IN THE INCOME TAX APPELLATE TRIBUNAL
"C" BENCH, AHMEDABAD

BEFORE SMT. ANNAPURNA GUPTA, ACCOUNTANT MEMBER &
SHRI SIDDHARTHA NAUTIYAL, JUDICIAL MEMBER

I.T.A. No. 296/Ahd/2019
(Assessment Year: 2013-14)

Sunflower Pharmacy, G-5, Rudra Arcade, Opp. Traffic Helmet Circle, Drive in Road, Memnagar, Ahmedabad-380052	Vs.	Income Tax Officer, Ward-3(3)(9), Ahmedabad
[PAN No.ABQFS1821A]		
(**Appellant**)	..	(**Respondent**)

Appellant by :	Shri S. N. Soparkar, Sr. Adv. & Shri Parin Shah, A.R.
Respondent by:	Shri Ashok Kumar Suthar, Sr. D.R.

Date of Hearing	02.08.2023
Date of Pronouncement	26.09.2023

O R D E R

PER SIDDHARTHA NAUTIYAL - JUDICIAL MEMBER:

This appeal has been filed by the Assessee against the order passed by the Ld. Commissioner of Income Tax (Appeals)-3, (in short "Ld. CIT(A)"), Ahmedabad in Appeal No. CIT(A)-3/ITO, Ward-3(3)(9)/11135/15-16 vide order dated 30.01.2019 passed for Assessment Year 2013-14.

2. The assessee has taken the following grounds of appeal:-

"1. The Learned Commissioner (Appeal) erred in fact and in law in considering assessee as allied healthcare industry even though assessee is in business of retail medical store.

2. The Learned Commissioner (Appeal) erred in fact and in law in considering commission paid as freebees in violation of provision of Indian Medical Council (Professional conduct, Etiquette and Ethics) Regulation, 2002, and CBDT Circular No. 5/2012 Dated 01/08/2012 is applicable and

therefore not admissible as business expenditure under Section 37(1) of the I.T. Act 1961 even though commission paid is against the advisory service received regarding inventory and purchase of medicines by the assess."

3. The brief facts of the case are that the assessee is engaged in the business of trading of drugs and medicines. During the year under consideration, the assessee has shown gross sales of Rs.4,62,10,464/- on which the assessee has earned gross profit of Rs.1,01,85,353/-. During the course of assessment, the Ld. Assessing Officer observed that on verification of the profit and loss account for the year under consideration it was noticed that the assessee had debited an amount of Rs.50,46,000/- on account of commission which was paid to the following Doctors namely (1) Dr. Ramanbhai S. Patel (ii) Dr. Ratilal G. Patel (Rs. 15,96,601/- plus Rs.34,49,3991= Rs.50,46,000). The Ld. Assessing Officer questioned the allowability of the aforesaid expenditure in view of the language of Circular issued by the Central Board of Direct Taxes being Circular No. 5 of 2012 dated 01.08.2012, which prohibits the aforesaid commission payments since they are in violation of the provision of Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulation, 2002 and therefore are not admissible under Section 37 of the Act. The Ld. Assessing Officer was of the view that in view of the said Circular of the Board, any expense incurred in providing gifts, travel facility, hospitality, cash or monetary grant from pharmaceutical and allied health sector industry or similar freebees in violation of the provision of Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulation, 2002 is not admissible under Section 37 (1) of Income Tax Act, 1961 being expenses prohibited by law. During the course of assessment proceedings, the assessee submitted that the Circular of the Board speaks about freebies and

the same is not applicable to the case of assessee as the commission expenditure cannot be termed as freebies to doctors from pharmaceutical retail stores. Further, it was submitted by the assessee that the aforesaid Circular is applicable to pharmaceutical industry and hence, the assessee is not covered within the scope of the aforesaid Circular. However, the Assessing Officer was of the view that the aforesaid argument of the assessee cannot be accepted as the said payment is covered by the CBDT Circular, being cash or monetary grant and is not for any research, study, etc. through approved Institutions. Further, the Ld. Assessing Officer held that the argument of the assessee that the said Circular is not applicable to the case of assessee as the same is applicable to pharmaceutical industry and the assessee is not a pharmaceutical industry is also not acceptable as the Circular equally applies to "allied health sector", and the assessee being one of suppliers of medicines which takes care of health of people, is covered within the scope of the aforesaid Circular. The Ld. Assessing Officer also observed that as per Column 32 of the Audit report. Form No. 3CD gross profit of the assessee was Rs.1,01,84,353/-,out of which the assessee has made payments of Rs.50,46,000/- to doctors by way of commission, which is more than twice the payments made by the assessee by way of remuneration to the 7 partners & salary payments to the 10 employees, including qualified pharmacists. Further, the Assessing Officer held that the version of the assessee that payments were made to the doctors for advisory services provided to the assessee is not verifiable on facts. Accordingly, the Assessing Officer disallowed the payment of Rs.50,46,000/- made by the assessee to the two doctors under Section 37(1) of the Act.

4. In appeal, Ld. CIT(Appeals) confirmed the additions with the following observations:

> *"2.3. I have carefully considered the facts mentioned in the Assessment Order and submission filed by the Appellant. On verification of the profit and loss account for the year under consideration it was noticed by the AO that the assessee had debited an amount of Rs.50,46,000/- on account of commission paid to the Doctors. The said commission was paid to the following Doctors:-*
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> |---|---|---|
> | *(i)* | *Dr. Ramanbhai S. Patel* | *Rs. 15,96,601/-* |
> | *(ii)* | *Dr. Ratilal G. Patel* | *Rs. 34,49,399/-* |
> | | ***Total*** | ***Rs. 50,46,000/-*** |
>
> *In view of the Circular issued by the Central Board of Direct taxes being Circular No. 5/2012 (F.No. 225/142/2012-ITAJI) dated 01 08/2012. The commission paid by the assessee is not an allowable expenses. Section 37(1) of I.T.Act,1961 provides for deduction of any revenue expenditure (other than those failing under Sections 30 to 36) from the business Income if such expense is paid out/expended wholly or exclusively for the purpose of business or profession. However, the explanation appended to this subSection denies claim of any such expense, if the same has been incurred for a purpose which is either an offence or prohibited by law. The claim of the assessee for commission payment to the Doctors as narrated hereinabove is in violation of the provisions of Indian Medical Council (Professional Conduct. Etiquette and Ethics) Regulations, 2002 therefore, the same shall be inadmissible u/s.37(1) of the Act being an expense prohibited by the law as clearly indicated in the Circular reproduced hereinabove. The reply in this regard has considered carefully and the same is not acceptable so far as the allowability of commission expenses debited to profit and loss account of the assessee. As per the said stipulations, it is very clear that a medical practitioner shall not receive any cash or monetary grants from any pharmaceutical and allied healthcare industry for individual purpose in individual capacity under any pretext, funding for medical research, study etc. can only be received through approved institutions by modalities laid down by law rules/guidelines adopted by such approved institutions, in a transparent manner. It shall always be fully disclosed. Thus, it is clear that the medical practitioners shall not receive any cash or monetary grant under any pretest from any pharmaceutical and allied healthcare industry but the same may be for some medical research, study, etc. through approved institutions by adopting the modalities laid down by law rules guidelines adopted by such approved institutions in a transparent manner. In the case of assessee the commission paid is not for such activities and as per the modalities laid down.*

Considering the fact as narrated above, it is clear that the Assessee has no requirement of any advice/guidance/service from doctors or no any evidence so as establish that the any service by way advice/guidance received from the doctors for which such payments of Rs.50,46,000/- made to the doctors. In view of the above payments made to doctors are in violation of the provision of Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulation 2002 and not admissible u/s. 37(1) of Income Tax Act. 1961 being an expense prohibited by law.

2.4. The assessee has submitted that the commission has been paid for giving guidance in respect of maintenance of stock of medicines and purchase of medicines. The doctors have also confirmed that they are giving guidance to sunflower pharmacy regarding purchase of medicines, quantity of medicines, name of medicines, location of suppliers of medicines, time of purchase etc. The appellant has submitted that it is not pharmaceutical and allied health care industries and the payment of commission to doctors is not freebies but against the services rendered by doctors. The commission paid for services received for the purpose of the business of the assessee have no correlation with the remuneration to partners and salary paid to staff. Further, it is submitted that the commission paid has also disclosed as income in the hands of doctors and over and above 10% of tax deducted, doctors have paid balance tax of 20% of fax i.e. tax on the said amount has been paid by the doctors at the same rate as rate of tax of firm.

2.5. After going through the facts of the case, it is seen that CBDT has issued circular number 5/2012 dated 01 08/2012 in respect of inadmissibility of expenses incurred in providing freebees to medical practitioner by pharmaceutical and ***allied health sector industry****. According to that circular the claim of expenditure incurred in providing gift, travel facility, hospitality, cash or monetary grant from pharmaceutical and allied health sector industry or similar freebees in violation of the provision of Indian Medical Council (Professional Conduct, etiquette and Ethics) Regulation, 2012 is not admissible u/s 37(1) of Income Tax Act, 1961 being an expense prohibited by law. The Circular issued by the Central Board of Direct faxes being Circular No.5 of 2012 dated 01/08/2012 clarifies in clear term that Section 37(1) of Income Tax Act provides for deduction of any revenue expenditure (other than those failing under Sections 30 to 36) from the business Income if such expense is laid out expended wholly or exclusively for the purpose of business or profession. However, the explanation appended to this subSection denies claim of any such expense, if the same has been incurred for a purpose which is either an offence or prohibited by law.*

2.6. In view of the said Circular of the Board, any expense incurred in providing gift, travel facility, hospitality, cash or monetary grant from

pharmaceutical and allied health sector industry or similar freebees in violation of the provision of Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulation, 2002 is not admissible u/s.37(1) of Income Tax Act, 1961 being expenses prohibited by law. As per the said stipulations, it is very clear that a medical practitioner shall not receive any cash or monetary grants from any pharmaceutical and ***allied healthcare industry*** *for individual purpose in individual capacity under any pretext, funding for medical research, study etc. can only be received through approved institutions by modalities laid down by law rules/guidelines adopted by such approved institutions, in a transparent manner.*

The appellant has argued that it is not pharmaceutical and allied health care industries and the payment of commission to doctors is not freebies but against the services rendered by doctors. It is to be noted that in CBDT has issued circular number 5/2012 dated 01/08/2012 in respect of inadmissibility of expenses incurred in providing freebees to medical practitioner by pharmaceutical and allied health sector industry. The appellant is falling in the category of ***allied health sector industry****. In the case of assesses the commission paid is not for such activities and as per the modalities laid down. Considering the fact as narrated above, it is clear that the Assessee has no requirement of any advice/guidance/service from doctors or no any evidence so as establish that the any service by way advice/guidance received from the doctors for which such payments of Rs.50,46,000/- made to the doctors. In view of the above discussion and in view of Circular of the Board reproduced hereinabove, it is clear that the payment of commission made by the assessee to the above said two doctors namely (i) Dr. Ramanbhai S. Pate/ Rs.15,96,601/- and (ii) Dr. Ratilal C. Pate/ Rs. 34,49,399/- totaling to Rs.50,46,000/- is not allowable u/s. 37(1) of the Act. The addition of Rs.50,46,000/- is* ***confirmed****. The grounds of appeal are* ***dismissed****.*

3. In result, the appeal of the appellant is ***dismissed****."*

5. The assessee is in appeal before us against the aforesaid order passed by Ld. CIT(Appeals) confirming the additions made by the Assessing Officer. Before us, the Counsel for the assessee drew our attention to order passed by ITAT Ahmedabad in assessee's own case for Assessment Year 2011-12 and also for Assessment Year 2014-15. Further, the Ld. Counsel for the assessee reiterated the argument taken before Ld. CIT(Appeals) that

the assessee is a pharmacy engaged in trading of medicines and hence is not covered by the provisions of the Circular, which is only applicable to pharmaceutical industry. Further, the Counsel for the assessee submitted that the aforesaid payment was made by the assessee to the doctors for providing advisory services, and therefore, the same does not qualify as freebies having been given to the doctors, and hence not covered within the scope of aforesaid Circular. It was further submitted that the assessee had duly deducted TDS on the aforesaid payments and hence on facts, the aforesaid payments were for receipt of advisory services from the doctors.

6. In response, the Ld. DR placed reliance on the observations made by Ld. CIT(Appeals) in the appellate order. The Ld. DR submitted that apparently no services have been provided by the doctors to the assessee. It was submitted that the payments have been made by the assessee to the doctors primarily to support the sale of medicines and hence the same qualify as commission payments. It was further submitted that pharmacy falls within the category of "allied services" as mentioned in the Circular and therefore, in view of the above, the payments are clearly prohibited by law. It was further submitted that there has been no formal agreement for rendering services. Accordingly, it was submitted that Ld. CIT (Appeals) has correctly confirmed the disallowances in the hands of the assessee.

7. We have heard the rival contentions and perused the material on record. The first issue for consideration is that in the prior Assessment Years, the Ahmedabad Tribunal in the assessee's own case for prior Assessment Years has allowed the appeal of the assessee on this issue. However, it may be noted that law on this issue has been clarified by the

Hon'ble Supreme Court in the case of **Apex Laboratories (P.) Ltd. 135 taxmann.com 286 (SC) vide order dated February 22, 2022**, wherein the Supreme Court held that since acceptance of freebies by medical practitioners was punishable as per Circular issued by Medical Council of India under MCI regulations, 2002, gifting of such freebies by assessee-pharmaceutical company to medical practitioners would also be prohibited by law and thus, expenditure incurred in distribution of such freebies would not be allowed as a deduction in terms of Explanation 1 to Section 37(1)of the Act. In this case, the Assessee, a pharmaceutical company incurred expenditure towards gifting freebies to medical practitioners for promoting its health supplement and claimed exemption for said expenses under Section 37(1) of the Act. The Assessing Officer by placing reliance on Circular No. 05/2012, dated 01.08.2012 and circular issued on 14.12.2009 by Medical Council of India under MCI Regulations, 2002, held that only expenses incurred till 14.12.2009 would be eligible for deduction and thus, partially disallowed exemption claimed by assessee. It was noted that Explanation 1 to Section 37(1) contained within its ambit all activities which were illegal or prohibited by law. The Hon'ble Supreme Court held that since acceptance of freebies by medical practitioners was punishable by MCI, distribution of such freebies would also fall within purview of prohibited by law and therefore, expenditure incurred by assessee-pharmaceutical company in distribution of such freebies would not be granted as deduction in terms of Explanation 1 to Section 37(1)of the Act. In the case of **Mead Johnson Nutrition (India) (P.) Ltd. 149 taxmann.com 298 (Mumbai - Trib.)**, the ITAT held that where assessee-company was engaged in trading of infant and children nutrition food,

expenses incurred on account of conference and seminar of doctors and healthcare/medical practitioners would fall within ambit of prohibited activities in view of Infant Milk Substitutes, Feeding Bottles and Infant Foods (Regulation of Production, Supply and Distribution) Act, 1992 and, hence, such expenses incurred by assessee were to be disallowed as per Explanation to Section 37(1)of the Act. In the case of **Stemade Biotech (P.) Ltd. 138 taxmann.com 368 (Mumbai - Trib.)**, the ITAT held that where assessee-company paid referral fees to doctors who referred potential customers for availing stem cell banking services of assessee-company, acceptance of such referral fee by a medical practitioner was in clear violation of regulation 6.8.1(d) of Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations, 2002 and thus assessee-company was not eligible to claim a tax deduction in respect of said expenditure. Accordingly, in view of the decision rendered by the Hon'ble Supreme Court of India on this issue, we are of the considered view that now this issue has been conclusively decided / adjudicated by the Hon'ble Supreme Court and accordingly, any freebies given by the assessees to doctors for sales promotion etc. are liable to be disallowed. Accordingly, in light of the observations made by the Hon'ble Supreme Court in the Apex laboratories decision *supra,* any reliance on decisions rendered by ITAT in assessee's own case for prior years shall stand superseded, in case the assessee comes within the four corners of the provisions of Circular No. 5 of 2012 dated 01.08.2012.

8. Now the next question for consideration is that whether in the instant facts, it can be held that the doctors had provided any professional advice to

the pharmacy and hence the payments were falling outside the purview of Circular issued by the Central Board of Direct Taxes being Circular No. 5 of 2012 dated 01.08.2012, which prohibits the aforesaid commission payments since they are in violation of in violation of the provision of Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulation, 2002 and therefore are not admissible under Section 37 of the Act. In our considered view, the assessee has not been able to demonstrate rendering of any services by the doctors the pharmacy so as to justify that the aforesaid payments were made by the assessee towards advisory services. The fact that TDS was deducted by the assessee on such payments is immaterial for the purpose of deciding whether the payments were made by the assessee for receipt of advisory services or otherwise. In the instant facts, we observe that there is no formal agreement between the assessee and the doctors for providing any advisory services (refer page 10 of CIT order). Further, the Assessing Officer has made a specific noting that the assessee operated the pharmacy from within the premises of the hospital and hence, the sales of the pharmacy were dependent primarily on the prescriptions made by both the doctors to whom the commission was paid (refer page 10 of CIT order). It was further noted by the Assessing Officer that the assessee has not submitted any correspondence or communication between itself and the doctors so as to establish any advice / services given / rendered by the doctors to the assessee (refer page 10 of CIT order) and further, out of the gross profit of Rs.1,01,84,353/- earned by the assessee, the assessee has made payments amounting to Rs.50,46,000/- by way of commission to the two doctors (refer page 10 of CIT order). Accordingly, looking into the totality of facts in the instant case, we are of the considered

view that the assessee has not been able to establish that the aforesaid payments were made by the assessee to the doctors for rendition of any professional / advisory services, and hence, in our considered view, the payments essentially qualify as commission payments made to doctors for promoting the sale of medicines.

9. Before us, the Ld. Counsel for the assessee has also taken an alternate argument that doctors to whom the amounts were paid have offered the same in their respective returns of income. Therefore, since both the assessee as well as the payees / doctors were assessed to tax at the same rate of taxation, it could not be said that the service charges were paid by the assessee to the doctors with a view to evade taxes. Accordingly, it was submitted that in view of the principles of tax neutrality, no disallowance is called for in the hands of the assessee. The Counsel for the assessee placed reliance on the case of Gujarat Gas Financial Services Ltd. 60 taxmann.com 483 (Guj.) in respect of the above contention. However, we are unable to agree with the argument put forth by the Ld. Counsel by the assessee for the reason firstly that the payees / doctors have not been able to demonstrate tax neutrality since it has not been demonstrated before us as to whether the doctors have paid taxes on the aforesaid amounts on gross basis or have claimed any corresponding expenditure against the aforesaid receipts from the assessee. Secondly, and importantly, the principle of tax neutrality typically applies where payments are made between associated enterprises and question before the Court is that when both the assessee company as well as the assessee's associated / parent company are assessed to tax at maximum marginal rate, could it be said that the charges were paid by the

assessee company to its associated / parent company at an unreasonable rate to evade taxes. However, in our considered view, the aforesaid principle of tax neutrality would not apply when payments made by the assessee have been disallowed in it's hand since such payments are illegal or prohibited by law. In the instant facts, the payments have been denied in the hands of the assessee on the ground that in view of Circular No. 5/2012 dated 01.08.2012 read with Explanation 1 to Section 37(1), the aforesaid payments are prohibited by law. In our respectful view, the principles of tax neutrality would not apply in cases the payments have been held to be illegal or are prohibited by law. Accordingly, we are of the considered view that decision of Gujarat Gas Financial Service Ltd. (supra) has been rendered on a different set of facts and would not apply to the assessee's facts.

10. The fourth issue for consideration before us is that whether it can be stated that the assessee being a pharmacy engaged in trading of medicines, is not covered by the provisions of the Circular, which is only applicable to pharmaceutical industry. We observe that the CBDT has issued Circular No. 5/2012 dated 01.08.2012 in respect of inadmissibility of expenses incurred in providing freebies to medical practitioners by pharmaceutical and "**Allied health sector industry**". In our considered view, the assessee is falling in the category of **Allied health sector industry** and hence covered within the scope of the Circular referred to above. In the case of in the case of **Confederation of Pharmaceutical Industry vs. CBDT in Writ Petition No. 10793 of 2012**, the HP High Court made the following pertinent observations in this regard:

"2. It is apparent that the Medical Council of India in exercise of the powers vested in it under the Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations, 2002 imposed prohibition on any medical practitioner or their professional associates from accepting any gift, travel facility, hospitality, cash or monetary grant from any pharmaceutical and allied health sector Industries. This regulation is a very salutary regulation which is in the interest of the patients and the public. ***This Court is not oblivious to the increasing complaints that the medical practitioners do not prescribe generic medicines and prescribe branded medicines only in lieu of the gifts and other freebies granted to them by some particular pharmaceutical industries. Once this has been prohibited by the Medical Council under the powers vested in it, Section 37(1) of the Income-tax Act comes into play****….."*

11. In view of the above observations, in our considered view, Ld. CIT (Appeals) has not erred in facts and in law in holding that the aforesaid payments made by the assessee to two doctors qualify as commission paid for promoting sale of medicines and hence are not allowable under Section 37(1) of the Act.

12. In the result, the appeal of the assessee is dismissed.

This Order pronounced in Open Court on 26/09/2023

Sd/-	**Sd/-**
(ANNAPURNA GUPTA)	**(SIDDHARTHA NAUTIYAL)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Ahmedabad; Dated 26/09/2023

TANMAY, Sr. PS ***TRUE COPY***

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

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

आदेशानुसार/ BY ORDER,

उप/सहायक पंजीकार (Dy./Asstt.Registrar)
आयकर अपीलीय अधिकरण, अहमदाबाद / ITAT, Ahmedabad