

**IN THE INCOME TAX APPELLATE TRIBUNAL
(DELHI BENCH 'E' : NEW DELHI)**

**BEFORE SHRI R.K. PANDA, ACCOUNTANT MEMBER
and
SHRI KULDIP SINGH, JUDICIAL MEMBER**

**ITA No.1763/Del./2016
(ASSESSMENT YEAR : 2012-13)**

JCIT (OSD),
Circle 12 (1),
New Delhi.

vs. M/s. Imperative Hospitality Pvt. Ltd.,
90, Bangla Sahib Road,
New Delhi – 110 001.

(PAN : AABCI6836L)

(APPELLANT)

(RESPONDENT)

ASSESSEE BY : Shri Gautam Jain, Advocate
Shri Lalit Mohan, CA

REVENUE BY : Ms. Paramita M. Biswas, CIT DR

Date of Hearing : 03.06.2019

Date of Order : 10.06.2019

ORDER

PER KULDIP SINGH, JUDICIAL MEMBER :

Appellant, JCIT (OSD), Circle 12 (1), New Delhi (hereinafter referred to as the 'Revenue') by filing the present appeal sought to set aside the impugned order dated 19.01.2016 passed by the Commissioner of Income-tax (Appeals)-4, New Delhi qua the assessment year 2012-13 on the grounds inter alia that :-

“1. On the facts and circumstances of the case and in law, Ld. CIT(A) has erred in deleting the disallowance

of pre-operative stage expenses debited in P&L of Rs.5,75,23,000/-.

2. On the facts and circumstances of the case and in law, Ld. CIT(A) erred in deleting the addition of Rs.3,39,98,6561- assessed under the head of income from other source.

3. On the facts and circumstances of the case and in law, Ld. CIT(A) erred in accepting the appellants alternate plea that interest earned was inextricably linked with setting up of the business.”

2. Briefly stated the facts necessary for adjudication of the controversy at hand are : Assessee company is into the hospitality business which is to manage, administer, own and carry out the activities/business of running hotels, guest house and similar other facilities. During the year under assessment, the assessee has not run any guest house or hotel but has carried out activities of construction of hotel and as such, no business receipts have been shown in the profit & loss account. Assessing Officer noticed that the assessee has claimed total loss of Rs.1,99,23,134/-, arrived at after setting off of other income of Rs.3,39,98,656/- against the total expenses of Rs.5,75,23,000/- and other adjustments in computation of income. Assessee claimed in the P&L account the expenses on account of depreciation, employee benefit expenses and operating & other expenses. The amount of Rs.5,75,23,000/- has been claimed by the assessee on revenue account. Declining

the contentions raised by the assessee, AO reached the conclusion that since the assessee has been undertaking only construction of projects which is still in progress, expenses amounting to Rs.5,75,23,000/- is capitalized to the cost of construction. AO also treated the amount of Rs.3,39,98,656/- as income from other expenses and made addition thereof to the total income of the assessee.

3. Assessee carried the matter by way of an appeal before the Id. CIT (A) who has deleted the addition after accepting the appeal. Feeling aggrieved, the Revenue has come up before the Tribunal by way of filing the present appeal.

4. We have heard the Id. Authorized Representatives of the parties to the appeal, gone through the documents relied upon and orders passed by the revenue authorities below in the light of the facts and circumstances of the case.

GROUND NO.1, 2 & 3

5. Ld. DR for the Revenue challenging the impugned order passed by the Id. CIT (A) contended that since business activities have been carried out by the assessee during the year under assessment, the Id. CIT (A) has erred in allowing the pre-operative stage expenses debited in the P&L account and also erred in deleting the addition of Rs.3,39,98,656/- assessed under the head

'income from other sources' and relied upon the order passed by the AO.

6. However, on the other hand, Id. AR for the assessee in order to repel the arguments addressed by the Id. DR for the Revenue contended inter alia that in the earlier years, similar expenses have been accepted by the Revenue u/s 143(1) of the Income-tax Act, 1961 (for short 'the Act') and in the subsequent years, similar expenses have been allowed by the Revenue by way of scrutiny assessment framed u/s 143 (3) of the Act; that the Id. CIT (A) has rightly allowed the expenses on the premise of setting off of business which is different from commencement of the business; that as per financial statement available at page 10 of the paper book, actual amount on account of pre-operative stage expenses debited in the P&L account is Rs.5,39,11,288/- and not Rs.5,75,23,000/-, as has been recorded by AO and relied upon the decisions rendered by Hon'ble High Court cited as *Western India Vegetable Productions Ltd. vs. CIT 26 ITR 161 (Bom.)*, *CIT vs. L.G. Electronics (India) Ltd. 149 taxman 106 (Del.)*, *CIT vs. Dhoomketu Builders & Development (P) Ltd. 34 taxmann.com 18 (Del.)*, *CIT vs. Jubilant Offshore Drilling (P) Ltd. 90 CCH 0240 and Indian Oil Panipat Power Consortium Ltd. vs. ITO 315 ITR 255.*

7. Undisputedly, similar pre-operative stage expenses have been allowed by the Revenue in the preceding years u/s 143 (1) as well as in the succeeding years 2013-14 & 2014-15 u/s 143 (3) of the Act as per assessment order available at pages 67 & 68 and 69 & 70 of the paper book. It is also not in dispute that the main business of the assessee company is to manage, administer, own and carry on activities of business of running hotels, guest house and similar other facilities. It is also not in dispute that the assessee has produced before AO details of capital work-in-progress.

8. In the backdrop of the aforesaid undisputed facts, when we examine the impugned order passed by the Id. CIT (A) as well as financial statement of the assessee, available at pages 1 to 25 of the paper book, it goes to prove that the Id. CIT (A) has clearly made a distinction between commencement of business and setting off of business by thrashing the facts brought on record.

9. Ld. CIT (A) has categorically recorded the finding of facts as to setting up of the business by the assessee by returning following findings :-

“4.The appellant has made elaborate submissions and has claimed that they had set-up the business. As per the submissions of the Appellant, substantial amounts of money have been raised through equity capital on 20/10/2010, business decisions had

been taken, key personnel were employed, lease agreements were signed to take hotel properties on lease and in fact the improvements to properties had also commenced prior to the year under consideration. I have considered the arguments of the appellant. The Hon'ble Jurisdictional High Court, in the case of Commissioner of Income-tax- IV vs Dhoomketu Builders & Development (P) Ltd. (2013) (supra) while deciding upon similar issue of set-up of business by an assessee engaged in real estate, held that the mere fact that the assessee could not acquire any land during the relevant assessment year would not mean that the business had not commenced. The Hon'ble Court held that actual acquisition of land may be a first step in commencement of business, but section 3 does not speak of commencement of business, rather it speaks of setting up of business. The Court further observed that when the assessee was in a position to apply for a tender for land and had borrowed money for the same, the business of the assessee would be considered to be set-up. The Hon'ble Court found the argument of the revenue unacceptable that an assessee's business would not be set-up till the time the assessee failed to acquire any land. Similarly, in the facts of present case, the argument of the AO, that the business of the assessee would not be considered to be set-up till the time the activities towards running of hotel are established, is unacceptable. In present case, the assessee has raised substantial funds, has taken substantive decisions and has also invested money in subsidiary company for furtherance of its business, I find enough merit in the arguments of the Appellant that though the commercial operations may not have commenced, but the business of the appellant is definitely set-up and thus, there is no reason why the expenses should be disallowed. There is a clear distinction between a person commencing a business and a person setting up a business and for the purposes of the Income-tax Act, 1961, the setting-up of the business' and not the 'commencement of the business' is to be considered. There may, however, be an interval between the setting up of the business and the commencement of the business and all expenses

incurred during that interval are permissible deductions.”

10. Perusal of the balance sheet and P&L account, available at pages 9 & 10 of the paper book, apparently shows that the assessee has raised substantial funds through equity capital, employee personnel, entered into lease agreements to take hotel properties on lease and started improvements on the properties and all these facts have been brought on record by the AO, but he has failed to make distinction between setting off of business or commencement of business. When the assessee has taken sufficient steps by way of raising sufficient funds employing skilled personnel and by entering into lease agreements with the hotels on which improvements have been started, it amounts to setting off of business and as such, previous year expenses incurred in the business are permissible deductions.

11. Hon'ble High Court of Bombay in case cited as *Western India Vegetable Productions Ltd.* (supra) decided the identical issue in favour of the assessee by returning following findings :-

“Section 37(1), read with section 3 of the Income-tax Act, 1961 [Corresponding to section 10(2)(xv) read with section 2(11) of the Indian Income-tax Act, 1922] - Business expenditure - Year in which deductible - Assessment year 1947-48 – Whether for purpose of a business it is only after business is set up that previous year of that business commences and in that previous

year expenses incurred in business can be claimed as permissible deductions - Held, yes - Assessee-company was registered on 29.12.1945 and received its certificate of commencement of business on 20.4.1946 - It purchased a groundnut oil mill on 1.11.1946 for running it - Assessee closed its accounts for first time on 31.3.1947 - Expenditure incurred from its inception was debited to profit and loss accounts - ITO held that business started on 1.11.1946 when assessee purchased ground-nut mill while AAC held that business started on 20.4.1946 when it received certificate of commencement of business - Tribunal found that first purchase of raw material was made in end of September, 1946 from which inference could be drawn that assessee had set up its business by that date - After scrutinizing various details of expenses, it came to conclusion that business was not set up prior 1.9.1946 and, therefore, allowed expenses subsequent to that date - Whether there was evidence before Tribunal to hold that assessee-company set up its business as from 1.9.1946 - Held, yes

Section 2(34) of the Income-tax Act, 1961 [Corresponding to section 2(11) of the Indian Income-tax Act, 1922 - Previous year - Assessment year 1947-48 - Whether for purposes of business, previous year begins from date of setting up of business - Held, yes

Words and phrases: Terms "setting up" and "commenced" occurring in section 2(11) of Indian Income-tax Act, 1922."

12. Similarly, Hon'ble High Court of Delhi in case of *CIT vs. L.G. Electronics (India) Ltd.* (supra) also allowed the expenses incurred by the assessee on travelling and conveyance, rent, etc. which were disallowed by the AO on the ground that the assessee has not yet commenced its business during the year under assessment by returning following findings :-

“Section 3 of the Income-tax Act, 1961 - Previous year - Assessment year 1996-97 - Assessee-company having set up its business on 21-2-1997 claimed deduction on expenses incurred on travelling and conveyance, rent, etc. - Assessing Officer, however, disallowed same on ground that it had not commenced its business during assessment year in question - On appeal, Commissioner (Appeals), set aside order of Assessing Officer and held that (a) there is a distinction between commencement of business and setting up of business and the two dates need not necessarily overlap and (by section 3 refers to date of setting up of business and as such it is only thereafter, that previous year of newly set up business would commence and, therefore, expenses incurred prior thereto could be taken into account for purpose of determining profits of a newly set up business - On further appeal, Tribunal confirmed said order - Whether orders of appellate authorities suffered from infirmity - Held, no.”

13. Similarly, Hon’ble Delhi High Court in case of *CIT vs. Dhoomketu Builders & Development (P) Ltd.* (supra) held the finding of facts returned by the Tribunal while allowing the similar expenses by making distinction between the commencement of business and setting off of business by returning following findings:-

“Section 28(i), read with section 3, of the Income-tax Act, 1961- Business - Commencement of [Illustrations] – Assessment year 2006-07 - Assessee, engaged in realty business, participated in an auction to acquire a piece of land – It obtained loan from its holding company and deposited same as earnest money to acquire land - However, it could not succeed in auction - It paid interest on borrowed fund and received interest on earnest money – It claimed differential between interest as loss and claimed for carry forward of said loss -

Assessing Officer found that current year was first year of existence of assessee and since it failed to acquire land, it could not be said that business was set up in relevant year - He disallowed said claim - However, Tribunal held that acts of applying for participation in tender, borrowing of monies on interest from holding company and deposit of borrowed monies on same day as earnest money clearly established that business had been set up – Whether finding returned by tribunal being finding of fact, no question of law arose for consideration - Held, yes [Para 91 [in favour of assessee]]”

14. In view of what has been discussed above, we are of the considered view that the Id. CIT (A) has rightly allowed the expenses of Rs.5,75,23,000/- (correct amount is Rs.5,39,11,288/-) having been incurred by the assessee after setting off of the business though before commencement of the business. Moreover, the assessee itself has capitalized many of its expenditure and only claimed the expenses which are of revenue in nature.

15. So far as question of deleting of Rs.3,39,98,656/- by the Id. CIT (A) assessed by the AO under the head ‘income from other sources’ is concerned, the Id. CIT (A) has brought on record the fact that the assessee has already offered to tax the interest income as ‘income from other sources’ but such income has been set off against loss under the head PGBP as per section 71 of the Act. AO relied upon the decision of Hon’ble Supreme Court in case of

Tuticorin Alkali Chemicals & Fertilizers Ltd. vs. CIT 227 ITR 172 (SC).

16. Hon'ble Delhi High Court in case cited as *Indian Oil Panipat Power Consortium Ltd. vs. ITO 315 ITR 255 (Del.)* decided the identical issue by considering the decision of Hon'ble Supreme Court in *Tuticorin Alkali Chemicals & Fertilizers Ltd. vs. CIT* (supra) relied upon by the AO by returning following findings :-

“The Tribunal had misconstrued the ratio of the judgment of the Supreme Court in the case of Tuticorin Alkali Chemicals & Fertilizers Ltd. (supra) and that of Bokaro Steel Ltd.'s case (supra). The test, which permeated through the judgment of the Supreme Court in Tuticorin Alkali Chemicals & Fertilizers Ltd.'s case (supra), was that if funds have been borrowed for setting up of a plant and if the funds are 'surplus' and then by virtue of that circumstance they are invested in fixed deposits, the income earned in the form of interest will be taxable under the head 'income from other sources'. On the other hand, the ratio of the Supreme Court judgment in Bokaro Steel Ltd.'s case (supra) is that if income is earned, whether by way of interest or in any other manner on funds which are otherwise 'inextricably linked' to the setting up of the plant; such income is required to be capitalized to be set off against pre-operative expenses. [Para 5]

The test, therefore, is whether the activity which is taken up for setting up of the business and the funds which are garnered are inextricably connected to the setting up of the plant. The clue is perhaps available in section 3 which states that for newly set-up business, the previous year shall be the period beginning with the date of setting up of the business. Therefore, as per the

provision of section 4 which is the charging section, income, which arises to an assessee from the date of setting up of the business but prior to commencement, is chargeable to tax, depending on whether it is of a revenue nature or a capital receipt. The income of a newly set-up business, post the date of its setting up, can be taxed if it is of a revenue nature under any of the heads provided under section 14 in Chapter IV. For an income to be classified as an income under the head 'profits and gains of business or profession', it would have to be an activity which is in some manner or form connected with business. The word 'business' is of wide import which would also include all such activities which coalesce into setting up of the business. Once it is held that the assessee's income is an income connected with business, as in the instant case in view of the finding of fact by the Commissioner (Appeals) that the monies which were inducted into the joint venture company by the joint venture partners were primarily infused to purchase land and to develop infrastructure, then it could not be held that the income derived by parking the funds temporarily with bank, would result in the character of the funds being changed inasmuch as the interest earned from the bank would have a hue different than that of business and be brought to tax under-the head 'Income from other sources'. It is well-settled that an income received by the assessee can be taxed under the head 'Income from other sources' only if it does not fall under any other head if income as provided in section 14. The head 'Income from other sources' is a residuary head of income. [Para 5.1]

In the instant case, it was clear upon a perusal of the facts as found by the' authorities below that the funds in the form of share capital were infused for a specific purpose of acquiring land and the development of infrastructure. Therefore, the interest earned on funds primarily brought for infusion in the business could not have been classified as 'income from other sources'. Since the income was earned in a period prior to commencement of business, it was in the nature of capital receipt and, hence, was required to be set off against pre-operative expenses. [Para 5.2]

In view of the discussion above, the Tribunal misdirected itself in applying the decision of the Supreme Court in Tuticorin Alkali Chemicals & Fertilizers Ltd, (supra) in the facts of the instant case. On account of the finding of fact returned by the Commissioner (Appeals) that the funds infused by the joint venture partners in the assessee-company were inextricably linked with the setting up of the power plant, the interest earned by the assessee could not be treated as 'income from other sources'. Therefore, the impugned judgment was to be set aside. [Para 7]”

17. As has been held in preceding paras, when it is proved that the assessee has set up the business, earned the income from interest during the construction period and has set off of the same against the loss under the head PGBP as per section 71 of the Act, the Id. CIT (A) has rightly deleted the addition as the funds parked in the bank on which interest has been earned were inextricably linked with the setting up of the hospitality business.

18. So, following the decision rendered by Hon'ble High Court in Indian Oil Panipat Power Consortium (supra), income earned by the assessee from interest during the period prior to the commencement of business and at the stage of setting up of business, the same is of the nature of capital receipt and as such loss incurred by the assessee under the head PBGP is eligible to be set off against the interest income earned during the year under assessment. So, we are of the considered view that the Id. CIT (A)

has rightly directed the AO that interest income of Rs.3,39,98,656/- be set off u/s 71 of the Act being inextricably linked with the business of the assessee.

18. In view of what has been discussed above, contentions raised by the Id. DR for the Revenue and the decision rendered by the coordinate Bench of the Tribunal in case of *Orient Cosmetics Ltd. vs. DCIT 74 ITD 135* is not applicable to the facts and circumstances of the case. Consequently, appeal filed by the Revenue is hereby dismissed.

Order pronounced in open court on this 10th day of June, 2019.

**Sd/-
(R.K. PANDA)
ACCOUNTANT MEMBER**

**sd/-
(KULDIP SINGH)
JUDICIAL MEMBER**

**Dated the 10th day of June, 2019
TS**

Copy forwarded to:

- 1.Appellant
- 2.Respondent
- 3.CIT
- 4.CIT(A)-I, New Delhi.
- 5.CIT(ITAT), New Delhi.

**AR, ITAT
NEW DELHI.**