

IN THE HIGH COURT OF KARNATAKA AT BENGALURU

DATED THIS THE 30TH DAY OF MARCH 2015

PRESENT

THE HON'BLE MR. JUSTICE VINEET SARAN

AND

THE HON'BLE MRS. JUSTICE S.SUJATHA

ITA NO. 301/2014 A/W I.T.A. NOS.295/2014 & 300/2014

BETWEEN

1. THE COMMISSIONER OF INCOME TAX,
LTU, JSS TOWERS, BSK III STAGE,
BANGALORE.
2. THE INCOME TAX OFFICER (TDS),
LTU, JSS TOWERS, BSK III STAGE,
BANGALORE – 560 085.

(BY SRI. K.V. ARAVIND, ADV.)

... APPELLANTS
(COMMON IN ALL ITAs)

AND

M/S. ALLERGAN INDIA PVT. LTD.,
PRESTIGE OBELISK, NO.3,
KASTURBA ROAD,
BANGALORE – 560 001.

(BY SRI. T. SURYANARAYANA – ADV.
FOR M/S. KING & PATRIDGE, ADVS.)

...RESPONDENT
(COMMON IN ALL ITAs)

THESE ITAs ARE FILED UNDER SECTION 260-A OF THE INCOME TAX ACT 1961, PRAYING TO SET ASIDE COMMON ORDER DATED 7.3.2014 PASSED BY THE INCOME TAX APPELLATE TRIBUNAL, 'B' BENCH, BANGALORE, IN ITA NOS.283/BANG/2013, 281/BANG/2013 & 282/BANG/2013 FOR THE ASSESSMENT YEARS 2011-12, 2010-11 AND 2009-10 RESPECTIVELY AND ETC.

THESE ITAs COMING ON FOR ORDERS THIS DAY,
VINEET SARAN J. DELIVERED THE FOLLOWING:

JUDGMENT

These three appeals arise out of a common order of the Income Tax Appellate Tribunal, 'B' Bench, Bangalore whereby the appeals filed by the Revenue have been dismissed by the Tribunal. These appeals relate to the Assessment Years 2009-10, 2010-11 and 2011-12.

2. The brief facts of the case are that the respondent/assessee is engaged in the business of trading of ophthalmic products. The manufacturing of the products is outsourced by the assessee to other companies, including Piramal Health Care Ltd. (PHL) (previously known as Nicholas Piramal India Ltd.). In the year 1995 the assessee Company had entered into a Contract Manufacturing Agreement with PHL under which PHL had agreed to manufacture and sell to the assessee certain pharmaceutical and contact lens care products on a principal to principal basis. The key features of the agreement have been noted in the order of the Tribunal which have not been disputed by the parties and hence, for convenience, are being reproduced below :-

- *The assessee grants to PHL a license to use the know-how, the product specification and the packing and labeling specification to manufacture the product (clause 2.1 of the Agreement);*
- *PHL shall manufacture the product at its facility and sell the products to the assessee at cost (clause 2.2(a)(i) and 2.2(a)(ii) of the Agreement);*
- *The assessee is required to place purchase orders for supply of the product and PHL shall deliver products at the specified time and destination mentioned in the purchase order (clause 3.2 of the Agreement);*
- *The property in the product passes from PHL to the Assessee only upon the delivery of the product to the Assessee (clauses 3.2 of the Agreement);*
- *PHL shall invoice to the Assessee for all purchases made by it at the time of shipment of the product to the Assessee (clause 3.2 and 3.3 of the Agreement);*
- *The Assessee shall not reimburse PHL for any packing components, work in progress or finished product, which are damaged, destroyed or which becomes obsolete or otherwise spoiled and cannot be sold or distributed due to the act or omissions of PHL (clause 4.3 of the Agreement); and*

- *The relationship of the parties as established by this agreement is solely that of the buyer and seller (clause 10.13 of the Agreement).*
- *The raw materials required in the manufacture of the product are obtained by PHL from a person other than the Assessee.*

Supply of Machinery

- *As per clause 2.10 of the Agreement, during the FY 1997-98, PHL had purchased the CLCP moulds [hereinafter referred to as 'machines'] for a consideration of Rest. 2.86 cores on behalf of, and upon receiving instructions from the Assessee.*
- *These machines were installed in the manufacturing facility of PHL and the machines were used by PHL for manufacturing the products during the FY 1997-98 and 1998-99 [relevant to AY 1998-99 and AY 1999-2000].*
- *Thereafter, the Assessee decided to import the products which were manufactured by those machines, hence the machines are not actually used in the subsequent financial years.*
- *During the FY 1998-99 [relevant to AY 1999-2000], the Assessee charged off an amount of Rs.20,625,000 in its profit and loss account as*

additional depreciation towards obsolescence of machines kept in the manufacturing facilities of PHL.

- *Accordingly, the machines were not used during the year in question either by the Assessee or PHL for manufacturing the products.*

3. According to the Revenue, for the said three assessment years, payments of Rs.88,25,70,426/- had been made by the assessee to PHL without deducting tax at source, which according to the Revenue should have been done at 2% under Section 194C of the Income Tax Act (hereinafter referred to as 'the Act' for brevity). The Assessing Officer, after holding that payments had been made for execution of contract work falling under Section 194C, further held that the assessee defaulted in deducting tax at source on the payments made to PHL and thus passed an order for payment of tax under Section 201(1) and for payment of interest under Section 201(1A) of the Act. Consequently, a total amount of tax and interest of Rs.2,25,70,387/- was levied by the Assessing Officer. The appeals filed by the assessee were allowed by the Commissioner of Income Tax (Appeals). Challenging the said order, the Revenue filed appeals before the Tribunal, which have also

been dismissed. Aggrieved by the same, these appeals have been filed raising the following questions of law :-

1. *Whether on the facts and in the circumstances of the case, the appellate authorities were correct in holding that the payment made by the assessee to M/s. Nicolas Piramal India Ltd., is towards sale and provisions of section 194C of the Act is not attracted without taking into consideration that the technical know-how for manufacture of the products was provided by the assessee to M/s. Nicolas Piramal India Ltd., and M/s. Nicolas was only a manufacturing agent and recorded a perverse finding?*
2. *Whether on the facts and in the circumstances of the present case the appellate authorities failed to take into consideration that the transaction between the assessee and M/s. Nicolas Piramal India Ltd., is not a sale transaction but it's a contract manufacturing attracting provisions of section 194C of the Act?*

4. We have heard Sri.K.V.Aravind, learned counsel appearing for the appellant as well as Sri.T.Suryanarayana, learned counsel appearing for the assessee/respondent in all the three appeals and have perused the record. With consent of the learned counsel for

the parties, these appeals have been heard and are being disposed of at the admission stage.

5. There can be the following three situations in a business of the respondent Pharmaceutical Company :

1) The Pharmaceutical Company itself manufactures the products and sells the same?

2) The Pharmaceutical Company gets the products manufactured from another manufacturer after supplying the raw material to such manufacturer and the product is thus manufactured on behalf of the Company by the manufacturer ?

3) The Pharmaceutical Company provides its specifications to their manufacturer for producing or manufacturing the pharmaceutical products and supply the same to the Company after affixing the trade mark or brand name of the Company but the Company does not supply any raw material to the manufacturer?

6. The present is a case which falls in the 3rd i.e., last category. The facts as noted above are not disputed by the parties. It is also not disputed that at no stage any physical raw material was supplied by the assessee to PHL for manufacture and supply of the pharmaceutical products to the assessee. Undoubtedly, the

specifications had been given, according to which the manufacturer (PHL) had to manufacture and supply the products. The only question which arises for consideration is that when the assessee had granted PHL (manufacturer) the licence to use the know-how, the product specification, the packaging and labelling specifications, would the same be covered within the meaning of 'contract for work' or would it be a 'contract for sale'.

7. Section 194C of the Act relates to 'payments to contractors' and the explanation to the said Section defines 'work'.

The relevant extract of Section 194C is produced below :-

"194C- Payments to contractors

(1) Any person responsible for paying any sum to any resident (hereinafter in this section referred to as the contractor) for carrying out any work (including supply of labour for carrying out any work) in pursuance of a contract between the contractor and a specified person shall, at the time of credit of such sum to the account of the contractor or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct an amount equal to -

(i) one per cent where the payment is being made or credit is being given to an individual or a Hindu undivided family;

(ii) two per cent where the payment is being made or credit is being given to a person other than an individual or a

Hindu undivided family, of such sum as income-tax on income comprised therein.

(2) xxxxx

(3) xxxxx

Explanation -For the purposes of this section,-

(i) xxxxx

(a) xxxxx

(b) xxxxx

(c) xxxxx

(d) xxxxx

(e) xxxxx

(f) xxxxx

(g) xxxxx

(h) xxxxx

(i) xxxxx

(j) xxxxx

(k) xxxxx

(l) xxxxx

(A) xxxxx

(B) xxxxx

(ii) xxxxx

(iii) xxxxx

(iv) "work" shall include -

(a) xxxxx

(b) xxxxx

(c) xxxxx

(d) xxxxx

(e) *manufacturing or supplying a product according to the requirement or specification of a customer by using material purchased from such customer.*

but does not include manufacturing or supplying a product according to the requirement or specification of a customer by using material purchased from a person, other than such customer.”

It is relevant to note that ‘work’ includes manufacturing or supplying a product according to a specification of a customer by using material supplied from such customer.

8. According to Sri.Aravind, learned counsel for the appellant, “material” would include the “know how” which was supplied by the assessee to the manufacturer and hence it would be a ‘contract for work’ and not merely a ‘contract for sale’ as the main ‘material’ was the ‘know how’ which was supplied by the assessee. What is relevant is that the aforesaid explanation provides for using of material purchased from the customer. Although ‘know how’ is not a ‘material’, but even if ‘know how’ is taken as a ‘material’ supplied by the assessee, there has to be a finding to the effect that the said ‘know how’ (material) was purchased by the manufacturer from the assessee. In the present case, there is a specific admission made by the appellant in the grounds raised by it before the Tribunal that the technical ‘know how’ for the manufacture of the product was with the assessee and no royalty was

received by the assessee for the technical 'know how'. This would clearly mean that there was no sale or purchase of the technical 'know how'. Thus, even if we consider the technical 'know how' to be a material, when there was no purchase of such 'know how' from the assessee, contract cannot be termed as 'contract for work' under the explanation to Section 194C of the Act.

9. The learned counsel for the appellant has placed reliance on the decision of this Court in the case of **Commissioner of Income Tax, Central Circle - vs - Nova Nordisk Pharma India Ltd.** reported in (2012) 341 ITR 451 to support his contention that in a case where the assessee company gets the product prepared or manufactured from another company, the same would be termed as a 'contract for work' and thus the provisions of Section 194C of the Act would be attracted.

10. Having gone through the said judgment what we notice is that the assessee therein had got the product manufactured by another company from the materials supplied by its foreign holding company and also by supplying technical know how. As such the foreign company, which supplied the raw material to the manufacturer, had a direct interest in the assessee company in India and even the

trade mark of the foreign supplier company was to be borne in the product to be marketed. It was after considering the agreements between the assessee and the manufacturer as well as the other agreements between the foreign holding company and the assessee etc. that this Court had come to the conclusion that the assessee therein would be one which fits into the definition and the situation contemplated under Section 194C of the Act.

11. The facts of the aforesaid case are thus different from the one in hand. Even otherwise, the aforesaid case relates to the Assessment Year 1997-98, when the said explanation in Section 194C was not there. Section 194C was substituted by Finance Act No.2 of 2009 with effect from 1.10.2009. Prior to the said amendment the explanation, as referred to above, was not there in Section 194C. As such also, the said judgment in the case of **Nova Nordisk Pharma India Ltd.** (supra) would not apply to the facts of the present case.

12. In the present case, admittedly no raw material was supplied by the assessee to the manufacturer and if the 'know how' was given to the manufacturer, it was not on payment of any licence fees or royalty. As such, on facts it is clear that even the 'know how', if termed

as a 'material', was not purchased by the manufacturer from the assessee.

13. A case similar to the one in hand came up before the Bombay High Court in the case of **Commissioner of Income-Tax – vs – Glenmark Pharmaceuticals Ltd.** reported in (2010) 324 ITR 199 (Bom) which has, in such facts, also held that in a case where no raw material is supplied by the assessee to the manufacturer, it could not be treated to be 'work' within the definition provided in the Explanation (iv) (e) of Section 194C of the Act and has thus answered the similar question, as raised in this case, in favour of the assessee and against the Revenue.

14. In view of the aforesaid facts and circumstances, we are of the firm opinion, no substantial question of law arises for consideration by this Court. Accordingly, *these appeals stand dismissed.*

Sd/-
JUDGE

Sd/-
JUDGE