

IN THE HIGH COURT OF GUJARAT AT AHMEDABAD**TAX APPEAL NO. 956 of 2007****With****TAX APPEAL NO. 957 of 2007****With****TAX APPEAL NO. 2231 of 2009****With****TAX APPEAL NO. 2232 of 2009****With****TAX APPEAL NO. 698 of 2008****With****TAX APPEAL NO. 700 of 2008****FOR APPROVAL AND SIGNATURE:****HONOURABLE MR.JUSTICE KS JHAVERI****and****HONOURABLE MR.JUSTICE G.R.UDHWANI**

1	Whether Reporters of Local Papers may be allowed to see the judgment ?	
2	To be referred to the Reporter or not ?	
3	Whether their Lordships wish to see the fair copy of the judgment ?	
4	Whether this case involves a substantial question of law as to the interpretation of the Constitution of India or any order made thereunder ?	

THE COMMISSIONER OF INCOME TAX AHMEDABAD - IV....Appellant(s)**Versus****TORRENT PHARMACEUTICALS LTD.....Opponent(s)**

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Appearance:

MR NITIN K MEHTA, ADVOCATE for the Appellant(s) No. 1

MR SN SOPARKAR, SR. ADVOCATE WITH MRS SWATI SOPARKAR,
ADVOCATE for the Opponent(s) No. 1

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CORAM: **HONOURABLE MR.JUSTICE KS JHAVERI**
and
HONOURABLE MR.JUSTICE G.R.UDHWANI

Date : 27/07/2016

ORAL JUDGMENT

(PER : HONOURABLE MR.JUSTICE KS JHAVERI)

1. In all these Tax Appeals, the assessee is the same. Therefore, they are heard together and disposed of by this common judgment.

2. Tax Appeal No.956/2007 arises out of the common order dated 29.12.2006 passed by the Income Tax Appellate Tribunal, Ahmedabad [for short, "the Tribunal"] in ITA No.1141/Ahd/1999 raising the following questions of law for our determination:

“(A) Whether the Appellate Tribunal was right in law and on facts in holding that for the purpose of computing deduction u/s 80HH and 80I, deductions u/s 35(1)(iv) are not to be deducted ?

(B) Whether the Appellate Tribunal was right in law and on facts in deleting the disallowance of redemption premium amounting

to Rs. 2,00,000/- payable to debenture holders ?”

2.1 Tax Appeal No.957/2007 also arises out of the common order dated 29.12.2006 passed by the Tribunal in ITA No.856/Ahd/1999 raising the following questions of law for our determination:

“(1) Whether the Appellate Tribunal was right in law and on facts in holding that for the purpose of computing deduction u/s 80HHC and 80I, deductions u/s 35(1)(iv) are not to be deducted ?

(2) Whether the Appellate Tribunal was right in law and on facts in holding that deduction for the use of technical know-how is allowable u/s.37 and deduction for the acquisition of technical know how is allowable u/s.35AB of the Act ?”

3. Tax Appeal No.698/2008 arises out of the common order dated 29.06.2007 passed by the Tribunal in ITA No.37/Ahd/2002 raising the following question of law for our determination:

“Whether the Appellate Tribunal is right in law and on facts in holding that deduction u/s.80HH is to be allowed on the eligible income without deduction u/s.35(2)(1a) ?”

3.1 Whereas, Tax Appeal No.700/2008 also arises out of the same common order dated 29.06.2007 passed by the Tribunal in ITA No.651/Ahd/2001

raising the following questions of law for our determination:

"[A] Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the CIT(A) holding that deduction u/s.80HH & 80I is to be allowed without deduction u/s.35AB and u/s.35(1)(iv)?

[B] Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the CIT(A) holding that redemption premium payable on debenture of Rs.2,00,000/- was an allowable deduction ?"

4. Tax Appeal No.2231/2009 is filed against the order dated 29.05.2009 passed by the Tribunal in ITA No.263/Ahd/2003 raising the following question of law for our determination:

"Whether the Appellate Tribunal is right in law and on facts in reversing the order passed by CIT(A) and thereby directing to allow deduction u/s.80HH of the I.T. Act, 1961 ?"

4.1 Whereas, Tax Appeal No.2232/2009 also arises of the order dated 29.05.2009 passed by the Tribunal in ITA No.590/Ahd/2003 raising the following question of law for our determination:

"(A) Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by CIT(A) in directing the Assessing Officer to allow the claim of the assessee

amounting to Rs 6,08,76,939/- being Market Development expenditure ?

(B) Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by CIT(A) in deleting the disallowance of Rs 1,47,75,524/- being interest expenditure ?

(C) Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by CIT(A) in deleting the disallowance of Rs 61,79.000/- being interest on funds utilised for non-business advances ?

(D) Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by CIT(A) in directing to allow deduction u/s 80HH of the I.T Act, 1961 ?

(E) Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by CIT(A) in holding that for computation of deduction u/s. 80HHC only net interest receipts should be excluded ?"

5. The assessee herein is a part of Torrent Group and is engaged in the manufacture and sale of pharmaceutical products. Its factories are situated in Ahmedabad and Mehsana Districts. The products of the assessee company are also exported through its sister concern, viz. Torrent Exports Ltd. & Ruainde Pharmaceuticals Ltd. For the purpose of this judgment, T.A. No.956/2007 is taken as the lead matter.

6. The assessee filed its return of income on

30.11.1995 for the A.Y. 1995-96 declaring total income of Rs.12,40,87,170/-. The said return was processed u/s.143(1)(a) of the Act. Subsequently, a revised return of income was filed on 19.03.1997 declaring total income at Rs.11,51,49,350/- for the reason that there was a change in the computation of relief u/s.80HH and 80I of the Act. Ultimately, the assessment order came to be passed on 30.03.1998. Against the said order, the assessee preferred appeal before the CIT(A), which was partly allowed vide order dated 15.03.1999. Being aggrieved by the same, the assessee preferred appeals before the Tribunal. Both the appeals were partly allowed by order dated 29.12.2006. Hence, the present Tax Appeals.

7. We have heard learned counsel for both the sides and perused the documents on record. For the sake of convenience, we shall deal with every Tax Appeal question-wise.

TAX APPEAL No.956/2007 :

8. Question No.(A) relates to deduction u/s.35(1)(iv) vis-a-vis deductions u/s.80HH and 80I of the Act. Section 35(1) of the Act allows deduction for revenue as well as capital expenditure. Section 35(1)(i) allows deduction for revenue expenditure while Section 35(1)(iv) allows deduction for capital expenditure incurred

on scientific research related to the business of assessee. Whereas, deductions u/s.80HH and 80I of the Act are computed as percentage of the profits and gains "derived from" eligible industrial undertakings. The purpose of the said two sections is to allow deductions only in respect of profit and gains, which is derived from eligible undertaking. The methodology used for both the sections are different from each other. Therefore, there should be direct linkage between the profit and the industrial undertaking. It must directly come out of the industrial undertaking. This means that while determining profit of eligible industrial undertaking, the income and expenditure which has direct nexus with the industrial undertaking must be taken into account.

8.1 It is not in dispute that research centre is an independent centre and that its main object is to conduct research for the business of the assessee. The research centre, therefore, in our opinion, is not directly linked with the eligible undertaking. Thus, for the purpose of computing deduction u/s.80HH and 80I, profit from eligible undertaking is to be computed on the basis of gross income by reducing expenditure which has been incurred for the eligible undertaking out of the gross income derived from the industrial

undertaking. In view of the aforesaid, question no.(A) is answered in favour of the assessee and against the Revenue.

9. As regards Question No.(B), it transpires that the assessee company had issued 2,00,000 and 1,20,000 secured redeemable non-convertible debentures on 29.03.1991 and 10.04.1991 respectively. On the face value of the debentures, the assessee was required to pay Rs.5/- to the investor at the time of redemption of the debenture amount.

9.1 It is pertinent to note that in the accounting period relevant to A.Y. 1991-92 and 1992-93, the assessee had not debited the aforesaid amount in the books of accounts. Before the A.O., the assessee claimed that the amount payable at the time of redemption by way of premium was deductible proportionately in each of the years during the life of the debenture and accordingly, claimed deduction of Rs.2,00,000/- for the year under consideration being $1/8^{\text{th}}$ of the redemption premium payable of Rs.16.00 Lacs. However, the A.O. and Tribunal disallowed the claim on the ground that the assessee had not debited its account with the amount of redemption premium in the accounting years relevant to A.Y. 1991-92 and 1992-93.

9.2 In our opinion, the conclusion arrived at by both the A.O. and the Tribunal is erroneous since the liability to pay Rs.105/- to the debenture-holders, was not contingent but, was dependable upon the exercise of option by the assessee company to repurchase the debentures before the period. In other words, the payment of Rs.105/- by assessee company against the collection of receipt of Rs.100/- from debenture-holders was not contingent upon the happening of any event in future. The company's obligation to pay Rs.105/- against receipt of Rs.100/- was certain *in praesenti* and known at the time when the debentures were issued and was to be payable in ordinary circumstances. It was only for the company to avoid payment of such liability if it decides to repurchase the debentures earlier. Such repayment prior to the due date, was contingent on exercise of option. It would not make the liability, which is certain *in praesenti*, to be contingent merely because on happening of a certain event, which could be avoided. In view of the aforesaid, the Tribunal was in error in confirming the order of A.O. of disallowing the expenditure towards redemption premium payable to debenture-holders. Consequently, we answer Question no.(B) in favour of the assessee and against the Revenue.

TAX APPEAL No.957/2007 :

10. Insofar as Question No.(1) is concerned, the same is already answered in Tax Appeal No.956/2007 in the form of Question No.(A). Consequently, Question No.(1) in this appeal is answered in favour of the assessee and against the Revenue.

11. Insofar as Question No.(2) is concerned, we find that the Tribunal has set aside the order passed by the revenue authorities on the issue and has remitted the matter to the file of A.O. with the direction that if the A.O. is of the view that consideration has been paid by the assessee for the use of technical know-how, then deduction should be allowed to the assessee as revenue expenditure. Considering the discussion made by the Tribunal on the issue, we concur with the view taken by the Tribunal and accordingly, keep the issue open for adjudication by the A.O. Accordingly, the issue is remitted to the file of A.O. for consideration afresh on merits. Consequently, Question No.(2) remains unanswered and is kept open for adjudication by the A.O.

TAX APPEAL No.2231/2009:

12. In this appeal, the sole question relates to deduction u/s.80HH of the Act. The A.O. did not

allow deduction u/s.80HH in view of the assessment orders for the A.Y. 1991-92 to 1996-97. Alternatively, the A.O. recorded a finding that subsequently, even if the claim is held to be allowable, it should be restricted to the following : (i) Job charges would not form part of the manufacturing activities; and (ii) Deduction u/s.80HH is to be allowed after reducing deduction u/s.35(2AB) and 35(1) of the Act. The CIT(A) deleted the addition relating to the issue of Job charges and sustained the order relating to the other issue, which was confirmed by the Tribunal. While entertaining the appeal, the Tribunal followed its earlier decision passed in the case of this very assessee in ITA No.446/Ahd/2002. We have gone through the elaborate discussion made by the Tribunal on the issue and accordingly, concur with the view taken by the Tribunal. Consequently, we answer the Question in favour of the assessee and against the Revenue.

TAX APPEAL No.2232/2009:

13. As regards Question No.(A), we find that the Tribunal has followed its earlier decision passed in respect of this very assessee in ITA No.446/Ahd/2002. In our opinion, the Tribunal rightly held that the assessee is entitled to weighted deduction in respect of the entire

expenditure incurred for the development of in-house "R&D" facility in terms of Section 35(2AB) of the Act. Consequently, we answer Question No. (A) in favour of the assessee and against the Revenue.

14. As regards Question No.(B), the A.O. found that the assessee had capitalized interest receipt amounting to Rs.1,47,45,524/- in its books of account but, while filing the return, had claimed it as deduction. The assessee stated that the company had paid interest on funds borrowed for the expansion project and since the project could not be completed, the interest expenditure was capitalized. But, as the expenditure was incurred for the purpose of business, it was claimed as deduction u/s.36(1) (iii) of the Act. The A.O. disallowed the interest expenditure. On appeal, the CIT(A) deleted the disallowance by following the decision of this Court in the case of *DCIT v. Core Healthcare Ltd.* v. CIT reported in 251 ITR 61 (Guj). The said decision of this Court has been confirmed by the Apex Court by judgment rendered in *DCIT v. Core Healthcare Ltd.* reported in [2008] 298 ITR 194 (SC). Thus, we answer Question No.(B) in favour of the assessee and against the Revenue.

15. As regards Question No.(C), the A.O. observed that the assessee company had paid substantial interest on loans borrowed by it but, had advanced interest free non-business advance to one M/s. Baldevbhai Dosabhai Group. The assessee had paid interest at the rate of 14% to 19% on the loans borrowed and therefore, the A.O. calculated interest at 18% on the advances made to M/s. Baldevbhai Dosabhai Group and disallowed the same out of the claim for interest expenses.

15.1 However, after considering the records, the Tribunal found that advance had been given for the purpose of business. It appears from the record that the assessee had earned income during the year to the extent of Rs.36 Crores. The assessee had submitted evidence to prove that it was having interest free funds to the extent of Rs.225.83 Crores with it. However, the said fact was not appreciated by the A.O. Nothing was on record to prove that the borrowed funds had been diverted by the assessee for making advances to M/s. Baldevbhai Dosabhai Group. Hence, we answer the Question in favour of the assessee and against the Revenue.

16. Insofar as Question No.(D) is concerned, we have already answered it in Tax Appeal No.2231/2009, as discussed herein above. Hence,

this issue will be governed by the decision rendered in Tax Appeal No.2231/2009. Consequently, the Question is answered in favour of the assessee and against the Revenue.

17. As regards Question No.(E), the same is covered by the decision of Apex Court in the case of *ACG Associated Capsules Pvt. Ltd. v. Commissioner of Income-tax*, [2012] 343 ITR 89 (SC) wherein, it has been held that ninety per cent of not the gross rent or gross interest but only the net interest or net rent, which had been included in the profits of business of the assessee as computed under the head "Profits and gains of business or profession", was to be deducted under clause (1) of Explanation (baa) to Section 80HHC for determining the profits of the business. In view of the above decision, this question is also answered in favour of the assessee and against the Revenue.

TAX APPEAL No.698/2008:

18. The sole question raised in this appeal is already answered by us in Tax Appeal No.956/2007 in the form of Question No.(A). Hence, this issue will be governed by the decision rendered for Question No.(A) in Tax Appeal No.956/2007. Consequently, this issue is also answered in favour of the assessee and against the Revenue.

TAX APPEAL No.700/2008:

19. Both the issues raised in this appeal are already answered in Tax Appeal No.956/2007 in the form of Question Nos.(A) & (B). Hence, both the issues shall be governed by the judgment rendered in Tax Appeal No.956/2007, discussed herein above. Consequently, both the questions are answered in favour of the assessee and against the Revenue.

20. In view of the above discussion, all the Tax Appeals stand disposed of. No order as to costs.

(K.S.JHAVERI, J.)

(G.R.UDHWANI, J.)

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