

IN THE INCOME TAX APPELLATE TRIBUNAL

"G" BENCH, MUMBAI

BEFORE MS. PADMAVATHY S, ACCOUNTANT MEMBER

SHRI SANDEEP SINGH KARHAIL, JUDICIAL MEMBER

ITA No.4006/MUM/2024
(Assessment Year : 2017-18)

**Shapoorji Pallonji Energy (Gujarat)
Private Limited,**

41/44, SP Centre, Minoo Desai Marg,
Colaba, Mumbai - 400005
PAN – AAMCS7570C

..... Appellant

v/s

**DCIT, Circle- 3(3)(1),
Mumbai**

..... Respondent

Assessee by : Shri Dharmesh Shah
Mitali Parekh

Revenue by : Shri Arun Kanti Datta, CIT(DR)

Date of Hearing – 10/06/2025

Date of Order – 29/07/2025

ORDER

PER SANDEEP SINGH KARHAIL, J.M.

The assessee has filed the present appeal against the impugned order dated 05.06.2024, passed under section 250 of the Income-tax Act, 1961 (*"the Act"*), by the learned Commissioner of Income Tax (Appeals), National Faceless Appeal Centre, Delhi (*"learned CIT(A)"*), for the assessment year 2017-18.

2. In this appeal, the assessee has raised the following grounds: –

"1. The learned NFAC / CIT Appeal erred in not considering the submission made by the appellant vide letter dated 19th February 2021.

2. *The learned NFAC / CIT Appeal erred in upholding the action of AO in holding that expenses incurred by the Appellant are pre-operative in nature and hence, not allowable as deduction.*
3. *The Appellant prays that the treatment of expenses incurred as pre-operative expenses is erroneous and unwarranted.*
4. *The learned NFAC has erred in treating income of Rs.12,34,61,000/- as "Income from Other Sources" as against "Income from Business and Profession".*
5. *The Appellant prays that the income of Rs. 12,34,61,000/- be treated as "Income from Business or Profession" instead "Income from Other Sources".*
6. *The learned NFAC has erred in treating the amount of Rs.15,47,000/- being exchange fluctuation in respect of foreign currency loan given to overseas party and hence, not in nature of taxable income.*
7. *The Appellant prays that the addition of Rs. 15,47,000/- to total income should be deleted.*
8. *The learned NFAC has erred in restricting the brought forward business loss to Rs.1,50,64,225/-.*
9. *The Appellant prays that the set off of brought forward business losses to be granted for Rs.10,59,57,718/-.*
10. *Each one of the above grounds of appeal is without prejudice to any of the others."*

3. Ground no.1 is general and therefore the same needs no separate adjudication.

4. Grounds no.2 and 3 raised in assessee's appeal pertain to disallowance of expenditure incurred by the assessee, which are debited to the profit and loss account, as pre-operative in nature.

5. The brief facts of the case as emanating from the record are: the assessee is a company incorporated under the provisions of the Companies Act, 1956 and is engaged in the business of setting up the Thermal Power Project. For the year under consideration, the assessee filed its return of

income on 02.11.2017, declaring a total income of ₹ 3,38,68,950 after setting off brought-forward losses of ₹ 10,59,57,718 and declaring a book loss of ₹ 10,55,88,530 under section 115JB of the Act. The return filed by the assessee was selected for scrutiny under the CASS, and statutory notices under section 143(2) and section 142(1) of the Act were issued and served on the assessee. During the assessment proceedings, it was observed from the details filed by the assessee that the assessee has not earned any income from its regular business activity, and the entire income credited in the statement of profit and loss was on account of other income. Against the said income, the assessee has claimed an expenditure of ₹ 23,19,15,000. Accordingly, the assessee was asked to justify its claim of expenditure with necessary supporting evidence. The assessee was also asked to show cause as to why the expenditure should not be disallowed by treating the same as "*pre-operative expenses*", in the absence of any business activity/revenue. In response, the assessee submitted that it incurred expenditure amounting to ₹ 32,03,46,000 during the year under consideration, out of which expenditure amounting to ₹ 8,84,31,000 was transferred to Capital Work in Progress, and the balance expenditure amounting to ₹ 23,19,15,000 was claimed in the profit and loss account statement for the year ending 31.03.2017.

6. The Assessing Officer ("AO"), vide order dated 18.12.2019 passed under section 143(3) of the Act, disagreed with the submissions of the assessee and held that in the present case there is no dispute regarding the

fact that the entire income credited in the profit and loss account is nothing but other income and the same has no direct relation to the main business activity of the assessee. The AO further held that it is an undisputed fact that the assessee has not derived any income from its business operations, and it has considered the part of the expenditure debited in the profit and loss account as work in progress and claimed part of the expenditure totalling ₹ 23,19,15,000 as revenue expenditure. The AO, by referring to the submission of the assessee that the power project normally takes 4 to 6 years for completion, held that there is no question of generating any revenue and therefore, the entire expenditure incurred till the completion of the project is required to be treated as pre-operative expenditure.

7. The learned CIT(A), vide impugned order, upheld the findings of the AO in treating the expenditure debited to the profit and loss account as pre-operative expenditure. Being aggrieved, the assessee is in appeal before us.

8. During the hearing, the learned Authorized Representative ("*learned AR*") submitted that the assessee was incorporated in the year 2008 with the object setting up of Thermal Power Project, and in this regard, had undertaken various activities such as applying for procurement of power for long term from Gujarat Urja Vikas Nigam Ltd. ("*GUVNL*"), entering in Power Purchase Agreement with GUVNL, acquisition of plots of land aggregating to 198.82 hectare, availing permission/clearances from various authorities, acquisition of equipment and other assets for running the business activity, deployment of project team, technical staff, administrative staff, etc., for the

project. Thus, learned AR submitted that the business of the assessee had already been set up and the assessee was entitled to claim deduction on account of expenses incurred during the year, even though no income was earned by the assessee. The learned AR further submitted that the expenditure directly attributable to the construction of the power plant was capitalised to the Capital Work in Progress and transferred to the Capital Work in Progress account. The learned AR by referring to the orders passed in preceding years submitted that identical disallowance was made in the assessment year for the assessment years 2013-14 and 2015-16 by treating the expenditure as pre-operative in nature, which was deleted by the learned CIT(A) following the decision of the coordinate bench of the Tribunal rendered in assessee's sister concern case.

9. The learned Departmental Representative ("*learned DR*"), vehemently relying upon the orders passed by the lower authorities, submitted that during the year under consideration, the assessee was still in the process of establishing a power plant and had no revenue from any business activity during the year under consideration. The learned DR thus submitted that the expenses incurred prior to the commencement of business or commercial operations have been correctly treated as pre-operative by the lower authorities. The learned DR further submitted that, on the one hand, the assessee chose to capitalise ₹ 8.84 crore of expenditure and transfer it to the Capital Work in Progress. However, on the other hand, without any basis, the assessee claimed ₹ 23.19 crore as revenue expenditure.

10. We have considered the submissions of both sides and perused the material available on record. In the present case, there is no dispute regarding the business profile of the assessee, that it is engaged in setting up the Thermal Power Project. Since during the year under consideration, the assessee did not earn any income from its normal business activity and the entire income credited in the statement of profit and loss was on account of other income, which had no direct relation to the main business activity of the assessee, the AO treated the expenditure amounting to ₹ 23,19,15,000/- debited to the profit and loss account as pre-operative expenditure and rejected the claim of the assessee. The primary contention of the assessee is that the allowability of expenditure is not dependent on earning of income during the year, and for allowability of the same, the expenditure must be incurred "*for the purpose of business*". Thus, as per the assessee, so long as the expenditure is incurred for the purpose of business, it is to be allowed as a deduction, irrespective of the fact that the assessee had any income from its business operations during the year under consideration. It is further the plea of the assessee that the expenditure incurred by the assessee after setting up of the business and before the commencement of the business is allowable and since in the present case, the assessee after its incorporation on 28.05.2008 had undertaken various steps for setting up of the Thermal Power Project in the state of Gujarat, therefore, the expenditure debited to the profit and loss account, during the year under consideration cannot be considered as pre-operative in nature.

11. In this regard, during the hearing, reference was made to the Power Purchase Agreement entered into by the assessee with GUVNL on 15.05.2010 pursuant to the bidding process for sale and supply of electricity in bulk for the aggregate contract capacity of 800 MW to GUVNL, forming part of the paper book-II from pages 145-251. We further find that the assessee purchased several plots of land for a total amount of ₹ 104.98 crore over the period of the year after its incorporation till the year under consideration, which is duly reflected in the financial statements of the assessee for the year under consideration at page 16 of the paper book-I. The assessee also placed on record the necessary permission/clearance from relevant authorities, such as the Airport Authority of India, Gujarat Energy Transmission Corporation Limited, Gujarat Maritime Board, and Gujarat Pollution Board, in respect of the aforesaid Thermal Power Project in the State of Gujarat. We find that the assessee has also recorded costs in respect of the acquisition of equipment and other assets, as well as design and building contracts, during the year under consideration, apart from expenditure incurred on employee benefits for the project team, technical staff, administrative staff, and financial personnel, among others, in its financial statement. Therefore, on the basis of all the aforesaid evidence, it is the plea of the assessee that its business of setting up the Thermal Power Project was already set up, and all the expenditure after setting up the business is allowable.

12. We find that the Hon'ble Bombay High Court in *Western India Vegetable Projects Ltd. vs. CIT*, reported in (1954) 26 ITR 151, drawing the fine distinction between "*setting up of business*" and "*commencement of business*" held that when a business is established and is ready to commence then it can be said that the business is set up and all expenditure incurred after setting up of the business and before the commencement of the business would be permissible deduction. The relevant observations of the Hon'ble Bombay High Court in *Western India Vegetable Project Ltd. (supra)* are reproduced as follows: -

"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 an 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 deductions under section 10(2)."

13. Therefore, in case of a business, the date of setting up of business is relevant and only the expenditure incurred after the business is set up can be claimed as permissible deduction, and all the expenditure till the time of business is set up, even if revenue in nature, would have to be capitalised.

14. We find that while deciding the similar issue in case of a taxpayer who was engaged in establishing captive power plant, the Co-ordinate bench of the Tribunal in *Orient Green Power Company Ltd. vs. ACIT*, reported in (2022) 138 taxmann.com 303 (Chennai-Trib), after considering various steps taken by the taxpayer for setting up the business held that the

business has already been set up as the assessee undertook of preliminary steps to commence the business. The relevant findings of the Co-ordinate bench of the Tribunal, in the aforesaid decision, are reproduced as follows: -

"9. Keeping in mind aforesaid principles, we find that the assessee has been incorporated during 2006. The main objective of the assessee was to generate electrical power by convention and non-conventional methods including coal, gas lignite oil, bio-mass, water, thermal, solar, hydel, geo-hydel, wind and tidal waves. The assessee was also engaged to establish captive power plant on a co-operative basis for a group of industrial and other consumers and supply to the participants in the cooperative effort either directly or through the transmission lines of the state Electricity Board or other authorities by entering into appropriate arrangements. Thus, the business objective could be achieved either directly or through joint ventures in association with other entities.

10. The perusal of financial statements, as placed on record, would show that the assessee has substantially increased its gross block from Rs. 2.16 lacs as on 31-3-2008 to Rs. 329.49 Lacs during this year which has shown further substantial increase in FY 2009-10. The major addition during FY 2008-09 is land for Rs. 320.94 Lacs which is also evident from sale deed of land as placed on page nos. 246 to 252 of the paper-book. The same would show that the assessee had already acquired the land to carry out the business activities. The nature of major expenses incurred by the assessee is employee's cost, misc. cost and depreciation which have shown significant increase during the year. The same would show that the assessee had hired the staff to carry out the business activities. The other expenses include expenses in the nature of rent, rates & taxes, travel, legal & professional charges etc. which would show the readiness of the business to commence the activities.

11. Further, the assessee, vide approval letter dated 11-4-2008 (page nos. 140-141 of the paper-book), had received registration for 10MW capacity biomass-based power plant in district Narsingpur from a MP Govt. undertaking i.e. Madhya Pradesh Urja Vikas Nigam Ltd. The registration was valid for 6 months during which the assessee was required to submit Assessment report, detailed project report which would have all the relevant details of technology and the detail of land as identified for the project. The assessee was required to submit a map indicating the location of the project site along with details of water availability. Pursuant to the same, the assessee had submitted detailed project report (page nos. 142 to 245 of the paper-book) as early as during October, 2008 giving all the vital details including technological framework and plant configuration, construction & layout including operations and maintenance. The list of the Equipments, cost of project, means of finance, profit projections etc. were also detailed in the report.

12. Proceeding further, the assessee has issued letter of intent to a vendor namely M/s Shriram EPC Limited to carry out Engineering, procurement and

construction (EPC) work for 10MW Bio-Mass Power Plant on 23-5-2009 wherein the vendor was to undertake EPC work after placing orders for necessary equipment (253-254 of the paper- book). The assessee had also made an application for environment clearance certificate from state level expert appraisal committee to carry out the project. The assessee also entered into memorandum of agreement with M/s D.Y. Patil Sahakari Sakhar Karkhana Ltd. to set-up 20MW cogeneration plant utilizing the bagasse generated from the Sugar Plant on Built, Operate and Transfer basis at the premises of the contractee. The detailed project report of the same was submitted by the assessee as early as June, 2008. The agreement in this respect was executed by the assessee during October, 2008 and the lease agreement, in this respect was executed on 16-1-2009. The assessee also entered into a power purchase agreement with Tata Power Trading Co. Ltd. on 22-12-2008 wherein the assessee agreed to sell the power generated from its bagasse-based cogeneration power plant. To facilitate the same, the assessee applied to Maharashtra State Electricity Transmission Company Ltd. requesting for transmission line for evacuation of power from the said power plant. Lastly, the assessee could set-up power plants on co-operative basis through their Special purpose vehicles (SPV). Pursuant to the same, the assessee had advanced funds for operating and managing those SPVs which were, in turn, advancing the assessee's business.

13. On the basis of all these facts and documentary evidences, it could be said that though the assessee's business had not commenced but the business had already been set-up and the assessee undertook all preliminary steps to commence the business. The gestation period, in the kind of business in which the assessee was engaged, would generally be long and it is quite natural that it would take substantial time to start the actual business operations and generate business income. Quite clearly, without necessary approvals and agreements, the assessee could have never been able to commence its business. All these documents were road-map to starting of actual business operations. Nevertheless, the business was established by procurement of land, staff etc. The assessee had recruited technical personnel for setting-up the power projects. The assessee had all the approvals, permissions in-hand and was in the process of commencing the business. The assessee had deployed technical personnel, obtained various approvals, placed purchase orders and also signed long-term Power Purchase Agreements with the clients. The signing of all these agreement would be important activity and very much integrated to the activities of the business of the assessee.

14. Upon perusal of assessment orders, we find that Ld. AO has based his reasoning solely on the fact that assessee-company's bio-mass power plant was synchronized to grid only from 4-7-2011. Therefore, the assessee was not ready to produce the power till 4-7-2011 and hence, the business was not set-up. However, the said reasoning stresses the proposition that expenditure could not be allowed till the generation of income. The said reasoning overlooks the various vital documentary evidences furnished by the assessee in support of the fact that the business had already been set-up. We are of the considered opinion that the generation of actual business income was not an essential element to allow the business expenditure. What was required to be seen was whether the business had been set-up or

not. In view of our observations in the preceding paragraphs as well as keeping in view the ratio of various judicial pronouncements as cited before us by Ld. AR during the course of hearing (preceding para-2), it could safely be said that the assessee's business had set-up during AY 2009-10 itself and therefore, the expenditure as claimed by the assessee would be allowable deductions."

15. It is also pertinent to note that in the aforesaid decision, the Co-ordinate Bench of the Tribunal also emphasised the aspect that the generation of actual business income is not an essential element to allow the business expenditure, and the only criterion which needs to be looked into is whether the business has been set up.

16. Therefore, from the perusal of the relevant facts of the present case as noted above, in the light of the decisions cited (*supra*), we are of the considered view that the business of the assessee of setting up Thermal Power Project was already set up and thus the expenditure incurred for the purpose of business after setting up of the business are allowable for deduction. Further, we are also of the considered view that the mere fact that the assessee did not derive any income from its business operation is not a condition precedent to allow the expenditure incurred for the purpose of business.

17. As noted in the foregoing paragraphs, the AO merely treating the expenditure debited to the profit and loss account as pre-operative, disallowed the same without examining the nature and details of these expenditures incurred by the assessee. As we have come to the conclusion that business of the assessee has been set up and the expenditure incurred

for the purposes of business is allowable, accordingly we direct the jurisdictional AO to allow the expenditure debited by the assessee to its profit and loss account after examining the nature and details of such expenditure if the same are found to have been incurred for the purpose of business. For this limited examination, this issue is restored to the file of the jurisdictional AO. As a result, grounds no.2 and 3 raised in assessee's appeal are allowed for statistical purposes.

18. The issue arising in grounds no.4 and 5, raised in assessee's appeal, pertains to treating the income of ₹ 12,34,61,000 as "*income from other sources*" as against "*income from business and profession*".

19. The brief facts of the case pertaining to this issue, as emanating from the record, are: During the year under consideration, the assessee earned interest income and other income on the funds parked as fixed deposits with the Banks. The AO, vide its order passed under section 143(3) of the Act, treated such income, which comprised interest on bank deposits, interest from related parties, and miscellaneous income, as income from other sources. Further, the AO also rejected the claim of the assessee under section 57(iii) of the Act on the basis that the assessee has not incurred any expenditure for earning this income.

20. The learned CIT(A), vide impugned order, upheld the conclusion of the AO on this issue and treated the income of ₹ 12,34,61,000 as income from other sources. Being aggrieved, the assessee is in appeal before us.

21. We have considered the submissions of both sides and perused the material available on record. During the year under consideration, the assessee received interest on bank deposits, interest from related parties and miscellaneous income, totalling ₹ 12,34,61,000, which was considered as business income by the assessee. It is an undisputed fact that this interest income was earned by the assessee from deposits maintained with the bank and loans/advances given to the sister concerns. According to the assessee, the advances given to the sister concerns were made from the funds generated by the issuance of non-convertible debentures, on which the assessee incurred finance costs. In the present case, it is pertinent to note that during the year under consideration, the assessee did not earn any revenue from operations, and as stated elsewhere, the same was the basis for disallowing the expenditure as pre-operative expenditure. It is also pertinent to note that in the present case, it is an accepted fact that the borrowed funds were not linked to the power project. As per the assessee, the funds were received for general business purposes. Thus, there is no material available on record to prove that granting of advances/loans to the sister concerns and maintaining the deposits in the bank was for the purpose of business. Therefore, we are of the considered view that the amount of ₹ 12,34,61,000 earned by the assessee from interest on bank deposits, interest from related parties and miscellaneous income can only be treated as "*income from other sources*".

22. From the perusal of the profit and loss account for the year ending 31.03.2017, we find that the assessee also incurred interest expenditure/finance costs. Accordingly, as the afore-noted interest income has been considered as income from other sources, therefore, we direct the jurisdictional AO to allow the deduction of interest expenditure/finance costs as per the provisions of section 57(iii) of the Act after examining the nexus of the same with interest income. We further direct that no order shall be passed without affording reasonable and adequate opportunity of hearing to the assessee. We further find that this interest expenditure/finance costs also forms part of the total expenditure of ₹ 21,54,24,243 debited by the assessee to its profit and loss account. As we have directed allowance of deduction of expenditure debited to the profit and loss account after necessary verification, we further direct that the interest expenditure/financial costs be allowed as deduction only once after necessary examination, i.e., either as an expenditure incurred for the purpose of business or as an expenditure allowable under section 57(iii) of the Act, if it satisfies necessary criterion. Grounds no.4 and 5 raised in assessee's appeal are decided accordingly.

23. The issue arising in grounds no.6 and 7, raised in assessee's appeal, pertains to addition on account of gain due to foreign exchange fluctuation in respect of loans given to overseas party.

24. We have considered the submissions of both sides and perused the material available on record. During the year under consideration, due to

foreign exchange fluctuations, the assessee earned mark-to-market gains in respect of loans given by the assessee to the overseas party. There is no evidence on record to suggest that the loan to the overseas party was on the revenue account. Since the foreign exchange fluctuation gain, in the present case, is only due to the reinstatement of the accounts at the end of the year by considering the year-end rate of exchange, no question arises for considering the said gain as income of the assessee for the year under consideration. Accordingly, we direct the AO to delete this addition. As a result, grounds no.6 and 7 raised in assessee's appeal are allowed.

25. Grounds no.8 and 9, raised in assessee's appeal, pertain to set off of brought forward business losses. Since the issue raised in these grounds is consequential in nature, the jurisdictional AO is directed to consider the same, as per law, while computing the total income of the assessee in compliance with the directions in this order. As a result, grounds no. 8 and 9 raised in assessee's appeal are allowed for statistical purposes.

26. The assessee, vide its application, sought admission of the following additional grounds of appeal: -

"1. On the facts and circumstances of the case, the Ld. CIT(A) ought to have allowed the expenses while computing the total income of the appellant. The Ld. CIT(A) also ought to have appreciated that the business of the appellant had already commenced in the earlier years.

2. Without prejudice to the above, if the expenses are held not allowable as deduction, on the facts and circumstances of the case, the Ld. CIT(A) ought to have appreciated that the excessive disallowance inadvertently made in the computation should have been reduced and the income ought to have been calculated accordingly."

27. In view of our findings in the foregoing paragraphs, these additional grounds need no separate adjudication.

28. In the result, the appeal by the assessee is allowed for statistical purposes.

Order pronounced in the open Court on 29/07/2025

**Sd/-
PADMAVATHY S
ACCOUNTANT MEMBER**

**Sd/-
SANDEEP SINGH KARHAIL
JUDICIAL MEMBER**

MUMBAI DATED: 29/07/2024

Prabhat

Copy of the order forwarded to:

- (1) *The Assessee;*
- (2) *The Revenue;*
- (3) *The PCIT / CIT (Judicial);*
- (4) *The DR, ITAT, Mumbai; and*
- (5) *Guard file.*

By Order

Assistant Registrar
ITAT, Mumbai