

IN THE INCOME TAX APPELLATE TRIBUNAL  
“G” Bench, Mumbai  
Before S/Shri B.R. Baskaran (AM) & Amarjit Singh (JM)

I.T.A. No. 10/Mum/2016 (Assessment Year 2009-10)

ACIT, Circle 7(1)1 Room No. 23 Aayakar Bhavan M.K. Road Mumbai-400 020.	Vs.	M/s. Goldman Sachs Assets Management (India) Pvt. Ltd. 951-A, Rational House Appasaheb Marathe Marg Prabhadevi, Mumbai-400025. PAN : AADCG0789J
(Appellant)		(Respondent)

Assessee by	Shri Madhur Agrawal
Department by	Shri V. Vidhyadhar
Date of Hearing	12.10.2017
Date of Pronouncement	25.10.2017

ORDER

Per B.R. Baskaran (AM) :-

The appeal filed by the Revenue is directed against the order dated 30.10.2015 passed by the learned CIT(A)-13, Mumbai and it relates to A.Y. 2009-10.

2. The Revenue is aggrieved by the decision of the learned CIT(A) in deleting the disallowance relating to pre-operative expenses and legal and professional fees paid.

3. The assessee is engaged in the business of undertaking asset management services and investment advisory services. The year under consideration is the first year of operation. The assessee was granted approval by SEBI for commencing Asset Management Services (AMS) on 1.9.2008. However, the approval for commencing advisory services was received on 10.12.2008. The assessee had capitalised all expenses incurred prior to 1.9.2008 as pre-operative expenses and claimed expenses incurred there after as revenue expenditure.

4. The Assessing Officer noticed that the assessee did not commence asset management services during the year under consideration. The Assessing Officer further noticed that the assessee has commenced only advisory services on 10.12.2008. Accordingly the Assessing Officer took the view that the expenses incurred after 10.12.2008 alone can be allowed as revenue expenditure. Accordingly, the Assessing Officer disallowed expenditure incurred by the assessee from 1.9.2008 to 10.12.2008 amounting to ₹ 326.51 lakhs treating the same as pre-operative expenses. The assessee had also paid legal and professional fees of ₹ 237.48 lakhs to two legal firms. Details thereof have been discussed by the Assessing Officer as under:-

5.1 *It is noticed from the submissions filed by the assessee that the assessee company has made following two payments under head Legal & Professional Fees*

Sr. No.	Name of the Party	On account of	Amount (Rs.)
1.	AZB & Partners	Legal Expenses	1,37,63,296
2.	Fried, Frank, Harris Shriver & Jacobson (London) LLP	Legal Expenses	99,85,451
		Total	2,37,48,747

5.2 *The assessee was asked to give the nature of the same. The assessee gave the details of the same vide letter dated 22/12/2011 which is as under:*

- *Legal & Professional charges paid to AZB & Partners are in relation to provision of legal advisory set-vices.*
- *Drafting and review of the statement of additional information and scheme information document for Goldman & Sachs mutt/al fund schemes.*
- *Drafting and review of the mutual fund subscription document, key information memorandum and application documents. Further, assistance in relation to the compliance required for Anti-Money Laundering.*
- *Drafting and review of agreements for appointment of the Fund accountant, registrar and transfer agent and the banker for the mutual fund schemes.*
- *Providing legal opinion on risks associated with the launch of a new*

*mutual funds scheme, research on various mutual fund regulations and other legal advices.*

- *Providing advice on various policies and procedures for all asset management company and preparation of the compliance manual.*
- *Further legal & professional charges paid to Fried, Frank, Harris Shriver & Jacobson (London) LLP is in relation to assistance in drafting offer documents such as statement of additional information and scheme, information document and drafting and reviewing of the scheme distribution agreements of Goldman & Sachs mutual fund schemes.*

5. The Assessing Officer took the view that the above said legal firms have provided services in respect of mutual fund schemes which are yet to be launched. Accordingly he took the view that these expenses cannot be allowed as revenue expenditure, but it should be capitalised. Accordingly the Assessing Officer disallowed claim of legal and professional charges of ₹ 237.48 lakhs treating the same as capital expenditure.

6. In the appellate proceedings, the learned CIT(A) accepted the contentions of the assessee that the date of setting up of business is 1.9.2008 and accordingly deleted the disallowance of ₹ 326.51 lakhs relating to pre-operative expenses.

7. In respect of legal and professional charges of ₹ 237.48 lakhs, the learned CIT(A) noticed that the assessee did not deduct tax on the amount of ₹ 99 lakhs paid to M/s. FFHS&J. Accordingly he issued enhancement notice to the assessee proposing to disallow the above said payment u/s. 40(a)(ia) of the Act. The assessee submitted that TDS has been credited in the Government treasury belatedly on 29.4.2011. Accordingly the assessee agreed for disallowance of amount of ₹ 99 lakhs paid to M/s. FFHS&J during the year under consideration. With regard to remaining amount of ₹ 137 lakhs, the learned CIT(A) took the view that they are revenue in nature. Accordingly he directed the Assessing Officer to delete the disallowance to the extent of ₹ 137

lakhs. Aggrieved by the order passed by the learned CIT(A), the Revenue has filed this appeal before us.

8. We heard the parties and perused the record. First issue relates to disallowance of ₹ 326.51 lakhs relating to pre-operative expenses. Submissions made by the assessee before the learned CIT(A) and decision taken by the learned CIT(A) on this issue are extracted below for the sake of convenience :-

*3.1.2 Appellant's contentions - According to AR, the appellant had received two approvals from SEBI viz, one for ASM (received on 1<sup>st</sup> September 2008) and another one for AS (received on 10<sup>th</sup> December 2008). The expenses incurred by the appellant prior to 1<sup>st</sup> September 2008 amounting to Rs. 7.86 crores had been voluntarily disallowed by it in its computation. The expenses incurred after 10<sup>th</sup> December 2008 were not in dispute, since the appellant not only got approval for AS on that date, but had also commenced provision of AS thereafter. The entire dispute is hence about the expenditure of Rs. 3.26 crores incurred between 1<sup>st</sup> September 2008 and 10<sup>th</sup> December 2008. The AO has taken a very simplistic interpretation of the date of commencement of business stating that the date of grant of approval by the regulator i.e. SEBI was of no consequence and that the date of actual commencement of business was important. On receipt of SEBI's approval on 1<sup>st</sup> September 2008, the appellant had immediately moved a specific application before SEBI on 4<sup>th</sup> September 2008 for launching a mutual fund scheme as part of its AMS activities. The said mutual fund scheme was to be known as Goldman Sachs India Equity Fund (hereinafter referred to as 'GSIEF'). However, before the receipt of SEBI's approval for launching GSIEF, the financial world was rocked on a global level with the collapse of the financial services giant Lehman Brothers. This crisis started around the middle of September 2008 and pushed the global financial markets in turmoil. On this background, the appellant felt that the environment was not conducive for launching a mutual fund scheme. Accordingly, it was after a very long time in August 2011 when the capital markets had stabilized that the appellant felt that it could go ahead with the launching of GSIEF. To this effect, the appellant had made appropriate disclosures in its Directors' reports for FYs 2008-09 and 2009-10, disclosing these facts to its shareholders. It can hence not be said that there was no commencement of business, the fact of the application to SEBI for GSIEF being an important piece of evidence in that direction. Towards this end, it relied on a catena of judgments whose details are as follows.*

1) *Western India Vegetable Products v. CIT [26 ITR 151 (Born)]*

- 2) *CIT v. Saurashtra Cement & Chemical Industries Limited* [91 ITR 170 (Guj)]
- 3) *CIT Vs. Sarabhai Management Corporation Limited* (192 ITR 151 (SC))
- 4) *CWT v. Ramaraju Surgical Cotton Mills Limited* [63 ITR 478 (SC)]
- 5) *Emirates Commercial Bank Limited* [ITA NO 4183/Mum/1985 (Mum)]
- 6) *Hughes Escorts Communications Limited v. JCIT* [106 TTJ 1065 (Del)]
- 7) *JP Morgan Chase Bank N. A. v. ADIT* [ITA no. 4311/Mum/2005]

3.1.2 The AR contended that the 'setting up of a business' had not been defined under Income Tax Act, 1961 (hereinafter referred to as the 'Act'). Generally, the date of setting up of a business is interpreted in the context of readiness to commence business insofar as service companies like the appellant are concerned. This readiness is generally determined on the basis of the date of appointment of key persons and other qualified personnel, the date of grant of regulatory approvals, the date on which the premises for carrying out the business are leased/purchased and the date of occupation of the business premises. According to the AR, the broad ratios of the case laws cited would demonstrate that the appellant's business had indeed been set up. As the appellant's readiness in this regard is evidenced by the commencement of expenditure by way of payment of salaries to all its personnel, payment of lease rent for its office premises, occupation of its office premises and obtaining of the regulatory approval, the actual date on the basis of which determination of pre-operative expenses should take place should be 1<sup>st</sup> September 2008. The AR also underlined the voluntary disallowance of Rs. 7.86 crores of pre-operative expenses, as opposed to the further disallowance of Rs. 3.26 crores made by the AO. He then pleaded for reversal of the entire disallowance made by the AO on this count.

3.2. Decision - I have carefully gone through the submissions of the appellant and the order of the AO. Apart from the case laws already cited in the previous subparagraphs, the AR has also filed the application made for GSIEF, its approval as also the general regulatory approvals for ASM and AS. Before going further, it would be instructive to know the background of the appellant-company. The appellant is a wholly owned subsidiary of Goldman Sachs Asset Management India

*Holding Limited and had applied for approval for commencing business in India during the previous year relevant to the assessment year under consideration. The two principal lines of its activities are AMS and AS. Under AMS, the appellant would typically launch and run mutual funds schemes, while under AS it would offer nonbinding investment advisory services. While AMS envisages actual control over the assets of the clients, AS entails giving of advice to clients which they may or may not follow. It would now become clear that the turmoil caused in the financial markets on a global level in September 2008 onwards would affect AMS far strongly than it would affect AS. To this extent, the commercial decision of the appellant not to launch GSIEF in spite of having requested for and obtained approval for the same appears logical. Equally so, the decision to commence AS forthwith also appears logical. This would be an important factor since it would demonstrate that the appellant was ready to go ahead but was compelled by forces beyond its control to wait for a while. There appears to be merit in the AR's arguments to this extent.*

*3.2.1 Once more, before proceeding further, it would be important to see the kind of financial arrangements the appellant had made. The consolidated Foreign Direct Investment policy of the Department of Industrial Policy and Promotion of Ministry of Commerce of Government of India lays down the norms for non-banking financial companies. In the sphere of asset management, the policy mandates infusion of US \$ 50 million, in case where foreign capital would exceed 75% of the total capital. The policy also lays down that US \$ 7.5 million thereof needs to be brought in upfront, while the balance US \$ 42.5 million could be brought in the following twenty-four months. The relevant extracts of the policy have been placed on the appellate record. Thus, it would be clear that the appellant had ensured injection of funds to the tune of about Rs. 250 crores (at the rough exchange rate of Rs. 50/- per US dollar), out of which about Rs. 38 crores had been brought in upfront. On this background, having put to use this massive capital infusion, the only reason why the actual mutual fund schemes could not be launched by the appellant would be the lack of market response due to the global meltdown, as has been explained by the AR. That in no way can detract from the fact that the appellant had actually set up its business by pouring in capital, leasing premises and hiring qualified persons. In other words, once more, the only reason that no mutual fund could be launched by the appellant was the overall depressed market condition. It in no way indicated the absence of setting up of the business.*

3.2.2 At this stage, it would be instructive to see the nature of expenses claimed as revenue expenses which had been disallowed by the AO as pre-operative expenses. While the overall expenses of the appellant as per the extract of the trial balance as on 9<sup>th</sup> December 2008 totalled Rs. 11.13 crores, the figure for the expenses as on 31<sup>st</sup> August 2008 was Rs. 7.86 crores. The differential amount of Rs. 3.26 crores had been added back by the AO. Out of the expenses of Rs. 11.13 crores as on 9<sup>th</sup> December 2008, the lion's share of Rs. 9.35 crores had been taken up by employee costs. The next large component of Rs. 0.33 crore was taken up by communication, followed by legal and professional expenses of Rs. 0.30 crore and lease rent of Rs. 0.22 crore. In other words, there is merit in the argument of the AR that the business of the appellant had been effectively set up with hiring of qualified personnel, leasing of rented premises etc. In the context of businesses which provide services such as those provided by the appellant, generally the majority of costs pertain to employees' remuneration. Keeping this in mind, on 10<sup>th</sup> December 2008 the appellant clearly had a business which had been set up rather than one which was to be set up.

3.2.3 At this stage, it would be useful to go through certain case laws cited by the appellant. In the case of J. P. Morgan Chase Bank N.A. ADIT (supra), the Hon'ble Mumbai Tribunal had occasion to deal with the expenditure incurred between the dates of grant of regulatory approval and actual commencement of business. In that case, the assessee was a non-resident banking company which had established a branch in India to carry out its banking business. In that context, the Honble Mumbai Tribunal had held as under:

*"There is no dispute about the legal proposition that if the business is set up in all respects and even if the business is not commenced but set up to commence, then the period between the business set up and business commence, the expenditure is to be allowed as revenue expenditure."*

3.2.4 In the case of CWT v. Ramaraju Surgical Cotton Mills Limited (supra), the Hon'ble Supreme Court had occasion to deal with the issue of setting LIP of a unit. It had then observed as under.

*"A unit cannot be said to have been set up unless it is ready to discharge the function for which it is being set up. It is only when the unit has been Put into such a shape that it can start functioning as a business or a manufacturing organization that it*

*can be said that the unit has been set up."*

*It would hence become clear that the appropriate definition of setting up of business would be putting into shape of the said business in such a way that it can start functioning. In other words, actual functioning may be delayed for some reasons - commercial or otherwise - but the expenditure incurred after the setting up of the business shall be treated as revenue expenditure. The Hon'ble Bombay High Court, while deciding the case of Western India Vegetable Products v. CIT (supra) had observed as follows in the context of the interval between the setting up and the commencement of business and the expenses incurred during such an interval.*

*" ... when a business is established and is ready to commence business then it can be said of that business that it is set up. But before it is ready to commence business it is not set up. But there may be an interregnum between a business which is set up and a business which is commenced and all expenses incurred after the setting up of the business and before the commencement of the business, all expense during the interregnum would be permissible deduction .....*"

*The Hon'ble Bombay High Court had very lucidly put forth the proposition that the expenditure incurred during the interregnum — after setting up of the business and prior to commencement thereof — shall be entitled to all permissible business deductions.*

*3.2.5 Admittedly, the above case decisions deal with the issues of regulatory approval in the context of businesses other than AMS or AS. However, there is immense clarity in the above cited decisions insofar as the issues of setting up of a business and the commencement thereof is concerned, all superior judicial authorities having held that expenditure incurred during such period has to be on the revenue account. Respectfully following the ratios contained in the decisions of the aforesaid superior judicial authorities. I have no hesitation in deciding that the expenses of Rs. 3,26,51,038/- disallowed by the AO as pre-operative expenses shall be permissible deduction as business expenditure. Ground no. 1 is accordingly allowed."*

9. We noticed that the learned CIT(A) has allowed the claim of the assessee by following decision rendered by various High Courts including Hon'ble Bombay High Court in the case of Western India Vegetable Products (supra), wherein it has been held that there may be an interregnum between a

business which is set up and business which is commenced. It was further held that all expenses incurred during the interregnum would be allowed as deduction. In the instant case also, the moment the approval from SEBI was received, i.e., on 1.9.2008 for commencement of AMS operation, it can be said that the business has been set up. The approval for advisory services is another activity of the assessee. Hence no fault can be found with the action of the assessee in taking the date of setting up of business as 01-09-2008. Hence all the revenue expenses incurred by the assessee after 1.9.2008 for running business enterprise cannot be treated as Pre-operative expenses and should be allowable as revenue expenditure. Accordingly, we do not find any infirmity in the decision rendered by the learned CIT(A) on this issue. Accordingly, we confirm the same.

10. Next issue relates to disallowance of legal and professional fees. The learned CIT(A) has decided the issue with following observations :

*“5.4 Decision - I have carefully gone through the AO's order and the AR's submissions. The expenditure in question is seen to have been made by way of payments to an Indian legal firm (viz. AZB) and a foreign legal firm (viz. FFHS&J). The services rendered by these two firms were by way of drafting of the mutual fund scheme of the appellant, drafting of the subsequent documents of the said mutual fund, key information memorandum, application documents, scheme information documents, compliance documents required for anti-money laundering, legal opinion on risks associated with the launch of a new mutual fund, research on mutual fund regulations, advice on policies and procedures for asset management companies, preparation of a compliance manual, etc. In other words, it can be concluded that these expenses have clearly been incurred in the context of AMS and not AS. As the AO had already disallowed expenditure incurred by way of AMS as being preoperative in nature, he appears to have extended the same logic and disallowed impugned addition has been made) were in the context of AMS. The AO inferred that the benefit that accrued on account of such advice and services stretched across several years. However, he has lost sight of the fact that he had himself concluded that there was no benefit which accrued to the appellant in the year under consideration. Accordingly, the more appropriate response would have been either to allow or to disallow the expenditure claimed; but there is certainly no scope for capitalizing it. In any case, as has been held by*

*me while deciding ground nos. 1 and 2 earlier in this order, the AMS business had actually been set up as on 1st September 2008. As such all the legal and professional expenses incurred by way of payment to AZB and FFHS&J too have to be allowed. As such, these expenses are allowable as deduction. However, it is also clear from the reply of the appellant to the notice of enhancement that the appellant had deposited tax on payment of legal fees of Rs. 0.99 crore to FFHS&J only during April 2011 i.e. more than two years after the end of the financial year relevant to the assessment year under consideration. There can hence be no doubt about the disallowance of the said amount in terms of provisions of section 40(a)(ia) of the Act. In all fairness, the appellant too has admitted to the correctness of this disallowance. Accordingly, the legal fees of Rs. 99,85,451/- paid to FFHS&J are disallowed and directed to be added back. The balance legal fees of Rs. 1.37 crore paid to AZB are to be allowed and are not to be subjected to any capitalization. The AO is directed accordingly. Ground no. 3 is hence partly allowed.”*

11. Since we have already held that the business has been set up on 1.9.2008 and further expenses paid to legal firm were related to drafting of mutual fund schemes etc, which are connected with the routine business activities, we are of the view that the learned CIT(A) has rightly held the same to be revenue in nature. Accordingly, we uphold the order passed by the learned CIT(A) on this issue also.

12. In the result, appeal filed by the Revenue is dismissed.

Order has been pronounced in the Court on 25.10.2017.

Sd/-  
(AMRAJIT SINGH)  
JUDICIAL MEMBER

Sd/-  
(B.R.BASKARAN)  
ACCOUNTANT MEMBER

Mumbai; Dated : 25/10/2017

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent
3. The CIT(A)
4. CIT
5. DR, ITAT, Mumbai

*M/s. Goldman Sachs Assets  
Management (India) Pvt. Ltd.*

6. Guard File.

//True Copy//

PS

BY ORDER,

(Asstt. Registrar/Sr. PS)  
ITAT, Mumbai