

---

**(1996) 09 P&H CK 0006**  
**In the Punjab And Haryana At Chandigarh**  
**Case No : IT Case No's. 31 to 33 of 1995**

COMMISSIONER OF INCOME TAX

APPELLANT

Vs

SMITHKLINE BEECHAM CONSUMER BRANDS LTD.

RESPONDENT

---

**Date of Decision :** 07-09-1996

**Acts Referred:**

Income Tax Act, 1961 — Section 256(2)

**Citation :** (1997) 143 CTR 167

**Hon'ble Judges :** N. K. Agrawal, J

**Bench :** Division Bench

---

## Judgement

N. K. AGRAWAL, J. :

These three petitions (IT Cases Nos. 31, 32 and 33 of 1995) filed by the CIT under s. 256(2) of the IT Act, 1961 (for short, "the Act"), relate to the asst. yrs. 1983-84, 1985-86 and 1982-83, respectively. Since the questions required to be referred arise from similar facts in all the years, these questions are being considered by this common order.

2. The questions of law required to be referred in these petitions are as under :

Questions of law arising from the order of the Tribunal for the asst. yr. 1982-83 (ITC No. 33 of 1995) :

(i) Questions of law arising out of R.A. No. 95A of 1993/ITA No. 986 of 1987.

"1. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in allowing weighted deduction on 50 per cent. of expenditure on travelling to foreign countries by the directors and officers of the company ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the company may not constitute agency or office outside India to avail of deduction under s. 35B on commission when provisions of this section are mandatory to have branch office or an agency outside India ?

3. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in allowing weighted deduction under s. 35B on advertisement and marketing expenditure ?

4. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in permitting the change in the method of accounting with regard to the valuation of closing stock from absorption cost method to direct cost method ?

5. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the change in the method of accounting with regard to the valuation of stock is bona fide and not with an intention to defeat the Revenue when the issue of determining items of direct cost is highly debatable ?

6. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in directing the AO to consider the decision of the Special Bench regarding valuation of closing-stock ?"

(ii) Question of law arising from R.A. No. 955 of 1993/ITA No. 1088 of 1987, -

"1. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in allowing extra shift allowance on new plant and machinery on the working of the concern as a whole even for the period when the new machinery was not available with the assessee ?"

Questions of law arising from the order of the Tribunal for the asst. yr. 1983-84 (ITC No. 31 of 1995) :

(i) Questions of law arising out of R.A. No. 956 of 1993/ITA No. 987 of 1987, -

"1. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that company may not constitute agency or office outside India to avail of deduction under s. 35B on commission, when the provisions of this section are mandatory to have branch office or an agency outside India ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that 50 per cent. expenditure on travelling to foreign countries by the directors/officers of the assessee-company is entitled for deduction under s. 35B ?

3. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in permitting the change in the method of accounting with regard to the valuation of closing stock from absorption cost method to direct cost method ?

4. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the change in the method of accounting with regard to valuation of stock is bona fide and not with an intention to defeat the Revenue when the issue of determining items of direct cost is highly debatable ?

5. Whether, on the facts and in the circumstances of the case, the Tribunal was

right in law in holding that the method of accounting with regard to valuation of closing stock is followed from year to year regularly and consistently ?"

(ii) Questions of law arising from R.A. No. 957 of 1993/ITA No. 1089 of 1987, -

"1. Whether, on the facts and in the circumstances of the case, the Tribunal is right in law in holding that expenditure on the purchase of air-conditioner, cooler, calculator and fans is entitled for deduction under s. 35(1)(iv)?

2. Whether, on the facts and in the circumstances of the case, the Tribunal is right in allowing extra shift allowance on new plant and machinery on the working of the concern as a whole even for the period when the new machinery was not available with the assessee ?"

Questions of law arising from the order of the Tribunal for the asst. yr. 1985-86 (ITC No. 32 of 1995) :

(i) Questions of law arising out of R.A. No. 958 of 1993/ITA No. 988 of 1987, -

"1. Whether, on the facts and in the circumstances of the case, the Tribunal was right in permitting the change in the method of accounting with regard to the valuation of closing stock from absorption cost method to direct cost method ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the change in the method of accounting with regard to valuation of stock is bona fide and not with an intention to defeat the Revenue when the issue of determining items of direct cost is highly debatable ?

3. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the method of accounting with regard to the valuation of closing stock is followed from year to year regularly and consistently ?

4. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in directing the AO to consider the decision of the Special Bench, regarding whether closing stock should be valued including excise duty or whether it conflicts with s. 43B when s. 43B is independent ?"

(ii) Questions of law arising out of R.A. No. 959 of 1993/ITA No. 1090 of 1987, -

"1. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that excise duty of Rs. 56,02,176 written back in the books of accounts after winning the case from the High Court is not includible in the taxable income of the assessee under s. 41(1) or under s. 43B of the IT Act ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that a refund of excise duty of Rs. 1,33,00,000 is not assessable to tax during the assessment year under consideration under s. 41(1) or under s. 43B ?

3. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in giving the same decision in respect of write back of excise duty of

Rs. 56,02,176 and refund of excise duty of Rs. 1,33,00,000 when one issue is being contested by the assessee and the other by the Excise Department before the Supreme Court ?

4. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding bad debts of Rs. 1,71,73,148 ?

5. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the medical expenses by way of payment of group insurance, reimbursement of medical expenses, electricity, water, gas charges and salaries to servants shall not be treated as perquisites for computing disallowance under s. 40(c) and s. 40A(5) ?

6. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in allowing extra shift allowance on new plant and machinery on the working of the concern as a whole even for the period when the new machinery was not available with the assessee ?"

3. Questions on the valuation of closing stock - The questions raised on the method of valuation of the closing stock in all the three asst. yrs. (1982-83, 1983-84 and 1985-86) arise from the change in the method of accounting adopted by the assessee in the asst. yr. 1982-83 and then followed in the subsequent assessment years. The assessee's plea was that valuation of the closing stock could be done either at cost or at the market value. The assessee opted for the valuation at cost. But the question did not rest there as the controversy arose in the year 1982-83 when the assessee switched over from the absorption cost method to the direct cost method with the plea that the latter method was a recognised, scientific and proper method of valuation. Reliance was placed on the decision of the Supreme Court in CIT vs. British Paints India Ltd. : [1991]188ITR44(SC). The assessing authority noticed that, while adopting the cost method, the assessee had excluded different overhead expenses relating to the production and milk collection. These expenses had earlier been included in the value of the closing stock but, from the asst. yr. 1982-83, various fixed and variable overhead expenses were excluded.

4. Certain questions of law have already been referred at the assessee's instance by the Tribunal to this Court under s. 256(1) of the Act on the method of valuation of the closing stock. Looking to the controversy, the following question of law arises for opinion :

"Whether, on the facts and in the circumstances of the case, change from the absorption cost method to the direct cost method in the valuation of the closing stock was rightly allowed to the assessee on the ground that it was a bona fide change being followed regularly and consistently in the subsequent years and was not adopted in order to defeat the Revenue ?"

The aforesaid consolidated question has been framed in the light of questions Nos. 4 and 5 raised in the asst. yr. 1982-83, questions Nos. 3, 4 and 5 in the

asst. yr. 1983-84, and questions Nos. 1, 2 and 3 in the asst. yr. 1985-86 in the applications filed under s. 256(2) of the Act.

5. Questions on weighted deduction under s. 35B - The assessee had claimed weighted deduction on certain expenditures. In the asst. yr. 1982-83, the AO disallowed weighted deduction, under s. 35B of the Act, incurred on advertisement and marketing, on foreign travel and on commission paid to the export agents. The Tribunal allowed 50 per cent. of the foreign travel expenditure for the purposes of deduction under s. 35B of the Act and allowed the whole of the expenditure on payment of commission and on advertisement and marketing. In the next assessment year, the assessee had again claimed weighted deduction on payment of commission to the foreign agents and also on foreign travelling.

6. The relevant sub-clause in s. 35B(1)(b) of the Act are as under :

"35B. Export markets development allowance, - (1) .....

(b) The expenditure referred to in cl. (a) is that incurred wholly and exclusively on -

(i) advertisement or publicity outside India in respect of the goods, services or facilities which the assessee deals in or provides in the course of his business; ...

(iv) maintenance outside India of a branch, office or agency for the promotion of the sale outside India of such goods, services or facilities; ...

(vii) travelling outside India for the promotion of the sale outside India of such goods, services or facilities, including travelling outward from, and return to, India;"

7. It is evident that the directors and the employees had undertaken foreign tours for the purposes of the company's business so as to promote the sales. The AO had taken the view that, since the assessee-company was an associate of the company, Beecham Products Overseas Ltd., and was controlled by the parent company, there was no need for the officers and the directors to go to foreign countries. The Tribunal did not agree with the view taken by the AO and permitted weighted deduction to the extent of 50 per cent. of the total travel expenditures on the ground that part of the travels related to the import business and part of it was for the purposes of promoting export sales. Commission and service charges had been paid to the foreign agents because they had obtained orders for exports and had publicised the assessee's products. They had rendered services in the foreign countries. The AO had made the disallowance on the ground that the assessee had not maintained a branch or agency outside the country for the promotion of sales. The Tribunal took the view that since the foreign agents had rendered services through their offices and branches in foreign countries, payment of commission to them did qualify for the purposes of weighted deduction. Similarly, expenditure incurred on advertisement and marketing was also allowed by the Tribunal, taking the view

that samples had been sent by the assessee-company to prospective buyers and, for that purpose, air freight and packing charges had been incurred. The AO had, without entering into any discussion, made the disallowance on advertisement and marketing expenditure.

8. The Tribunal has taken the correct view in the light of the express provisions contained in the various sub-clauses of cl. (b) of s. 35B(1) of the Act. No question of law, therefore, arises.

Question Nos. 1, 2 and 3 in the asst. yr. 1982-83 and questions Nos. 1 and 2 in the asst. yr. 1983-84 are, therefore, not found to be questions of law and are accordingly not required to be referred to this Court for opinion.

9. Questions on extra shift allowance. - The assessee-company had claimed extra shift allowance on the plant and machinery in all the asst. yrs. 1982-83, 1983-84 and 1985-86. The AO took the view that such allowance could be allowed only on the basis of the number of days the machinery had worked extra shift during the year and not on the basis of the entire year. The decision of the Madras High Court in *South India Viscose Ltd. vs. CIT* (1982) 135 ITR 206 was relied upon. The assessee's plea was that the undertaking engaged in production should be taken as a whole and there was no justification to allow depreciation for the specific number of days on which a particular plant or machinery had worked. It was stated that, normally, depreciation is allowed on the plant and machinery even if such plant was acquired on the last day of the accounting period. Normally, depreciation did not depend on the number of days. The Tribunal agreed with the assessee's plea and allowed extra shift allowance on concern basis.

10. The following question of law arises in each of the three assessment years :

"Whether, on the facts and in the circumstances of the case, extra shift allowance on new plant and machinery is to be allowed on the basis of the working of the undertaking as a whole or on the basis of the number of days the machinery had worked extra shifts during the year ?"

11. Questions on inclusion of excise duty in the value of closing stock, - Question No. 6 in the asst. yr. 1982-83 and question No. 4 in the asst. yr. 1985-86 relate to the inclusion of excise duty in the value of the closing stock. From a perusal of the Tribunal's order, it is noticed that the assessee had not debited a sum of Rs. 94,35,617, to the P&L a/c though this amount had been paid by way of excise duty on the goods produced but not sold. The assessee took the plea that this payment was not claimed as deduction inasmuch as the goods had not been sold. The AO took the view that the assessee had paid the excise duty on the goods manufactured by it and, therefore, this payment shall form part of the cost of the goods. The Tribunal directed the AO to consider the decision of the Special Bench of the Tribunal in *Modi Rubber Ltd.s case*. A similar question was under examination before the Special Bench of the Tribunal in another case (*Modi Rubber Ltd.s case*) and, therefore, the Tribunal found it appropriate to await the

decision of the Special Bench in that case.

Since the matter has not been finally decided by the Tribunal, and a direction has only been given to the AO to consider the decision of the Special Bench of the Tribunal in the case of Modi Rubber Ltd., no question of law arises from the controversy.

12. Question on cessation of excise duty liability under s. 41(1). - Questions have been raised in the asst. yr. 1985-86 on the cessation of liability relating to the excise duty payable by the assessee. The assessee had made certain provisions in the earlier years regarding the excise duty liability. A sum of Rs. 56,02,176 was, however, written back in the books of account in the asst. yr. 1985-86. At the time of assessment, the assessee took the plea that, though an entry had been made in the books of account, yet the amount so written back should not be treated as a case of cessation of liability inasmuch as no refund had been received from the Government. The AO, on the basis of the entry made by the assessee, took the view that it was a case of cessation of liability under s. 41(1) of the Act and, therefore, was a part of the assessee's income. When the matter reached the Tribunal in appeal, it was argued by the assessee that though the matter regarding certain excise duty had been decided by the Delhi High Court in the assessee's favour but SLP was pending before the Supreme Court and, therefore, liability had actually not ceased. It was a case of incorrect entry passed by the assessee on the auditors advice. It is also pointed out that the assessee has offered the amount for payment of tax in the subsequent assessment years after the matter was finally decided by the Supreme Court in 1987-88.

13. From the above facts, it is apparent that the assessee had actually not received any refund of excise duty and, therefore, no income can be said to have accrued. In *Morvi Industries Ltd. vs. CIT* ITR 835 the Supreme Court had held that if income by way of commission has accrued, that could be treated to be income though the payment had been deferred. Income accrues when it becomes due and the postponement of the date of payment did not affect the accrual of income. In the present case, the income actually had not accrued at all, because the Department had chosen to file SLP before the Supreme Court and, therefore, the matter had not been finally settled and the refund was under a cloud. In *Union of India and another Vs. M/s. J.K. Synthetics Ltd.*, it has been held by the Supreme Court that liability to tax under s. 41 would depend on the outcome of the appeal. The assessee's writ petition in that case challenging its liability to pay the excise duty had been accepted by a single judge of the High Court but the matter was pending in appeal before a Division Bench. Therefore, s. 41 of the Act could not be invoked.

In view of the aforesaid decision of the Supreme Court in *J. K. Synthetics Ltd.*'s case (*supra*), questions Nos. 1, 2 and 3 sought in the asst. yr. 1985-86 are declined.

14. Question on bad debt. - The assessee had written off a sum of Rs. 1,71,73,148, treating this amount as bad debt. The AO noticed that this amount was to be received by the assessee from G. Atherton and Co. (P) Ltd., Calcutta, who were the sole agents of the assessee for certain territories. A civil suit had been filed by the assessee against the said company, wherein a restraint order as well as an attachment order had been passed by the High Court. An appeal was said to be pending before the Supreme Court. The board of directors of the assessee-company passed a resolution on 6th June, 1984, requiring the management of the company to write off part of the debt. In consequence of the said resolution, an entry was made in the books of account. The AO took the view that the accounting year of the assessee-company ended on 30th April, 1984, and since the resolution had been passed by the board of directors in the month of June, 1984, there was no justification for writing off the debt in the asst. yr. 1985-86. The Tribunal agreed with the plea of the assessee that though the resolution had been passed in the month of June, 1984, the entry regarding bad debt was made in the previous year relevant to the asst. yr. 1985-86 because the books were open and the resolution had authorised the company to make the entry during that relevant year. The financial position of the debtor had been examined and thereafter the decision was taken.

15. Shri R. P. Sawhney, senior advocate, learned counsel for the petitioner, has contended that, looking to the resolution dt. 6th June, 1984, there was no reason to write off certain debt in the earlier year. Moreover, the matter was pending in the Court and, therefore, it was premature to treat the money due as irrecoverable. The money had not actually become a bad debt. Learned counsel for the assessee has, on the other hand, relied on a decision of the Calcutta High Court in Commissioner of Income Tax Vs. Mansata Film Distributor, for the proposition that the question whether a particular amount was bad debt or not depended on a finding of fact and, therefore, did not give rise to a question of law.

16. Looking to the facts of the case, especially the resolution passed by the board of directors in the next year, the following question of law is found to arise in the matter :

"Whether, on the facts and in the circumstances of the case, deduction on account of bad debt of Rs. 1,71,73,148 was rightly allowed in the asst. yr. 1985-86".

17. Question on perquisites under s. 40(c) and s. 40A(5) of the Act. - The AO noticed, that certain expenditures on group medical insurance, medical reimbursement of medical expenses, electricity, water and gas charges had been incurred in connection with the amenities and benefits provided to the directors of the assessee-company. These expenditures were, therefore, treated within the ambit of perquisites while working out the disallowance under s. 40(c) of the Act. The Tribunal, however, took the view that these expenses are not to be treated as perquisites while computing disallowance under s. 40(c) and s. 40A(5) of the

Act.

18. The question has been finally settled by the Supreme Court in Commissioner of Income Tax, Bombay, etc. Vs. M/s. Mafatlal Gangabhai and Co. (P) Ltd., . It was held that cash payments by an assessee to its employees do not fall within the ambit of s. 40(a)(v) or s. 40A(5)(a)(ii), as the case may be.

In the light of the decision of the Supreme Court in Mafatlal Gangabhais case (supra), the question sought to be referred is found to be no more a question of law.

19. Expenditure on scientific research. - The assessee had incurred certain expenditure on the purchase of air-conditioner, coolers, calculators, and fans. Deduction under s. 35(1)(iv) of the Act had been claimed on the plea that these items had been purchased by way of facility in connection with scientific research. The AO did not allow the claimed deduction on the ground that these items had been used in the office and these were not in the nature of scientific equipment used for the research work. The AO, therefore, held that expenditures on these items was to be capitalised and depreciation was allowable thereon. The Tribunal agreed with the assessee's plea that air-conditioner, coolers, etc., had been purchased in the research and development wing maintained by the assessee and, therefore, these things were directly connected with the facilities related to the research.

20. Shri R. P. Sawhney, senior advocate, learned counsel for the petitioner, had argued that the items purchased were not at all instruments and equipment connected with the research work and, therefore, expenditure on these items was simply in the nature of capital expenditure and not revenue expenditure to be allowed as deduction under s. 35(1)(iv) of the Act.

21. Shri G. C. Sharma, senior advocate, learned counsel for the assessee, has pointed out that, as per s. 43(4)(ii) of the Act, an expenditure on scientific research includes an expenditure incurred for the prosecution or the provision of facilities for the prosecution of scientific research. In view of this provision, expenditure on air-conditioners, coolers, etc., does qualify for the purpose of deduction.

22. The controversy arising from the facts gives rise to the following question of law :

"Whether, on the facts and in the circumstances of the case, expenditure on the purchase of air-conditioners, coolers, calculators and fans in the research and development wing was eligible for deduction under s. 35(1)(iv) of the IT Act, 1961 ?"

23. In the result, the Tribunal is directed to state the case and refer to this Court for its opinion the questions of law framed in the foregoing paragraphs on -

(i) the valuation of the closing stock,

- (ii) extra-shift allowance,
- (iii) bad debt, and
- (iv) expenditure on scientific research.

Ordered accordingly. No costs.