

**IN THE INCOME TAX APPELLATE TRIBUNAL
“A” BENCH: BANGALORE**

**BEFORE SHRI N.V. VASUDEVAN, VICE PRESIDENT
AND
SHRI B.R. BASKARAN, ACCOUNTANT MEMBER**

ITA No.3163/Bang/2018
Assessment Year : 2015-16

E-Land Systems Pvt. Ltd. No.#6B, 6 th Floor Shobha Pearl Opposite Mayo Hall Commissariat Road Bangalore 560 025 PAN NO : AADCE8309G	Vs.	ITO Ward-2(1)(4) Bangalore
APPELLANT		RESPONDENT

Appellant by	:	Shri Sandeep Chalapathy, A.R.
Respondent by	:	Shri Sankar Ganesh K., D.R.

Date of Hearing	:	21.02.2022
Date of Pronouncement	:	22.02.2022

ORDER

PER B.R. BASKARAN, ACCOUNTANT MEMBER:

The assessee has filed this appeal challenging the order dated 28.9.2018 passed by Ld. CIT(A)-2, Bengaluru and it relates to the assessment year 2015-16. The main grounds of appeal urged by the assessee is whether the Ld. CIT(A) was justified in holding that the assessee has not set up its business during the year under consideration and hence, the A.O. was justified in disallowing the claim of loss.

2. The assessee has also filed an additional ground stating that the return of income filed by the assessee was selected for limited scrutiny for verifying "Minimum Alternate Tax (MAT) liability mismatch", but the AO has proceeded to examine the issue of "date of setting up of business", which was not within the scope of limited scrutiny and hence, the impugned assessment order is bad in law. At the time of hearing, we enquired Ld. A.R. as to whether the assessee has inspected the assessment record in order to find out the availability of approval, if any, obtained by A.O. from Principal CIT for converting the limited scrutiny into complete scrutiny? The Ld. A.R. fairly admitted that the assessee has not inspected the assessment record.

3. It is well settled proposition of law that the legal issue can be urged at any stage provided all the facts relating to the same are already available on record. We notice that the assessee is not sure as to whether the approval from PCIT has been obtained by AO or not. As per the Instruction No.5/2016 issued by CBDT, the AO can convert the limited scrutiny into complete scrutiny after obtaining administrative approval from PCIT/CIT/PDIT/DIT. In the instant case, it is the assessee which has raised the additional ground and hence, it is the bounden duty of the assessee to ascertain and ensure that all the facts relating to the additional ground are available on record. Since the assessee is not sure whether all the relevant details relating to the additional ground are already available facts, it can only be said that the assessee has raised this ground only on presumption that the AO might not have obtained required approval. Such kind of presumptions have no place in judicial proceedings and such practice of raising legal issues by way of additional grounds without ascertaining the relevant facts unnecessarily waste the time of Court also. Hence, we are unable to admit the additional ground urged by the assessee.

4. The facts relating to the main grounds are stated in brief. The assessee company was incorporated on 17.12.2014. Hence, the year under consideration is the first year for the assessee. The assessee is engaged in the business of providing information technology application management support and BPO services to M/s. E Land Group companies. During the year under consideration, the assessee incurred the expenditure to the tune of Rs.18,78,529/-. The assessee claimed that it has already set up the business during the year under consideration and accordingly claimed the above said loss under the head "Income from business" and also claimed that it should be carried forward to next year.

5. The A.O. noticed that the assessee did not commence business during the year under consideration. He noticed that the assessee has entered into a Service agreement with a group company named M/s. K. Swiss Inc. for providing service with effective from 1.4.2015. He noticed that the above said agreement was signed by the assessee on 26.11.2015 and by the above said group company on 23.11.2015. The first invoice was raised by the assessee company only on 19-10-2015. The AO also noticed that the assessee did not generate any revenue during the year under consideration. The A.O., relying on the decision rendered by Hon'ble Supreme Court in the case of CWT Vs. Ramaraj Surgical Cotton Mills Ltd. (1967) 63 ITR 478 observed that "A Unit cannot be said to have been set up unless it is ready to discharge function for which it is being set up". Accordingly, the A.O. held that the business of the assessee was not set up and hence the expenditure incurred prior to setting up of business is not deductible. Accordingly, he rejected the claim of business loss of Rs.18,78,529/- and determined the total income as nil.

6. The Ld. CIT(A) called for annual report of the assessee company and referred to the observations made in the Director's report, wherein the objective of the company have been mentioned as under:-

“The main objective is to tap into abundant IT/ITES talent available in India and provide best in class IT/ITES services to our sister companies under E-Land Group starting April 1st 2015. We will commence our IT/ITES services support to K. Swiss Global Brands one of our sister concern. During this financial year (2015-2016) we are expecting a team size of 25 team members providing IT/ITES support anticipating an annual revenue of around \$500,000 USD. We will be making significant investments in attracting right talent nurturing them to meet the technology skills and expertise needed to lead the accelerated growth planned for next 5 years.”

Accordingly, the Ld. CIT(A) took the view that the business of the assessee is commencing from April 1st, 2015 only. Prior to that date, the assessee has recruited only 2 employees only, even though it is required select 25 team members. Accordingly, the Ld CIT(A) took the view that the assessee has not created the required technological capability to start the support services during the year under consideration. Accordingly, he took the view that the assessee was not fully ready to start the services and hence it cannot be said that the assessee has set up the business during the yar under consideration. Before Ld. CIT(A), the assessee placed reliance on the decision rendered by Hon'ble High Court of Delhi in the case of OmniGlobe Information Tech India in ITA No.257/2012 (369 ITR 1). However, the Ld. CIT(A) held that the above said decision is distinguishable from the facts prevailing in the present case. Accordingly, he dismissed the appeal filed by the assessee.

7. We heard the parties and perused the record. The Ld A.R took us through the financial statements relating to the year under consideration. He submitted that the assessee has already set up its

office during the year under consideration by purchasing Computer equipment for Rs.4,31,199/-, Computer software for Rs.71,072/- Furniture and fixtures for an amount of Rs.19,465/- and Office equipment for Rs.4,64,874/-. He further submitted that the expenses incurred by the assessee would show that the assessee has already employed certain employees, taken an office premises on rent, incurred communication expenses. He submitted that all these expenses are core expenses that are required to be incurred after setting up of business. He submitted that the observation made by the directors in their report, which has been extracted by Ld CIT(A) in his order, refer to the assessment of Marketing and market environment. He further submitted that there is difference between setting up of business and actual commencement of business. He submitted that the expenses incurred after setting up of business is allowable as deduction, even though the actual commencement may take place on a subsequent date. The Ld A.R placed his reliance on various case laws in support of his contentions. He further submitted that the decision rendered by Hon'ble Delhi High Court in the case of Omniglobe Information Tech India P Ltd (supra) is squarely applicable to the facts of the present case and hence the Ld CIT(A) was not justified in observing that the said decision is distinguishable.

8. The Ld D.R, on the contrary, submitted that there is no dispute that the expenses incurred after setting up of business is allowable as deduction. He submitted that the very fact that the agreement was signed with its group company in November, 2015 would show that the assessee could not have set up its business before 31.3.2015. Further, the assessee has not employed the full technical team, without which it could not have commenced the business. He submitted that the assessee could be said have "set up" its business, only when it is fully ready to commence its operations. He submitted

that, in the facts of the present case, it cannot be said that the assessee has set up its business.

9. We heard the parties and perused the record. There is no dispute with regard to the fact that there could be a time gap between “setting up of business” and actual “commencement of business”. It is also settled principle that the expenses incurred after setting up of business is allowable as deduction. We may gainfully take support from the following observations made by Hon’ble Bombay High Court in the case of Western India Vegetable Products Ltd vs. CIT (1954)(26 ITR 151)(Bom):-

“It seems to us, that the expression “Setting up” means, as is defined in the Oxford English Dictionary, “to place on foot” or “to establish”, and in contradistinction to “commence”. The distinction is this that 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 a interregnum, there may be an interval 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 expenses during the interregnum, would be permissible deduction under sec. 10(2).”

10. Hence the answer to the question as to whether the assessee has set up its business or not would depend upon the facts prevailing in each of the case. We notice that, in the instant case, the Ld A.R has shown to us that the assessee has taken a premises on rent, employed few employees, purchased certain assets. In the case of Omniglobe Information Tech India P Ltd (supra), the Hon’ble Delhi High Court was considering the question of “setting up” of business in the context of a BPO Service industry. The Hon’ble Delhi High Court observed as under:-

“Keeping in view the nature of business activity of the appellant-assessee, we do not think that it can be held that training, imparting skills to employees recruited, or, testing their performance can be treated as a pre-set up expenditure. The appellant-assessee had either employed or taken help of trainers/seniors for the said purpose. The moment employees were recruited and entrolled and infrastructure to use their

Page 7 of 8

service was in place, set up was complete. It was indicative of the fact that business operations had been set up. In the BPO industry, training of employees is an important, essential and integral element of the business activities and when the assessee has the infrastructure in place, the business can be treated as set up.”

The above said observations have been made in the context of a BPO company.

11. For determining the question as to whether the assessee has “set up” its business or not, in our considered view, what is required to be seen is whether the assessee is ready to commence its business. As rightly pointed out by Ld CIT(A) that the essential man power is the heart and soul of ITES service Industry. Since the assessee is in service industry providing IT application maintenance support services its requirement of man power and electronic equipment would depend upon the nature and type of work, i.e., type of IT application, it is getting. Hence, in the instant case, the assessee could plan its further recruitment of employees, depending upon the nature and type of work it is getting, which is essential to determine the skill set required for executing the said work.

12. We notice that the Ld CIT(A) has referred to the service agreement entered in the succeeding year by the assessee, wherein the management has visualized requirement of 25 technical employees. Since the assessee has not recruited that much number of employees, the Ld CIT(A) has taken the view that the assessee is still in the process of setting up of business. In our view, the directors have stated in the Directors’ report that the nature of work required to be performed under the agreement entered with its AE would require 25 employees. In the instant case, in our view, this kind of decision is taken after setting up of business but before actual commencement of operations. Accordingly, we are of the view that

Page 8 of 8

the Ld CIT(A) was not justified in observing that the assessee is in the process of setting up of business, since it has not yet completed recruitment of 25 employees.

13. Accordingly, in the facts and circumstance of the case, we are of the view that the assessee has set up its business during the year under consideration. Accordingly, the expenses incurred by the assessee are allowable as deduction and in the case of loss, it is entitled to carry it forward. Accordingly, we reverse the order passed by Ld CIT(A) and direct the AO allow the expenses and also carry forward of loss.

14. In the result, the appeal filed by the assessee is partly allowed.

Order pronounced in the open court on 22nd Feb, 2022.

Sd/-
(N.V. Vasudevan)
Vice President

Sd/-
(B.R. Baskaran)
Accountant Member

Bangalore,
Dated 22nd Feb, 2022.
VG/SPS

Copy to:

1. The Applicant
2. The Respondent
3. The CIT
4. The CIT(A)
5. The DR, ITAT, Bangalore.
6. Guard file

By order

Asst. Registrar, ITAT, Bangalore.