IN THE HIGH COURT OF JUDICATURE AT BOMBAY

ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO. 267 OF 2024

Pr. Commissioner of Income Tax, Central-1, Mumbai ...Appellant
Versus
Macelods Pharmaceuticals Ltd. AY 2012-13 ...Respondents

Mr. Akhileshwar Sharma for Appellant.
Dr. K. Shivaram, Sr. Adv. a/w Shashi B. for Respondent.

CORAM: G. S. KULKARNI & AARTI SATHE, JJ.

DATE: 03 JULY 2026

Oral Judgment (Per:- G. S. Kulkarni, J.)

1. This appeal, filed under Section 260A of the Income-Tax Act, challenges an order dated 31 January 2023 passed by the Income-Tax Appellate Tribunal, Mumbai Bench, whereby the Revenue's appeal against the common order dated 27 June 2018 passed by the Commissioner of Income-tax (Appeals), Mumbai, has been rejected. The assessment year in question is assessment year 2012-13.

2. The only question of law as urged on behalf of the revenue in this appeal is as under:

> "Whether, on the facts and circumstances of the case in law, the ITAT justified in holding the research and development expenditure as allowable deduction under the provision of Section 80IB/IC of the Income-Tax Act, wherein profits and gains in multiple units are granted deduction from the total income and hence, no expenditure relevant to such units can be allowed as deduction?"

3. We have perused the record. Considering the facts and circumstances of

the case as borne out by the record, we find that there is no case made out on behalf of the revenue in the present appeal, and more particularly, considering the question of law as proposed to be urged being quite illusory. In fact, the issue is more factual in nature, as appropriately observed by the Tribunal in the impugned order. In such context the tribunal has observed that the allocation of research and development expenditures to the units eligible for deduction under Section 80IB/IC of the Act, it was noticed from the record that the assessee had claimed a deduction of Rs.102.18 crores under Section 35(2AB) of research and development expenditure incurred by its two units, located in Mumbai, which were approved by the Department of Scientific and Industrial Research (DSIR). The assessing officer, however, apportioned the expenditure among the units eligible for deduction under Section 80IB/IC aggregating to Rs.50,21,51,424/-.

4. It appears that, before the assessing officer as also the Commissioner of Income-tax (A), the assessee contended that the issue relating to the allocation of research and development expenditure was in fact independent to the Research Unit, and not in any manner connected to the manufacturing units of the assessee enjoying deduction under Section 80IB/IC. Such position in law is recognised in the decision of this Court in **Zandu Pharmaceutical Works Ltd. Vs. CIT (ITA No.8 of 2007)**[1], is the assessee's contention. The relevant observations made by the Division Bench in the said judgment reads thus:-

> "**9.** There is no dispute that the assessee is entitled to the benefits of the provisions of sections 80HH, 80-I and 80-IA. Section 80-I provides that where the gross total income of an assessee includes any profits and gains derived from an industrial undertaking, there shall be allowed, in computing the total income of the assessee, a deduction from such profits and gains an amount equal to twenty per cent. thereof. Section

1 (2013) 350 ITR 366

80-IA provides that where the gross total income of an assessee includes any profits and gains derived from any business of an industrial undertaking, there shall be allowed, in computing the total income of the assessee, a deduction from such profits and gains of an amount specified therein. Section 80HH provides that whether the gross total income of an assessee includes any profits and gains derived from an industrial undertaking, there shall be in accordance with law and subject to the provisions of the section be allowed in computing the total income of the assessee a deduction from such profits and gains of an amount equal to 20 per cent. thereof.

10. While computing the profits and gains of the concerned undertaking, only expenses relating thereto can be deducted. In other words, the expenses must be incurred, for and on behalf of the concerned undertaking. The expenses attributable to any other unit or the head office expenses which have no relevance to the industrial undertaking, cannot be deducted in respect of the said undertaking while computing the profits and gains of the undertaking.

11. In *CIT* v. *Sterling Foods*(1999) 237 ITR 579 (SC); (1999) 4 SCC 98, the following question was considered by the Supreme Court (page 581):

> "Whether, on the facts and in the circumstances of the case, the Tribunal was justified in law in holding that the receipt from the sale of import entitlements could not be included in the income of the assessee for the purpose of computing the relief under section 80HH of the Income-tax Act, 1961?"

12. The question, therefore, was converse to the one before us. The Supreme Court held as under (page 584):

> "Crude petroleum is refined to produce raw naphtha. Raw naphtha is further refined, or cracked to produce the said products. This is not controverted. It seems to us to make no difference that the appellants buy the raw naphtha from others. The question is to be judged regardless of this, and the question is whether the intervention of the raw naphtha would justify the finding that the said products are not'derived from refining of crude petroleum'. The refining of crude petroleum produces various products at different stages. Raw naphtha is one such stage. The further refining, or cracking, of raw naphtha results in the said products. The source of the said products is crude petroleum. The said products must, therefore, be held to have been derived from crude petroleum.
>
> We do not think that the source of the import entitlements can be said to be the industrial undertaking of the assessee. The source of the import entitlements can, in the circumstances, only be said to be the Export Promotion Scheme of the Central Government whereunder the export entitlements become available. There must be, for the application of the words 'derived from', a direct nexus between the profits and gains and the industrial undertaking. In the instant case, the nexus is not direct but only incidental. The industrial undertaking exports processed seafood. By reason of such export, the Export Promotion Scheme applies. Thereunder,

the assessee is entitled to import entitlements, which it can sell. The sale consideration therefrom cannot, in our view, be held to constitute a profit and gain derived from the assessee's industrial undertaking."

13. The Supreme Court held that there must be for the application of the words "derived from" a direct nexus between the profits and gains and an industrial undertaking. Sections 80-I and 80-IA also use the expression "derived from". If there must be a direct nexus between the profits and gains and an industrial undertaking, it must follow equally that there must be a direct nexus between an industrial undertaking and the expenses which are sought to be apportioned/attributable to it. Expenses which do not relate to an industrial undertaking/unit under consideration and they relate to other units or to the head office of the assessee, cannot be taken into consideration while computing the deduction under the said provisions.

14. ….

15. We are in respectful agreement with the judgment, the basis of which is that unless the expenditure incurred on the R & D work relates to the undertaking/unit in question, the same cannot be apportioned to it.

16. Mr. Suresh Kumar submitted that any research and development activity carried out by the head office would automatically enure to the benefit of the units/industrial undertakings. He submitted that the head office itself does not manufacture any medicines, the benefit of the research and development would be utilized for manufacturing the products and the products would obviously be manufactured by the units.

17. The submissions proceeds on an erroneous basis and does not take into consideration the facts of the case at all. As we noted earlier, in the present case, the said R & D activities were in relation to the new drugs. There is nothing to indicate that in the event of the assessee deciding to commercially exploit the benefits of the R & D work, the products would be manufactured by the said units. The fallacy in the submissions proceeds on the hypothetical basis that the said products would be manufactured by each of the units or any one of them.

18. The fallacy also arises on account of an erroneous presumption that the benefit of any R & D activity can only be exploited by an enterprise utilizing the same in its manufacturing activities. That is not so. An enterprise can always assign the benefit thereof to a third party. It can always grant a licence in respect of any patent or design to a third party. In that event, the other units would not derive any benefit in respect thereof. The presumption of a nexus between the R & D activities and the units is not well founded."

5. The assessees thus submitted that the research and development activities are not directly related to its manufacturing units, as its research and development division is engaged in developing future products, innovations, and launches, and not the products presently manufactured by the eligible units. A categorical stand was also taken that research and development expenses are on futuristic research and the result of research is uncertain and none of the items on which research is being undertaken, were being manufactured by these undertakings. It was also the assessee's case that the R&D units were found in separate buildings, far away from its manufacturing units, and are "standalone" independent units. Also independent and separate financial statements are prepared and audited. Further all the data in regard to the detail tabulation showing year wise details of formulations developed by the R&D wing and status of such products were furnished before the Assessing Officer, to contend that it was clear that R&D expenditure was totally unrelateable to the manufacturing activities of the assessee. The CIT(A) accepted the assessees case to hold that on examining the record it was evident that R&D carried out by the assessee has not been applied for manufacturing units eligible for deduction under Section 80IB/IC of the Act. Also a detailed list of items manufactured by the units eligible under Section 80IB/IC of the Act and also the formulation items under development in R&D units to record finding of fact that there is no nexus between what is undertaken in the R&D units and the manufactured units. The relevant observations in that regard, as made by the Tribunal on the factual examination of the record are required to be noted, which reads thus :

> "18. On perusal of list of products manufactured in eligible units and drug under development and R&D units, we find that products manufactured under the units eligible for 80IB and 80IC unit are totally unrelated with the product under development in R&D units. In some cases, variant of formulation like injectable form etc., have been under development in R&D Units, which are different from tablet of same drug manufactured in eligible / non-eligible units. Moreover, in research and development units the formulations or the drugs developed, firstly, undergo a process of 4 to 5 years, before those formulations or drugs undergo manufacturing. From the submission filed before the lower authorities, which have been filed before us also, it is verified that at least in the current assessment year, the research and development expenditure incurred is not related to the units eligible for deduction under section 80IB and 80IC of the Act. The Ld. CIT(A) has made a general comment that drugs manufactured in exempted unit and research carried out in R&D unit are in respect of the same items. The Lt. CIT(A) has not pointed out as to which drugs or formulation under development in R&D unit has been manufactured by particular unit eligible under 80IB or 80IC of the Act. Accordingly, the finding of the Ld. CIT(A) being contrary to facts, same are set aside and the disallowance for reduction under section 80IB and 80IC of the Act corresponding to the allocation of R&D expenditure is hereby deleted."

6. We are at loss to understand as to what basis, the assessing officer could come to a conclusion to add the income of the R and D unit without any materials to support his stance that the R&D expenditure as claimed by the assessee in fact pertained to the units which were claiming deduction under Section 80IB/IC of the Act In the absence of any such materials we do not find that there was any basis for the assessing officer to make the addition in question.

7. In the light of the aforesaid discussion, we do not find that the appeal raises any substantial question of law.

8. It is accordingly rejected. No costs.

(AARTI SATHE, J.) **(G. S. KULKARNI, J.)**

Signed by: Kiran Kawre
Designation: PA To Honourable Judge
Date: 10/07/2026 14:21:50 Kiran Kawre