

IN THE INCOME TAX APPELLATE TRIBUNAL, MUMBAI BENCH 'D', MUMBAI

**BEFORE SHRI SAKTIJIT DEY, HON'BLE VICE PRESIDENT
AND SHRI AMARJIT SINGH, HON'BLE ACCOUNTANT MEMBER**

**ITA No.4123/Mum/2023
Assessment Year: 2017-18**

Mohalla Tech Private Limited No. 2, 26, 27 and 3, Sona Towers, 1 st Floor, Krishna Nagar Industrial Area, Hosur Main Road, Bangalore- 560029. PAN: AAJCM 5415 D (Appellant)	vs	ACIT, Circle - 7(2)(2), Mumbai (Respondent)
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Present for:

Assessee by : Shri Chavali Narayanan (Hybrid)
Revenue by : Smt. Sanyogita Nagpal, CIT, DR

Date of Hearing : 21.11.2024

Date of Pronouncement : 11.12.2024

ORDER

PER AMARJIT SINGH, AM:

This appeal of the assessee for the assessment year 2017-18 is directed against the order dated 20.09.2023 passed u/s 250 of the Income Tax Act, 1961 by the ld. Commissioner of Income-tax (Appeal), NFAC, Delhi. The assessee has raised the following grounds of appeal:

"1. Ground No. 1-The impugned order passed by the learned NFAC is bad in law

1.1 On the facts and in the circumstances of the case and in law, the learned NFAC has erred, both on facts and in law, in confirming the disallowance of the expenditure under section 37(1) of the Act without providing any cogent reasoning and without taking into consideration any submissions filed by the Appellant, by merely making false statements/allegations in the order.

1.2 The order passed by the learned NFAC is bad in law in-as-much as the order was passed without giving opportunity of being heard in spite-of specific request being made.

2. Ground No. 2-Unsustainable disallowance under section 37(1) of the Act

21 That the learned NFAC has further erred both in facts and in law, in concluding that the impugned expenditure of Rs. 10,38,17,111 pertains to pre-commencement of business instead of adjudicating whether the expenditure is capital in nature as alleged by the learned Assessing officer ("AO").

2.2 On the facts and in the circumstances of the case and in law, the learned NFAC has erred, both on facts and in law, in confirming the disallowance of the expenditure incurred by the appellant under section 37(1) of the Act amounting to INR 10,38,17,111 on the ground that the same pertains to the period before the commencement of business.

2.3 That the learned NFAC has erred, both on facts and in law, in not accepting the fact that the Appellant was in existence since 8 January 2015 and also ignored the Assessment Orders passed for the AY 2016-17 and AY 2018-19, wherein there was no dispute with regard to the fact of Commencement of the Appellant.

2.4 That the learned NFAC has erred in stating that the all the direct and indirect tax expenses ought to have been capitalized as WIP and further erred in stating that the expenses are being incurred for developing the software.

2.5 That the learned AO and NFAC has erred in fact and in law in stating/observing that the Appellant had no intention to earn revenue and the expenses are not allowed as there was no revenue earned during the year under consideration.

2.6 That the learned NFAC has heavily relied on the decision Hon'ble Supreme Court in the case of Tuticorin Alkali Chemicals & Fertilizers Ltd vs CIT 227 ITR 172, which is distinguishable from the facts of the Appellant's case both on facts and in law.

3. Ground No. 3-Contravention of principles of consistency

3.1 On the facts and in the circumstances of the case and in law, the learned NFAC has erred, both on facts and in law, by disregarding the fact that the Appellant has debited the similar expenses in AY 2016-17 and AY 2018-19 and the same was accepted by the learned AO and by National Faceless Assessment Centre during the assessment proceedings of AY 2016-17 and AY 2018- 19 without making any disallowances under section 37(1) of the Act.

3.2 Without proving any change of facts and circumstances for the impugned AY 2017-18 vis-à- vis AY 2016-17 and AY 2018-19, the learned NFAC erred in disregarding the principles of consistency and confirming disallowance under section 37 of the Act.

4. Ground No. 4-Erroneous assertions and conclusion of facts

4.1 On the facts and in the circumstances of the case and in law, the learned NFAC erred in making a number of erroneous statements/assertions of facts, but not limited to the following:

- a) The Appellant did not recognize any revenue from their main business operations in AY 2018-19;*
- b) The Appellant declared in AY 2016-17 that the company commenced its activities, which is contrary to the facts on record;*
- c) The Appellant debited the large expenditure against the interest income without commencement of business.*

5. Ground No. 5-Inter-head adjustment of business loss

5.1 On the facts and in the circumstances of the case and in law, the learned NFAC erred in confirming the interest income of Rs. 78,40,198/- to be taxed as income from other sources without adjusting it against the business loss of the same assessment year.

5.2 That the learned NFAC has erred in law in not allowing the set off of business losses against the income from other sources of the same year in line with the provisions of section 71 of the Act.

6. Ground No. 6-Initiation of penalty proceedings under section 270A of the Act

6.1 On the facts and in the circumstances of the case and in law, the learned NFAC erred in upholding the action of the learned assessing officer for initiating penalty proceedings under section 270A of the Act.”

2. Fact in brief is that the return of income declaring loss of Rs. 9,44,54,033/- was filed on 23.10.2017. The case was subject to scrutiny assessment and notice u/s 143(2) of the Act was issued on 16.08.2018. The assessee company has developed a mobile application i.e. 'sharechat' which was available only on Android Operating System (Mobile). During the course of assessment, the assessee has furnished copy of P&L A/c, balance sheet along with its schedule. On perusal of the detail filed by the assessee company, the AO noticed that assessee has claimed expenditure under the head other expenses being 'Analytics and other Tools', 'Marketing and Promotion Expenses', 'Server Rent' etc. On perusal of the P&L A/c, the assessing officer noticed that assessee has not shown any Revenue from operation of the assessee company during the year under consideration whereas the assessee had booked huge expenses under the head revenue expenses. The assessing officer further observed that assessee company has incurred expenditure of Rs. 10,38,17,111/- without charging any revenue, the AO opined that there was no certainty of revenue generation to the assessee company. Therefore, the whole expenditure incurred by the assessee of Rs. 10,38,17,000/- was

treated as capital expenditure and claim of revenue expenditure was disallowed u/s 37(1)n of the Act.

3. The assessee filed appeal before the ld. CIT(A). The ld. CIT(A) has dismissed the appeal of the assessee.

4. During the course of appellate proceedings before us, the ld. Counsel referred the copy of P&L A/c for the year ended 31.03.2017 placed in the paper book filed by the assessee and the detail of other income replaced in Schedule 11 to the statement of P&L A/c of Rs. 78,40,198/- comprising profit on sale of investment, interest income and participation income reflected in the P&L A/c. The ld. Counsel also submitted that lower authorities have treated the expenses incurred by the assessee as capital nature expenses without disproving the submission of the assessee that the expenses were incurred after the commencement of the business of the assessee company as operating expenses. The ld. Counsel has also placed reliance on the decision of Hon'ble Supreme Court in the case of CIT vs Rajendra Prasad Moody on the proposition that it is not necessary that any income should infact have been earned as a result of expenditure.

5. On the other hand, the ld. DR referred page no. 17 to 20 of the order of ld. CIT(A) wherein the ld. CIT(A) has stated that except showing gain on sale of mutual fund and interest income there was no income earned and recognized out of business activities of the assessee company. The ld. DR also referred the return of income filed by the assessee on the point that assessee has not shown any income generated from the business carried out during the year under consideration. The ld. DR has supported the order of lower authorities.

6. Heard both the sides and perused the material on record. The assessing officer has completed the assessment for the year under consideration by disallowing the expenditure of Rs. 10,38,17,111/- debited to P&L A/c on the ground that assessee had not recognized any revenue from operation in the relevant assessment year. The assessee company was incorporated on 08.01.2015 under the Companies Act, 2013. The assessee company has developed a mobile application (app) i.e. 'sharechat' which was a social media app available on Android Operation System (Mobile) and I-phone Operation System (IOS). During the year under consideration, the assessee has claimed business loss to the amount of Rs. 9,44,54,033/- under normal provisions of the Act and book loss amounting to Rs. 9,58,66,303/- u/s 115JB of the Act. The nature of expenses incurred by the assessee as claimed in the P&L A/c are as under:

<i>Sl. No.</i>	<i>Expense Head</i>	<i>Amount in Rs.</i>	<i>Nature of Expense</i>
1	<i>Employee benefits expense</i>	33,820,268	<i>Expenditure towards salaries of employees & staff welfare. This payment is made on a monthly basis to the employees of the Company towards the services rendered. Payment of employee benefit expenses is revenue in nature does not create any intangible asset.</i>
2	<i>Server Rent</i>	28,437,634	<i>This expense pertains to payment made for consumption of space on the cloud for user data. Payment of server rent is revenue in nature and does not create any intangible asset.</i>
3	<i>Marketing & Promotion Exp</i>	15,285,191	<i>This expense is towards advertisement on digital medium to target new users. Through such advertisement, users are made aware about the app. Such expense is revenue in nature and does not create any intangible asset.</i>
4	<i>Analytics & Other Tools</i>	10,392,853	<i>This relates to expense incurred on tools which help in analysing the user data &</i>

			<i>day to day notifications in the application. It helps in understanding the user behavior to enable the Company deliver better solutions. Such expense is revenue in nature and does not create any intangible asset.</i>
5	<i>Office Rent</i>	<i>3,965,000</i>	<i>This pertains to expense incurred on account of rent of office space and is revenue in nature.</i>
6	<i>Communication Expense</i>	<i>3,846,159</i>	<i>Expenses towards Broadband (internet) charges and telephone Expenses.</i>
7	<i>Rates & Taxes</i>	<i>2,587,730</i>	<i>Relates to statutory payments required to be paid under various laws. Out of this, Rs 11,66,943 pertains to service tax and Rs 8,38,003 pertains to equalization levy.</i> <i>Rs 2,84,107 (not included above) is already disallowed as it is incurred in relation to raising/ increasing authorized capital</i> <i>In any case, payment of rates & taxes is revenue in nature and does not create any intangible asset.</i>
8	<i>Legal & Professional Fees</i>	<i>1,214,887</i>	<i>Relates to Legal & Professional Fees for services received during the year</i> <i>Out of this Rs 11,71,282 is already disallowed as it is incurred in relation to raising/increasing authorized capital</i>
9	<i>Depreciation</i>	<i>1,056,282</i>	<i>Relates to depreciation on fixed asset and does not result in creation of any tangible asset</i>
10	<i>Total</i>	<i>100,606,002</i>	<i>Total expenses in P&L account is Rs. 103,817,111/-</i>

7. It is evident from the nature of expenses as referred above that these expenses were incurred during the ordinary course of the business of the assessee company. The expenses were mainly incurred towards salary of employees and staffs, payment of server rent, marketing and promotion expenses, office rent, communication expenses etc. The app developed by the assessee company was downloaded 53,92,801 times by 31.03.2017 which was 13.48 times as

compared to previous year which demonstrate that assessee company had already commenced its business. However, the assessee company has not charged any fees to its user for down loading the app as it was focusing on increasing the user base. These material facts show that business of the assessee company have already been commenced and the assessee has incurred the various operating expenditure of Rs. 10,38,17,111/- as referred above. From the break-up of the nature of expenditure given, it is evident that this expenditure was not incurred for acquisition of any capital asset and same were of the nature of operating expenditure which were incurred after the commencement of the business of the assessee company. It is also established from the financial account filed by the assessee that expenditure mentioned under the head employees benefit expenditure, financial cost, depreciation and amortization expenses and other expenses were incurred for the ordinary operation of the assessee company and same were of revenue nature. The assessing officer has not brought any material on record to prove that assessee has not commenced its business and also not disproved the undisputed fact that assessee has already developed the mobile app which had been down loaded number of times during the year as discussed supra in this order. We have also perused the judicial pronouncement referred by the ld. Counsel in the case of Rajendra Prasad Moody (1978) 115 ITR 519 (SC) wherein on the proposition that it is not necessary that any income should infact has been earned as a result of expenditure.

8. After taking into consideration, the facts and circumstances as discussed above in this order, we consider that decision of ld. CIT(A) in sustaining the disallowance of expenditure by the assessing officer is

not justified, therefore, grounds no. 1 to 5 of appeal filed by the assessee are allowed.

9. Ground No. 6 of Appeal: On initiation of penalty is premature at this stage, therefore, the same is dismissed.

10. In the result, the appeal of the assessee is allowed.

Order pronounced in the open court on 11.12.2024

Sd/-

**(SAKTIJIT DEY)
VICE PRESIDENT**

Sd/-

**(AMARJIT SINGH)
ACCOUNTANT MEMBER**

Mumbai: 11.12.2024
Biswajit, Sr. P.S.

Copy to:

1. The Appellant:
2. The Respondent:
3. The CIT,
4. The DR .

//True Copy//

By Order

Assistant Registrar
ITAT, Mumbai Benches, Mumbai