

A ESKAYEF (NOW KNOWN AS SMITHKLINE BEECHAM
PHARMACEUTICALS (INDIA) LTD. ETC.

v.

COMMISSIONER OF INCOME TAX, KARNATAKA—II,
BANGALORE.

B JULY 20, 2000

[S.P. BHARUCHA AND MS. RUMA PAL, JJ.]

C *Income Tax Act, 1961—Section 37—Liability to pay surtax—Whether
an admissible deduction in computing total income—Held, not deductible.*

*Section 37(3A)—Expenditure incurred on distribution of free samples
of prescription drugs to doctors—Whether in the nature of advertisement or
publicity or sales promotion falling within the restrictive provisions of the
section—Held yes.*

D *Drugs and Magic Remedies (Objectionable Advertisements) Act, 1954—
Section 3—Prohibition of publication of advertisement of a drug—Held,
prohibition not applicable to physician's samples.*

E **In these appeals, the following two questions were raised:**

1. **Whether the surtax liability is an admissible deduction under
section 37 of the Income Tax Act, 1961?**
2. **Whether expenditure incurred on distribution of free samples of
prescription drugs to doctors is in nature of advertisement falling
within the restrictive provisions of section 37(3A) of the Act?**

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G **Appellant-assessee contended that the expenditure incurred on
distribution of free samples of prescription drugs to doctors did not amount
to advertisement or publicity or sales promotion and thereby not subjected to
restrictions under sub-section 3A of section 37. The Income Tax Appellate
Tribunal and the High Court rejected the contention of the assessee.**

H **In appeal to this Court, the assessee submitted that the purpose of the
distribution of drugs was to obtain a feedback from the medical profession as
to the efficacy of the distributed drugs. The assessee further submitted that
section 3 of the Drugs and Magic Remedies (Objectionable Advertisements)**

Act, 1954, prohibits the publication of any advertisement of the drugs. A

Dismissing the appeals, this Court

HELD: 1. With regard to the first question, i.e. whether the surtax liability is an admissible deduction, the master is no longer *res integra*.

[636-G] B

Smith Kline and French (India) Ltd. & Ors. v. Commissioner of Income Tax, (1996) 219 ITR 581, relied on.

2. The target for any advertisement or publicity or sales promotion of the drugs could only be the doctors who would prescribe them. The object of distribution of the samples of the drugs to the doctors is to make them aware that such drugs are available in the market in relation to the cure of a particular affliction and therefore to persuade them to prescribe the same in appropriate cases. So doing is tantamount to publicity and sales promotion. The assessee has not produced filled up questionnaires or letters from doctors in support of its claim that the free samples of prescription drugs were distributed to doctors for obtaining feedback from them. [639-D-E] C

3. The prohibition under the Drugs and Magic Remedies (Objectionable Advertisements) Act, 1954 is not applicable to physician's samples. What is barred thereby is publication and that is amply clear when one refers to the definition of "advertisement" in the Act. [639-H; 640-A] D E

Smith Kline and French (India) Ltd. v. Commissioner of Income Tax, (1992) 193 ITR 582, approved.

Commissioner of Income Tax v. J & J Dechane Laboratories (P) Ltd., (1996) 222 ITR 11, distinguished. F

Commissioner of Income Tax v. Ampro Food Products, (1995) 215 ITR 904, referred to.

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 2717 of 1996. G

From the Judgment and Order dated 11.3.91 of the Karnataka High Court in I.T.R.C. No. 182 of 1985.

WITH

Civil Appeal Nos. 4545-4577/1996.

H

A D.A. Dave, Ms. Pratibha M. Singh, Ms. Kavita Wadia, Ramesh Singh, Maninder Singh and S. Syal for the Appellant.

M.L. Verma, G. Venkatesh Rao and Ms. Sushma Suri for the Respondent.

The Judgment of the Court was delivered by

B **BHARUCHA, J.** Civil Appeal No. 2717 of 1996 :

The appeal relates to the Assessment year 1980-81. It is on a certificate of fitness to appeal granted by the High Court. The certification was only in respect of one question which read thus:

C “Whether on the facts and in the circumstances of the case, the liability to pay surtax is an admissible deduction in computing the total income?”

The answer to this question is covered against the assessee by the decision of this court in the assessee’s own case, 219 I.T.R. 581. The question is, accordingly, answered in the negative and in favour of the Revenue.

The civil appeal is dismissed.

No order as to costs.

E *Civil Appeal Nos. 4545-4547 of 1996:*

These are appeals from the judgment and order of the Division Bench of the Karnataka High Court in Income Tax References. The questions that the High Court was called upon to answer read thus:

F “*Question of law in ITRC 144 of 1993*

(a) Whether on the facts and in the circumstances of the case, the liability to pay surtax is an admissible deduction in computing the total income?

G (b) Whether on the facts and in the circumstances of the case, the expenditure incurred on physician’s samples is in the nature of advertisement expenditure falling within the restrictive provisions of Section 37 (3A) of the Income Tax Act?

Question of law in ITRC 143 of 1993.

H (a) Whether on the facts and in the circumstances of the case, the

liability to pay surtax is an admissible deduction in computing the total income? **A**

Question of law in ITRC 171 of 1994.

Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that the applicant was not entitled to the deduction of surtax levied while computing the total income of the applicant?" **B**

It is common ground that the questions that relate to surtax must be answered in the negative and in favour of the Revenue by reason of the judgment of this Court in the case of *Smith Kline and French (India) Ltd. and Ors. v. Commissioner of Income Tax*, (1996) 219 ITR 581. They are so answered. **C**

The issue that is canvassed at the bar relates to the physician's samples that the assessee, a pharmaceutical company, distributes to the medical profession. It is the assessee's case that these are all samples of prescription drugs, and we proceed upon that basis. Learned counsel for the assessee submitted that the distribution of physician's samples to doctors did not amount to advertisement or publicity or sales promotion and, therefore, all the expenditure incurred by the appellants on such distribution was exempt, under the provisions of section 37 of the Income-Tax Act, 1961 (for short 'the Act') as expenditure incurred wholly and exclusively for the purpose of the appellants business and not subject to the restrictions on allowability contained in sub-section (3A) thereof. **D**

The submission did not find favour with the Income-Tax Appellate Tribunal and with the High Court. The High Court, in the order under appeal, followed its earlier judgment in the case of *Smith Kline and French (India) Ltd. v. Commissioner of Income Tax*, 193 ITR 582, (which also concerned the assessee). The High Court there had said : **E**

"We do not think that we should discuss the principle pertaining to the interpretation of statutes referred to above in detail because the idea behind the contention is to convey that advertisement, publicity or sales promotion should be confined to the act of media propaganda and a direct approach to the consumers by publicising the product through newspaper advertisements, posters or some other similar methods. We do not think that such a limited meaning should be given to the three words. The nature of the advertisement or publicity **F**

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A depends upon the nature and quality of the article in question. An inducement to the public to buy a particular commodity may be formulated in a mode most suitable to the article in question.

B The members of the public would not buy a drug just because it is advertised repeatedly or publicised through posters or announced on the T.V. etc. The members of the public should have confidence about the curative value of the drug and such confidence could be created mainly by the medical practitioners prescribing the said drug or when the medical practitioners give the same to patients towards treatment. The media through which the drug could get publicised and earn goodwill will be the media of prescription by the medical practitioner. Further, the real persons who could create a market for a particular drug are the medical practitioners themselves having regard to the nature of the drug, when compared to other industrial products. A drug is not an ordinary article of consumption. It is consumed only to get rid of some ailment. Before the drug gets circulated, its reputation will have to be confirmed to the medical practitioners and that is why free samples are supplied to them.

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E If the object of supplying free samples is only to find out the reaction of the medical practitioners about the efficacy or curative value of the drug, the supply of free samples would have been confined during the initial stages of production of a new drug. However, that is not the case of the assessee here. The assessee nowhere contends that free samples were given to the medical practitioners only at the time when a drug is introduced for the first time.

F Learned counsel for the Revenue also pointed out that the assessee in its original return of income has included these sums under the head "Advertisement, publicity and sales promotion". Therefore, the assessee's first impression about the nature of the free samples was the correct approach and the assessee has properly disclosed the same under an appropriate head in the return. Subsequently, the assessee sent a letter modifying the original return of income and offered to confine the claim under this head to a part of the expenditure.

G Learned counsel for the Revenue is justified in pointing out the above circumstance as an additional factor in support of the conclusion arrived at by the Appellate Tribunal.

H Each of the three words "advertisement, publicity and sales

promotion” cannot always be confined to distinct and different concepts. Some aspects of one word could naturally overlap with the meaning attributed to the other word. No doubt, in a commercial sense, the purpose of these activities is to gain goodwill and a market but the mode of achieving this object cannot be confined to the limited meaning attributed to them by learned counsel for the assessee.”

Learned counsel for the assessee submitted that the physician’s samples were distributed only to doctors and, therefore, the expenditure incurred thereon could not be said to be for advertisement or publicity or sales promotion. He submitted that the purpose of such distribution was to obtain a feedback from the medical profession as to the efficacy of the distributed drugs. As to the first point, we are entirely in agreement with the view taken in the judgment under appeal. Having regard to the fact that these are prescription drugs, the target for any advertisement or publicity or sales promotion thereof could only be the doctors who would prescribe them. The object, we have no doubt, of distribution of the samples of the drugs to the doctors is to make them aware that such drugs are available in the market in relation to the cure of a particular affliction and therefore, to persuade them to prescribe the same in appropriate cases. So doing is, in our view tantamount to publicity and sales promotion. Regarding the submission that the distribution of the physician’s samples of the drugs is meant only for obtaining feedback from the doctors, we should have thought that the assessee would have backed it up by the production of such feedback in the form of filled up questionnaires or letters as it might have received from doctors in the past, if any. It is an eloquent answer to the submission that there has been no such production.

Learned counsel for the assessee drew our attention to the provisions of the Drugs and Magic Remedies (Objectionable Advertisements) Act, 1954. Sec 3 thereof prohibits the publication of any advertisement referring to any drug the terms of which suggest or are calculated to lead to the use of that drug for “(d) the diagnosis, cure, mitigation treatment or prevention of any disease, disorder or condition specified in the Schedule, or any other disease, disorder or condition”. Learned counsel’s submission was that we should not decide in a manner which would lead to the conclusion that the assessee had advertised by means of physician’s samples, drugs contrary to the prohibition under the Drugs and Magic (Objectionable Advertisements) Act 1954. We do not read the prohibition therein as applicable to physician’s samples. What is barred thereby is publication and that is amply clear when

A one refers to the definition of “advertisement” in that Act.

B Learned counsel for the assessee cited the judgment of a division Bench of the Andhra Pradesh High Court in the case of *Commissioner of Income-Tax v. Ampro Food Products*, 215 ITR 904. The judgment, substantially, takes the view the karnataka High Court had taken in the assessee’s case cited above except that it said “Expenditure of the nature which is essential to the running of the business—a bare minimum to carry on the trade—would not fall within the meaning of the three expressions, i.e., advertisement publicity and sales promotion. The other expenditure, incurred under any of the three heads, would be within the mischief of the provisions of sub-section (3A) of sec 37 of the Act and therefore, will have to be scaled down.” The judgment C in *Ampro Food Products* (supra) was followed by the *Andhra Pradesh High Court* in *Commissioner of Income-Tax v. J & J Dechane Laboratories (P) Ltd.*, (1996) 222 ITR 11. This was a case that related to physician’s samples. The High Court said :

D “In the instant case, the assessee claimed expenditure on distribution of physicians, samples under sec 37 general head. In view of the principles settled by this court in the aforesaid decision, if the expenditure falls within the bare minimum it will not be caught by sub-section (3A) of sec 37, but if it is of the nature which is not essential E to the carrying of the business, it will be within the net of sub-section (3A). Physicians’ samples are necessary to ascertain the efficacy of the medicine and to introduce it in the market for circulation and it is only by this method the purpose is achieved. In such cases giving F physicians samples for a reasonable period is essential to the business of manufacture and sales of the medicine. But if a particular medicine has been introduced into the market and its uses are established, giving of free samples could only be as a measure of sales promotion and advertisement and would thus be hit by sub-section (3A). As in G this case there is a finding of the Commissioner (Appeals) and confirmed by the Tribunal that the expenditure was incurred to test the efficacy of the drug, the expenditure would be within the ambit of bare minimum to carry on the business. For these reasons, it has to be held that the expenditure on physicians’ samples distributed to H doctors is outside the scope of sub-section (3A) of section 37 of the Act. Therefore, the appellate authority as well as the Tribunal are right in directing the exclusion of the expenditure on free samples supplied to the doctors in working out disallowance under section 37 (3A) of

the Act.”

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We find it difficult to draw the distinction that the Andhra Pradesh High Court made between expenditure that is essential to the running of the business and other expenditure, all this expenditure being incurred for the same purpose. If all this expenditure on distribution of physician's samples is incurred for the purposes of publicity or sales promotion as we think it is it falls within the scope of Section 37 (3A) of the Act and would be subject to the limitations as to allowability therein contained. Further, it should be noted that in the case of *J & J Dechane Laboratories (P) Ltd.* (supra), the Commissioner (Appeals) and the Tribunal had found as a fact that some expenditure had been incurred to test the efficacy of the concerned drug. There is no such finding in the case before us.

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In the result, we are not persuaded to take a view other than that taken by the High Court. The question relating to physician's samples is therefore, answered in the affirmative and in favour of the Revenue. The appeals are dismissed with costs.

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B.S.

Appeals dismissed.