

IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCHES “ B ” BENCH: BANGALORE

**BEFORE SHRI B.R. BASKARAN, ACCOUNTANT MEMBER
AND
SHRI PAVAN KUMAR GADALE, JUDICIAL MEMBER**

ITA Nos.2191 & 2192/Bang/2018
(Assessment Years : 2013-14 & 2014-15)

M/s.Stelis Biopharma Pvt. Ltd.,
No.293, Jigani Indl. Area, Jigani Link Road,
Bommasandra, Anekal Taluk,
Bangalore-560 105

....Appellant

Vs.

1. Assistant Commissioner of Income Tax,
Circle 6(1)(2), Bangalore.
2. Dy. Commissioner of Income Tax,
Circle 6(1)(2), Bangalore.

.....Respondent.

Assessee By:	Shri Chythanya K.K., Advocate.
Revenue By:	Shri Priyadarshi Misra, JCIT (D.R)

Date of Hearing :	02.06.2020.
Date of Pronouncement :	15.06.2020.

ORDER

PER BENCH :

The assessee has filed the appeals against separate orders of Commissioner of Income Tax (Appeals), Bangalore, passed u/s. 143(3) and u/s 250 of the Income Tax Act, 1961 for the Asst. Years 2013-14 and 2014-15. Since both the appeals

have common issues, for the sake of convenience, are clubbed and heard and consolidated order is passed. We shall take up the assessee's appeal in ITA No.2191/Bang/2018 and facts narrated therein..

3. The assessee has raised the following grounds of appeal as under :

1. The Order of the Learned Commissioner (Appeals) is not justified in law and on facts and circumstances of the case.

2. As regards disallowance of expenses of Rs. 1,52,18,533/-:

2.1. The Learned Commissioner (Appeals) is not justified in upholding the action of the Learned Assessing Officer by way of a cryptic and non-speaking order.

2.2. The Learned Commissioner (Appeals) is not justified in upholding the action of the Learned Assessing Officer in disallowing the total expenditure of Rs.1,52,18,533/- merely for the reason that there was no revenue from the operations during the impugned year.

2.3. The lower authorities have failed to appreciate that law does not require the presence of receipt to justify the deduction of an expense.

- 2.4.** The lower authorities have failed to appreciate that the Appellant's business was set up long before and expenses are allowable as soon as the business is set-up which is anterior to commencement of business, whether or not there is revenue from the operations.
- 2.5.** The lower authorities have failed to appreciate that the Appellant being a Company, following the mercantile system of accounting, is governed by the Accounting Standard I issued under Section 145(2), which provides for recognition of cost when they are incurred and recorded in the financial statements of the period to which they relate.
- 2.6.** The lower authorities are not justified in disallowing the impugned expenses of Rs.1,52,18,533/- [which consists of employee benefit expenses, finance cost and other expense claimed under Section 37 and depreciation under Section 32], when the Appellant satisfied all the conditions of Section 37 and Section 32.
- 2.7.** Without prejudice to the above, the Learned Assessing Officer has misinterpreted the matching principle in the instant case, without appreciating that if expenses incurred in one year are deferred to the year of income, the same become prior-period expenses and hence not allowable under the Act.

- 2.8.** Without prejudice to the above, the lower authorities are not justified in treating the impugned expenses as 'preliminary expenses' under Section 35D which is not applicable to the Appellant's business which was already set-up, and is a going concern.
- 2.9.** The Learned Commissioner (Appeals) is not justified in treating the impugned expenses as capital in nature by perversely holding that there is no commencement of commercial production, when the business actually commenced in the year 2008.
- 2.10.** The Learned Commissioner (Appeals) is not justified in perversely holding that the Appellant has failed to produce the details of expenses, the purpose for which they were incurred, ignoring the submission dated 16.03.2018 and undisputed information in the profit and loss account.
- 2.11.** The lower authorities are not justified in failing to follow the principles of consistency, when the similar expenditure was allowed by the Assessing Officer in the case of the Appellant for the AY 2012-2013, based on the same facts and circumstances of the case.
4. The Brief facts of the case are that the assessee company is engaged in the business of development of biological drugs and filed the Return of Income for the Asst. Year 2013-14 on 27.09.2013 with a total loss of Rs.1,64,28,715/-. Subsequently, the case was selected for scrutiny and Notice under Section 143(2)

of the act was issued. In compliance, the learned Authorized Representative of the assessee appeared from time to time and the case was discussed. The Assessing Officer, on perusal of the profit and loss account found that the assessee has not offered revenue from operations, but has claimed expenditure along with depreciation. The Assessing Officer is of the opinion that the assessee company has not commenced its production activities and the expenditure claimed is in the nature of Pre operative expenses, further there is no matching concept of income offered against expenditure in the said financial year. Whereas, the assessee by letter dt.23.3.2016 explained that the company has commenced its operations in the earlier years and has complied with Accounting Policies and Accounting Standards, and where ever the expenditure incurred on product development activity being capital expenses in nature, is capitalized and only revenue expenditure is claimed in the profit and loss account but the Assessing Officer has overlooked these facts and is of the opinion that since no commercial operations have started, the expenditure has to be considered as preoperative expenditure as the products are in developmental stage, and also no revenue from operations and non compliance of matching concept. The A.O.applied the concept of amortization of expenses and is of the opinion that the expenditure cannot be allowable for the said assessment year and disallowed the claim and Assessed total loss of Rs.11,13,932 and passed the order under Section 143(3) of the Act dt.28.03.2016.

Aggrieved by the order, the assessee has filed an appeal with the CIT (Appeals), whereas the CIT (Appeals) considered the grounds of appeal, written submissions and findings of the Assessing Officer and has concurred with the view of the Assessing Officer that the expenditure claimed is preoperative expenditure and not current year revenue expenditure and sustained the addition and dismissed the appeal. Aggrieved by the order of the CIT (Appeals), the assessee has filed an appeal with the Tribunal.

5. At the time of hearing, the learned Authorized Representative submitted that the assessee company was incorporated on 12.06.2007 and commenced business operations from 2.5.2008. The assessee is continuing the business from the A.Ys 2008-09 to 2012-13 with the main activity of development of biological drugs and R&D. Whereas the income tax Department has accepted the assessee claim of revenue expenditure in the profit and loss account for the asst year 2012-2013 in the assesment. The LdAr supported his arguments with details in Paper Book and prayed for allowing the appeal. Contra, the learned Department Representative supported the order of the CIT (Appeals).

6. We heard the rival submissions and perused the material on record. Prima facie, the sole matrix of the disputed issue is with respect to the allowing of revenue expenditure claimed by the assessee in the profit and loss account.

Whereas the Assessing Officer is of the opinion that the expenditure is in the nature of preoperative expenses and also matching concept does not exist as no revenue was offered by the assessee in the assessment year under consideration. The learned Authorized Representative submitted that the assessee is in the development of biological drugs and started commercial production from the F.Y. 2008-09 and referred to page 157 of the Paper Book, where the details of revenue from operations are submitted before the CIT (Appeals) for the A.Ys 2008-09 to 2012-13. The Id. AR demonstrated the profit and loss account placed at Page 125 of Paper Book, where the assessee has claimed expenses at Sl. No. IV aggregating to Rs.1,52,82,533/- Further, where the expenditure is of enduring nature is capitalized under Capital work in process,(product under development) disclosed at page132 of paper book in the Annexure of Fixed Assets as on 31.03.2013. The LdAr referred to the Accounting Policies and notes on the financial statements at Page 150 of the Paper Book where expenditure incurred on intangible assets developed by the company post research stage is recognized as an asset marked as

-

“Capital Work in Progress

Projects under which assets are not ready for its intended use and other Capital Work in Progress are carried at cost, comprising direct cost, related incidental expenses and attributed finance costs.

“ Intangible Assets developed by the Company

Expenditure incurred on Intangible Assets developed by the company, post research stage is recognized as an asset, if and only if the future economic benefits attributable are probable to flow to the company and costs can be measured reasonably.

The cost of Technical Know how developed is being amortised equally over its estimated life.

With effect from 1.1.2011, direct operating expenses incurred on product development have been treated as Capital Work in progress and will be capitalized as Technology Know how, on completion of certain technical milestones. These costs are in the nature of development of products, which have the potential to be exploited commercially and hence can generate future economic benefit.”

We find that the assessee has been following the same system of accounting and the Income tax department has accepted in earlier years. Further in the Asst. Year 2012-13, where the facts are similar, the Assessing Officer has considered the assessee's claim and assessment was completed. The learned Authorized Representative's contentions are that there is no change in the facts and system of accounting in comparison with the earlier assessment years, hence the observations of the Assessing Officer and the appellate authority that the assessee company has not commenced its commercial production cannot be tenable.. We found strength in the submissions of the learned Authorized Representative supported with details. we find that the Assessing officer has passed assessment order under Section 143(3) of the Act for the Asst. Year 2012-13 ,where the assessee line of business is

similar to current years. We consider it appropriate to refer to the submissions of the assessee in assessment proceedings for the Asst year 2012-13 at Page174-176 of paperbook.

December 11, 2014

The Deputy Commissioner of Income-tax
Circle - 11(4),
#14/3, 5th Floor, R.P.Bhavan,
Nrupathunga Road,
Bangalore - 560 001

Dear Sir,

Subject: Assessment Proceedings under section 143(3) of the Income-tax Act, 1961

Ref: a) PAN - AABCI7084A
b) Assessment Year ('AY') 2012-13 (financial year 2011-12)
c) Notice dated Oct. 24, 2014 issued under section 142(1) of the Income tax Act, 1961 ("the Act")
d) Our submission dated November 10, 2014, November 25, 2014 and December 5, 2014.

We refer to the on-going assessment proceedings of Inbiopro Solutions Private Limited ('Inbiopro' or 'the Company'). We also refer to the discussion we had with your office on December 5, 2014.

In connection with the above we wish to submit as under:

1. Note on allowability of expenditure incurred during the year is enclosed as Annexure 19.

We request you to kindly take the submission on record.

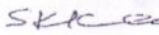
We have submitted all the information/ documents sought by your goodself to the best of our knowledge. We shall however be glad to furnish any further information/ documents upon hearing from your goodself.

We request your goodself to grant us an opportunity of being heard before concluding the assessment proceedings.

Thanking You,

Yours faithfully,

For Inbiopro Solutions Private Limited


K. Sudhir
Authorized Signatory



Encl.: As above

Note on allowability of expenditure incurred during the year

During the course hearing your goodself sought explanation so as to why the expenditure incurred during the year should be allowed in view of lower revenue earned in FY 2011-12.

In connection with the above, the Company wishes to submit as under:

1. Expenditure incurred for product development

- a. The Company commenced its operation on May 2, 2008. The Company is engaged in development of biological drugs (bio-similars, bio-betters and NBE's) with the objective of providing biotechnology process development services to healthcare units.
- b. The Company is primarily engaged in the product development activity for its own benefit and intends to register the products in its name, post development and approval. As the development is still in progress, no significant operating revenue was earned during the FY 2011-12.
- c. The product development generally takes 3 to 5 years until the final product is ready for registration and approval, post which the products can be manufactured for commercial purpose. During the period (which includes time taken by the regulatory authorities for approval), the Company would be required to incur the necessary expenditure for the purpose of product development. In case the Company desires to carry on the development activity for any third party, the revenue will be accounted / recorded appropriately.

2. Incidental activities and one off transactions

- a. In addition to the product development, the Company also undertook testing and analysis services in its R&D unit which is an incidental activity of the Company. The testing and analysis services to third parties *inter alia* includes testing of samples for analysis of products, method of development and partial validation of the batches.
- b. The cost incurred for testing and analysis services has been debited to profit and loss account. Similarly, the consideration received for services rendered to its customers has been appropriately credited to profit and loss account.
- c. The Company during FY 2011-12 has earned an income of Rs. 143,783/- from the testing and analysis services and the same has been offered to tax.
- d. Further, during the FY 2013-14, the Company had supplied certain consumables to certain parties. The Company submits that the supply of consumables was one off transaction and the amount of Rs. 287,513/- received as consideration has been credited to profit and loss account and offered to tax.

3. Accounting principles and amount deductible under tax provisions

- a. The expenditure debited to the profit and loss account are recognized based on the accounting standards and accounting policies followed by the Company on a consistent basis and such expenditure have been incurred during the course of carrying out of the business of the Company.
- b. The expenditure incurred are revenue in nature and are incurred in the ordinary course of business.
- c. There can be no quid pro quo between income and expenditure in the ordinary course of business and hence the matching principle would not be applicable.
- d. In this regard It is pertinent to note that the provisions of section 28 postulates that profits and gains of any business or profession which was carried on by the assessee at any time during the previous year is taxable under the said provisions.
- e. Under the provisions of section 28, the charge is in respect of the profits that have accrued to the business during the previous year. The profits of the annual period have to be computed in accordance with the method of accounting regularly employed by the assessee on the basis of income accrued during the and expenditure incurred during the year.

In the instant case, the revenue on product development has not accrued while all other revenue that has accrued has been accounted and offered to tax. Similarly, all expenditure that has been incurred during the year has been debited to Profit and Loss Account and claimed as deduction in accordance with the provisions of Income Tax Act.

- f. Therefore expenditure incurred by the Company in the course of carrying on of business would be claimed and required to be allowed as deduction as per the provisions of section 28 of the Act.

4. Items of expenditure incurred in the course of business are deductible to arrive at the taxable income

- a. What are chargeable to tax are the profits and gains of the year and the in assessing the amount of profit and gains, one must necessarily take the expenditure incurred during that year into account for revenue determining the taxable income.
- b. Further, the deduction should be claimed in the year in which the expenditure is incurred.

5. Conclusion

In view of the above submission and considering the facts of the case, the Company submits as under:

- a. The Company has commenced its operations and expenditure debited to the profit and loss account are revenue in nature and which are incurred during the course of business and have been accounted in accordance with the accounting policy and accounting standards
- b. Expenditure incurred towards product development activity and which are capital expenditure have not been debited to the profit and loss account

Hence, the Company is entitled for the deduction of the expenditure debited to profit and loss account.

Considering the submissions of the assessee and they were accepted by the revenue authorities for the AsstYear 2012-2013, we are of the opinion that there is

no change in facts in the present assessment year, and the Assessing Officer cannot consider the expenditure claimed as preoperative expenditure and the basis of matching concept. Accordingly, we set-aside the order of the CIT (Appeals) and restore entire disputed issue to the file of Assessing Officer with the above directions. And the A .O. shall provide adequate opportunity of hearing to the assessee and we allow the appeal of the assessee for statistical purposes.

7. Similarly, for the Asst. Year 2014-15 where the facts are identical, the decision of the appeal for Asst. Year 2013-14 shall equally apply to Asst. Year 2014-15. Accordingly, We set aside the order of CIT (Appeals) and restore the disputed issues to the file of Assessing Officer and allow the appeal of the assessee for statistical purposes.

8. In the result, the assessee's appeals for Asst. Years 2013.14 & 2014-15 are allowed for statistical purposes.

Pronounced in the open court on the date mentioned on the caption page.

Sd/-

(B.R. BASKARAN)
ACCOUNTANT MEMBER

Sd/-

(PAVAN KUMAR GADALE)
JUDICIAL MEMBER

Dated: 15.06.2020.

*Reddy GP

Copy to

1. The appellant
2. The Respondent
3. CIT (A)
4. Pr. CIT
5. DR, ITAT, Bangalore.
6. Guard File

By order

Assistant Registrar
Income-tax Appellate Tribunal
Bangalore