

**आयकर अपीलीय अधिकरण, मुंबई “सी” खंडपीठ**  
**Income-tax Appellate Tribunal -“C”Bench Mumbai**

सर्वश्री राजेन्द्र,लेखा सदस्य एवं पवनसिंह,न्यायिक सदस्य

**Before S/Sh.Rajendra,Accountant Member and Pawan Singh,Judicial Member**

**आयकर अपील सं./I.T.A./5970/Mum/2012,निर्धारण वर्ष /Assessment Year: 2008-09**

PIZI Marketing Services Pvt. Ltd. (formerly known as PHL Pharma Pvt. Ltd.) Piramal Tower, Ganpatrao Kadam Marg, Lower Parel,Mumbai-400 013. <b>PAN:AACCN 5346 B</b>	Vs.	DCIT , Circle-8(2) Aayakar Bhavan, 2 <sup>nd</sup> floor, M.K. Road Mumbai-400 020.
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**आयकर अपील सं./I.T.A./6084/Mum/2012,निर्धारण वर्ष /Assessment Year: 2008-09**

DCIT , Circle-8(2) Mumbai-400 020.	Vs.	PIZI Marketing Services Pvt. Ltd. (formerly known as PHL Pharma Pvt. Ltd.), Mumbai-400 013.
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(अपीलार्थी /Appellant)

(प्रत्यर्थी / Respondent)

**Revenue by:S/Shri M. Dayasagar-CIT-DR and Vijay Kumar-DR**

**Assessee by: Shri Yogesh Thar**

**सुनवाई की तारीख / Date of Hearing: 28.06.2016**

**घोषणा की तारीख / Date of Pronouncement: 29.07.2016**

**आयकर अधिनियम,1961 की धारा 254(1)के अन्तर्गत आदेश**

**Order u/s.254(1)of the Income-tax Act,1961(Act)**

**लेखा सदस्य राजेन्द्र के अनुसार PER RAJENDRA, AM-**

Challenging the order,dated 27/07/2012,of the CIT(A)-17,Mumbai the assessee and the Assessing Officer(AO)have filed cross-appeals for the year under consideration.Assessee-company,engaged in the business of consultancy and detailing services,filed its return of income on 29/09/2008,declaring a loss of Rs.34.73 crores.The AO completed the assessment on 27/12/2010,u/s.143(3) of the Act,determining the income of the assessee at loss of Rs. 10,00,82,110/-.

**ITA/6084/MUM/2012:**

**2.**First ground of appeal,raised by the AO,is about deleting the disallowance of Rs.9.31 crores,made u/s.40 (a) (ia) of the Act.During the course of assessment proceedings, the AO found that the assessee had reimbursed the sum of Rs. 12. 18 crores to NPHL,as per the terms of the MOU, that the assessee had not detected any tax before making the payment, it argued before the AO that there was no element of profit in the sum reimbursed to NPHL.The AO, however, disagreed with the assessee and referring to the terms of the MOU,he held that relationship between the assessee and NPHL was that of contract and contrac -tee,that the provisions of section 194C were attracted on the reimbursed the amount.After giving credit of Rs.2.87 crores, for the sum already disallowed as the incorporation expenses,the AO disallow -ed the balance amount of Rs.9.31 crores u/s.40 (a) (ai) of the Act.

**2.1.** Aggrieved by the order of the AO, the assessee preferred an appeal before the First Appellate Authority (FAA) and argued that there was no contractor-contractee relationship between the assessee and NPHL, it was purely a reimbursement of expenditure incurred for it on which no tax was liable to be deducted at source, that there was no element of income in these reimbursements. The assessee relied upon cases of Industrial Engineering Projects Private Limited (2021TR1014), Coca-Cola India (7SOT71) and Bangalore International Airport Ltd. (116 ITD446). After considering the submission of the assessee and the assessment order, the FAA held that as per the terms of the MOU it was a simple case of reimbursement of expenses by the assessee, that there was no evidence to show that an element profit was embedded in the said reimbursement, that the MOU did not establish a contractor-contractee relationship to be hit by the provisions of section 194C of the Act. Relying upon the cases, referred by the assessee, the FAA held that TDS provisions would not apply to the reimbursement of expenses. Finally, he deleted the addition made by the AO.

**2.2.** During the course of hearing before us, the Departmental Representative (DR) supported the order of the AO. The Authorised Representative (AR) stated that payment was purely reimbursement and hence provisions of section 194C were not applicable.

**2.3.** We have heard the rival submissions and perused the material before us. We find that the AO had made the disallowance of Rs. 9.31 crores, as he was of the opinion that there was contract-contractee relationship between the assessee and NPHL. After going through the MOU, we are of the opinion that there is nothing in the document to prove that assessee was a contractor. The assessee had agreed to reimburse the expenditure incurred by the other party. Provisions of chapter XVIIIB of the Act are not applicable for reimbursement expenses. In the case under consideration, the FAA had given a categorical finding of fact that payments in question were reimbursement. Therefore, we are of the opinion that there is no need to interfere with the order of the FAA. Confirming his order, we decide first ground of appeal against the AO.

**3.** Second ground of appeal is about disallowance of Rs. 7.05 crores, under the head advertising and sales promotion. During the assessment proceedings, the AO noted that assessee had incurred an expenditure of Rs. 14.27 crores towards advertisement and sales promotion. The assessee contended that it was required to make said expenditure as per the terms of the MOU, that the said expenditure was mainly with regard to samples, printing material and other promotional items, that it was incurred for the purpose of business and was allowable as

per the provisions of section 37 (1) of the Act, that the expenditure did not bring into existence any asset and was therefore revenue nature. However, the AO did not agree with the submissions made by the assessee and held that the amount was incurred for building brand/goodwill of NPHL, that the expenditure incurred by the assessee towards the detailing services was not for its own business but for the business of NPHL, that the expenditure was incurred for expansion of the business and therefore was A nature, that the benefit of the expenditure went to NPHL, that the expenditure on advertisement and same promotion could not be allowed as same was not incurred for business purposes. Out of the total expenditure of Rs.21.75 Crores, the AO disallowed expenditure of Rs.7.05 crores.

**3.1.** During the course of hearing before the FAA, the assessee argued that expenditure was incurred wholly and exclusively for the purpose of its own business, that it was part of the profit earning process and was incurred to enable it to carry on its business more profitably, no asset or advantages of enduring nature had been brought into existence by incurring the said expenditure, that the expenses were incurred to promote sales and increase brand visibility and the doctor/ consumers all over India. The assessee relied upon the cases of Agra Beverage Corporation (200 Taxman 43), Eastern Investments Ltd. (20 ITR 1) and Sales Magnesite (P.) LTD. (81 Taxman 334). After considering the submission of the assessee, the FAA held that the expenditure incurred on advertisement and sale promotion was revenue in nature. He referred to the case of Kopran Ltd. (48 SOT 225). He also discussed the issue of benefit arising out of the expenditure to NHPL vis-a-vis the assessee and observed that there was no dispute about incurring of expenditure as per the terms of the MOU, that the expenditure incurred by the assessee was allowable u/s. 37 (1) of the Act, even if it would indirectly benefit the NPHL.

**3.2.** Before us, the DR supported the order of the AO and the AR relied upon the order of the FAA. We find that the AO had not doubted the genuineness of incurring of expenditure - his only objection was that the expenditure incurred by the assessee benefited NPHL. He also held that the expenditure was capital in nature. We are unable to agree with the AO, as the expenditure incurred on account of advertisement and sale promotion never brings any asset of enduring benefit - it is a pure and simple revenue expenditure. No authorities required to hold the expenses incurred for promoting own business have to be allowed as per the provisions of section 37(1) of the Act. Details of products given as sales promotion article and print material for sales promotion (pg.148-50 of PB) clearly prove that the expenditure incurred by the assessee was for its own business.

Here we would like to refer to the matter of N.G.C.Network (India) P. Ltd.(368 ITR 738) of the Hon'ble jurisdictional High Court.Facts of the case were that the assessee was a company incorporated in India and engaged in the business of distribution of television channels. It also acted as airtime advertising sales representative for its principals. For the assessment year 2005-06, it declared a total income of Rs.4,85,16,730/-and also filed Form 3CEB in view of the inter -national transactions with its associated enterprises. The items mentioned in Form 3CEB were referred to the TPO,who accepted the arm's length price declared by the assessee.The AO noted that the assessee had incurred expenses towards advertising and publicity which benefited not only the assessee but also the foreign principals.Since it did not disclose such benefit to the members as part of Form 3CEB,he held that the entire expenditure under the head advertis-ing and promotion,amounting to Rs.6.21crores was not allowable as deduction u/s.37(1) of the Act.He restricted the deduction,u/s.37(1) of the Act, to 33.33% of the expenditure claimed.The FAA held that the entire expenditure was allowable as revenue expenditure and that since the payments were made to Indian residents they were not covered in Form 3CEB as section 92 covers only international transactions.The Third Member of the Tribunal upheld the decision of the FAA.On appeal the main grounds on which the Revenue had questioned the order of the Tribunal were non-disclosure in Form 3CEB of the fact that the principal was also a beneficiary of the advertising expenses,that the advertising and promotional expenses were not wholly for the benefit of the assessee but also the foreign principal which was an associated enterprise, that advertising and publicity expenses were far higher than the revenue earned and, lastly, that although the foreign principals,i.e.,associated enterprise benefited from advertising and publicity no compensation was paid by the foreign principals to the assessee to avail of such benefits.Dismissing the appeal the Hon'ble Court held as under:

*“.....the contention that there was no proper disclosure of the benefit before the Transfer Pricing Officer could not be a reason to entertain the questions and the order of the Transfer Pricing Officer was final. The assessee was an agent of the foreign principal and the principal would naturally benefit from advertising carried on by the agent in India. However, these benefits were not ascertainable. The benefits were not ascertainable or taxable in view of the extra territory. The assessee had not suppressed any information. It offered to tax its income from both business, namely, distribution business as well as advertisement and promotion business. The Assessing Officer had proceeded to grant 33.33 per cent. of the total advertising expenses as allowable deduction. There was no justification for such restriction of the expenses. Furthermore, the Revenue's case was that the fact of the foreign principal benefiting had been disclosed in Form 3CEB and the Transfer Pricing Officer “could” have taken a different view. Admittedly, therefore, the Transfer Pricing Officer had followed a possible view which could not now be faulted.*

*(ii) That there was no doubt that in view of the decision of the Supreme Court it could not be said that the expenditure was not wholly or exclusively for benefit of the assessee. **The mere fact that the foreign principals also benefited was not ground to deny the deduction under section 37(1)** .(emphasis by us).Furthermore, all the amounts earned by the assessee were brought to tax, especially in view of the fact that the payment of expenses were made to the Indian residents and their payments were not required to be included in Form 3CEB since section 92 which governs the effect of Form 3CEB covers only international transactions. The assessee's income from subscription fee was variable and through commission received on the advertising sales was 15 per cent. of the value of ad-sales. The Assessing Officer's contention that the assessee received fixed income was not justified and there was certainly a direct nexus between the amount spent on advertising and publicity and the assessee's revenue.*

*(iii) That it was also not necessary that the foreign enterprise must compensate the Indian agent for the benefit it received or may receive from the advertisement and promotion of its channels by the agent in India. The agent in India earned commission from ad-sales and distribution revenue, both of which had sufficiently compensated the assessee. The Revenue could not be expected to determine the sufficiency of the compensation received by the agent and as such there was any justification in this ground either."*

Considering the above,we are of the opinion,that there is no need to interfere with the orders of the FAA,so,confirming his order,we decide the second ground of appeal against the AO.

**ITA/5970/Mum/2012:**

**4.**First Ground is about disallowance of loss pertaining to period prior to incorporation. During the course of assessment proceedings,the AO noted that the assessee company was incorporated on 15.6.07 in the name of MBIL Pharma Services Pvt.Ltd.(MBIL),that on 14.08.2008,the name of the company was changed to PHL Pharma Pvt. Ltd.,that expenses pertaining to period 01.04. 07 to 15.6. 2007,i.e. prior to the date of incorporation,had been included.He directed the assessee to file explanation in that regard.He found that a company called NPIL Healthcare Pvt.Ltd.(NPHL),was incorporated to do the business of manufacture, promote and market Mass Market Branded Formulation (MMBF) Products,that it wanted to outsource certain critical functions in running of MMBF Products Business,that for that purpose it approached J.C.Saigal (JCS),erstwhile director of Nicholas Piramal Group to provide consultancy and retailing services,that JCS agreed to provide NPHL the required services,that they entered into a Memorandum of Understanding(MOU) on 29.03.2007.In the MOU it was decided JCS would provide certain consultancy and retailing services to NPHL w.e.f. 1.4.2007, that for this purpose he would incorporate a Private Ltd.Co.,that after its incorporation it would adopt the obligation of JCS with regard to services to be provided to NPHL,that JCS would within a period of three months incorporate a Pvt. Co. Limited by shares(Newco) having as part of its object clause the power to provide consultancy, that incorporation of Newco the promoter would adopt the rights and obligations under the MoU by passing appropriate resolution,that the promoter would obtain a license for carrying on

business, that after the license was obtained NPHL would transfer and Newco would take over the employment with continuity of service of such employees of NPHL who were involved in the business activity of marketing and selling of MMBL products, that the Newco would reimburse NPHL the expenses incurred by it on marketing detailing and promotional expenses including all the expenses related to employees w.e.f. 1.4.2007. The AO further observed that the assessee company was incorporated on 15.6.07, that on the same date an MOU adoption agreement was entered into between JCS, NPHL and the assessee, that the said agreement stipulated that all acts, deeds and things done by JCS under the MOU w.e.f. 1.4.2007 would be deemed to have been undertaken on behalf of the assessee company, that all expenses and liabilities incurred or to be incurred attributable to the promoter (JCS) would be borne and be payable by NPIL Pharma. He held that the expenses incurred prior to the incorporation of the company were not allowable. Finally, he made a disallowance of Rs.8.34 crores and reduced it from the total loss of the assessee.

**4.1.** Aggrieved by the order of the AO, the assessee preferred an appeal before the First Appellate authority (FAA). Before him, the assessee made elaborate submissions. Relying upon the case of Andhra Pradesh Tourism Corporation Limited (5SCC425), it argued that the acts of the promoter before incorporation of a company was binding after incorporation, the AO had not disputed the fact of incurring of expenditure and resultant loss, that the loss incurred by it should be carried forward for set off in the subsequent AY.s

After considering the submission of the assessee and the assessment order, the FAA referred to the provisions of section 3 of the Act and deliberated upon the the concept of previous year. He relied upon the case of Kikabhai Premchand (24ITR506) and held that any expenses incurred in a year, or as the case could be years prior to the commencement of previous year could not be deducted out of the profits of the previous years. He referred to the MOU's entered into between MIPL and JCS and called for details of licenses necessary for commencement of business. He observed that the assessee company was registered for the service tax purposes on 29.10.2007. He held that the effective date of setting up of business was not earlier than 31.7.2007 that the date of incorporation was 15.6.2007, that the provisions of Specific Relief Act were not applicable to the Act, that the AO was justified in holding that expenses of a company can be allowed after incorporation only, that by no stretch of imagination it could be argued that business of the company had been set up prior to its birth. He directed the AO to disallow the expenses up to the period 31.7.2007.

**4.2.**Regarding the quantum of disallowance,he held that the assessee had objected to the disallowance made by the AO,that it had stated that pre-incorporation period expenses were of Rs.4.78 crores and not Rs.9.66 crores as determined by the AO, that if actual figures were taken the resultant disallowance would be Rs.3.46crores.

After considering the above objections of the assessee,the FAA observed that the assessee was directed to produce all original bills and vouchers amounting to Rs.12.18 crores being the sum reimbursed by aeeaeess to NPHL.As per the FAA the assessee could produce details and vouchers amounting to Rs.4.78 crores only.He directed the AO to disallow the loss incurred for the period 1.4.2007 to 31.3.2007 on the basis of actual book results.he also observed that of the assessee failed to produce original vouchers/books of account the AO would be at liberty to adopt the basis of the assessment order .

**4.2.**Befoer us,the AR argued that the promoter was incurring expenses as per the agreement, that after incorporation the company had decided to take over the liabilities of the erstwhile entity.She referred to page 17 of the PB and the provisions of the Specific Relief Act and relied upon the cases of City Mills Distributors(219ITR1), Dalmiya Cement Ltd. (237 ITR 617)and Zuari Agro Chemicals Ltd.(30taxmann.com.101)He further argued that the FAA had directed to disallow expenses till 31.07.2016,that it resulted in enhancing the income of the assessee,that the FAA had not issued the notice u/s.251(1)of the Act,before enhancement, that provisions of service tax cannot govern the tax liability of an assessee.With regard to the quantification,the AR stated that the AO had taken expenditure for the whole year and had made a proportionate disallowance,that even if any sum was to be disallowed it should have been restricted to actual expenditure.The DR supported the order of the FAA and stated that pre-incorporation expenses could not be allowed,that the AO had rightly taken the expenses for the entire year and had made the disallowance following the time and margin ratio method,that the provisions of specific relief Act were not applicable to the Income tax proceedings.

**4.3.**We have heard the rival submissions and perused the material.We find that the first MOU was entered into on 29/03/2007 between the client and the promoter,that the promoter was to float a private company,that the new company had takeover the pre-existing liabilities/ profit and loss of the company floated by the promoter,that the company was incorporated on 15/07/ 2007, that the AO disallowed the expenditure incurred for the period from 01/ 04/2007 to 15<sup>th</sup>,July,2007,that the FAA held that expenditure incurred by the assessee up to 31/

07/2007 should be disallowed, that the FAA had not issued a notice u/s.251(2) of the Act, before holding that disallowance should be made for remaining part of the month of July, 2007. In our opinion, to that extent the order of the FAA cannot be endorsed, as it resulted in enhancement of the income of the assessee. He should have issued a notice, as required by the provisions of the Act.

Now, we would take up the balance disallowance i.e. expenditure incurred up to 15/07/2007. We find that MOU between NPHL and JCS stipulated that he would provide consultancy and detailing services from 01/04/2007, that he would form and incorporate a private company, limited by shares, to be controlled by him, that on incorporation the said company would adopt the obligations of JCS with regard to consultancy and detailing services to be provided to NPHL, that the details in the scope of the consultancy services was provided in schedule-I, that the detailed and scope of detailing services was provided in schedule-II, that JCS would be entitled to a consultancy fees of Rs.35 lakhs per month, that in addition to the above fee if the net sales of MMBF products exceeded Rs.30 crores for the year under consideration he would be entitled to an additional payment at the rate of 5% of the net sales in excess of Rs. 30 crores, that he would be entitled to detailing fees of 4% of the net sales of the products sold by NPHL. It was further agreed that JCS would within a period of three months incorporate a private limited company having as part of its object clause the power to provide consultancy and detailing services. Clause 9 of the MOU reads as under:

*“9. Upon incorporation of Newco, the Promoter shall procure the Newco to adopt the rights and obligations assumed by the Promoter under this MOU by passing appropriate resolution in a duly constituted meeting of the Board of Directors of Newco.”*

The MOU adoption agreement, dated 15/06/2007 was entered into by three parties i.e. JCS, NPIL Pharma Services Private Ltd. and NPIL Healthcare Private Ltd. Vide clause 3 of the agreement it was agreed that all expenses and liabilities incurred/to be incurred/attributable to the Promoter under the MOU with effect from 01/04/2007 would be born and payable by NPIL Pharma. As per the agreement assessee company had to adapt the MOU, dated 29/03/2007, in favour with effect from 01/04/2007. It was also decided that all acts, deeds and things done by JCS under the MOU with effect from first April, 2007 would be deemed to have been undertaken on behalf of the company and were to be adopted by it. It was also decided that the assessee company would take over the employment, with continuity of service, of such employees of NPIL who were involved in the business activities of marketing and selling of MMBF products.

We would like to refer to the matter of The Bilji Cotton Mills Ltd.(23 ITR 278).In that case a firm had entered into an agreement to purchase a mill for a company which they intended to float and obtained possession of the mill in December,1942,on behalf of the company.The company was floated one year after the purchase took place i.e.in December,1943.The sale deed was executed in its favour on in January, 1945. The company chose to accept the profits made before its incorporation and treated the promoters as accountable for all profits made during the period December,1942-Dec.1943.Matter travelled up to the Hon'ble Allahabad High Court,where following question was framed:

*2. Whether in the circumstances of the case the income of the period from 11th December, 1942, to 10th December, 1943, could be legally assessed in the hands of the assessee company which was incorporated on 11th December, 1943?"*

The Hon'ble Court dealt the matter as under:

*"The facts found in the appellate order of the Income-tax Tribunal and which are stated in the statement of the case are that Messrs. David Mills Ltd. were previous owners of the Bijli Cotton Mills at Hathras. Messrs. Shyamlal Chimanlal, a partnership firm, thought of acquiring the Bijli Cotton Mills for a sum of Rs. 15 lacs on behalf of a company, which they were going to get incorporated. Messrs. Shyamlal Chimanlal paid the stipulated price to Messrs. David Mills Ltd., purporting to do so on behalf of the company which they were going to float. On 10.12.1942, they obtained possession of the Bijli Cotton Mills as representing the purchaser company which had not yet come into existence but which they specifically mentioned they had decided to get incorporated. On 11.12.1943, the company was duly incorporated and on the 02.01.1945, a formal conveyance was executed by Messrs. David Mills Ltd. in favour of the new company, called the Bijli Cotton Mills Ltd., Agra. On 1.03.1945, the AO assessed the Bijli Cotton Mills Ltd., on the income from the 11.12.1942, to the 31.12.1943. This assessment could only be on the basis that the Bijli Cotton Mills Ltd. had earned profits from the date that Messrs. Shyamlal Chimanlal had commenced business after taking over possession of Bijli Cotton Mills from Messrs. David Mills Ltd. The Bijli Cotton Mills Ltd. had claimed certain sums of money as depreciation. They were not satisfied with the depreciation allowed by the AO and filed an appeal.*

*While the appeal was still pending the Income-tax Officer thought that he had made a mistake in assessing the Bijli Cotton Mills Ltd. on the income from the 11.12.1942, and came to the conclusion that he should have assessed the Bijli Cotton Mills Ltd. only from the date of its incorporation and that the liability for the payment of income-tax for the period from the 11.12.1942 to 10.12.1943, was of Messrs. Shyamlal Chimanlal, the promoters, who had during that period continued the business.*

After noting the facts that the FAA cancelled the assessment and that the Tribunal had decided the issue in favour of the assessee,the Hon'ble Court held as follow:

*"Coming to the second question, the facts stated above, which have been reproduced from the statement of the case, show that Messrs. Shyamlal Chimanlal entered into an agreement to purchase the Bijli Cotton Mills not for themselves but for a company which they were going to float. It also appears that when they took possession they made it clear that they were not taking possession of the Bijli Cotton Mills in their own right but on behalf of the private limited company which they were going to have incorporated. The company was no doubt incorporated almost one year afterwards, i.e., on the 11th of December, 1943, and the sale deed in its favour was not executed till the 2nd of January, 1945, by Messrs. David Mills Ltd. who were the owners. It further appears from the statement of the case that, after the assessee*

company was incorporated, the assessee chose to accept the profits made before its incorporation and treated the promoters as accountable for all profits made during the period 11th December, 1942, and 10th December, 1943. In the circumstances the question arises whether it can be said that the business was carried on by the assessee, during the relevant period.

Learned counsel for the Department has laid great stress on the language of Section 10 of the Indian Income-tax Act and has pointed out that under Section 10 tax is payable by an assessee in respect of the profits or gains of any business carried on by him. The argument is that the assessee cannot be said to have been carrying on a business prior to its incorporation on the 11th of December, 1943, when it did not exist and during the period from the 11th of December, 1942, to the 10th of December, 1943, the promoters, Messrs. Shyamlal Chimanlal, must be deemed to have been carrying on the business and they are, therefore, the persons who are liable to assessment.

*It is true that under the law the assessee, the Bijli Cotton Mills Ltd., came into existence only on its incorporation on the 11th of December, 1943, and it is not possible to hold that the legal title in the business or its profits vested in it before its incorporation. It is, however, well settled that if the promoters of a company buy a property or carry on a business on behalf of a company which they intend to float, on the incorporation of the company, the company has a right to either accept what has been done on its behalf by the promoters or repudiate the same. If the company accepts what the promoters have done on its behalf it has a right to claim from the promoters the entire income of the property since its purchase or the entire income for the period during which the business was carried on for the benefit of the company.(emphasis added.)*

The question whether the promoters can be said to be trustees for a company not in existence and what exactly is the relationship between a promoter and a company, which comes into existence later, has been the subject-matter of several decisions. Though, strictly speaking, it cannot be said that a person is a trustee for a beneficiary not in existence, it has been held that, on the company being floated, the relationship between a promoter and the company that he has floated must be deemed to be a fiduciary relationship from the day the work of floating the company had been started. In *Lydney and Wigpool Iron Ore Company v. Bird* Lord Justice Lindley said that although the promoter is "not an agent of the company nor a trustee for it before its formation, the old familiar principles of the law of agency and of trusteeship have been extended, and very properly extended, to meet such cases; and using the word 'promoter' to describe a person acting as James Bird did, it is perfectly well settled that a promoter of a company is accountable to it for all moneys secretly obtained by him from it just as if the relationship of principal and agent or of trustee and cestui que trust had really existed between them and the company when the money was so obtained." In *Omnium Electric Palaces v. Baines* it was doubted whether this was strictly accurate and whether it did not merely confuse matters to attempt to identify the fiduciary duties of a promoter with ordinary out and out trusteeship. Buckley in his *Companies Acts*, 12th edn. at page 108, dealing with this matter says:-

*"The case of a promoter is a strong case of fiduciary relationship, inasmuch as the trustee or agent, so far from being selected by his cestui que trust or principal, actually creates the principal in whose affairs he acts."*

*If, therefore, the promoters have not bought some property or business for their own use but on behalf of or for the benefit of a company which they were about to float, though the company when floated may have the option to accept the benefit of the contract entered into by the promoters, or buy the property purchased for its benefit, the promoters have no right to refuse to give the property or the business or the benefit derived therefrom to the company if the company wants to acquire that property or the business.*

*There is, therefore, no doubt that Messrs. Shyamlal Chimanlal, as promoters, were accountable to the assessee, Bijli Cotton Mills Ltd., on its incorporation on nth of December, 1943, for the entire profits made from the nth of December, 1942, when they commenced business after getting possession of the property on behalf of the assessee. The fact that the assessee could not claim legal title from the 10th of December, 1942, would for purposes of income-tax make no difference as on equitable grounds the assessee could claim the entire profits of the business run from the nth of December, 1942, and in the case before us it did and realised the whole amount. It must be held, therefore, that the business was run on its behalf.*

Referring to certain cases the Hon'ble Court further held as under:

*"These cases, however, make it clear that under Sections 9 and 10 of the Income-tax Act, it is not only the legal ownership that has to be looked to but the courts can also go into the question of beneficial ownership and decide who should be held liable for the tax after taking into account the question as to who is as a matter of fact in receipt of the income which was going to be taxed.*

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*.....If we are correct in this view, then there can be no doubt that after the assessee had adopted the action of the promoters and had decided to take over the business the profits for the whole of the period, during which the promoters ran the business which they had to hand over to the company and which they could not claim that they had a right to keep for their own benefit, became income of the assessee. It will be of interest in this connection to quote the observations of Lord Justice Cotton in Ladywell Mining Company v. Brookes, Ladywell Mining Company v. Huggons where he said:-*

*"The money was all paid by Palin and his friends and in my opinion they bought for themselves, and without putting themselves into such a position as to entitle the company when formed to say, 'You were acting for us; you were in a fiduciary position as regards this property, and now, therefore, as you have purported to sell this to us, we are entitled to take it at the price you originally gave for it'."*

*In that case on the evidence it was held that the promoters had got the mine for their own benefit but if it had been found that the promoters had got the mine for the benefit of the company which they were going to float, the judgment of Lord Justice Cotton makes it clear that the promoters could not have kept all the profits they made by selling the mine to the company at a higher price than the price they paid for it.*

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*We have already held that in the case before us though the assessee company came into existence almost a year afterwards, the assessment proceedings were started at a time when the assessee company had already decided to accept what had been done on its behalf by the promoters and take over the property and business and the income made therefrom from the 11th of December, 1942, and it was in the same position as a beneficiary for whom the income was earmarked as payable to it. The case is, therefore, to our minds governed by the principle laid down in Trustees of Sir Currimbhoy Ebrahim Baronety Trust case and the income from the 11th of December, 1942, to 10th of December, 1943, could be legally assessed in the hands of the assessee."*

If the principles laid down in the above case are considered it becomes clear that agreement entered in to by the promoter can bind the succeeding entity of earlier liabilities. In the case under consideration, the new company had agreed to take over the liabilities and expenses incurred/to be incurred/attributable to the Promoter under the MOU with effect from 01/04/2007. As the income can be taxed in the hands of the succeeding entity, expenditure can

also be allowed in the hands of the new company. Therefore, we hold that the expenditure incurred by the erstwhile entity has to be allowed in the hands of the assessee.

**4.4.** We have principally held that the expenditure incurred by the assessee has to be allowed u/s.37(1) of the Act. But, the quantum of allowance has to be decided. We find that the FAA has given a categorical finding that all the bills and vouchers evidencing the incurring of expenditure were not produced before him. We are reproducing the relevant portion of the order of the FAA and same reads as under:

*“During the course of appellate proceedings, vide notings dt.18.04.2012, the appellant was asked to produce all the original bills and vouchers for Rs.12,18,96,889/-, being the sum reimbursed by the assessee to NPHL. However as per noting, dt.3.7.12 the appellant could only produce details and vouchers pertaining to Rs.4,78,15,177/- .”*

Nothing was brought on record to prove that an application u/s.154 of the Act was filed before the FAA by the assessee challenging the factual mistake in his order about non producing of the bills/vouchers. No arguments were made before us or any details were filed in the paper books to prove that bills/vouchers of balance amount were produced before the AO in pursuance of the order of the FAA. In these circumstances, the incurring of expenditure was not proved before him. So, if he has observed that if the assessee fails to produce the original vouchers or books of accounts the AO would be at liberty to adopt the basis of assessment. In our opinion, the decision of the FAA to that extent does not suffer from any infirmity. So, considering the peculiar facts and circumstances of the case, we decide the first ground of appeal in favour of the assessee, in part.

As we have decided the effective ground in favour of the assessee, so, alternate ground (GOA-2) is not being adjudicated.

As a result, appeal filed by the AO stands dismissed and the appeal of the assessee is partly allowed.

फलतः निर्धारिती अधिकारी द्वारा दाखिल की गई अपील नामंजूर की जाती है और निर्धारिती की अपील अंशतः मंजूर की जाती है.

Order pronounced in the open court on 29<sup>th</sup> July, 2016.  
आदेश की घोषणा खुले न्यायालय में दिनांक 29 जुलाई, 2016 को की गई।

**Sd/-**

(पवन सिंह / Pawan Singh)

न्यायिक सदस्य / JUDICIAL MEMBER

मुंबई Mumbai; दिनांक Dated : 29.07.2016.

Jv. Sr. PS.

**आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :**

1. Appellant /अपीलार्थी

2. Respondent /प्रत्यर्थी

3. The concerned CIT(A)/संबद्ध अपीलीय आयकर आयुक्त, 4. The concerned CIT /संबद्ध आयकर आयुक्त

5.DR “ C ” Bench, ITAT, Mumbai /विभागीय प्रतिनिधि, खंडपीठ,आ.अ.न्याया.मुंबई  
6.Guard File/गार्ड फाईल

सत्यापित प्रति //True Copy//

आदेशानुसार/ **BY ORDER,**  
उप/सहायक पंजीकार **Dy./Asst. Registrar**  
आयकर अपीलीय अधिकरण, मुंबई /**ITAT, Mumbai.**