He would also contend that when a claim is made for weighted deduction under Section 35(2AB) of the Act, the Assessing Officer no doubt cannot sit in judgment over the certificate issued by the DSIR or the prescribed authority, but it does not prevent the Assessing Officer from examining as to whether any expenditure incurred and claimed for allowance would fall within the definition clause of sub-section (4) of Section 43 of the Act. He would also elaborate his submission by contending that if any question arises under Section 35(2AB) namely, as to whether and if so to what extent any activity constitutes or any asset is or was being used for scientific research, then such issue is required to be referred by the Board to 'Central Government' if such question relates to any activity under clauses (ii) & (iii) of sub-section (1) and to 'Prescribed Authority' when such question relates to any activity other than the activity specified in clause (a) of sub-section (3) and in both eventualities such decision would be final and issue regarding admissibility of such

expenditure would be within the domain of the assessing Officer to examine. He would submit that assessing Officer having examined this issue has rejected the claim for weighted deduction and as such he prays for rejection of the writ petition.

10. Having heard the learned Advocates appearing for the parties and on perusal of the records and the case laws relied upon by the learned Advocates appearing for the parties, this Court is of the considered view that following points would arise for consideration:

- (1) Whether Writ Petition is liable to be dismissed on the ground of petitioner not having availed alternate remedy of filing an appeal before jurisdictional Income Tax Appellate Tribunal as provided under Section 253(4) of the Act?**
- (2) If the answer to the above question is in the negative; Whether impugned order dated**

**31.01.2014 - Annexure-R
passed by first respondent is
liable to be interfered for any
reason whatsoever?**

(3) What order?

RE: POINT No.(1)

11. Learned Advocate appearing for respondents has raised a preliminary objection with regard to maintainability of writ petition.

12. Availability of alternate remedy would be a good ground to refuse the relief under Article 226 of the Constitution of India. The power of this Court to issue writs under Article 226 of the Constitution of India being plenary in nature is not limited by any other provisions of the Constitution of India. This Court has discretion to entertain or not to entertain a writ petition. However, availability of alternate remedy would be the normal rule for this Court to refuse to exercise its jurisdiction under Article 226 of the Constitution. But,

it is not an inviolable rule and the availability of an alternate remedy would not act as a bar for this Court to exercise the extraordinary power. The self imposed judicial restraint one of which is that of availability of alternate remedy would be a reason for the writ Court not to issue prerogative writs. Exceptions to this general principles are (1) for enforcement of Fundamental Rights; (2) violation of principles of natural justice; (3) where the order or proceedings under challenge is attacked or being vitiated on the ground of such authority acting without jurisdiction; and (4) where constitutional validity of a provision in a statute or statute is itself under challenge.

13. After analyzing plethora of judgments, the Hon'ble Apex Court in **WHIRLPOOL CORPORATION vs REGISTRAR OF TRADE MARKS, MUMBAI AND OTHERS** reported in **(1998)8 SCC 1** has held exercise of jurisdiction by the High Court to entertain a writ petition under Article 226 of the Constitution of India,

in spite of availability of alternative statutory remedies is not affected where the authority against whom the writ is sought for is shown to have exercised its jurisdiction which it had none or had usurped the jurisdiction without any legal foundation. The Hon'ble Apex Court in conclusion has held as under:

“20. Much water has since flown under the bridge, but there has been no corrosive effect on these decisions which, though old, continue to hold the field with the result that law as to the jurisdiction of the High Court in entertaining a writ petition under Article 226 of the Constitution, in spite of the alternative statutory remedies, is not affected, specially in a case where the authority against whom the writ is filed is shown to have had no jurisdiction or had purported to usurp jurisdiction without any legal foundation.

21. That being so, the High Court was not justified in dismissing the writ petition at the initial stage without examining the contention that the show-cause notice issued to the appellant was wholly without jurisdiction and that the Registrar, in the circumstances of the case, was not justified in acting as the “Tribunal”.

14. Thus, keeping this salutary principle in mind, when the facts on hand are examined, it would indicate that in the instant case, petitioner at the time of filing its return of income on 29.09.2009 claimed weighted deduction under Section 35(2AB) contending interalia that it is an allowable deduction. The assessing officer at paragraph 4.9 has held that approval issued by Department of Scientific and Industrial Research (for short 'DSIR') is a pre requisite to claim deduction under Section 35(2AB) but it cannot be held to be the only condition for claiming deduction under Section 35(2AB) of the Act.

15. Section 43 of the Act would indicate that definition of certain terms relevant to "*income from profits and gains of business or profession*" has been defined. Under sub-section (4) of Section 43, the word "**Scientific Research**" has been defined. On the one hand, the assessee is contending that once a certificate is issued by the prescribed authority, the jurisdictional

assessing officer would be out of bounds to examine the correctness of the said certificate. On the other hand, Revenue is contending that without going into the issue of the correctness of such certificate or its contents thereof, the power of the assessing officer to disallow the claim made by an assessee under Section 35(2AB) which does not include any expenditure incurred in the acquisition of rights, in, or arising out of scientific research would be within the domain of the jurisdictional assessing Officer. In other words, the issue of jurisdiction of assessing officer to examine such claim, is an issue which requires to be examined by this Court in this writ petition.

16. In the event of this Court coming to a conclusion that contention of the Revenue deserves to be accepted, then, the natural course which this Court will adopt is to dismiss the writ petition as being not maintainable since petitioner has an alternate remedy of filing statutory appeal. However, if it is being held that

such power is not available to the assessing officer, it will have to be necessarily held as writ petition being maintainable. In other words, when issue of jurisdiction is under consideration, it cannot be held that writ petition is not maintainable at the threshold. In that view of the matter, this Court is of the considered view that subject to the answer on Point No.2, this Court would answer Point No.1.

Re: Point No.2

17. In order to adjudicate the point No.2 relevant statutory provisions which will have bearing on the issue requires to be extracted and they are extracted herein below:

“Expenditure on scientific research.

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

(i) any expenditure (not being in the nature of capital expenditure) laid out or expended on scientific research related to the business.

(ii) to (iv) xxx

(2) For the purposes xxx of Section 32.

(2A) Where xxx of Section 32A.

(2AA) Where the assessee xxx authority.

(2AB) (1) Where a company engaged in the business of [bio-technology or in [any business of manufacture or production of any article or thing, not being an article or thing specified in the list of the Eleventh Schedule]] incurs any expenditure on scientific research (not being expenditure in the nature of cost of any land or building) on in-house research and development facility as approved by the prescribed authority, then, there shall be allowed a deduction of [a sum equal to [two] times of the expenditure] so incurred.

[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 Acts, 1970 (39 of 1970).]

(2) No deduction shall be allowed in respect of the expenditure mentioned in clause (1) under any other provision of this Act.

(3) No company shall be entitled for deduction under clause (1) unless it enters into an agreement with the prescribed authority for co-operation in such research and development facility and for

audit of the accounts maintained for that facility.

(4) The prescribed authority shall submit its report in relation to the approval of the said facility to the [Principal Director General or] Director General in such form and within such time as may be prescribed.

(5) No deduction shall be allowed in respect of the expenditure referred to in clause (1) which is incurred after the 31st day of March, [2017].

(6) No deduction shall be allowed to a company approved under sub-clause (C) of clause (iia) of sub-section (1) in respect of the expenditure referred to in clause (1) which is incurred after the 31st day of March, 2008.

(2B)(a) to (d) xxx

(3) If any question arises under this section as to whether, and if so, to what extent, any activity constitutes or constituted, or any asset is or was being used for, scientific research, the Board shall refer the question to-

- (a) the Central Government, when such question relates to any activity under clauses (ii) and (iii) of sub-section (1), and its decision shall be final;
- (b) the prescribed authority, when such question relates to any activity other than the activity specified in clause (a), whose decision shall be final.

- (4) The provisions xxx depreciation.
- (5) Where, in a scheme of amalgamation, xxx asset.”

Definitions of certain terms relevant to income from profits and gains of business or profession.

43. In sections 28 to 41 and in this section, unless the context otherwise requires—

- (1) "**actual cost**" means xxx section 47.
- (2) "**paid**" means actually xxx profession.
- (3) "**plant**" includes xxx fittings.
- (4)[(i) "**scientific research**" means any activities for the extension of knowledge in the fields of natural or applied science including agriculture, animal husbandry or fisheries;]
- (ii) references to expenditure incurred on scientific research include all expenditure incurred for the prosecution, or the provision of facilities for the prosecution, of scientific research, but do not include any expenditure incurred in the acquisition of rights in, or arising out of, scientific research;
- (iii) references to scientific research related to a business or class of business include—
 - (a) any scientific research which may lead to or facilitate an extension of that business or, as the case may be, all businesses of that class;

(b) any scientific research of a medical nature which has a special relation to the welfare of workers employed in that business or, as the case may be, all businesses of that class;

(5) "**speculative transaction**" means xxx this purpose.

(6) "**written down value**" means xxx this Act.

INCOME TAX RULES, 1961

Prescribed authority for expenditure on scientific research.

6. (1) For the purposes of clause (i) of sub-section (1) and sub-section (2A) of section 35, the prescribed authority shall xxx Government of India.

(1A) For the purposes of sub-section (2AA) of section 35, the prescribed authority shall be-

- (a) in the case xxx case may be;
- (b) in the case xxx Government of India.

(1B) For the purposes of sub-section (2AB) of section 35, the prescribed authority shall be the Secretary, Department of Scientific and Industrial Research.

(2) Omitted w.e.f. 30.10.2006

(3) The application for obtaining approval under sub-section (2AA) of section 35

shall be made by a sponsor in Form No.3CG.

Explanation: For the purposes of this rule “sponsor” means a person who makes an application in Form No.3CG

(4) The application required to be furnished by a company under sub-section (2AB) of section 35 shall be in Form No. 3CK.

(5) The head of the National Laboratory or the University or the Indian Institute of Technology [or the Principal Scientific Adviser to the Government of India] shall, if he is satisfied that it is feasible to carry out the scientific research programme then, subject to other conditions prescribed in this rule and section 35 (2AA) of the Act, pass an order in writing in Form No.3CH:

Provided that a reasonable opportunity of being heard shall be granted to the sponsor before rejecting an application:

Provided further that an order under this rule shall be passed within two months of the receipt of the application under sub-rule (1A):]

Provided also that the Principal Scientific Adviser to the Government of India may authorize an officer who is not below the rank of a Deputy Secretary to issue such order, after the scientific research programme has been approved by him.

(5A) The prescribed authority shall, if he is satisfied that the conditions provided in this rule and in sub-section (2AB) of

section 35 of the Act are fulfilled, pass an order in writing in Form No.3CM:

Provided that a reasonable opportunity of being heard shall be granted to the company before rejecting an application.

(6) The National Laboratory, University, Indian Institute of Technology or specified person] shall issue a receipt of payment for carrying out an approved programme of scientific research under sub-section (2AA) in Form No.3CI.

(7) xxx

(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) The facility should not relate purely to market research, sales promotions, quality control, testing, commercial production, style changes, routine data collection or activities of a like nature;

(b) The prescribed authority shall submit its report in relation to the approval of in-house Research and Development facility in Form No.3CL to the Director General (Income-tax Exemptions) within sixty days of its granting approval;

(c) The company shall maintain a separate account for each approved facility; which shall be audited annually and a copy thereof shall be furnished to the Secretary, Department of Scientific and Industrial Research by 31st day of October of 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 subsection (2) of section 288 of the Income-tax Act, 1961;

(d) Assets acquired in respect of development of scientific research and development facility shall not be disposed of without the approval of the Secretary, Department of Scientific and Industrial Research.

18. A plain reading of Section 35(2AB)(1) would indicate that where a company is engaged in the business of biotechnology or any business of manufacture or production of any article or thing, not

being an article or thing specified in the list of the Eleventh Schedule incurs any expenditure on “**Scientific Research**” (not being expenditure in the nature of cost of any land or building) on in-house, research and development facility “**as approved by the prescribed authority,**” such assessee would be entitled to a deduction of a sum equal to one and half times of the expenditure so incurred. The word “Scientific Research” has been defined under subsection (4) of Section 43 of the Act, which is extracted supra and same would indicate expenditure incurred in such scientific research includes all expenditure incurred for the prosecution or the provision of facilities for the prosecution of such scientific research. However, it does not include expenditure incurred in the acquisition of rights in or arising out of scientific research. Such expenditure incurred should be approved by the authority prescribed under Section 35(2AB) of the Act read with Rules framed thereunder. The authority prescribed to grant such approval under

Rule 6(1B) of the Income Tax Rules, 1961 is the Secretary, Department of Scientific and Industrial Research.

19. A perusal of the above rule would clearly indicate that the prescribed authority for the purposes of sub-section (1) of Section 35(2AB) is the Secretary, Department of Scientific and Industrial Research. Sub-section (3) of the Section 35(2AB) would indicate that no company would be entitled for deduction under clause (1) unless it enters into an agreement with the prescribed authority for cooperation in such research and development facility and for audit of accounts maintained for that facility. Said authority is required to examine the application and if satisfied that conditions provided under Section 35(2AB) are satisfied would pass an order in writing in Form No.3CM. In the event of such application of assessee is being rejected by the prescribed authority, an opportunity of being heard would be extended by the prescribed authority to

the assessee. As per sub-section (4) of Section 35(2AB) the prescribed authority would in turn submit its report to the approval of the said facility to the Director General (Income tax Exemptions) in Form No.3CL within 60 days as per Rule 7(A)(b) of the Rules. Approval of such expenditure incurred by a company under Section 35(2AB) would be subject to conditions stipulated in clauses (a) to (d) of Rule 7A of the Rules. This would clearly indicate that the prescribed authority after receiving the application under Rule 3CK would examine the said application in the background of the definition found in sub-section (4) of Section 43 and on being satisfied that such application satisfies the criteria prescribed under the Act, then alone it would issue the certificate by granting its approval to the expenditure incurred by a company. To put it differently, the prescribed authority is the authority under the Act which would examine the claim for grant of approval under Section 35(2AB). Pursuant to such application filed by assessee to the prescribed authority,

a report would be submitted by the prescribed authority to the Director General (Income tax Exemptions) in Form No.3CL in order to entitle the assessee to weighted deduction and such report by the prescribed authority would be forwarded to Director General (Income tax Exemptions) within 60 days from order of approval. This order in Form No.3CM would be passed by the prescribed authority only after being satisfied that the conditions provided in Rules (7A) and in sub-section (2AB) of Section 35 of the Act are fulfilled. Facts on hand would clearly indicate that application had been filed by assessee on 07.01.2009 and after calling for documents/information from assessee and on examination and scrutiny of such documents/information furnished by assessee, Order of approval came to be granted in favour of assessee on 18.11.2009 in Form No.3CM vide Annexure-G.

20. It would be apt to point at this juncture itself that in the event of any question would arise before the

assessing officer under Section 35 as to whether amounts certified by the prescribed authority is eligible for being allowed as expenditure and to what extent and whether such activity constitutes or constituted, or any asset is or was being used for scientific research in that regard, then assessing officer has to request the Board to refer such question to the prescribed authority as provided under clause (b) of Section 35(3). In other words, the correctness or otherwise of the order passed by the prescribed authority is not examined by the assessing officer or by the Income Tax Authority and this exercise is outsourced by the Income Tax Department and same is being done by the prescribed authority namely, Department of Scientific and Industrial Research. This is the plain meaning which can be deciphered from the perusal of above said statutory provisions.

21. Thus, reading of Section 35 (3) of the Act would clearly indicate that where the assessing officer

does not accept the claim of the assessee made under Section 35(2AB), he has to refer the matter to the Board, which in turn, will refer the question to the prescribed authority. The decision of the prescribed authority would be final as could be seen from clause (b) of subsection (3) of Section 35. Thus, it would emerge from above analysis that neither the assessing officer nor the Board is competent to take any decision on any such controversy relating to report and approval granted by "Prescribed Authority" as it involves expert view or opinion. The controversy arising out of certificate issued by the prescribed authority if any, has to be referred to the prescribed authority by the Board on such doubt being raised by assessing Officer and also on his request. It is the prescribed authority alone which would be competent to take a decision with regard to correctness or otherwise of its order of approval granted in Form No.3CL as prescribed under Section 35(2AB) of the Act read with Rule 7A of the Rules.

22. Aforesaid view is also fortified by the judgment rendered by the High Court of Gujarat in the case of **DEPUTY COMMISSIONER OF INCOME TAX (ASSTT.) VS MASTEK LIMITED** reported in **(2013) 263 CTR Guj 671**, wherein it has been held that whenever question arises as to whether and if so to what extent, any activity constitutes or constituted or any asset is or was being used for scientific research, the Board, as provided under Section 35(3) of the Act would have to refer the issue for the decision of the prescribed authority, whose decision would be final. It has been held as under:

“27. We are, however, of the opinion that insofar as the second aspect of the matter is concerned, the Tribunal was perfectly justified in holding in favour of the assessee. Section 35(3) of the Act as noticed requires a reference to be made by the Board to the prescribed authority when a question arises as to whether and if so to what extent, any activity constitutes or constituted or any asset is or was being used for scientific research. The decisions of the prescribed authority on such a question would be final. **In our opinion, therefore, whenever any such question arises, the Assessing Officer**

cannot decide the issue but must place the issue before the Board who, in terms of section 35(3) of the Act, would refer the question to the prescribed authority. The decision of the prescribed authority would govern the parties.

Therefore, if an assessee puts forth a claim of deduction under section 35(1) for expenditure incurred on scientific research and if the Assessing Officer is not inclined to accept such a claim, the question can be stated to have arisen, in such a situation, the Assessing Officer cannot take a decision but must seek the opinion of the prescribed authority. We may hasten to add that only when such a question arises that the reference would be competent. For example, if in a given case, the assessee lodges a claim without any supporting material, it cannot be stated that the question has arisen which would require a reference by the Board. Similarly, if the Assessing Officer accepts the claim of the assessee, no such question can be stated to have arisen. We are, however, unable to accept Shri. Bhatt's contention that such a question would arise only when the assessment is finally framed and that thereafter the onus would be on the assessee to seek a reference. No such intention is emerging from section 35(3) of the Act. Whenever an Assessing Officer is not inclined to accept the assessee's case for deduction, we fail to see how at that very stage, the question cannot be stated to have arisen."

(emphasis supplied)

23. Turning my attention back to the facts on hand, case-papers would indicate that on return of income being filed by the assessee, same came to be processed by the first respondent by issuing notices under Section 143(2) and 142(1) of the Act. After clarification called for and on discussion with the assessee's representative, draft assessment order dated 27.03.2013 came to be forwarded to the assessee wherein the income was proposed as against the loss returned in the return of income. On receipt of the draft assessment order, assessee filed its objections before the Dispute Resolution Panel – DRP i.e., second respondent herein who, after hearing the assessee issued directions on 30.12.2013 under Section 144C(5) of the Act and in compliance of the directions issued by the DRP, first respondent – assessing Officer concluded the final assessment. The assessing Officer under the assessment order dated 31.01.2013 disallowed the deduction claimed by the assessee under Section 35(2AB) of the Act on the following grounds:

(i) assessee has incurred expenditure of ₹ 13,95,73,315/- in respect of incompleting projects as the new products have not yet been developed;

(ii) ₹ 11,00,79,095/- which are treated as capital expenditure by the assessee represents know-how/technology ready for use contributing to increase in revenue and thereby of enduring benefit to the assessee and as against claim of ₹ 16,51,18,640/-, 25% of such expenditure representing know-how was allowed.

(iii) ₹ 9,14,82,154/- treated as capital work in progress was held as expenditures incurred on incomplete projects as the new products have not yet been developed and as such, do not qualify for deduction as revenue expenditure and accordingly, the weighted deduction claimed at ₹ 13,72,23,231/- came to be disallowed.

24. Thus, an amount of ₹ 48,41,82,071/- out of deduction of ₹ 89,35,48,193/- claimed under Section

35(2AB) was disallowed and added to the income of the assessee. It has been held by the second respondent that the mandate of the prescribed authority is limited to certifying to what extent, any activity constitutes or constituted, or any asset is or was being used for, scientific research. It is further held by the second respondent that allowability or otherwise of the expenditure will be governed by the express provisions of the Act. It has been held by the second respondent in the direction issued to the first respondent on 30.12.2013 under Annexure – Q as under:

“11.8 . Thus the mandate of the prescribed authority is limited to certifying to what extent, any activity constitutes or constituted, or any asset is or was being used for, scientific research. The allowability or otherwise of the expenditure will be governed by the express provisions of the Act. Where the express provision of the Act exclude certain kind of expenditure from the purview of section 35 of the Act, such expenditure cannot be allowed under section 35 of the Act and when certain expenditure does not fall in the scope of Section 35 of the Act the report of prescribed authority cannot be considered as far as such excluded expenditure is

considered. The certificate of the prescribed authority cannot overrule the express provisions of the Act. Thus the stand of the AO that such expenditure gives rise to patents on products/processes which are intellectual property rights and therefore such expenditure is capital in nature (Capital work in progress as the project is incomplete) and cannot be allowed u/s 35(i) of the Act is justified. As regards the allowability of depreciation on such capital work in progress, it has already been held that no depreciation is allowed on CWIP.

25. Insofar as disallowance under Section 35(2AB) of the Act is concerned, the DRP reiterated its above finding and held that where the express provisions of the Act exclude certain kind of expenditure from the purview of Section 35 of the Act, such expenditure cannot be allowed under Section 35 of the Act when such expenditure does not fall within the scope of Section 35 of the Act. Second respondent while issuing direction to first respondent on 30.12.2013 under Annexure – Q has held as under:

“12.1 We have carefully gone through the order passed by the Assessing Officer and by the TPO and the objections filed by the assessee as well as the records

of the case of the assessee. It has already been decided in para 11 above that where the express provisions of the Act exclude certain kind of expenditure from the purview of section 35 of the Act such expenditure cannot be allowed under section 35 of the Act and when certain expenditure does not fall in the scope of section 35 of the Act, the report of prescribed authority cannot be considered as far as such excluded expenditure is considered. The certificate of the prescribed authority cannot overrule the express provisions of the Act. It has also been held that product development expenditure gives rise to patents on products/processes which are intellectual property rights and therefore such expenditure is capital in nature (capital work in progress as the project is incomplete) and cannot be allowed u/s 35 of the Act. The arguments of the assessee in the said objection are essentially the same as in objection raised in para 11 above. Therefore the principle decided while dealing with such objection squarely applies to this objection also.

Accordingly, the assessing officer disallowed the deduction claimed by the assessee under Section 35(2AB) of the Act incurred by assessee in a sum of ₹ 48,41,82,071/- as against the total deduction of ₹ 89,35,48,193/- claimed by the assessee under Section 35(2AB) of the Act.

26. A perusal of the report submitted by the prescribed authority to the Director General of Income – Tax (Exemptions) under Section 35(2AB) in Form No.3CL dated 10.04.2013 vide Annexure-M would clearly indicate that as against claim of ₹ 8,935 lakhs made by the assessee for weighted deduction in its return of income, the prescribed authority allowed a sum of ₹ 6,904 lakhs only though the Audit Certificate dated 10.04.2013 – Annexure – E issued by the auditor of the assessee indicated ₹ 7,009 lakhs as weighted deduction.

27. A plain reading of Section 35(2AB) would clearly indicate that where a company is engaged in the business of [bio-technology or in any business of manufacture or production of any article or thing, not being an article or thing specified in the list of the Eleventh Schedule incurs any expenditure on scientific research (not being expenditure in the nature of cost of any land or building) or in-house research and

development facility as approved by the **prescribed authority**, then, they shall be allowed a deduction of a sum equal to one and a half times of the expenditure so incurred. The word used '**shall**' in the above said provision would ordinarily mean that it should be understood in the context in which it is used and there cannot be departure in this regard. The said provision would also indicate that such expenditure as approved by the prescribed authority would be entitled for being allowed as a weighted deduction. There being no dispute to the fact that DSIR being the prescribed authority in the instant case, had issued the report in Form No.3CL – Annexure – M certifying the total R & D expenditure (excluding land and buildings) as prescribed under Section 35(2AB) for a sum of ₹ 4,601.9 lakhs as against the claim of ₹ 5,957 lakhs made by the assessee in the return of income and as such, neither the second respondent nor first respondent could have sat in judgment over the said certificate issued by the prescribed authority. In other words, when the

prescribed authority had certified the extent of expenditure which would be allowable, the assessing officer could not have sat in appeal over such certification made by the prescribed authority. The allowability or otherwise of such expenditure cannot be the subject matter of scrutiny by the assessing officer. It would also be required to be noticed that the assessing officer would be out of bounds to examine as to whether such expenditure as certified by the prescribed authority can be allowed or disallowed under Section 35 of the Act. In other words, the assessing officer is precluded from examining the correctness or otherwise of the certificate issued by the prescribed authority on the ground that it is either being contrary to facts or contrary to the express provisions of the Act. It would not be out of context to state that when assessee files the report issued by the prescribed authority, as indicated under Section 35(2AB), before the jurisdictional assessing officer and seeks for allowability of such expenditure, the assessing Officer

would be exceeding in his jurisdiction, if he were to undertake the exercise of examining as to whether the certificate issued by the prescribed authority is within the parameters of statutory provisions of the Act or otherwise. Keeping in mind that such contingency may arise, Parliament has incorporated sub-section (3) to Section 35 of the Act which would be a complete answer to such situations. Thus, if any question arises as to what extent, any activity constitutes or constituted or an asset is or was being used for scientific research, then the assessing Officer would be required to refer such question to the Board for being referred to the prescribed authority. The decision of the prescribed authority in this regard would be final, inasmuch as, the certification of such expenditure is being examined by an expert body and undisputedly, such exercise has been outsourced by the Revenue under the Act itself, since the prescribed authority being possessed of requisite expertise, it would be in a better position to certify as to whether such expenditure claimed by the

assessee under Section 35(2AB) would fall within the said provision or outside. This exercise of examining the correctness of the Certificate issued by the prescribed authority is not available to the assessing Officer as could be seen from scheme of Section 35 of the Act.

28. It is in this background, sub-section (4) of Section 43 will have to be considered, which defines as to what activities would constitute “scientific research” as indicated under the said Section namely, Section 43(4). As to whether any expenditure incurred in the acquisition of rights in or arising out of scientific research as indicated in clause (ii) of sub-section (4) of Section 43 is an issue which requires to be examined by the prescribed authority itself and it would not be in the domain of the assessing authority to undertake such an exercise. When Section 35(2AB), Section 35(3) and Section 43(4) of the Act are read harmoniously, the irresistible conclusion that has be drawn would be that assessing officer cannot sit in judgment over the report

submitted by the prescribed authority in Form No.3CL. This view is also supported by the judgment of the High Court of Gujarat in **DCIT vs MASTEK LIMITED** referred to supra.

29. For the myriad reasons aforesaid, Point No.(2) formulated herein above will have to be answered in the affirmative i.e., in favour of petitioner – assessee and by concluding that the impugned order dated 31.01.2013 – Annexure – R and consequential demand notice dated 31.01.2014 – Annexure – R1 are without jurisdiction.

30. In view of the finding that assessing Officer – first respondent had no jurisdiction to sit in judgment over the report submitted by the prescribed authority in Form No.3CL as required under Section 35(2AB) of the Act read with Rule (7A)(b) of Income Tax Rules, 1961, it has to be held that the issue of entertaining the writ petition on the ground of alternate remedy would recede to background and it has to be held that present writ

petition would be maintainable in the facts obtained in the present case as discussed herein above and writ petition cannot be dismissed on the ground of petitioner having alternate remedy of appeal. Thus, facts on hand would fall within the exception carved out in **WHIRLPOOL's** case referred to supra.

31. In the result, I proceed to pass the following:

ORDER

- (1) Writ Petition is hereby allowed.
- (2) Assessment order dated 31.01.2013 (Annexure-R) and the consequential demand notice dated 31.01.2014 (Annexure-R1) are hereby quashed to the extent of addition made by the assessing Officer by disallowing the deduction under Section 35(2AB) of the Income Tax Act, 1961 and on all other issues, assessment order stands and no opinion is expressed in that regard and this order would not come in the way

of either parties to pursue their grievance if any before appellate authorities, if so advised.

- (3) It is also made clear that in the event of assessing Officer disputing the report of the prescribed authority dated 10.04.2013 (Annexure-M), he would be at liberty to seek reference to the prescribed authority through Central Board of Direct Taxes and on receipt of report from prescribed authority, pass assessment orders afresh on the said issue after granting opportunity to the petitioner.

- (4) No costs.

Ordered accordingly.

**Sd/-
JUDGE**

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