IN THE INCOME TAX APPELLATE TRIBUNAL "B"
BENCH, MUMBAI
BEFORE SHRI G. S. PANNU, VP AND SHRI AMARJIT SINGH, JM

आयकर अपील सं/ I.T.A. No.4701/Mum/2012
(**निर्धारण वर्ष** / Assessment Year: 2006-07)

M/s. Bharat Serums And Vaccines Ltd. 17th Floor, Hoechst House, Nariman Point, Mumbai-400021	**बनाम**/ Vs.	ACIT, Circle 3(1) Room No. 607, 6th Floor, Aayakar Bhavan, Mumbai-400020.

(ITA. No. 5228/Mum/2012)
(**निर्धारण वर्ष** / Assessment Year: 2006-07)

ACIT, Circle 3(1) Room No. 607, 6th Floor, Aayakar Bhavan, Mumbai-400020.	**बनाम**/ Vs.	M/s. Bharat Serums And Vaccines Ltd. 17th Floor, Hoechst House, Nariman Point, Mumbai-400021.
स्थायी लेखा सं./जीआइआर सं./PAN/GIR No. : AAACB2431M		
(अपीलार्थी /**Appellant**)	..	(प्रत्यर्थी / **Respondent**)

Revenue by:	Shri Rajeev K. Gubgotra (DR) /V. Justin (DR)
Assessee by:	Shri P.J. Pardiwala & Nitesh Joshi

सुनवाई की तारीख / Date of Hearing: 01/05/2019
घोषणा की तारीख /Date of Pronouncement: 24/05/2019

आदेश / O R D E R

PER AMARJIT SINGH, JM:

The Revenue as well as assessee have filed the above mentioned appeals against the order dated 12.06.2012 passed by the Commissioner of Income Tax (Appeals)-5, Mumbai [hereinafter referred to as the "CIT(A)"] relevant to the A.Y.2006-07.

ITA. NO.5228/M/2012 & 4701/Mum/2012

2. The Revenue as well as assessee have filed the above mentioned appeals against the order dated 12.06.2012 passed by the Commissioner of Income Tax (Appeals)-5, Mumbai [hereinafter referred to as the "CIT(A)"] relevant to the A.Y.2006-07

3. The Revenue has raised the following grounds: -

> "1. On the facts and in the circumstances of the case and in law, the Ld. CIT(A) has holding that the sum of Rs.5,25,00,000/- received on assignment of know-how, be taxed as capital gain as per the provisions of section 55(2) instead of Business Income as held by AO, without appreciating the fact that know how acquired is due to its R&D activities which is a normal business activity of the assessee and it has already claimed all the expenses for research & development in the P&L A/c. As, such the sum received on assignment of know-how ought to be assessed as revenue income.
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> 2. The appellant prays that the order of CIT(A) on the above ground be set aside and that of the AO be restored.
>
> 3. The appellant craves leave to amend or alter any ground or add a new ground which may be necessary."

4. The assessee has raised the following grounds.:-

> *"1. The Ld. Commissioner of income tax(Appeals) erred in holding that consideration of Rs.5,25,00,000/- received on assignment of know-how is chargeable to tax as Capital Gains'.*
>
> *It is submitted that 'know-how 'assigned is as self generated asset does not have identifiable cost or acquisition and as such the consideration received on assignment of 'know-how' is a capital receipt not chargeable to tax.*

5. The brief facts of the case are that the assessee filed its return of income on 29.11.2006 declaring loss to the tune of Rs.11,75,42,363/-. Thereafter, the case was selected for scrutiny and notices u/s 143(2) and u/s 142(1) of the Act were issued and served upon the assessee. The assessee is engaged in the business of manufacture of Serums and Vaccines. The assessee is also engaged in the research activities in Bio-medical/Bio-technical Fields. It has got many patents to it's credit. The assessee company is an approved research-facility in the field of Biomedical and Biotechnical and is the owner of several patents. The total sales turnover of the company was to the tune of Rs.90.50 crores as compared to Rs.90.32 crores in last year. In the year under assessment, the assessee received in sum of Rs.5.25 crores from BSV Research and Development Pvt. Ltd. as consideration for assignment of know how relating to scientific, medical and technical documents relating to development and manufacture of non-pegylated liposomal doxorubicin an oncology product under development. The terms of assignment were set out in agreement dated 26.10.2005. The assessee claimed this amount as

exempt as capital receipt. The AO arrived at this conclusion that the said receipt is chargeable to tax u/s 41(3) of the Act and the loss was assessed to the tune of Rs.6,45,69,391/-. Feeling aggrieved, the assessee filed an appeal before the CIT(A) who treated the said amount to be taxable as capital gain as per the provisions of Section 55B of the Act instead of u/s 41(3) of the Act, therefore, the revenue has filed the present appeal before us. However, the assessee has also filed the above mentioned appeal claiming that the said amount is capital in nature and is not liable to be taxed.

ISSUE NO. 1:-

6. Under this issue the revenue has challenged the order of the CIT(A) in which the CIT(A) has assessed amount of Rs.5,25,00,000/- received on assignment of know-how as capital gain in view of the provisions of Section 55(2) of the Act instead of 41(3) of the Act. In brief, the assessee received the sum of Rs.5,25,00,000/- from BSV Research and Development Pvt. Ltd. as consideration for assignment of know how relating to the scientific, medical and technical documents relating to development and manufacture of non-pegylated liposomal doxorubicin an oncology product under development and agreement dated 26.10.2005 was executed. The assessee has claimed exempt being capital receipt. The AO taxed the said amount in view of the provisions u/s 41(3) of the Act whereas the CIT(A) is of the view that an amount in question is liable to be taxed in view of the

provisions u/s 55(2) of the Act. Before going further, we deemed it necessary to advert the finding of the CIT(A) on record.:-

> *"2 3 I have considered the submission of the appellant and perused the assessment order. Appellant received Rs.5.25 Crores from BSV Research and Development Pvt. Ltd. as consideration for assignment of know how relating to scientific, medical and technical documents relating to development and manufacture of nonpegylated liposomal doxorubicin an oncology product under development.*
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> *2 3.i First grievance of the appellant is AO treating the receipt as reimbursement of expenses incurred over a period of time chargeable to tax under Section 41(3) of the Act. In my opinion the provisions of Section 41(3) are attracted only if an asset representing expenditure of a capital nature on scientific research is sold Know-how assigned during the year is a self generated capital asset and was an asset acquired or purchased from outside, sources. Therefore, same could not have, been allowed as deduction under section 35 of the Act I am inclined to agree with the learned AR that amount received on assignment of know-how cannot treated as a revenue receipt chargeable to tax under section 41(3).*
>
> *2.3.ii. Appellant no expenditure was incurred for acquiring said knowhow. In this context it is relevant 'to refer to Assignment Agreement dt. 26-10-2005 between the appellant company (the assignor) and the BSV Research and Development Pvt. Ltd. (the assignee). Relevant portion is reproduced hereunder:*
>
> *"WHEREAS*
>
> *A) The Assignor manufactures and markets biological, pharmaceutical and biotechnology products and has a range of products based on strong research and development initiatives and efforts.*
>
> *B) The Assignor has developed and owns the intellectual property rights in the Product (as hereinafter defined).*
>
> *C) The Assignor has incorporated the Assignee as its 100% subsidiary, for the purpose of conducting research and development of oncology and other products and procuring patents and intellectual property rights and licensing or assigning the Product and other oncology products*

developed, to third parties for commercially exploiting the Product and other oncology products developed, in India and in the rest of the world.

d) The Assignor has, as a result of research and development efforts since 1999 or thereabouts, developed and is possessed of the Know- how (as hereinafter defined) for the development and manufacturing of the Product.

E) The Assignee is desirous of acquiring the Know-how for its business activities in India and in the rest of the world and has requested the Assignor to transfer and assign all its right, title and interest in the Know-how 10 the Assignee and the Assignor has agreed to assign all its rights. title, and interest in the Know-how to the Assignee on the terms and conditions hereunder contained.

Thus, the appellant has developed an invention. The said invention is for the purpose to have right to manufacture, produce or process any article or thing. In other words, it was for the purpose of commercial exploitation. It was transferred/assigned to the assignee for Rs.5.25 cr. For the purpose of commercial exploitation.

"Provisions of Sec. 55(2) are reproduced as under:
Section 55(2)(a)
(a) in relation to a capital asset, being goodwill of a business (or a trade mark or brand name associated with a business) (or right to manufacture, produce or process any article or thing) (or right to carry on any business), tenancy rights, stage carriage permits or look hours (emphasis supplied)"

The above provision clearly covers a right to manufacture, produce or process any article or thing as taxable capital asset and cost to be taken at Nil.
2.3.iv. The facts of the present case is squarely covered by the provision of sec. 55(2), hence, the receipt of Rs.5.25 crores is to be taxed as capital gain. The AO is directed to act accordingly."

7. On appraisal of the above said finding, we noticed that the assessee received a sum of Rs.5,25,00,000/- from BSV Research and Development Pvt. Ltd. as consideration for assignment of know how relating to the scientific, medical and technical documents relating to

development and manufacture of non-pegylated liposomal doxorubicin an oncology product under development. CIT(A) discussed the term and condition of the Agreement dt 26-10-2005 executed between Assessee and BSV research and development Pvt, Ltd. Accordingly, It is clear that the transfer was for commercial exploitation. On seeing the nature of the transaction,we are of the view that the provision of Section 55(2) of the Act is applicable to the facts of the present case. The section 55(2) is hereby reproduced as under.:-

> *"Provisions of Sec. 55(2) are reproduced as under:*
> *Section 55(2)(a)*
> *(a) in relation to a capital asset, being goodwill of a business (or a trade mark or brand name associated with a business) (or right to manufacture, produce or process any article or thing) (or right to carry on any business), tenancy rights, stage carriage permits or look hours (emphasis supplied)"*

8. By going through the transactions effected between the BSV Research and Development Pvt. Ltd. and assessee and also considering the provisions in Section 55(2) of the Act, we are of the view that no doubt it is a capital gain, therefore, in the said circumstances, the question arises whether the capital gain is liable to be treated as capital receipt not chargeable to tax or chargeable to tax. During the year under consideration, the assessee had received an amount of Rs.5,25,00,000/- as consideration for transfer of know-how with respect to a product called 'Non Pegylated Liposomal Doxorubicin', which was in the development stage. Though the

CIT(A) held that section 41(3) will not apply to the present case, he took the view that the entire amount would be assessable as capital gains with the cost of acquisition being taken as 'Nil'. For this purpose, he considered the capital asset that was transferred as a right to manufacture, produce or process an article or thing and in terms of section 55(2)(a) of the Act the cost thereof was deemed to be Nil. The issue that arise in the appeal of the assessee is whether the receipt of Rs.5,25,00,000/- could be brought to tax as capital gains in the absence of any ascertainable cost of acquisition in respect of the know-how.

9. The fact relevant for disposal of the aforesaid issue are that the assessee is engaged in the business of manufacture of Serums and Vaccines. It is also engaged in research activities in Bio-Medical/Bio-Technical fields. In this regard, it has research facility at Airoli, New Mumbai which is approved in terms of Section 35(2AB) of the Act.

10. That one of the products on which the assessee was carrying on research was Non-Pegylated Liposomal Doxorubicin', which was an oncology product and was in a development stage. It was felt that taking the research in respect of the said product to a stage where it could be commercial exploited would be highly expensive with no certainty of achieving that stage. It would also require substantial clinical research work and development, which was beyond the work which was carried out by the assessee. Therefore, the assessee was of

the view that further research and development in respect of the said product should be carried out in a joint venture. With this end in mind on 14.10.2005, the assessee formed a 100% subsidiary being BSV Research and Development Private Limited. On 26.10.2005, the assessee entered into an agreement with BSV Research and development Private Limited for assignment of technical know-how with respect to 'Non-Pegylated Liposomal Doxorubicin', which was still under the development stage for a consideration of Rs.5,25,00,000/-. On 18.11.2005, Cadila Healthcare Ltd. acquired 50% stake in BSV Research and Development Private Limited, and hence, the transferee Company become a 50:50 Joint Venture between the assessee and Cadila Healthcare Ltd.

11. In its return of income the amount of Rs.5,25,00,000/- was treated as a capital receipt not chargeable to capital gains as the know-how was a self-generated asset and its cost of acquisition thereof was not ascertainable. It is an undisputed fact that the asset which was the subject matter of transfer was research that was under development in respect of 'Non-Pegylated Liposomal Doxorubicin'. Hence, the said transaction should normally give rise to capital gains chargeable to tax under section 45 of the Act. However, as held by the Hon'ble Supreme Court in CIT Vs. B.C. Srinivasa Setty 128 ITR 294, the computation machinery for computation of capital gains should fail where the cost of acquisition of the asset, which is the subject matter

of transfer, is not ascertainable. The principle laid down therein was reiterated by the Supreme Court in the context of tenancy rights in case of CIT Vs. D.P. Sandu Bros. (Chembur) Pvt. Ltd. 273 ITR 1) and CIT Addl. Vs. Ganapati Raju Jogi 200 ITR 612). In the present case the know-how under development is a self-generated asset of which the cost of acquisition cannot be ascertained, and therefore, the consideration for the transfer thereof cannot be brought to tax under the head 'capital gains'as the computation mechanism fails.

12. The CIT(A) has held that the cost of acquisition is to be determined in the present case by relying on the fiction contained in section 55(2)(a) of the Act. According to him the capital asset which was transferred in the present case was a right to manufacture, produce or process any article or thing and hence, the cost of acquisition must be deemed to be Nil. In the present case, first of all the know-how was under development and therefore, as a consequence of its transfer, the transferee did not acquire any right to manufacture, produce or process any article or thing at this stage. Further, the simplicitier transfer of knowhow cannot be equated to a right to manufacture as contemplated by section 55(2)(a). The know-how when fully developed would énable'manufacture or production or processing of an article or thing. However, it would not give any 'right' in respect thereof. It is well settled position in law that know-how with respect to a product would give knowledge about how the

product is to be manufactured. The said know-how is not registered. Therefore, it does not confer any rights on its owner. The said knowledge only enables the manufacture of the product but does not confer any manufacturing rights. In view thereof, transfer of know-how cannot be regarded as transfer of 'right'to manufacture or produce or process an article or thing for the purposes of Section 55(2)(a) of the Act. What the section contemplates is the grant of a right to manufacture say by grant of a license to use a patent. Moreover, section 55(2)(a) of the Act makes no reference to know-how, which is the asset under consideration. Hence, the CIT(A) was not justified in holding that the capital gains should be computed with the cost of acquisition in respect of the said asset being taken as Nil. He ought to have held that the cost of acquisition of know-how under development being a self-generated asset is not ascertainable, and hence, no chargeable capital gains would arise. We held accordingly.

13. In result the appeal filed by Revenue is hereby ordered to be dismissed and appeal of the assessee is hereby allowed.

Order pronounced in the open court on 24/05/2019

Sd/-	Sd/-
(**G. S. PANNU**)	**(AMARJIT SINGH)**
VICE PRESIDENT	JUDICIAL MEMBER

मुंबई Mumbai दिनांक Dated : 24/05/2019
Vijay

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. आयकर आयुक्त(अपील) / The CIT(A)-
4. आयकर आयुक्त / CIT
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, मुंबई / DR, ITAT, Mumbai
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

सत्यापित प्रति //True Copy//

उप/सहायक पंजीकार /(Dy./Asstt. Registrar)
आयकर अपीलीय अधिकरण, मुंबई / **ITAT, Mumbai**