

INCOME TAX APPELLATE TRIBUNAL  
DELHI BENCH "A": NEW DELHI  
BEFORE SHRI H.S.SIDHU, JUDICIAL MEMBER  
AND  
SHRI PRASHANT MAHARISHI, ACCOUNTANT MEMBER

ITA No. 5877/Del/2015  
(Assessment Year: 2010-11)

DCIT, Circle-13(1), CR Building, New Delhi	Vs.	Jatra Ruchi Cosmetics (india) Pvt. Ltd, Shop No. 1 to 4, World Trade Centre, Barakhamba Road, New Delhi PAN: AACCCJ2047F
(Appellant)		(Respondent)

Revenue by :	Shri Janardan Das, Sr. DR
Assessee by:	None
Date of Hearing	18/02/2019
Date of pronouncement	20/02/2019

O R D E R

PER PRASHANT MAHARISHI, A. M.

1. This is an appeal filed Id AO against the order of the Id CIT(A)- 5, New Delhi dated 28.08.2015 for the Assessment Year 2010-11.
2. The revenue has raised the following grounds of appeal:-
  - “1. *That on the facts and in the circumstances of the case and in law, the Id CIT(A) has erred in deleting the disallowance of Rs. 2,82,63,076/- made by the AO on account of pre-operative expenses.*
  2. *That the order of the Id CIT(A) is erroneous and is not tenable on facts and in law.*
  3. *That the grounds of appeal are without to each other.”*
3. The brief facts of the case shows that the assessee is a company engaged in the business of trading in cosmetics and skin care products. It filed its return of income declaring a loss of Rs. 27859204/-. The Id AO noted that the assessee company was incorporated on 27.07.2009 and has not done any business activity except earning of interest income on fixed deposits.

Therefore, the Id AO show caused the assessee that why not the business loss may be disallowed as there is no business set up by assessee. The assessee explained with enaggenemnt of employees, office space, training and other programme that assessee has already set up the business and therefore, it is eligible for allowance of the loss. The Id AO rejected the contention of the assessee and held that the expenses of Rs. 28263076/- incurred by the assessee are preoperative expenses and are disallowable. Accordingly, the order u/s 143(3) of the Act was passed on 04.03.2013 determining total income of the assessee of Rs. 403870/- against the return loss of Rs. 27859204/-.

4. The assessee preferred an appeal before the Id CIT(A) who allowed the claim of the assessee holding that the assessee has set up its business and therefore, the assessee is eligible for carry forward of the losses. He further held that since the business was set up from the date of incorporation and all the activities for undertaking business are fulfilled, he allowed the deduction of above expenditure. The Id AO aggrieved with the order of the Id CIT(A) has preferred this appeal.
5. The Id Sr. DR stated that the assessee has merely incorporated itself and has not carried out any activity, therefore, it is business is not set up. He further submitted that the assessee is a private limited company and therefore, it is incorporation does not have any impact of setting up of the business. He stated that the Id CIT(A) has grossly erred in holding that the business of assessee is setting up from the date of incorporation. It has only earned interest on Fixed deposit which is chargeable to tax uner the head income from other sources.
6. Despite notice none appeared on behalf of the assessee and therefore, this appeal is decided on the facts of the case available on record.
7. We have carefully considered the rival contentions of the Id Sr. DR and also perused the orders of the lower authorities. The Id CIT(A) has decided this issued from para No. 3.1 to 4.6 as under:-

3.1 Ground no. 1 is general in nature and does not require any separate adjudication. The second ground contests the finding of the AO that the business was not set up and therefore, the expenditure was preoperative in nature. On this ground, the submission of the Ld ARs is that this is the first year of operation of the company and therefore, certain activities were undertaken in order to set up and commence the business operations, which related to the direct selling of cosmetics and skin care products manufactured by the joint venture partner B.V. Vorwerk and Co. The details of the activities undertaken during the year are mentioned in the written submissions along with the case relied upon which are for sake of convenience reproduced herein under:

1 The Appellant is engaged in the business of direct selling of cosmetics and skincare products. It is a Joint Venture (JV) between Jafra Holding Company B.V., Vorwerk & Co., and Ruchi Multitrade Private Limited having the following equity participation:

<b>S. No.</b>	<b>Name of the JV Partner</b>	<b>Equity participation</b>
1.	Jafra Holding Company B. V./ Vorwerk& Co.	70%
2	Ruchi Multitrade Private Limited/ Dinesh Shakra	30%

2 The Appellant was incorporated on 27 July 2009 and undertook the following activities in India to set up and carry on its business operations during the year under consideration:

2.1 Appointment of key personnel - On the date of incorporation of the Appellant, Mr. Harish Singla and Mr. Neeraj Ojha were deputed to the position of Director and General Manager respectively to assume the following responsibilities:

- a. Mr. Harish Singla had been working on the plans and processes for administration and compliance works even before the incorporation of the Appellant. Such plans and processes, such as commission model, market survey, planned inventory etc. were required to be instilled in the systems of the Appellant immediately upon its incorporation. Having a vast experience of more than 11 years in the field of Sales and Marketing, Mr. Singla assumed responsibility as a Director with the Appellant immediately upon its incorporation i.e., 27 July 2009 and was deputed to work with the Appellant from the said date.
- b. Mr. Neeraj Ojha, who was working on the plans and processes prior to joining the Appellant, was responsible for creating accounting and financial systems for day-to-day business and ongoing operations of the Appellant. He was deputed to the position of General Manager of the Appellant on the date of incorporation of the Appellant.

*Mr. Johan Wicklund, who was an expert in the line of business of the Appellant, was nominated by one of the JV partners of the Appellant for creating business processes and systems for sales and marketing activities of the Appellant. Mr. Wicklund started working on the marketing plans and creating systems much before Jafra Ruchi India was incorporated and such systems were implemented immediately after its incorporation. However, owing to delay in obtaining regulatory approval, Mr. Wicklund could formally join the Appellant as an employee director on 29 September 2009.*

*As on 31 March 2010, the Appellant had a total of 14 employees on its payroll who were appointed on as and when need basis based upon the growth of the business of the Appellant in terms of interest of its customers.*

- 2.2 Office Space - The Appellant carried out its business from Its office located at 4 Statesman House, Barakhamba Road, New Delhi with effect from its date of incorporation. The office was taken on lease by Ruchi Multi trade India Private Limited ('Ruchi Multitrade'), one of the shareholders of the Appellant with effect from 19 July 2009. However, the premises were occupied by the Appellant from the date of its incorporation itself i.e., with effect from 27 July 2009. In order to secure an office space, Ruchi Multitrade entered into the rent agreement for a period starting from 19 July 2009 till 31 October 2009. Thereafter, the Appellant renewed the rent agreement in its name. The Appellant reimbursed the amount of rent paid by Ruchi Multitrade to the landlord for the period July to October that was incurred by Ruchi Multitrade on behalf of the Appellant.*
- 2.3 Consultants Agreement and Registration Form: As stated above, the director of the Appellant was already working on the plans and processes of the Appellant even before it was incorporated. The Appellant put in place Independent Jafra Consultant Agreement ('Agreement') and Jafra Business Consultant Registration Form ('Registration Form') immediately upon incorporation in order to ensure that as and when a Consultant joins the business of the Appellant, the agreement is entered into and the products can be sold by the Appellant. A copy of the standard Agreement is enclosed herewith as Annexure 1 for your reference. Further, the commission model of the Appellant and payable to the consultants was also in place along with the Agreement.*
- 2.4 Training Programs - The Appellant carried out training programs for prospective Consultants to equip them with appropriate knowledge about the products, information and details of the brand and its global presence and basic systems and processes to be undertaken in direct selling business. In this regard, the Appellant even hired a professional trainer in order to equip its existing and prospective sales team with more traits to approach potential customers.*

3 In the assessment order, the Ld. AO has alleged that the Appellant has not carried out any business activity during the year under consideration and therefore, business of the Appellant cannot be said to have been set up. Accordingly, expenditure incurred prior to the date of setting up of business could not be allowed. The Ld. AO has arrived at this conclusion without appreciating the business model of the Appellant and simply relied upon certain case laws. Thus, the conclusion of the Ld. AO is totally misplaced.

4 As the date of set-up has not been defined in the Act, the Appellant wishes to bring to your attention the principles of the date of set up as held by Courts. Section 3 of the Act defines "previous year" and it says that the first previous year commences from the date of "setting up of the business". It is well settled that there is a difference between the date of setting up of a business and the date of commencement of the business. This distinction has been brought out by the Bombay High Court in *Western India Vegetable Products Ltd. v. CIT* [1954] 26 ITR 151 by observing that when a business is established and is ready to commence business then it can be said that it has been "set up" but before it is ready to commence business it is not "set up". There may be an interregnum between the date of setting up of the business and the date of actual commencement of the business but under the Act all expenses incurred after the date of setting up are allowed as a deduction under section 28. This decision has been applied by the Hon'ble Jurisdictional Delhi High Court in the case of *CIT v. Hughes Escorts Communications Ltd.* [2007] 165 Taxman 318 wherein it has been held that where the business has been set up, though the same has not been commenced, the expenditure incurred after the date of setting up has to be allowed as a deduction. It may thus be seen that the question when a business may be said to have been set up is dependent on the facts of each case and largely on the nature of the business proposed to be undertaken.

5. The Appellant wishes to submit that all the essential activities that are required for its business to commence. The essential activities are as under:

- The Appellant hired key employees required for rendering the essential business activities.
- The Appellant hired office space for undertaking its business activities.
- Agreement was finalized and put in place by the Appellant in order to ensure that as and when a Consultant joins the business of the Appellant, the agreement is entered into and the products can be sold by the Appellant.
- Trainings were rendered to resellers at appropriate time intervals as a marketing as well as strategy for explaining the business to the resellers.

Therefore, the Appellant was ready to deliver the essential activities required to run its business which is selling its products to customers directly. Thus from

*the above facts, it is established that the business of the assessee had been set up immediately upon its incorporation.*

6. *In this regard, the Appellant would like to place reliance on the recent decision of the Hon'ble jurisdictional High Court in the case of Care four WC & C India (P.) Ltd. v. Deputy Commissioner of Income-tax[2015] 53 taxmann.com 289 (Delhi). Briefly, the facts of the case are that the assessee was incorporated on September 2007 to carry on trading activities which primarily included wholesale trading of all kinds of consumer goods, durables, articles and products. During the relevant previous year, the assessee acquired leased office premises and opened a bank A/c in October 2007. Further, the assessee incurred routine business expenses such as legal and professional expenses, travel and conveyance, meeting and conference, salary and wages etc. Further, the assessee also employed key employees such as IT director, FMCG-director, Merchandise Director, Finance Director, Accountants, other supporting staff etc. capable of rendering business development, marketing and financial support activities in relation to the products proposed to be traded by the assessee. In view of these facts, the assessee claimed that its business was set up from the date of incorporation and its expenses to be allowed as business expenses during the relevant assessment year.*

*The assessing officer, disallowed the entire expenditure claimed by the assessee holding that since no business activities have been carried out, no business can be said to have been set up.*

*The Hon'ble Jurisdictional High Court of Delhi, after taking into consideration various other judgments including that of the Hon'ble Supreme Court of India concluded that to set up a business, the following activities become relevant:*

*Preparation of a business plan; establishment of a business premises; research into the likely markets or profitability of the business; acquiring assets for use in the business; registration as an entity and under the local laws, etc.' The said list of activities is not exhaustive and facts of each case need to be considered. Indeed purchase of goods would amount to commencement of business, but before the said act, spade work and efforts to commence have to be undertaken. A trader before actual purchase would possibly interact and negotiate with manufacturers, landlords, conduct due diligence to identify prospective customers, spread awareness, etc. These are all integral part and parcel of the business of a trader. The said activities continue even post first sale/purchase. When first steps are taken by a trader, the business is set up, commencement of purchase and then sales is post set up*

*The Hon'ble Jurisdictional High Court of Delhi noticed that the company before its incorporation the assessee had been in correspondence with few well-known companies. Immediately upon its incorporation, the assessee took office premises on rent, opened a bank account and hired employees. /As per the Hon'ble High Court,the aforesaid*

activities demonstrated setting up of the business by the assessee and depict a dear commitment of commencement of the business. The High Court held that, nothing barred or prevented the assessee from making first purchases, but the fact that the assessee wanted to commence actual trading after negotiations with several parties, would not postpone the date when the business was set up. Thus the High Court held based on the above facts, the first activity essential for conducting business is fulfilled and therefore, business of the assessee can be considered to be set up. (Copy of the decision has been enclosed as Annexure 2)

#### **Applicability to the Appellant**

In the case of the Appellant, the key activities like hiring of key employees, having a standard Agreement in place to be undertaken with the consultants as and when they join the Appellant, taking office on lease, rendering trainings to consultants, expenses on marketing and sales promotion had been done by the Appellant immediately upon its incorporation. Directors of the Appellant were involved in conducting meetings with prospective clients/ customers in order to secure business for the Appellant. Taking the principles laid down by the Hon'ble Delhi High Court in the aforesaid case, it can be held that the activities undertaken by the Appellant, demonstrate that business of the Appellant was set up upon its incorporation date.

- 7 The Jurisdictional Tribunal in case Whirlpool of India Ltd.<sup>114</sup> TTH 211h held that where the assessee undertook primary activities such as having an office space, branch and regional managers and staff, computers installed for carrying business, in order to carry out activities in accordance with the object clause of the Memorandum of Association, it was held that the business had been set up and expenditure will be allowable. (Copy of the decision enclosed as Annexure 3).

#### **Applicability to the Appellant**

In the instant case, the Appellant had hired the key employees, acquired office premises, had Agreement and commission model in place and started conducting meetings from the very stage of its incorporation. Further, employees were being hired as per the requirement of the Appellant on as and when need basis. This shows that the business of the Appellant was set up upon its incorporation date and accordingly, expenses incurred for conducting business are allowable under the Act.

- 8 The Jurisdictional Hon'ble High court of Delhi in case Sauer Danfoss (P.) Ltd., [2012] 22 taxmann.com 251 (Delhi) held that when it had premises on lease, opened its bank account then it can be said to be set up of its business and was ready to commence. There is no dispute to the well settled legal proposition at that point of time, the assessee is in a complete state of readiness to undertake its activity, it can be said that it has set up its business, the actual commencement of business may be at a later date. The trading business of the assessee was ready to commence upon set up of requisite

infrastructure i.e. acquisition of place of business, commencement of hiring of suitable personnel, identifying clients. (Copy of the decision has been enclosed as Annexure 4).

**Applicability to the Appellant**

In the case of the Appellant, the appellant had the Agreement in place, office space, hiring of employees etc. Therefore, the facts of the aforesaid case squarely apply to the Appellant and accordingly, it is submitted that the business of the Appellant was set up upon its incorporation date.

9 The Jurisdictional Delhi High Court in the case of E. Funds International India, [2007] 162 TAXMAN 1 (DELHI), wherein it was held that the assessee being engaged in the software industry might not have earned revenue during the relevant previous year, the fact could not be denied that assessee had taken all steps necessary to obtain business including efforts for marketing itself showed that assessee had commenced business in relevant previous year. Therefore, Assessing Officer was not justified in disallowing assessee's claim of loss in said business on ground that assessee had not commenced business in relevant previous year. (Copy has been enclosed as Annexure 5).

10 The view taken in the decision of E.Funds International India has been endorsed by In the case of CIT vs. Aspentech India (P.) Ltd\ [2010] 157 TAXMAN 25 (DELHI), the Jurisdictional Delhi High Court has held that the assessee did not earn revenue during the year under consideration and had claimed expenses incurred for conduct of business in the normal course. However, the efforts made during the year under consideration resulted into revenue in the succeeding assessment year and therefore, it can be held that expenses incurred during the year under consideration were towards achieving business objectives and therefore, allowable. (Copy has been enclosed as Annexure 6).

**Applicability to the Appellant**

In the facts of the case of the Appellant, the Appellant also earned revenue of more than Rs. 2 crores in the very subsequent year for the efforts made during the year under consideration in the subsequent years. A copy of the extract of the P&L A/c for AY 2011-12 has been enclosed as Annexure 7 for your reference. Therefore, based on the view taken by the Hon'ble jurisdictional High Court of Delhi in the aforesaid case laws, the business of the Appellant should be considered to have been set up.

11 The Ld. AO, while disallowing the business expenses claimed by the Appellant, placed reliance on certain judicial precedents of various courts. In this regard, the Appellant wishes to submit that the reliance placed by the Ld. AO on those decisions is misplaced as they are on different set of facts and principles and thus cannot be applied in the present case. The Appellant submits below the facts and issues dealt with in these decisions and the distinguishing facts from the Appellant's case:

S. No	Judicial Precedent relied upon by Ld. AO	Facts as per decision cited by the Id. AO	Facts of the Appellant
1	<p>Hotel Banjara Ltd. vs. ITO (1986) (16 ITD 692, 701 (Hyd)= Taxation 82 (4)-112)</p> <p>-----</p>	<p>In this case, the assessee is a hotel that was ready to commence business and undertook its trial run by inviting specific guests three months before the date it was opened for public for actual business operations. The Assessing Officer disallowed the expenses incurred between the date of setting up and the date on which the hotel was opened for general public for actual business purposes, holding that the hotel was not ready to commence business even on the date of trial run. However, the CIT (A) and the Tribunal held in favour of the assessee and allowed expenses from the date of trial run of the business.</p>	<p>The Appellant was ready to commence business from the date of its incorporation. In the instant case, the Appellant had taken on lease an office space to operate its business and also started the marketing activities for creating customers and securing orders from them.</p>
		<p>Distinguishing factor</p> <p>In the case of the Appellant, it was ready to commence business from the date of its incorporation. Whereas in the case law cited by the Ld. AO, as held by the Hon'ble Hyderabad Tribunal, the hotel was ready to commence business from the date of its trial run.</p> <p>Therefore, the case law cited by the Ld. AO is actually, in favour of the Appellant and against the Revenue.</p>	
2	<p>CIT vs. Sponge Iron India Ltd. (1993) (201 ITR 770) (AP)</p>	<p>During the assessment proceedings, the assessee claimed deduction under the head 'Exploration and general administration'. Later on, it came to the notice of the assessing officer that assessee had claimed expenditure without its business being ready to commence since the essential activity for setting up of business the assessee was production and exploration of</p>	<p>The Appellant had business of direct selling of cosmetic products. It had been working on creating business processes and systems in order to accomplish its business objectives of direct selling. The Appellant had taken on lease office space to operate its business and also started marketing activities for creating</p>

	<p>raw materials through a machine. The installation of such machinery was complete over a period of three years after the incorporation of the assessee.</p> <p>The assessing officer therefore, disallowed expenses from the date of incorporation to the date on which the machinery was installed holding those as preoperative expenses not allowable.</p>	customers and securing orders from them.
	<p>Distinguishing factor</p> <p>The machinery was a critical pre-requisite for the \ starting up of the business of exploration in the decision cited by the Ld. AO, whereas in the case of the Appellant, the Appellant is in the business of direct selling and no use of machinery is relevant for the business of the Assessee.</p> <p>Therefore, the facts in the case law cited by the Ld. AO are different and distinguishable from the facts of the Appellant.</p>	
3. CIT vs. Sa Sons (P.) Ltd. (1973) (90 ITR 318) (Guj.)	<p>In the decision, new business of assessee was of manufacturing scientific instrument and communication equipment and it could not be said to be ready to discharge the function until the machinery necessary for the purpose of manufacture was installed.</p>	<p>The Appellant business was set up from the day of its incorporation as the required work necessary for the purpose was completed during the preoperative period. The Appellant had taken on lease an office space to operate its business and also started the marketing activities for creating customers and securing orders from them</p>
	<p>Distinguishing factor:</p> <p>The machinery was a critical pre-requisite for the starting up of the business in the case cited by the Ld. AO, whereas in the case of the Appellant, the Appellant is in the business of direct selling and no use of machinery is not relevant for the business of the Assessee.</p> <p>Therefore, the facts in the case law cited by the Ld. AO are different and distinguishable from the facts of the</p>	

		appellant	
4.	CIT Vs. Industrial Solvents & Chemicals Pvt.   Ltd. (1979) (119ITR 608 (Bom))	In this case, expenses claimed by respondent are on the basis of experiments before the commencement of the business and not for carrying on actual business activities. The marketable products were manufactured by the assessee only in a subsequent assessment year. It was held that business can be said to be commenced post the manufacture of marketable products.	In the present case, the Appellant is into the business of direct selling of products which are already being sold outside India. Further, expenses incurred by the Appellant are for the purpose of running its business and not for undertaking any sort of trial / experimenting activities.
		<p>Distinguishing factor</p> <p>In the case cited by the Ld. AO, expenses are related to trials and not for carrying on the business. As opposed to this, expenses incurred by the Appellant are wholly and exclusively for day-to-day business activities in order to inculcate new customers and secure orders from them.</p> <p>Therefore, the facts in the case law cited by the Ld. AO are different and distinguishable from the facts of the Appellant.</p>	
5.	Saurashtra Cement & Chemical Industries Limited Vs. Commissioner of Income-tax (159 ITR 624)	In this case, it has been held that business would be considered to have been set up from the date on which the first activity essential for the business of the Company has been undertaken.	The Appellant was ready to commence business from the date of its incorporation. In the instant case, the Appellant had taken on lease an office space to operate its business and also started marketing activities for creating customers and securing orders from them.
		<p>Distinguishing factor</p> <p>In the case cited by the Ld. AO, expenses have been claimed and allowed from the date in which the first activity essential for business of the company has been undertaken. In the case of the appellant, the expenses claimed are from the date of hiring of key/ employees/ directors who are responsible for marketing the products which is an essential business activity for the appellant.</p> <p>Therefore, the case law cited by the Id AO is actually in</p>	

		favour of the appellant and against the revenue.	
6.	Ramaraju Surgical Cotton Mills Ltd. Vs. Commissioner of Wealth-tax (159 ITR 624)	The case law referred to by the Ld. AO refers to computation of wealth of the assessee and deductions to be taken in a particular year.	The Appellant has been assessed under the provisions of the Income tax Act, 1961.
		Distinguishing factor The case law cited by the Id AO is in context of wealth tax and therefore, would not be applicable to the appellant's case.	

*As can be seen above, the case laws cited by the Ld. AO are based on a completely different set of facts and the same does not apply to the facts of the Appellant. In fact, in a couple of decisions cited by the Ld. AO, the facts are in favour of the Appellant. In the case of the Appellant, the business was set up from the date of its incorporation. The Appellant hired key employees, had in place the standard Agreement and the commission model. Further, the Appellant had taken on lease an office space to operate its business and also started the marketing activities for identifying customers and securing orders from them. Accordingly, the condition for undertaking essential activity for set up of business of the Appellant has been fulfilled and therefore, the business of the Appellant shall be considered to have been set up.*

12 *After referring to the cases of the jurisdictional High Court on identical facts and distinguishing the case laws cited by the Ld. AO, the Appellant wishes to place reliance on the following additional decisions wherein it has been held that where the essential activities of carrying on business are fulfilled, the business should be considered to have been set up:*

a) *Hon'ble Supreme Court of India in CIT v. Sarabhai Management Corporation Ltd. [1991] 192 ITR 151 (SC) held that when the respondent was in a position to offer services and paid salaries to employees, expenditure on like repairs, legal and stationery charges, printing, stationery and conveyance charges, the business is said to set up and expenditure is allowable while computing income for business and profession. (Copy has been enclosed as Annexure 8)*

**Applicability to the Appellant**

*In the case of the Appellant, it was ready to secure orders and deliver goods to its customer as soon as the customer decides to join the direct selling business of the Appellant. Accordingly, business of the Appellant should be said to have been set up upon the date of its incorporation.*

b) *Hon'ble Gujarat High Court in the case of CIT vs Western India Seafoods (P) Ltd 199 ITR 777 held that assessee business of processing of marine products for which fish and other marine products are required, can be said to set up when actual infrastructure required for running the business is available and all revenue expenditure incurred in relation will be allowable as deduction under section 37 even if collection of fish started on later stage and observed as under:*

*"For setting up of business of processing marine products, the assessee during the assessment year in question had to make all preparations and had also to provide on spot, necessary infrastructure. Even conceding that entering into advance contracts with fishermen for collection offish during the monsoon season might not be taken as first step towards setting up of business, at least from 15-8-1970 when the assessee acquired godown where the processing of marine products could start when fish became available after monsoon, it could be said that that was the starting point of setting up of business of processing marine products. Actual arrival offish later on would not postpone the setting up of such business. The Tribunal was, therefore, right in concurring with the AAC's view that expenditure incurred by the assessee after 15-8-1970 and before 6-10- 1970 when collection offish was to actually start, could be treated as business expenditure and would get covered under section 37."*

*A copy of the decision has been enclosed as Annexure 9).*

#### **Applicability to the Appellant**

*In the case of the Appellant, immediately after its incorporation it started approaching potential customers and incur marketing and training costs for obtaining business from the market. The Appellant hired key employees, had in place the standard Agreement and had the commission model in place. Therefore, applying the principles of the above case law, the business of the Appellant is considered to have been set up.*

*c) In the case of Accor Radhakrishna Corporate Services (P.) Ltd. vs. JCIT, [2007] (13 SQT 652) (Mumbai ITAT) assessee-company engaged in business of providing services of luncheon voucher. The assessee- company had appointed various senior executives and salaries were also paid. The assessee had also acquired office premises and invested amount on computer system for purpose of business. The tribunal observed that where a business is established and is ready to be commenced, it can be said that business is set-up and further that ail expenses of an assessee are allowable as a deduction from the time the business is set-up. It is possible that there is a time gap between the setup of business and the commencement of business, but expenses are allowable as soon as the business is set-up. In the instant case, the business of the assessee had been set-up and had also commenced during the previous year. The words 'ready to commence' would not necessarily mean that all the integrated activities are fully carried out and/or fully completed.(Copy of the decision has been enclosed as Annexure 10).*

#### **Applicability to the Appellant**

*The Appellant was ready to commence its business from the date of incorporation. It had key employees / directors and a standard Agreement to be entered into with customers, an office space and workstations etc. which is required for an efficient conduct of business of the Appellant. Accordingly, based on the aforesaid judgement, it can be held that the business of the Appellant was set up upon the date of its incorporation.*

13 *As can be seen from the above, the principles laid down by the decisions cited by the Appellant equally apply in the case of the Appellant. The Appellant hired key employees*

and had the standard Agreement in place to be used at the time of entering into an agreement with the customers. The Appellant has appointed executives and staff during the year under consideration as and when required and paid salaries to them. Further, the Appellant had acquired office premises and paid rent on the same from the date of its incorporation. In fact, the Appellant was ready to accomplish its business objectives as per its Charter documents. The Appellant rendered trainings to resellers, incurred expenses on marketing and sales promotion etc. The directors of the Appellant started conducting meetings with the prospective customers in order to secure business. Overall, the infrastructure and the workforce coupled together was capable enough of rendering business development, marketing and financial support activities in relation to the direct selling business and products of the Appellant. Therefore, the essential activities for conducting business have been fulfilled. Accordingly, based on the facts of the Appellant and in light of the judicial precedents including those of the Hon'ble Supreme Court and the Jurisdictional High Court, it is submitted that the business of the Appellant should be considered to have been set up.

- 14 Based on the above discussions, the Appellant has prayed to your Honour to consider the business of the Appellant as being set up and accordingly the disallowances made by the Ld. AO treating the entire expenditure of the Appellant as pre-operative expenses be directed to be deleted.

3.1.1 During the appellate proceedings held on 11.08.2015, the appellant was requested to substantiate the expenditure incurred with certain additional details such as the name, designation, job profile and date of joining of employees, details of professional and consultancy expenses alongwith the TDS compliances thereon. This information was furnished during the hearing held on 21.08.2015 and is reproduced herein under:

1. List of employees as on 31 March 2010

We would like to mention that as on 31 March 2010, the Appellant had 14 employees on its payrolls. A list of employees including their names, designation, job profile and date of joining are enclosed herewith as Annexure I.

S.No.	Name of employee	Designation	Job Profile	Date of Joining
1	Harish Singla	Director	Incharge of overall vendor management function, customer service, accounting and finance	27-Jul-09
2	Niraj Ojha	General Manager - Services	Creation, operation and maintenance of customer service, accounting and	27-Jul-09
3	Ritika K Chowdhry	Executive Assistant	Person responsible for attending calls and accepting mailers and other	1-Aug-09

4	Johan Wicklund	Director	Creation of business processes and systems for enabling and enhancing the sales and marketing process of the Appellant	29-Sep-09 (formally appointed on this date, working with the Appellant)
5	Anjali Datta	Marketing Manager	Involved in marketing of products traded by the Appellant	30-Sep-09
6	Priya Bhandari	General Manager - Training	Managing and supervising the training team involved in training the	26-Oct-09
7	Vyjayanthi Veeraraghavan	Brand & Communication	Reviewing the designing and branding of the products as per Jafra	4-Nov-09

8	Rohit Ahuja	Accounts	Involved In maintenance of accounts and other Secretarial work of the	27-Nov-09
9	Ritu Singh	General Manager - Sales	Involved in planning and managing of sales and finding out ways on how to	5-Jan-10
10	Rishi Kapoor	Training Incharge	Involved in training the consultants and imparting information about the	10-Jan-10
11	Malvika Garg	Training Incharge	Involved in training the consultants and imparting information about the	1-Feb-10
12	Inderjit Kaur	Training	Involved in training the consultants and	1-Feb-10
13	Arun Girotra	Senior Manager - Logistics	Maintenance of logistics support to the Appellant such as maintenance of stock through imports, delivery of products	4-Feb-10
14	Anil Sharma	IT Officer	Support for Information Technology (IT) related activities	2-Mar-10

4. I have given careful consideration to the facts emerging out of the assessment as well as appellate proceedings and the detailed submissions made. The appellant company was incorporated on 27.07.2009 as a joint venture between the Dutch holding company M/s BV Vorwerk & Co. (70%) and Ruchi Multitrade Pvt. Ltd. (30%). Since this was the first year of business operations, there was no direct selling during the year under consideration and the appellant company engaged itself in setting up of the office premises, hiring of management personnel including the employee director nominated by the J.V Partner of the appellant and other miscellaneous activities preparatory to the actual business of direct selling of cosmetic and pharma products. Since the business model involved consultants who would directly sell the products of the appellant company, the appellant put into place the consultant's agreement and registration form as also finalized the commission payable to the consultants. The appellant also hired a professional trainer in order to train existing and prospective sales personal regarding the processes to be undertaken in direct

*selling business. Very often, there could be a time difference or interval between the date of setting up of a business and the date of actual commencement of the business but what has to be assessed as business income u/s 28 of the Income Tax Act and consequently expenses to be allowed u/s 37 follow from the date of setting up of the business. Therefore, even though the actual business operations may not have commenced, when looked at from the commercial point of view, that is, when no trading has taken place, the expenses incurred still have to be allowed after the date of the setting up of the business, as has happened in the case of the appellant. It was so held by the Bombay High Court in the case of Western India Vegetable Products Ltd. (26 ITR 151). According to the Bombay High Court, the previous year of the business commences only when it is set up and in that previous year, the expenses incurred can be claimed as permissible deductions. This decision had been followed by the large number of other decisions including the Delhi High Court decisions in the case of LG Electronics (India) Ltd (149 Taxman 166) and Hughes Escorts Communication Ltd. (165 Taxman 318)*

*4.1 The facts of the appellant case are similar to the facts before the Delhi High Court in the case of Carefour WC & C India (P) Ltd. vs. Deputy Commissioner of Income tax [2015] 53 taxmann.com 289 (Delhi). Briefly, the facts of the case are that the assessee was incorporated on September 2007 to carry on trading activities which primarily included wholesale trading of all kinds of consumer goods, durables, articles and products. During the relevant previous year, the assessee acquired leased office premises and opened a bank account in October 2007. Further, the assessee incurred routine business expenses such as legal and professional expenses, travel and conveyance, meeting and conference, salary and wages etc. Further, the assessee also employed key employees such as IT director, FMCG-director, Merchandise Director, Finance Director, Accountants, other supporting staff etc. capable of rendering business development, marketing and financial support activities in relation to the products proposes to be traded by the assessee. In view of these facts, the assessee claimed that its business was set up from the date of incorporation and its expenses to be allowed as business expenses during the relevant AY. The AO, disallowed the entire expenditure claimed by the assessee holding that since no business activities have been carried out, no business can be said to have been set up. The Hon'ble Jurisdictional High Court of Delhi, after taking into consideration various other judgements including that of the Hon'ble Supreme Court of India concluded that to set up a business, the following activities become relevant:*

*"Preparation of a business plan; establishment of a business premises; research into the likely markets or profitability of the business;*

*acquiring assets for use in the business; registration as an entity and under the local laws, etc. The said list of activities is not exhaustive and facts of each case need to be considered. Indeed purchase of goods would amount to commencement of business, but before the said act, spade work and efforts to commence have to be undertaken. A trader before actual purchase would possibly interact and negotiate with manufacturers, landlords, conduct due diligence to identify prospective customers, spread awareness, etc. These are all integral part and parcel of the business of a trader. The said activities continue even post first sale/purchase. When first steps are taken by a trader, the business is set up, commencement of purchase and then sales is post set up."*

4.2 *The Jurisdictional Tribunal in the case of Whirlpool of India Ltd. (114 TTJ 211) held that where the assessee undertook primary activities such as having an office space, branch and regional managers and staff, computers installed for carrying business, in order to carry out activities in accordance with the object clause of the Memorandum of Association, it could be said that the business had been set up and expenditure will become allowable.*

4.3 *The Jurisdictional Hon'ble High Court of Delhi in case Sauer Danfoss (P). Ltd.,[2012] 22 taxmann.com 251 (Delhi) held that when it had taken premises on lease, opened its bank account then it can said to be set up of its business and was ready to commence. There is no dispute to the well settled legal proposition at that point of time, the assessee is in a complete state of readiness to undertake its activity, it can be said that it had set up its business; although the actual commencement of business may be at a later date. The trading business of the assessee was ready to commence upon set up of requisite infrastructure i.e. acquisition of place of business, commencement of hiring of suitable personnel, identifying clients.*

4.4 *The Jurisdictional Delhi High Court in the case of E. Funds International India, [2007] 162 Taxmann 1 (Delhi), has held that the assessee being engaged in the software industry might not have earned revenue during the relevant previous year, but the fact could not be denied that assessee had taken all steps necessary to obtain business including efforts for marketing itself, which showed that assessee had commenced business in relevant previous year. Therefore, Assessing Officer was not justified in disallowing assessee's claim of loss in said business on ground that assessee had not commenced business in relevant previous year.*

4.5 *The view taken by the High Court in the aforesaid case has been endorsed by the High Court in the subsequent decision of Aspentech India (P) Ltd. wherein it was held that where the efforts made during the year resulted into revenue in the succeeding assessment year and the expenses incurred were*

*for achieving business objectives, they were thus allowable. In the present case, the appellant earned revenue exceeding Rs. two crores in the subsequent assessment years and the copy of the relevant extract of the P&L account for A.Y. 2011-12 is evidence to this fact.*

4.6 So far as the case laws relied upon by the AO are concerned, the first decision is the AP High Court In the case of *Sponge Iron India Utd. (supra)* which is distinguishable since the installation of machinery was a critical prerequisite for the setting up of the business of production and exploration of raw materials. Similarly, Gujarat High Court decision in *Sarabhai Sons (supra)* is distinguishable since Installation of machinery was essential for the business of manufacturing of scientific Instruments and communication equipment, In *Industrial Solvents' and Chemicals Pvt. Ltd. (supra)* decided by the Bombay High Court, the expenses claimed were for experimental marketable products which were actually manufactured in the subsequent assessment year and therefore it was held that business can be said to have commenced post the manufacture of marketable products. In the case of *Saurashtra Cement & Chemical Industries Ltd. (supra)* it was held that business would be considered to be set up from the date on which the first activity essential for the business was undertaken. In fact this decision is actually in favour of the appellant, as in the present case, the appellant had set up the business and started activities for creating customers and securing orders from them, which is supported by the Gujarat High Court which held that all the activities which go to make up a business need not be started simultaneously in order that the business may commence. In the case of the appellant, since the business was set up from the date of incorporation and all the conditions for undertaking essential business activities were fulfilled, it is held that the AO is not justified in disallowing the entire expenses incurred during the impugned year. Ground no. 2 is allowed."

8. On careful consideration of the order of the Id CIT(A), it is apparent that though the assessee is incorporated on 28<sup>th</sup> July 2009, it undertook the activities of appointment of key personnel, obtaining the office space on rent, conducting market research and also the training programme. On appreciation of these facts the Id CIT(A) after considering the judicial precedents, including the decision of the Hon'ble Delhi High Court, has held that the business of the assessee was set up during the year, allowed the claim of the assessee. Though we are of the view that merely incorporation of company does not satisfy the requirement of setting up of the business but the business activities must have commenced during the previous year. Setting up of the business starts as soon as the

company starts entering into the various contracts for its business activities. On careful consideration of finding of the Id CIT(A), we do not find any merit in the appeal of the revenue, hence, ground NO. 1 of the appeal of the revenue is dismissed.

9. Accordingly, the appeal of the revenue is dismissed.

Order pronounced in the open court on 20/02/2019.

-Sd/-

(H.S.SIDHU)  
JUDICIAL MEMBER

-Sd/-

(PRASHANT MAHARISHI)  
ACCOUNTANT MEMBER

Dated: 20/02/2019  
A K Keot

Copy forwarded to

1. Applicant
2. Respondent
3. CIT
4. CIT (A)
5. DR:ITAT

ASSISTANT REGISTRAR  
ITAT, New Delhi