

HUNDRED AND SEVENTY-FOURTH REPORT

PUBLIC ACCOUNTS COMMITTEE (1983-84)

(SEVENTH LOK SABHA)

IRREGULAR ALLOWANCE OF CONTRIBUTION TO SCIENTIFIC RESEARCH

MINISTRY OF FINANCE
(DEPARTMENT OF REVENUE)

[Paragraph 2.21 of the Report of the Comptroller and Auditor General of India for the year 1980-81—Union Government (Civil), Revenue Receipts, Vol. II—Direct Taxes]



Presented to Lok Sabha on _____
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LOK SABHA SECRETARIAT
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13-1-1983 (F.N.);

6-12-1983

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(1983-84)**

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INTRODUCTION

1. The Chairman of the Public Accounts Committee, do present on their behalf this Hundred and Seventy-Fourth Report of the Public Accounts Committee (Seventh Lok Sabha) on paragraph 2.21 of the Report of the Comptroller and Auditor General of India for the year 1980-81, Union Government (Civil), Revenue Receipts, Volume-II, Direct Taxes relating to 'irregular allowance of contribution to scientific research'.

2. The Report of the Comptroller and Auditor General of India for the year 1980-81, Union Government (Civil), Revenue Receipts, Volume-II, Direct Taxes, was laid on the Table of the House on 31 March, 1982.

3. The Committee have in this Report dealt with the case of an assessee viz., M s. Carborandum Universal Ltd., Madras which contributed a sum of Rs. 8,50,000 to two research centres—(i) A.M.M. Murugappa Chettiar Research Centre, Madras (Rs. 7,50,000) and Nehru Centre Bombay (Rs. 1,00,000). The assessee was allowed an extra deduction of 33-1/3 per cent of the contribution even though there was no approval for any sponsored research programme to be undertaken by the two institutions which was a pre-requisite for the grant of *extra deduction* of 33-1/3 per cent under section 35(2A) of the Income Tax Act, 1961.

4. The examination of the above case has led the Committee to the general question as to how far the large exemptions given under the Income Tax Laws for scientific research are being utilised for the intended purpose. The Committee note in this regard that there are 1018 institutions (including renewals) approved for scientific research under Section 35(i)(ii) and (iii) of the Income Tax Act, in addition to 126 specific approved programmes of scientific research under Section 35(2A). Besides, there are over 800 in-service research institutions. As till recently, the prevailing system was to give long-term|perpetual approvals and there were no periodical|annual reviews of the work done by approved institutions, it is difficult for the Committee to say how far the exempted funds have been utilised for the intended purpose or diverted to other purposes. However, a statement of 40 institutions, whose approvals have been withdrawn in recent years, makes shocking revelations. From this statement, the Committee observe that some of the approved institutions which had enjoyed exemption under Section 35 for as many as 25 years or even more had not done any research work whatever. Some of the institutions, when asked to submit the annual return indicating the scientific research activities being conducted

(vi)

by them, had not given any reply. In case of one institution—Research Institute of Ancient Scientific Studies, New Delhi (approved in February 1965 and de-recognised in August 1980), the letter asking the Institute to submit the annual return indicating the scientific research activities conducted by it was returned by the postal authorities as no such Institute seemed to be existing.

5. The Committee also note that the provisions on the subject are spread over in a number of sections, sub-sections, clauses and Explanations of the Income Tax Act. These are quite cumbersome and complex and frequent amendments have made them even more so. Section 35 alone has undergone as many as 11 amendments in the last few years. The Committee have desired that in the interest of promotion of research and development activities in the country and also in the interest of revenue, early steps should be taken to rationalise and simplify these provisions.

6. The Public Accounts Committee (1982-83) examined the Audit paragraph in question at their sitting held on 13 January, 1983. The Public Accounts Committee (1983-84) considered and finalised the Report at their sitting held on 6 December, 1983. Minutes of the sitting form Part-II* of the Report.

7. For reference of facility and convenience, the observations and recommendations of the Committee have been printed in thick type in the body of the Report and have also been reproduced in Appendix III of the Report.

8. The Committee place on record their appreciation of the commendable work done by the Public Accounts Committee (1982-83) in taking evidence and obtaining information for this Report.

9. The Committee also place on record their appreciation of the assistance rendered to them in the examination of this paragraph by the Comptroller and Auditor General of India.

10. The Committee would like to express their thanks to the officers of the Ministry of Finance (Department of Revenue) for the cooperation extended by them in giving information to the Committee.

SUNIL MAITRA,

NEW DELHI,
December 9, 1983

*Chairman,
Public Accounts Committee*

Agrahayana 18, 1905 (S)

*Not printed. One cyclostyled copy laid on the Table of the House and five copies placed in Parliament Library.

REPORT

IRREGULAR ALLOWANCE OF CONTRIBUTION TO SCIENTIFIC RESEARCH

Audit Paragraph

1.1. In computing the business income of an assessee under the Income-tax Act, 1961, any sum paid by him to a scientific research association, university, college or other institution for scientific research, is an admissible deduction, provided that such association, university, college or institution is approved by the prescribed authority. With a view to encouraging development of indigenous technology and self-reliance in industry, the Act was amended in 1974 to provide that, if the contribution was to be used for specific research undertaken by the institution under a programme approved by the prescribed authority having regard to the social, economic and industrial needs of India, a deduction of a sum equal to one and one-third times of the contribution so paid shall be allowed.

1.2. In the previous year relevant to the assessment year 1976-77, an industrial company in which the public were substantially interested contributed a sum of Rs. 8,50,000 to two scientific research centres approved by the Council of Scientific and Industrial Research, which is the prescribed authority. In the assessment completed in April 1979, the department allowed the assessee's claim for extra deduction of 33-1/3 per cent of the contribution. Audit check, however, revealed that there was no approval from the prescribed authority for undertaking the specific research programme. This being so, the extra deduction of Rs. 2,83,333, being 33-1/3 per cent of the contribution, was not admissible under the Act. This resulted in short levy of tax by Rs. 1,63,626 and surtax by Rs. 29,927.

1.3. The Ministry of Finance have accepted the objection and stated that remedial action is being initiated. Further report is awaited (December 1981).

[Para 2.21 of the Report of the Comptroller and Auditor General of India for the year 1980-81, Union Government (Civil) Revenue Receipts, Vol. II—Direct Taxes].

1.4. The facts of the case were as follows. The assessee in the present case, viz., M/s. Corborandum Universal Ltd., a public Ltd., Co. of Madras paid a contribution of Rs. 8,50,000 to (i) A.M.M. Murugappa Chettiar

Research Centre, Madras (Rs. 7,50,000) and Nehru Centre, Bombay (Rs. 1,00,000) and claimed weighted deduction under Section 35(2A) of the Income Tax Act. The I. T. O. allowed the claim in the assessment completed on 6 April, 1979 under Section 143(3) read with Section 144B. It was noticed in Audit that though the two institutions were approved by the Council of Scientific and Industrial Research for the purpose of Section 35(1) (ii) of the Act, there was no approval for any sponsored research programme to be undertaken by the two institutions which was a pre-requisite for the grant of the weighted deduction. Without such approved programme only the actual expenditure could be allowed under Section 35(1)(ii) and not weighted deduction under Section 35(2A).

1.5. As regards the circumstances in which the mistake had occurred in this particular case, the Ministry have in a written note stated as follows:

"It is not possible to pinpoint the reasons for the mistake as the explanation of the concerned I. T. O., who completed the assessment, has not been obtained since he has already retired from service on 31-1-1980. Perhaps, it did not occur to him that for the purpose of allowance of deduction u/s 35(2A) in addition to the approval of the institution by the prescribed authority u/s 35(1)(ii), it was also necessary that the amounts paid to them should have been used by them for scientific research undertaken under a programme approved in this behalf by the prescribed authority. This specific provision appears to have been overlooked by the I. T. O. and the matter came to light only when the Revenue Audit raised the objection on 1-11-1980."

1.6 The Committee desired to know if the assessment was checked by internal audit and, if so, how it escaped their notice. In a written reply, the Ministry have stated:

"The assessment for the assessment year 1976-77 was completed on an income of Rs. 1,70,23,620/-. It was therefore, a case of priority audit. The assessment was checked by the Special Audit Party on 10-10-1980 but the mistake could not be detected by it. It seems that the Special Audit Party missed the point that, besides the Centres being approved for the purpose of normal allowance u/s 35(1)(ii) of the I. T. Act, it was also necessary that the programme of research undertaken, should itself be approved by the prescribed authority for the purpose of weighted deduction u/s 35(2A). It appears to have been a bonafide human error.

The explanation of the I. T. O. Special Audit Party has not been called by the CIT since the concerned I. T. O. has already retired on 30-11-1980. It is, therefore, not possible to find out the exact reason for the mistake escaping notice of the departmental audit."

1.7. During evidence, the Chairman, Central Board of Direct Taxes added:

"In this case, unfortunately for us the ITO who framed the assessments and the I.T.O. incharge of Special Audit Party have retired with the result that we have not been able to get their explanations. But from the facts which are available from the files, I would like to mention that under the provision two approvals had to be sought—one approval of the institution and the other specific approval of the scientific research programmes. One approval was obtained but the other approval in respect of specific research programmes was not obtained. The I.T.O. to some extent was misled by the Counsel of the assessee when he stated that necessary approval had been obtained. He probably, thought that both the approvals had been obtained."

1.8 As regards the remedial action, the Ministry have in a written note stated:—

"Remedial action in the shape of action under section 147(b) of the I.T. Act, 1961, was taken and re-assessment for this year was completed on 24-3-1983 raising an additional demand of Rs. 1,74,520. The tax effect pertaining to income-tax on account of audit objection is Rs. 1,63,626. This additional demand stands collected by adjustment.

So far as the sur-tax assessment is concerned, the original sur-tax assessment was completed on 14-11-1979. This assessment was later reopened u/s 7 of the Sur-tax Act consequent on the re-opening of the Income-tax assessment. The sur-tax re-assessment was completed on 15-7-1982 raising an additional demand of Rs. 31,920. The demand raised as per this order has not so far been collected since the assessee has requested for stay of this demand on the ground that the corresponding re-assessment under the I.T. Act is under appeal.

Although the assessee has filed appeals against the income-tax and sur-tax re-assessments, its Counsel has since, *inter alia*,

stated, *vide* his letter dated 31.12.82 addressed to the I.A.C. (Audit), Madras, as under:—

'I wish, however, to submit that since it was subsequently realised that the weighted deduction would be allowable only if the contribution was made to a programme approved in that behalf by the prescribed authority, the claim for the weighted deduction was given up by my clients.'

1.9 The Committee then enquired how much amount was contributed by the assessee company—M/s. Carborandum Universal Limited—to each of the two research centres referred to in the Audit paragraph, and whether there was any connection or relationship between the assessee company and the research centres. In a written note, the Ministry have stated:—

“The assessee company contributed a sum of Rs. 8,50,000/- during the previous year relevant to the assessment year 1976-77 to the following two institutions approved u/s 35(1)(ii):

(i) A.M.M. Murugappa Chettiar Research Centre, Madras	Rs. 7,50,000
(ii) Nehru Centre, Bombay	Rs. 1,00,000

	Rs. 8,50,000

It appears that A.M.M. Murugappa Chettiar Research Centre is floated by the Murugappa Chettiar Group. M/s. Carborandum Universal Ltd. is a company in which the Murugappa Chettiar Group has substantial interest.”

1.10 The other research centre to whom the assessee company had contributed Rs. one lakh was Nehru Centre, Bombay. It was approved by the Council of Scientific and Industrial Research, the then prescribed authority for purposes of clause (ii) of Section 35(1) of the Income Tax Act with effect from 1-4-1974. The approval given to the Centre in 1974 was for perpetuity. The case was reviewed by the Department of Science and Technology, who after considering the facts and circumstances of the case, decided that the earlier approval for perpetuity be superseded and be substituted by a time-bound approval which will be valid up to 31-3-1982. The Nehru Centre had indicated the following lines of research:

- (i) Studies of cosmic rays with space shuttle;
- (ii) Solar flare studies;

- (iii) Study of the track recording properties of nuclear track detectors;
- (iv) Impact of asteroidial bodies with planets and their consequences; and
- (v) A search for fallen meteorites in collaboration with Amateur Astronomers Association, Bombay.

1.11 However, according to the evidence given by representatives of the Ministry of Science and Technology before the Committee, the Centre had not done any research work by 1978. It is not known whether it has done any research work since. It had by 31-3-1979 enjoyed an exemption of nearly Rs. 48 lakhs; it has upto 31-3-1982 enjoyed an exemption of Rs. 137 lakhs.

1.12 The Committee pointed out that this case attracted Government's attention as an objection had been raised by Audit. But there might have been several other cases due to the mistake of the same ITO or other ITOs. They desired to know whether the Department had gone deeply into such other cases. The Chairman, CBDT stated:

"When it came to our notice, we got a quick review conducted in Delhi in respect of similar cases which might have happened here. We intend to get a review of such cases in Calcutta and other bigger metropolitan towns to see whether such mistakes have been committed. A review conducted in Delhi has not revealed any mistake of this type."

Guidelines for approval of research programme Under Section 35(2A)

1.13 Weighted deductions are allowed for research undertaken under approved programmes of research. As regards the guidelines issued for the approval of such research programmes, the Ministry of Finance in their note have explained as under :—

"Section 35(2A) was inserted by the Direct Taxes (Amendment) Act, 1974 with effect from 1-4-1974. In the explanatory notes on the Clauses of the Amendment Act, circular No. 145 dated 9-9-1974, instructions issued by the Board regarding these provisions are as under :—

"Under this section, a weighted deduction equal to one and one-third times the actual expenditure incurred by a tax payer after 31-3-1973 on sponsored research in approved laboratories will be allowed. It is not necessary that the sponsored research should be related to the tax payer's business but the

weighted deduction will be allowed only if the scientific research is undertaken by a research association or a university or a college or other institution referred to in Section 35(i)(ii) under a programme approved by the prescribed authority having regard to the social, economic and industrial needs of the country. Where a deduction is allowed under the new sub-section (2A) of section 35, no deduction in respect of the same expenditure will be allowed under section 35(i)(ii)."

1.14 At present, there is only one prescribed authority, namely, the Secretary, Department of Science and Technology for purposes of Section 35 of the I.T. Act, 1961. The guidelines issued by the prescribed authority, viz. Department of Science and Technology regarding the eligibility and approval of programmes u/s 35(2A) of the I.T. Act are as under:—

1. "Any programme of scientific research which aims to create or develop :
 - (a) any new source of energy, which is capable of being commercially exploited or to improve the efficiency of any existing method of energy generation/distribution;
 - (b) any new source of proteinous and/or other nutritional food for human consumption.
2. to conserve energy, food or any of the scarce material resources by devising new methods of processing/manufacture used in agriculture, industry etc;
3. to devise new or better techniques for the utilisation or recycling of wastes;
4. to develop new or better techniques for pollution control/reduction;
5. to develop new/improved cheaper basic drugs|medicines for the treatment of any of the more commonly prevalent human/animal diseases;
6. to develop new/improved|cheaper techniques or methods of family planning, which are likely to find wider acceptance among the masses in general;
7. to develop new/improved techniques of house-building or construction or discover new building materials with a view to achieve cost reduction, substitution of scarce materials and the like, with special reference to rural areas;

8. to develop new/improved cheaper kinds of fertilizers|other plant nutrients, plant protection chemical etc. with a view to achieve greater yield per hectare from agriculture;
9. to devise new techniques of manufacture or production of goods which result in substantial conservation of foreign exchange by way of import substitution/export promotion;
10. to achieve such other objectives which the prescribed authority in its discretion, considers important for the social economic and industrial needs of India would be eligible for being considered for approval under section 35(2A) of the Income-tax Act, 1961.

Before a scientific research project/programme is considered for approval under the provisions of section 35(2A) by the prescribed authority, the institution concerned with the implementation of such project/programme would be required to establish that it has necessary facilities and competence for undertaking the proposed research programmes.

A programme which relates purely to market research, sales promotion, quality, control, testing, commercial production, style changes and routine data collection etc., would not qualify for being considered for approval."

1.15 As regards the procedure for approval of research programmes under Section 35(2A), the Ministry had added:

"All applications should, *inter-alia* be accompanied by the following particulars/documents:—

- (a) Essential profiles of the Scientific Research programmes proposed to be undertaken and their broad objectives;
- (b) time phasing of each project or programme;
- (c) financial outlays for each project or programme;
- (d) justification in assessee's own terms as to how the Scientific Research Programme in question is considered to be of importance to the social, economic and industrial needs of India;
- (e) particulars of institutions, where the Scientific Research Programmes are proposed to be executed including number and date of the Government Notification under which the institution is approved under Section 35(1)(ii);

- (f) brief details of building, equipments, staff and other facilities available in the institution where such programmes are to be carried out;
- (g) a letter of willingness from the institution to undertake the research work within the specified time limits, and furnishing detailed break-up in the format with justification, of the estimated cost of each project;
- (h) any other points considered relevant by the applicant.

The sponsors/institutions concerned would be responsible for submitting to the Secretary, Department of Science & Technology, in respect of each accounting year, Annual Statements showing progress of implementation of each project, actuals of the expenditure incurred thereon, and other details. A copy of this Annual Return would also be sent by them to the Income-tax Officer having jurisdiction over the Institution.

After the receipt of the recommendation of the prescribed authority, the same is processed and a notification valid for a specified period for which the programme has to run is issued by the Central Board of Direct Taxes."

1.16 In reply to a question as to whether any machinery exists to ensure that the funds are actually used for the approved research programme and also for evaluation of such programmes, the Ministry of Finance have stated as under:—

"The Department of Science & Technology have advised that after the approval u/s 35(2A) of the I.T. Act is conveyed, the Organisation concerned is requested to give a progress report regarding the implementation of the approved project. This progress report is examined in that Department to see whether scientific research has been conducted and required expenditure incurred thereon. The proforma in which the progress on the implementation of the scientific research project approved u/s 35(2A) of the Income-tax Act, 1961, is required to be submitted is given at Annexure." (Appendix-I).

Approval of research institutions for tax concessions under Section 35(1) (ii) & (iii)

1.17 During evidence, the Committee desired to know how after an institution had furnished all the required information, the prescribed autho-

city decided upon the approval. The Director in the Department of Science and Technology explained as under:—

“At the time we approve, very often, it was only due to a good intention on their part that they would get from the society a few people who could join together and promote research in certain fields. They would be able to mobilise resources, if only the approval is given to them. They should give a project report. That they give very often. They have given a project report and we find it difficult at this stage to judge whether they will realise that amount. We ask them: Do you have scientific people to come and join? They say that they would be able to join as members of Advisory Committee, and on the basis of that, they will go. At the stage of approval, usually, it is only a promise that they hope to pursue this and, only when they realise the amount that they would be able to fulfil some of the promises. We are giving approval in anticipation of the hope that they would be able to do something. It is sometimes difficult to say whether they would be able to reach the target or not. Only a few institutions could achieve the objectives.”

1.18 In reply to this Committee's recommendation contained in para 1.33 of their 187th Report (Fifth Lok Sabha) the Ministry of Finance had stated that approvals were being accorded to research institutions for limited periods, generally not exceeding 3 years at a time, and the prescribed authorities were conducting an annual review to see that the funds were utilised exclusively for research purposes. The Committee desired to know the total number of universities, institutions etc. approved under various provisions of the law for scientific research and in how many of these, approvals had been accorded for period exceeding 3 years. The Committee were informed as follows:—

“...the number, including renewals, comes to 1018. Earlier the approvals were generally granted without reference to time. Later on, in 1979 instructions were issued to the prescribed authorities that the approvals may be recommended only for a prescribed period generally not exceeding 3 years. As such, all approvals accorded thereafter are for a specified period and after the expiry of the period, the institutions have to ask for the renewal of the approvals.”

1.19. The Committee then enquired whether annual reviews had been carried out by the prescribed authorities in all the cases and if so, what were the results of the reviews. They also enquired whether there were any cases where the annual reviews had not been carried out and where

the funds under approval had not been used exclusively for research purposes and, if so, the action taken in such cases. In a written reply, the Ministry of Finance have stated:—

“The Department of Science and Technology which is the only prescribed authority with effect from 1-6-1982, have stated that they have been following a system of carrying out annual reviews in all cases. It has been added by them that based upon these annual reviews, they had taken action in regard to 41 scientific research associations/institutions, out of which approvals in 19 cases have been withdrawn, in 10 cases the approvals have been converted into time bound approvals and in 12 cases renewals have not been allowed. Approvals in 21 more cases were withdrawn on the recommendations of the other prescribed authorities.”

1.20 As to the number of research institutions approved for the tax concessions under Sections 35(i) (ii) and (iii), the Chairman, CBDI added in evidence as follows:

“The figure of 1018 includes also the universities and other educational institutions which have also been approved. The break up would be as follows:

Universities	87
Colleges & other management institutions	64
Cooperatives, Public Sector institutions	133
Others	574
Total	858

Of these 1018 institutions that we approved, we withdraw later on the approval in forty cases. So, the balance comes to 978. Out of these, 120 are renewals. Of those which have been approved, the net figure comes to 858. So, this is the break up.”

Review of work done by Research Institutions and withdrawal of approvals

1.21 During evidence, the Committee desired to know the procedure for withdrawal of approvals of research institutions for the purpose of tax

concessions. The Director in the Department of Science and Technology stated as under:—

“We have basically a system. We ask these institutions to submit their annual reports to us. On the basis of that, we have an indication as to whether they have started some work or whether they have recruited some persons and have created some scientific areas and they have made some progress. What generally happens is this. When the approval is given they would not have got money. This is only a promise. It takes some time for them to get the money and create the assets. If in three years nothing is reported, we ask them to indicate what really is the progress made and whether they are able to do something or not. They come with an explanation that the land has not yet been acquired or some such thing. When we think that such an explanation is reasonable, we give them another chance. If they have collected huge money at this stage, we have to know how they are invested. They are supposed to invest in such form which will invariably be in Government securities or bank deposits. If within five or six years, they do not seem to start any work, we tell them that the approval will be withdrawn. They might make a reference at this stage saying that the Science Director is not coming with the programme of work etc. Very many institutions have been revived. In spite of that if they do not do anything, then we come to the conclusion by saying that they are given another chance to formally hear them. Normally two types of punitive action are taken. The first action is that we tell them that we have done our best for them and if they do not start the work, the approval will expire at the end of one or two years. We have given the limited approval only. At this stage, they would not be able to benefit much out of that. Alternatively, if we find that there is absolutely no intention of doing anything about it or if somebody whom they had in mind is no longer continuing to do that work, we tell them that the approval is hereby withdrawn. We then inform the Finance Ministry about it. After that this thing comes to an end. The particular reason that they did not initiate any work at all and when we are convinced that they will not at any research work than in such cases, the approval is withdrawn. It is done through a review committee and the recommendations of the review committee are shown to the Secretary also.”

In reply to a question, he added:

“The position is that approval given to an institution is for three years and not for a programme. These institutions had originally a long-term approval. Now, the institutions have got a maximum of three years’ approval. If within three years, they do everything O.K., they may be continued. If they do not do, automatically it ceases if they do not come forward for renewal. This is one implication following the Choksi Committee report. In the earlier days, they were given long-term approvals. In their cases, the first line of punishment would be to restrict them to three years.”

1.22. In their reply to the recommendations of the Committee made in para 1.33 of their 187th Report (Fifth Lok Sabha), the Ministry of Finance had stated that the Central Board of Direct Taxes had instructed the Income-tax Officers to examine the annual accounts of the research institutions by issue of notice under Section 139(2) to see whether the funds were utilised in carrying out scientific research and to report deviations, if any, noticed therein. The Committee desired to know the results of the review and also whether the instructions issued by the Board were of a continuing nature or were there for only one time review. In their reply, the Ministry of Finance have stated:

*A list of approved research institutions under Section 35(1) (ii)/(iii) of I.T. Act, 1961, was prepared and circulated to all the Commissioners of Income-tax requesting them that the Income-tax Officers should examine the annual accounts of these research institutions by issue of notices u/s 139(2) to see whether the funds received have been utilised in carrying on the scientific research. It was further desired that in case any deviation is noticed, it may be referred to the prescribed authority for decision u/s 35(3) of the I. T. Act through the Board.

The system adopted by the Board in 1975 is not a one time measure because the Commissioners were again requested by the Board, vide their letter F. No. 203/22/79-ITA-II dated 23-2-79, to send a report to the Board immediately on the action taken in respect of its earlier letter of 1975 and also requesting similar action in respect of the new cases which were included in the list prepared u/s 35(1) (ii)/(iii) and enclosed with the above mentioned letter. Yet again, the Board have circulated a further list of instructions approved u/s 35(1) (ii), 35(1) (iii) as also the research programmes approved u/s 35(2A) to all the CSIT,

vide its letter No. 203/241/82-ITA.II dated 27-12-1982, requesting the CsIT to ask the ITOs to take a similar exercise and send a report to the Board by 30-4-1983.

As a result of the reviews in 1975 and 1979, four cases were recommended for action. In one case, the recognition was withdrawn. In another case, the approval was continued after the prescribed authority *viz.*, the Department of Science & Technology had examined the matter and recommended the renewal of approval. In the remaining two cases, the matter is under examination of the prescribed authority."

1.23. During evidence, the Chairman, CBDT stated that the following were four cases recommended for action as a result of reviews made by the ITOs in 1975 and 1979:

- "(1) Sadiq Memorial Agricultural University, Srinagar.
- (2) Dalmia Institute of Scientific and Industrial Research.
- (3) Birla Institute of Scientific Research.
- (4) Indian Lac Cess Committee, Ranchi."

The witness added:

"The recognition granted in the first case was withdrawn with effect from 18-4-1975. In the second case, a notice u/s 148 was issued but the same was quashed by the Court. In the remaining two cases, the matter was under the examination of the prescribed authority."

1.24. As to the circumstances in which the approval of the Sadiq Memorial Agricultural University, Srinagar was withdrawn, the Ministry have in a note stated as under:—

"The Board by its instructions No. 896 (F. No. 203/8/75-ITA.II) dated the 4th November, 1975 had directed that the Income-tax Officers should examine the annual accounts of the research institutions approved under section 35(1)(ii)/(iii) by issue of notices under section 139(2) of the Income-tax Act, 1961 and to see whether the funds received had been utilised in carrying on the scientific research. In response to these instructions, the Commissioner of Income-tax, Amritsar informed that enquiries made revealed that the proposal for setting up Sadiq Memorial Agricultural University had not been agreed to by the Jammu & Kashmir, Government and that such a university had not started functioning. Thereupon, the approval granted to the University

was withdrawn and the withdrawal was made effective retrospectively from the date from which it was originally approved.

It has been reported that at present, there is nobody to give information whether any sums were paid to this University. Hence, it has not been possible to collect the desired information."

1.25. As regards the review carried out by the Department of Science and Technology, the representative of the Department stated in evidence:

"...when an industrial is approved, it indicates its various projects. Now the projects as such are not specifically approved. We have found that some of these institutions have carried on the projects and they have got some indication of the results. For example, we ask them whether they have carried out any publication. Have the resources been put to use? Many of them would have taken patents also. So, this is one category. In the annual review there may be something very outstanding that these institutions would have done. They also qualify for national awards. That is one category where we note that they are doing some useful work. The second category is, under another Section of the Income-tax Act we have approved some specific programmes. In these programmes when the programme is completed, we ask them to give us an indication about their achievement. The period for these programmes is sometimes 2 to 3 years."

In reply to a question, the witness added:

"In the normal run, if they say it is for 2 or 3 years' period, they will give some indication. Then some investigations have to be carried out. If they say within three years' time, we normally allow. Our experience is that sometimes they say that they have not been able to complete the programme in three years and they want some extension. Then we allow them the extension of time. There have been some cases where a long period is indicated. We suggest them that approval is for three years so that the important programme is not delayed indefinitely, if still they give some important reasons, we allow them for more than 4 years. Second question is how do we evaluate. We have some guidelines... Sometimes, the programme is very wide. Then at the end of the programme we see what progress has been achieved. It is generally done within the department because we have got variety of disciplines in our own department. Wherever

necessary, we even consult some outside experts. This is the broad process of evaluation. . . . In the Department of Science and Technology about 90 such programmes must have been evaluated and my impression is about half of such programmes must have been completed."

1.26 As regards annual review, the Director, Department of Science and Technology stated in evidence:

"We carry out an annual review. We collect the data and we review. If by some chance somebody does not submit them within time we chase them up and ask them to submit it. We follow it up by correspondence also."

In reply to another question he added:

"We have a standing committee which meets one a month or so. They will be able to cover most of them. . . . within a period of three years, all the institutions would be covered."

The Chairmen, CBDT added:

"One point, I want to make clear, that is, when we issue a notification we make it obligatory that they should comply with three conditions. One is, that so and so will maintain separate accounts for the sums received by it for scientific research. Second is, so and so will furnish an annual return of its scientific research activities to the prescribed authority for every financial year in such form as may be laid down and intimated to them for this purpose. The third condition is that so and so will submit by 30 June each year a copy of the audited statement of accounts showing their actual income, the actual expenditure and the actual liabilities and assets, with a copy of each of these documents to the concerned Income-tax Commissioner. These are the three conditions on which the notification is issued."

1.27 During evidence, the Director, Department of Science and Technology admitted that out of 19 cases of withdrawal of approval at the instance of the Department of Science and Technology, in some cases approval had been given under the old Income-tax Act, that is before the 1961 Act, e.g., in the case of Mysore Iron and Steel Works, the approval existed for a long time and they did not do anything in research.

1.28 From a statement of 40 institutions where approval was subsequently withdrawn (Appendix XII). The Committee noted that some of the institutions included in the statement had enjoyed exemption under Section 35 for as many as 25 years and more. While some of these had

not undertaken any research work, others when asked to submit the annual return indicating the scientific research activities conducted by them, had not given any reply. The institutions which had enjoyed exemption for over 30 years included two limited Companies—Tata Iron and Steel Company, Jamshedpur and Mysore Iron & Steel Works, Bhadravati. In case of one institution Research Institute of Ancient Scientific Studies, New Delhi (approved in February 1965 and de-recognised in August 1980), the letter asking the Institute to submit the annual return indicating the scientific research activities conducted by it was returned by the postal authorities as no such institute seemed to be existing.

1.29 When asked how such institutions enjoyed approval for such a long time if these cases were reviewed after every three to five years, Director, Department of Science and Technology stated as follows:—

“...around 1974 or so the Department of Science and Technology came into the picture and at that time we were made one of the prescribed authorities. Around 1975 or 1976 we started the work and the present work that we have done thus relates to last five years.”

1.30 The Committee enquired whether there was any mechanism available with the Finance Ministry or any other Department of the Government of India before the Department of Science and Technology came into being, to see that the approved institutions were actually carrying on research work or not. They further enquired whether any evaluation or monitoring was done or any review was made. The Chairman, CBDT stated:

“Prior to 1-6-82 there were four prescribed authorities. For Medical Institutions, it was Indian Council of Medical Research. Similarly, others were there. They were supposed to carry out such types of review and to see that the amounts given were spent for the purposes of scientific research. Now 20 reviews have been made.”

1.31 The Committee enquired whether the Central Board of Direct Taxes had issued any instructions that in case of de-recognition the earlier assessments of such institutions were to be re-opened and charged to tax. The Chairman CBDT stated:

“We did not issue instructions; but we take it that when we withdraw the approval all consequential action should be taken by the field officers.”

1.32 Further asked whether the witness was in a position to tell the Committee categorically if the field officers had taken action to re-open past assessments of de-recognised institutions, the Chairman CBDT stated:

“Not at this stage.”

1.33 In reply to a post-evidence question from the Committee about the reopening of assessment cases, raising of demands, etc. in respect of 40 institutions whose approval under Section 35 had been withdrawn, the Ministry have stated that information in respect of the donations received, the amount of tax foregone, assessments reopened, etc. could not be collected in entirety within the time available.

The Committee then enquired about the recognition of in-house research institutions and the approval of their programmes. The Director, Science and Technology stated:

“...the same procedure is there. They are also given limited recognition for one year or a maximum of three years and they have to submit the annual returns and it is only on the basis of the review, they will be given extension... Currently there are more than 800 institutions.”

The Chairman, CBDT added:

“If a person claims weighted deductions in the case of in-house it is 125 per cent he has to furnish a certificate from the prescribed authority that the particular project of programme for which this amount was to be deducted has been completed. If he does not furnish the certificate we can withdraw the deductions.”

1.34 When asked to cite cases, if any, in which large expenditure is made in the name of research but actually that has increased production facilities, the representative of the Department of Science and Technology stated:

“There are two categories of overlap. One is the distinction between the pure quality control work and research and development. Now, they say that they have one very sophisticated equipment which they use for research and also for quality control purposes, which is strictly not research. That is one category... For weighted deduction purposes, they should at least complete the programme. I think in principle, they can use it for any programme once the object for

which it was there has been fulfilled...A few cases are there with us to show all this. The *pilot plant* is the one under consideration. Model operation is a very important operation...The Pilot plant in a growing economy is very necessary in research and development activity. If the pilot plant has reasonable dimensions, we normally treat it as for research and development."

1.35 At the instance of the Committee, the Ministry of Finance have furnished details as to how approvals under Section 35 were first given to the following institutions and later on withdrawn:—

- (i) Belle Vue Clinic, Calcutta.
- (ii) Tata Iron and Steel Industry, Jamshedpur .

(i) *Belle Vue Clinic, Calcutta*

On the recommendations of the then prescribed authority, the Indian Council of Medical Research, a notification No. 22 (F. No. 10/12/66-ITA. I) dated 31-3-67 was issued granting approval to the Belle Vue Clinic, Calcutta u/s 35 (1) (ii) of the I.T. Act, 1961. The scientific research to be undertaken by this institution was in the field of medical research. The Indian Council of Medical Research reviewed the research work undertaken by this institution during the year 1974 and the special Committee of the Council was of the view that no aspect of the work presented in the report could be said to be of nature of research. The Committee was also of the opinion that the Clinic was only a good nursing home and did not qualify for tax exemption u/s 35(1) (ii). Accordingly, the Council decided to withdraw its recommendation. *Vide* Notification No. 1225 (F. No. 203/143/75-ITA.II) dated 12-2-76, the CBDT issued a Notification withdrawing the approval with effect from 1-4-76. The Commissioners were also appropriately informed.

(ii) *Tata Iron and Steel Industry, Jamshedpur.*

The Tata Iron & Steel Industry, Jamshedpur was notified u/s 10(2) (xiii) of the I.T. Act, 1922, *Vide* Notification No. 34 dated 24-11-46. The Department of Science & Technology requested them for the annual return regarding their scientific research activities. A reply was received wherein it was indicated that the company was a public limited company. The matter was examined in the Department of Science & Tech-

nology and it was considered that u|s 35(1)(ii) of the I.T. Act, a public limited company was not eligible. Accordingly, the matter was referred to the Ministry of Finance for deletion of their name from the list of tax exempted categories. The Ministry informed the Department of Science & Technology that the name from the list can be deleted only on the recommendations of the prescribed authority. Accordingly, the matter was placed before the prescribed authority and after their approval, recommendations were sent to the Ministry of Finance and the Notification of 24-11-46 was withdrawn on 2-8-79."

Evaluation of the effect of tax concession on the development of indigenous technology.

1.36 In reply to a question whether any over-all evaluation has been made by Government of the impact of the tax concessions on the development of indigenous technology, the Ministry of Finance have in a note stated as under:—

"...No overall evaluation in this regard seems to have been undertaken. It may be stated that it may not be possible to evaluate the direct co-relation of the effect of the tax concessions technology. However, it is undeniable that the indigenous technology in the country has been developing. The Government is examining the question of entrusting a study to the National Institute of Public Finance and Policy regarding the impact of various tax concessions under the Income tax Act like Export Market Development Allowance and Scientific Research concessions."

1.37 In computing business income an assessee, the following deductions are admissible in respect of scientific research under the Income Tax Act:—

- (i) Income of a scientific research association approved by the prescribed authority for purposes of Section 35(1)(ii) of the Act, which is applied solely to the purposes of that association is totally exempt from tax [S. No. (21)]
- (ii) Revenue expenditure on scientific research relating to the business carried on by the assessee is allowable as deduction in the computation of business income [Sec. 35(1)(i)]
- (iii) Any amount paid to a scientific research association or a University, college or other institution, having as its object the undertaking of scientific research (not necessarily related to

the business of the assessee), is admissible as a business expense provided the recipient is approved for the purpose and the amount is to be used for scientific research [Sec. 35(1) (ii)].

- (iv) Any amount paid to a University, college or other institution which is approved for the purpose for use on research in social sciences or statistical research connected with the class of business carried on by the assessee is allowed deduction in computing income from business [Sec. 35(1) (iii)]
- (v) From the assessment year, 1968-69, any expenditure of a capital nature incurred after the 31st March, 1967 on scientific research related to the business carried on by the assessee [Sec. 35(2) (ia)] is allowable in full.
- (vi) From 1-4-1974, a weighted deduction of 1-1/3 times the amount paid to a scientific research association, University, college or other institution or to a public sector company is admissible if the amount is to be used for scientific research under a programme approved by the prescribed authority having regard to the social, economic and industrial needs of India [Sec. 35(2A)]
- (vii) From 1-9-1980, a weighted deduction equal to 1-1/4 times the expenditure incurred by any tax payer in approved in-house research and development units on carrying out any research programme approved by the prescribed authority having regard to the social, economic and industrial needs of India, is allowed as a business expense. Both revenue and capital expenditure (except expenditure on land and buildings) qualify for this weighted deduction [Sec. 35(2B)].
- (viii) From 1-4-1980, any sums paid by a tax-payer other than a business assessee to a research association which has as its object the undertaking of scientific research or to a University, college or other institution, to be used for scientific research are deducted while computing total income provided the recipient institution is approved by the prescribed authority for the purposes of [Sec. 35(1) (ii) Sec. 80 GGA].

1.38 Nothing that the legal provisions regarding concessions for scientific research were spread over a number of sections, sub-sections, clauses and explanations of the Income Tax Act which had made the relevant law quite cumbersome and complex, the Committee enquired whether it would not be in the interest of genuine research and development

activity in the country as much as in the interest of revenue to rationalise and simplify these provisions. In their note, the Ministry have stated as follows:—

“The Government would examine the suggestion made by the Committee in depth in the light of, *inter alia*, the recommendations which might be made on this subject by Economic Administrative Reforms Commission and in consultation with Ministry of Law, Justice and Company Affairs (Legislative Department).”

Research institutions connected with large industrial houses

1.39 In para 1.33 of their 187th Report (Fifth Lok Sabha), the public Accounts Committee had expressed an apprehension that the provisions of the law were rather ambiguous and there was a tendency on the part of some big industrial houses to sponsor so-called scientific research associations with a view to claiming deductions from taxable income. The Committee enquired as to how many of the approved institutions were directly connected with big industrial houses. The Ministry of Finance have replied as under:—

“It is difficult to correlate any particular institution/association as having a direct connection with any particular large industrial house. However, *prima facie*, from the names, 51 institutions/associations could be listed as relating to big industrial houses... *vide* Appendix.

1.40 In reply to a question as to how many of in-service research institutions enjoying exemption had connection with large industrial houses, the representative of the Department of Science & Technology stated, “...my impression is that about 115 or 116 have connection with large houses.”

1.41. In para 1.16 of their 51st Report (Sixth Lok Sabha), the public Accounts Committee had reiterated their apprehensions about the inadequacy of checks and control in the matter of tax concessions for scientific research institutions and *inter alia* reiterated the suggestion for amendment of the law to curb the tendency on the part of big industrial houses setting up so-called research institutions which do not in fact engage in any meaningful research. The Committee desired to know the action taken by Government on the above recommendation of the Committee. In their reply, the Ministry have stated:

“Kind attention of the Committee is invited to the Ministry’s Office Memorandum dated 15th May, 1979 in reply to para 1.16 of 51st Report of the PAC wherein it was stated that in view

of the elaborate system of obtaining detailed information from the institutions/associations by the prescribed authorities before the grant of approvals; the insistence of the prescribed authority on the furnishing of annual reports and returns by these institutions for examining whether the funds are utilised for research purposes; the system of periodical review by the prescribed authorities and the withdrawal of approval in a number of cases as also the action being taken by the ITOs to examine the accounts of these institutions by issue of notices under section 139(2) etc., a ceiling on the contributions would not be feasible as the amounts required for carrying out any particular scientific research programme would depend upon its nature and would vary from programme to programme. It was also stated that in view of these checks and controls etc. no change in the existing provisions of the law was considered necessary.

However, the Economic Administration Reforms Commission is seized of the matter regarding amendments in the structure of Direct Taxes and if any recommendation in respect of concessions to scientific research associations is made, the same would be examined by the Government."

1.42 The Committee desired to know whether the Ministry had any suggestion or amendment in mind regard to the existing exemption provisions in the Direct Taxes Laws which were necessary for effective implementation of the laws and for prevention of tax avoidance. The Ministry of Finance have in their note stated as follows:

"Section 10(21) of the I.T. Act 1961 lays down that the income of an approved scientific research association is exempted from tax to the extent it is applied solely for the purposes of the association, Under a proposed amendment in the Finance Bill, 1983, this exemption will not be available if any sums received by the association by way of contributions or invested or deposited after 28th February, 1983, otherwise than in one or more of the forms or modes specified in relation to investment of funds of charitable or religious trusts and institutions. Exemption from tax will also be forfeited if any funds of the association, invested or deposited before 1st March, 1983 (otherwise than in the forms or modes referred to above) continue to remain so invested or deposited after 30th November, 1983. Further, such association will also forfeit tax exemption if they hold any shares in companies

(not being a Government company or statutory corporation) after 30th November, 1983.

The proposed amendment will plug the non-application|mis-application of the income of the approved association.”

1.43. Under the provisions of the Income Tax Act, 1961, in computing the business income of an assessee, any sum paid by him to a scientific research institution or to any other institution for scientific research is an admissible deduction provided that such association or institution is approved by the prescribed authority for the purpose. The Act was amended in 1974 to provide that if the contribution was to be used for specific research undertaken by an institution under a programme approved by the prescribed authority having regard to the social, economic and industrial needs of India, a deduction of a sum equal to one and one-third times of the contribution so paid, hereafter called 'weighted deduction', shall be allowed.

1.44. In the previous year relevant to the assessment year 1976-77, an industrial company, M/s. Carborandum Universal Limited, contributed a sum of Rs. 8.50,000 to two scientific research centres—Rs. 7.50,000 to A.M.M. Murugappa Chettiar Research Centre, Madras and Rs. 1,00,000 to Nehru Centre, Bombay—both of which were approved under Section 35(1)(ii) of the Income Tax Act by the Council of Scientific and Industrial Research, the prescribed authority. In the assessment completed in April 1979, the Department allowed the assessee's claim for extra deduction of 33-1/3 per cent of the contribution even though there was no approval for any sponsored research programme to be undertaken by the two institutions which was a pre-requisite for the grant of the 'weighted deduction'. The extra deduction of Rs. 2,83,333 being 33-1/3 per cent of the contribution, which was not admissible under the Act, resulted in short-levy of Income-tax and Surtax.

1.45. The Committee note that on the mistake being pointed out by Audit, an additional demand of Rs. 1,74,520 was raised by the Department which has since been collected. As regards Sur-tax, an additional demand of Rs. 31,920 was raised by the Department. Although this demand had not been collected, the assessee's counsel had agreed to withdraw his objection and make payment.

*The amendment has been made in Section 10(21) of the Income Tax Act, 1961, *vide* Finance Act, 1983. O

1.46. Although the Department has since collected the short-levy on account of Income-tax and is expected also to collect the short-levy on account of Sur-tax, the Committee cannot help observing that the Special Audit Party of the Income Tax Department which had also checked the assessment in the present case had failed to detect the mistake. The I.T.O. who had passed the original assessment order having since retired, the Department could not give a satisfactory explanation as to how the I.T.O. had allowed the weighted deduction in this case. Likewise, the I.T.O., Special Audit Party who had checked the assessment having also retired, the Department could not also explain satisfactorily as to why the Special Audit Party had not been able to detect the mistake. In any case, it is apparent to the Committee from the facts of the case that both the Income Tax Officer who had made the original assessment as also the Special Audit Party which had checked the assessment had failed to do their jobs properly.

1.47. The Committee observe that one of the institutions referred to in the Audit Paragraph—A.M.M. Murugappa Chettiar Research Centre, Madras—to whom the assessee company (M/s. Carborandum Universal Limited) had contributed Rs. 7,50,000 was floated by the Murugappa Chettiar group who have a substantial interest in M/s Carborandum Universal Limited. The second institution—Nehru Centre, Bombay—to whom the assessee company had contributed Rs. one lakh, had, from the date of its approval in April 1974 to 1978 not done any research work. This leads the Committee to the general question as to how far the huge exemptions given under the Income Tax law for scientific research are being utilised for the intended purpose.

1.48. The Committee note that there are 1018 institutions (including renewals) approved for scientific research under Section 35(1)(ii) and (iii) of the Income Tax Act, in addition to 126 specific approved programmes of scientific research under Section 35(2A). Besides, there are over 800 in-service research institutions. As till recently, the prevailing system was to give long-term/perpetual approvals and there were no periodical/annual reviews of the work done by approved institutions, it is difficult for the Committee to say how far the exempted funds have been utilised for the intended purpose or diverted to other purposes. However, a statement of 40 institutions, whose approvals have been withdrawn in recent years, makes shocking revelations. From this statement, the Committee observe that some of the approved institutions which had enjoyed exemption under Section 35 for as many as 25 years or even more

had not done any research work whatever. Some of the institutions, when asked to submit the annual return indicating the scientific research activities being conducted by them, had not given any reply. In case of one institution—Research Institute of Ancient Scientific Studies, New Delhi (approved in February 1965 and de-recognised in August 1980), the letter asking the Institute to submit the annual return indicating the scientific research activities conducted by it was returned by the postal authorities as no such Institute seemed to be existing.

1.49. A tax exemption involves loss of public revenue. This tax expenditure is justified only if the purpose behind it is really achieved. A heavy responsibility is therefore cast on the authorities granting exemption to evolve proper checks and procedures to ensure this. The Committee observe with distress that in the case of exemptions for scientific research, the authorities concerned had, after giving long-term/perpetual approvals, done precious little in this regard in the past. In para. 1.32. of their 187th Report (Fifth Lok Sabha) presented to the House on 29 January 1976, the Public Accounts Committee were surprised to find that the Central Board of Direct Taxes had not even considered necessary to issue guidelines to assessing officers on what constitute "expenditure on scientific research". In para 1.16 of their 51st Report (Sixth Lok Sabha), the Committee reiterated their impression that the checks and controls exercised till then had been perfunctory. In para 1.4.24 of their Final Report (September 1978), the direct Tax Laws Committee observed that "hardly any attempts were made in the past to ensure that the huge sums paid to research institutions by big business houses were spent, usefully and effectively or to ascertain the nature of the research activities carried on with the aid of such funds and the results achieved". The Committee observe that it is only very recently that a system of time-bound approvals and annual reviews has been evolved.

1.50. The Committee note that there are 51 scientific research institutions connected with large industrial houses. In addition, there are about 110—120 in-house research institutions connected with large industrial houses. In para 1.33 of their 187th Report presented to the House on 29-1-76, the Committee had expressed an apprehension that the provisions of the law were rather ambiguous and there was a tendency on the part of some big industrial houses to sponsor so-called scientific research associations with a view to claiming deductions from taxable income. The Committee had desired that loopholes in the Act should be plugged. In para

1.16 of their 51st Report (Sixth Lok Sabha), the Committee reiterated their earlier recommendation. The Committee are glad to note that Government have recently taken an important step to de-link the financial interests of scientific research institutions from those of industrial houses and thereby to prevent diversion of funds to unintended purposes. By the Finance Act, 1983, Section 10(21) of the Income Tax Act, which lays down that the income of an approved scientific research association is exempted from tax to the extent it is applied solely for the purposes of the association, has been amended to regulate the investments. The Committee hope that the amendment will go a long way to prevent mis-application of the resources of approved associations. They further trust that Government would make an in-depth study of the problem and take such further measures, legal or procedural, as might be necessary to effectively prevent mis-application of resources of scientific research institutions for non-research purposes.

1.51. The Committee feel that the problem cannot be wholly solved so long as the institutions getting approval under Section 35 know that they can get away with the past exempted funds not applied to the purpose allowed for. The Committee enquired whether the Central Board of District Taxes had issued any instructions that in cases where the approved institutions were subsequently de-recognised, the earlier assessments of such institutions should be re-opened. The Chairman, Central Board of Direct Taxes, stated that they had not issued such instructions but they took it that when an approval was withdrawn, all consequential action would be taken by the field officers. The Committee are surprised at this complacent approach of the Central Board of Direct Taxes. They desire that clear instructions should be issued by the Board that in case an institution approved under Section 35 is subsequently de-recognised for not having done any scientific research work, the assessing officers should re-open all the past assessments of the institution under the law, and recover the tax due.

1.52. In para 1.4.24 of their Final Report (September 1978) the Direct Tax Laws Committee (Choksi Committee) expressed the view that while the Income Tax Department may be in a position to enquire into some of the peripheral aspects of activities of scientific research associations such as maintenance of proper accounts of the sums collected and the utilisation of such sums, the Income Tax Officer is hardly in a position to make an informed technical enquiry into the content and quality of the institution's research activities. This function belongs legitimately to the prescribed authority which grants the approval to the institution

in the first instance and it should be in a position to make technical appraisal of the association's activities from the qualitative angle. The Committee appreciate the above view and desire that continued exemption should be subject to periodic appraisal of the activities of the associations by the prescribed authority to ensure the quality. The Committee would await the procedure evolved in this regard.

1.53. The Committee note that the object underlying the tax exemptions under Section 35 was to encourage scientific research with the aim of developing indigenous technology and self-reliance in industry. Although the income-tax exemptions for scientific research have been existing from pre-Independence days, the Ministry of Finance have not yet cared to conduct a study to see how far the object underlying the tax exemption has been achieved. The Committee understand that Government are now examining the question of entrusting a study to the National Institute of Public Finance and Policy regarding the impact of various tax concessions for scientific research under the Income Tax Act. The Committee desire that this should be done without any further delay. They also desire that the National Institute of Public Finance and Policy may also be asked to make an assessment of the annual amount of revenue forgone on account of various tax concessions given under Section 35 of the Act.

1.54. The Committee note that the provisions on the subject are spread over in a number of sections, sub-sections, clauses and Explanations of the Income Tax Act. These are quite cumbersome and complex and frequent amendments have made them even more so. Section 35 alone has undergone as many as 11 amendments in the last few years. The Committee desire that in the interest of promotion of research and development activities in the country and also in the interest of revenue, early steps should be taken to rationalise and simplify these provisions. The Committee wish to emphasise that bona fide research institutions should be encouraged and that the legal and procedural devices employed in connection with the grant of exemption from tax of the funds collected and utilised by such institutions should be such as would help rather than hinder the pursuit of their objectives.

NEW DELHI;
December 9, 1983.

Agrahayana 18, 1905 (Saka).
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SUNIL MAITRA
Chairman,
Public Accounts Committee.

APPENDIX I (Vide para 1-16)

ANNEXURE _____

Progress in Implementation |

ACCOUNTING YEAR _____

**PROGRESS ON THE IMPLEMENTATION OF THE SCIENTIFIC RESEARCH PROJECT APPROVED UNDER SECTION 35(2A)
OF THE INCOME TAX, ACT, 1961**

S. No.	Title of the Research Project (with Brief Details)	Notification No. & Date of Approval	Name(s) & Address(s) of the Sponsorer(s)	Name & Address(s) of the Im- plementaing Laboratory/ Institu- tion	Date of Commencement	Date of Completion
1	2	3	4	5	(6a)	(6b)

Actual Expenditure Incurred						Results Achieved (Attach a Separate sheet, if necessary)	Social, Economic & Industrial needs of the country Fulfilled	Remarks (if any)
Lands & Buildings	Equipment & Machinery	Salaries	Raw Materials	Other items Please specify	Total			
7(a)	7(b)	7(c)	7(d)	7(e)	7(f)	8	9	10

Signature _____

Head of the Laboratory/Institute

APPENDIX II*(Vide para 1-28)***LIST OF INSTITUTIONS / ASSOCIATIONS IN WHOSE CASES APPROVAL UNDER SECTION 35(1) (ii)/35(2A) WAS GIVEN AND SUBSEQUENTLY WITHDRAWN**

Sr. No.	Name & the addresses of the institution	Date of approval	Date of withdrawal of approval	Date of effect of withdrawal	Reasons
1	2	3	4	5	6
1	Balle Vue Clinic 9, Dr. Brahmachari Street, Calcutta-17	31-3-1967	12-2-1976	1-4-1976	No aspect of work presented in the report for the year 1974 could be said to be of research in nature. As such the approval has been withdrawn.
2	Indian Crucible Company Limited, Howrah . . .	23-11-1946	23-4-1980	1-1-1979	No scientific research activities have been undertaken by the Institute. As such the approval has been withdrawn.
3	Bengal Potteries, Calcutta	23-11-1946	27-12-1980	25-5-1980	The Company was requested to submit the annual return indicating the scientific research activities being conducted by them. No reply was received by the Prescribed Authority from the Company. As such the approval has been withdrawn.
4	Botanical Survey of India, Calcutta	23-11-1946	17-2-1981	13-1-1981	The Botanical Survey of India was not interested in the tax exemption approval since whole of the expenditure of Botanical Survey of India has met out of the consolidated fund of India. As such the approval has been withdrawn.

5	Statistical Publishing Society, 201, Barrackpore Trunk Road, Calcutta-36.	6-9-1965	10-8-1982	24-6-1982	The Society was informed by the Prescribed Authority that they are not covered under section 35(1)(ii) and then they applied to the Ministry for approval u/s 35(1)(iii). The Ministry of Finance have issued the Notification u/s. 35(1) (iii) of the I.T. Act. After considering the facts & circumstances of this case the Prescribed Authority has decided that the approval granted to the Society u/s. 35(1) (ii) may be withdrawn.
6	Tamil Nadu Eye Relief Association, Madurai, 240, Naicker New St., Madurai-1.	11-12-1972	15-7-1977	10-6-1977	The Association had neither collected any funds nor had undertaken any research activities since 1974. As such the approval has been withdrawn.
7	R.N.T. Medical College, Udaipur	27-3-1974	1-8-1975	27-3-1974	As no research work had been done at the Institute, the approval has been withdrawn.
8	B.B. & C.I. Railway Workshop, Ajmer	10-4-1978	23-7-1980	25-5-1980	The Prescribed Authority asked the Institute to submit annual returns of research activities. The Institute replied that as the Institute was not covered under the Income tax Act as a scientific research Institute, they were not under taking any research. As such the approval was withdrawn.
9	Sadiq Memorial Agricultural University, Srinagar (J & K)	18-4-1975	26-3-1977	18-4-1975	As the proposed university has not been established, the approval has been withdrawn.

1	2	3	4	5	6
10	Invention Promotion Board, 39, Ring Road, Mulchand Hospital Corner, New Delhi-24.	1-1-1972	27-7-1976	1-4-1973	The Institute has been merged with the NRDC and it no longer exists as a separate entity. As such the approval has been withdrawn.
11	Birla Archaeological and Cultural Research Institute Hyderabad	15-9-1969	6-12-1979	1-4-1975	No research activity has been carried out since April 1975 and as such the approval has been withdrawn.
12	Nutrition Society of India Hyderabad	30-4-1974	26-12-1980	1-4-1980	The Society had not carried out any research work during 1978 & 1979. As such the approval has been withdrawn.
13	Mysore Iron and Steel Works, Bhadravati	24-11-1946	18-4-1978	17-3-1978	The Association was converted into a limited company; as such the approval has been withdrawn.
14	N.M. Wadia Institute of Cardiology, 32, Sascon Road, Poone-1	10-6-1969	17-1-1976	31-1-1976	The work related only to collection of data and hence there was no component of research in the activities undertaken by this institution. As such the approval has been withdrawn.
15	Systems Research Institute, Pune	22-12-1977	21-8-1981	15-8-1977	It was brought to the notice of the Prescribed Authority that the Institute could not collect any funds from any assessee. As such the Prescribed Authority withdrew the approval granted by it earlier.
16	Sri Ganga Rzm Trust Society, Rajinder Nagar, New Delhi	19-2-1974	22-7-1975	1-4-1973	Detailed report of the research work carried out during the year 1977 not submitted. Thus the Prescribed Authority recommended withdrawal of approval.

17	Indian Association for the Advancement of Education, Madras.	7-7-1969	17-2-1976	1-4-1976	Inspite of repeated reminders the Association failed to submit a report of the research work and the statement of income and expenditure for the year 1974. As such the approval has been withdrawn.
18	Medical Education Foundation, Madras	15-2-1972	17-2-1976	1-4-1976	Inspite of repeated reminders, the foundation failed to submit the report of the research work and the statement of income & expenditure for the year 1974. As such the approval has been withdrawn.
19	L. Madan Mohan Lal Ayurvedic Research Society, Post Box No. 1185, Bara Hindu Rao, Delhi-6	9-3-1971	17-2-1976	1-4-1976	Inspite of repeated reminders, the Trustee of the Society failed to submit the report of the research work and statement of income and expenditure for the year 1974. As such the approval has been withdrawn.
20	Invention Promotion Board, 39, Ring Road, Mulchand Hospital Corner, New Delhi-24	1-1-1972	27-7-1976	1-4-1973	The Institute has been merged with the NRDC and it no longer exists as a separate entity. As such the approval has been withdrawn.
21	Research Institute of Ancient Scientific Studies, New Delhi	15-2-1965	23-7-1980	25-8-1980	The Prescribed Authority requested the Institute to submit the annual return indicating the scientific research conducted by them. The letter was returned by the postal authorities. As no such institute seemed to be existing, the approval was withdrawn.
22	The Association of Otolaryngologists, Bombay	25-11-1970	19-2-1976	1-4-1976	There was very little component of research activities and that the activities of organising annual conferences, publication of journal did not fall within the purview of research. As such the approval has been withdrawn.

1	2	3	4	5	6
23	Gujarat Research Society, Samshodhan Sadan, South 1 Avenue, Khar, Bombay.	26-10-1974	19-2-1976	1-4-1976	The approval was withdrawn as no research work had been done by the Society.
24	B.Y.L. Nair Hospital & T.N. Medical College Research Society, Bombay.	6-11-1967	31-1-1976	31-1-1976	Majority of research projects carried out related to purely conduct of clinical trials of standard drugs manufactured by well known firms. As such the approval has been withdrawn.
25	Society for Prevention of Heart Disease & Rehabilitation, India House No. 2, Kamp's Corner, Bombay-36.	26-9-1972	17-2-1976	1-4-1976	The investigation carried out was purely routine and ordinary clinical examinations and cannot be said to be of the nature of research. As such the approval has been withdrawn.
26	Society for Pharmaceutical & Industrial Research, Kalina Santa Cruz (East) Bombay-29.	20-12-1972	12-7-1976	1-6-1976	The society had collected large sums of the money but actually spent only a small fraction of it for the purpose of research. The bulk of funds were used for advances/loans to the college of Pharmacy. As such the approval has been withdrawn.
27	Rose Foundation, Bombay.	10-5-1972	30-8-1977	21-3-1977	In spite of repeated reminders, the foundation failed to submit a report of the research work and the statement of income and expenditure for the year 1975 as such the approval has been withdrawn.
28	Industrial Foundation, Bombay.	11-3-1954	5-1-1980	4-12-1979	The Foundation have not conducted any scientific research in the field of natural and applied sciences. As such the approval has been withdrawn.

29	Protein Foods and Nutrition Association of India, Bombay.	8-11-1973	23-4-1980	17-3-1980	The PFNDAI has not conducted any scientific research in the field of natural and applied sciences. As such the approval has been withdrawn.
30	Kailash Seva Sadan, Bombay.	15-3-1978	7-2-1980	11-14-1979	The sadan requested the Prescribed Authority that the tax exemption benefit granted to it may be withdrawn. As such the approval was withdrawn by the Prescribed Authority w.e.f. 1-4-1979.
31	Stock Exchange, Bombay.	22-11-1968	16-8-1977	31-3-1977	The approval was originally granted u/s 35(1) (ii) which was later on converted in an approval u/s 25(1) (iii) only.
32	M. Visweswaraya Industrial Research & Development Centre, Bombay.				The files are not readily available.
33	Industrial & Scientific Research Association, Madras.	6-9-1965	3-4-1978	11-2-1978	No scientific research work was carried out by the Institute. As such the approval has been withdrawn.
34	The Indian Institution of Plant Engineers, Madras.	6-8-1976	24-4-1980	1-1-1979	The Institute failed to submit the Annual return and the report of its scientific research activities. As such the approval has been withdrawn.
35	Cadila Laboratories, Manufacturer of Pharmaceuticals] Products, Hari Nagar, Ahmedabad-8.	27-2-1974	23-2-1976	1-4-1976	The research and development activity forms a part & parcel of the production & testing activity of the organisation for promotion of their financial projects and as such the approval has been withdrawn.
36	Sardar Patel Institute of Economic and Social Research, Post Box No. 4062, Navrangpura, Ahmedabad-9.	30-6-1965	30-3-1978	26-11-1977	The report of research activities submitted by the Institute for the year 1975-76 showed that the areas of research of the Institute is social sciences. As such the approval u/s 35 (1) (ii) has been withdrawn.

1	2	3	4	5	6
37	B.J. Medical College, Ahmedabad]	6-11-1967	8-7-1977	1-4-1977	Inspite of repeated reminders, the Institution failed to submit the report of the research work and statement of income and expenditure for the year 1975. As such the approval has been withdrawn.
38	Tata Iron & Steel Industry, Jamshedpur.	24-11-1946	2-8-1979	1-1 1978	The company informed the Prescribed Authority that the said company is a commercial undertaking. Therefore a shown cause notice was issued to the company by the Prescribed Authority. The company did not propose to make any representation in this regard. As such the approval was withdrawn.
39	Family Planning Foundation, New Delhi.				The files are not readily available.
40	The Institute of Chartered Accountants, New Delhi ;				— do. —

APPENDIX III

(vide Introduction)

CONCLUSIONS/RECOMMENDATIONS

S. No.	Para No.	Ministry/Department	Recommendations
1	2	3	4
1	1-43	Finance (Revenue)	Under the provisions of the Income Tax Act, 1961, in computing the business income of an assessee, any sum paid by him to a scientific research institution or to any other institution for scientific research is an admissible deduction provided that such association or institution is approved by the prescribed authority for the purpose. The Act was amended in 1974 to provide that if the contribution was to be used for specific research undertaken by an institution under a programme approved by the prescribed authority having regard to the social, economic and industrial needs of India, a deduction of a sum equal to one and one-third times of the contribution so paid, hereafter called 'weighted deduction', shall be allowed.
2	1-44	Do.	In the previous year relevant to the assessment year 1976-77, an industrial company, M/s. Carborandum Universal Limited, contributed a sum of Rs. 850,000 to two scientific research centres and Rs. 7,50,000 to A.M.M. Murugappa Chettiar Research Centre, Madras and Rs. 1,00,000 to Nehru Centre, Bombay—both of which were approved under Section (35 (i) (ii) of the Income Tax Act by the Council of Scientific and Industrial

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Research, the prescribed authority. In the assessment completed in April 1979, the Department allowed the assessee's claim for extra deduction of 33-1/3 per cent of the contribution even though there was no approval for any sponsored research programme to be undertaken by the two institutions which was a pre-requisite for the grant of the 'weighted deduction'. The extra deduction of Rs. 2,83,333 being 33-1/3 per cent of the contribution, which was not admissible under the Act, resulted in short-levy of Income-tax and Surtax.

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Finance (Revenue)

The Committee note that on the mistake being pointed out by Audit, an additional demand of Rs. 1,74,520 was raised by the Department which has since been collected. As regards Sur-tax, an additional demand of Rs. 31,920 was raised by the Department. Although this demand had not been collected, the assessee's counsel agreed to withdraw his objection and make payment.

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Do.

Although the Department has since collected the short-levy on account of Income-tax and is expected also to collect the short-levy on account of Sur-tax, the Committee cannot help observing that the Special Audit Party of the Income Tax Department which had also checked the assessment in the present case had failed to detect the mistake. The I.T.O. who had passed the original assessment order having since retired, the Department could not give a satisfactory explanation as to how the I.T.O. had allowed the weighted deduction in this case. Likewise, the I.T.O., Special Audit Party who had checked the assessment having also retired, the Department

could not also explain satisfactory as to why the Special Audit Party had not been able to detect the mistake. In any case, it is apparent to the Committee from the facts of the case that both the Income Tax Officer who had made the original assessment as also the Special Audit Party which had checked the assessment had failed to do their jobs properly.

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Do.

The Committee observe that one of the institutions referred to in the Audit Paragraph—A.M.M. Murugappa Chettiar Research Centre, Madras—to whom the assessee company (M/s. Carborandum Universal Limited) had contributed Rs. 7,50,000 was floated by the Murugappa Chettiar group who have a substantial interest in M/s. Carborandum Universal Limited. The second institution—Nehru Centre, Bombay—to whom the assessee company had contributed Rs. one lakh, had, from the date of its approval in April 1974 to 1978, not done any research work. This leads the Committee to the general question as to how far the huge exemptions given under the Income Tax law for scientific research are being utilised for the intended purpose.

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1948

Do.

The Committee note that there are 1018 institutions (including renewals) approved for scientific research under Section 35(1)(ii) and (iii) of the Income Tax Act, in addition to 126 specific approved programmes of scientific research under Section 35(2A). Besides, there are over 800 in-service research institutions. As till recently, the prevailing system was to give long-term/perpetual approvals and there were no periodical/annual reviews of the work done by approved institutions, it is difficult for the Committee to say how far the exempted funds have been utilised for the intended purpose or diverted to other purposes. However, a statement of

40 institutions, whose approvals have been withdrawn in recent years, makes shocking revelations. From this statement, the Committee observe that some of the approved institutions which had enjoyed exemption under Section 35 for as many as 25 years or even more had not done any research work whatever. Some of the institutions, when asked to submit the annual return indicating the scientific research activities being conducted by them, had not given any reply. In case of one institution—Research Institute of Ancient Scientific Studies, New Delhi (approved in February 1965 and de-recognised in August 1980), the letter asking the Institute to submit the annual return indicating the scientific research activities conducted by it was returned by the postal authorities as no such Institute seemed to be existing.

A tax exemption involves loss of public revenue. This tax expenditure is justified only if the purpose behind it is really achieved. A heavy responsibility is therefore cast on the authorities granting exemption to evolve proper checks and procedures to ensure this. The Committee observe with distress that in the case of exemptions for scientific research, the authorities concerned had, after giving long-term/perpetual approvals, done precious little in this regard in the past. In para 1.32 of their 187th Report (Fifth Lok Sabha) presented to the House on 29 January, 1976, the Public Accounts Committee were surprised to find that the Central Board of Direct Taxes had not even considered necessary to issue guidelines to assessing officers on what constitutes "expenditure on scientific research". In para

1.16 of their 51st Report (Sixth Lok Sabha), the Committee reiterated their impression that the checks and controls exercised till then had been perfunctory. In para 1.4.24 of their Final Report (September 1978), the Direct Tax Laws Committee observed that "hardly any attempts were made in the past to ensure that the huge sums paid to research institutions by big business houses were spent usefully and effectively or to ascertain the nature of the research activities carried on with the aid of such funds and the results achieved". The Committee observe that it is only very recently that a system of time-bound approvals and annual reviews has been evolved.

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Do.

The Committee note that there are 51 scientific research institutions connected with large industrial houses. In addition, there are about 110-120 in-house research institutions connected with large industrial houses. In para 1.33 of their 187th Report presented to the House on 29-1-76, the Committee had expressed an apprehension that the provisions of the law were rather ambiguous and there was a tendency on the part of some big industrial houses to sponsor so-called scientific research associations with a view to claiming deductions from taxable income. The Committee had desired that loopholes in the Act should be plugged. In para 1.16 of their 51st Report (Sixth Lok Sabha), the Committee reiterated their earlier recommendation. The Committee are glad to note that Government have recently taken an important step to de-link the financial interests of scientific research institutions from those of industrial houses and thereby to prevent diversion of funds to unintended purposes. By the Finance Act, 1983, Section 10(21) of the Income Tax Act, which lays down that the income of an approved scientific research association is exempted from

tax to the extent it is applied solely for the purposes of the association, has been amended to regulate the investments. The Committee hope that the amendment will go a long way to prevent misapplication of the resources of approved associations. They further trust that Government would make an in-depth study of the problem and take such further measures, legal or procedural, as might be necessary to effectively prevent misapplication of resources of scientific research institutions for non-research purposes.

The Committee feel that the problem cannot be wholly solved so long as the institutions getting approval under Section 35 know that they can get away with the past exempted funds not applied to the purpose allowed for. The Committee enquired whether the Central Board of Direct Taxes had issued any instructions that in cases where the approved institutions were subsequently de-recognised, the earlier assessments of such institutions should be re-opened. The Chairman, Central Board of Direct Taxes, stated that they had not issued such instructions but they took it that when an approval was withdrawn, all consequential action would be taken by the field officers. The Committee are surprised at this complacent approach of the Central Board of Direct Taxes. They desire that clear instructions should be issued by the Board that in case an institution approved under Section 35 is subsequently de-recognised for not having done any scientific research work, the assessing officers should re-open all the past assessments of the institution under the law, and recover the tax due.

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In para 1.4.24 of their Final Report (September 1978) the Direct Tax Laws Committee (Choksi Committee) expressed the view that while the Income Tax Department may be in a position to enquire into some of the peripheral aspects of activities of Scientific research associations such as maintenance of proper accounts of the sums collected and the utilisation of such sums, the Income Tax Officer is hardly in a position to make an informed technical enquiry into the content and quality of the institution's research activities. This function belongs legitimately to the prescribed authority which grants the approval to the institution in the first instance and it should be in a position to make technical appraisal of the association's activities from the qualitative angle. The Committee appreciate the above view and desire that continued exemption should be subject to periodic appraisal of the activities of the associations by the Prescribed authority to ensure the quality. The Committee would await the procedure evolved in this regard.

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The Committee note that the object underlying the tax exemptions under Section 35 was to encourage scientific research with the aim of developing indigenous technology and self-reliance in industry. Although the income-tax exemptions for scientific research have been existing from pre-Independence days, the Ministry of Finance have not yet cared to conduct a study to see how far the object underlying the tax exemption has been achieved. The Committee understand that Government are now examining the question of entrusting a study to the National Institute of Public Finance and Policy regarding the impact of various tax concessions for scientific research under the Income Tax Act. The Committee desire

that this should be done without any further delay. They also desire that the National Institute of Public Finance and Policy may also be asked to make an assessment of the annual amount of revenue forgone on account of various tax concessions given under Section 35 of the Act.

The Committee note that the provisions on the subject are spread over in a number of sections, sub-sections, clauses and Explanations of the Income Tax Act. These are quite cumbersome and complex and frequent amendments have made them even more so. Section 35 alone has undergone as many as 11 amendments in the last few years. The Committee desire that in the interest of promotion of research and development activities in the country and also in the interest of revenue, early steps should be taken to rationalise and simplify these provisions. The Committee wish to emphasise that *bona fide* research institutions should be encouraged and that the legal and procedural devices employed in connection with the grant of exemption from tax of the funds collected and utilised by such institutions should be such as would help rather than hinder the pursuit of their objectives.

