



IN THE HIGH COURT OF DELHI AT NEW DELHI
SUBJECT : INCOME TAX MATTER

Date of Decision : September 17, 2007

ITA NO 1687 of 2006

COMMISSIONER OF INCOME TAXPETITIONER
Through : Ms. P.L. Bansal, Advocate

versus

M/S. HUGHES ESCORTS COMMUNICATIONS
LIMITEDRESPONDENT
Through: Mr. Ajay Vohra with Ms. Kavita Jha, Advocate

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CORAM:
HON'BLE MR. JUSTICE MADAN B. LOKUR
HON'BLE DR. JUSTICE S. MURALIDHAR

1. These appeals under Section 260(A) of the Income Tax Act, 1961 ('Act') are directed against the common order dated 31st May, 2006 passed by the Income Tax Appellate Tribunal ('Tribunal') Delhi Bench "C", New Delhi in ITA No. 191 & 184/Del/2003 for the Assessment Year 1995-96.
2. The Assessee company which was incorporated on 17th March, 1992, is in the business of setting up satellite business communication systems for which a very small aperture terminal ('VSAT') equipment is used. As per the objects of the



Assessee Company, its main activities are to provide products and services Digital Satellite market place in India and to initially import and gradually produce in India, the “Personal Earth Station” that is otherwise known as VSAT. The VSAT can be used only after establishing, maintaining and using the communication facilities on a licence from the Department of Telecommunications (‘DOT’), Government of India. The Assessee made an application to the DOT for grant of such licence. On 3rd August, 1994 a licence agreement was entered into between the Assessee and the DOT.

3. The Assessee placed a purchase order dated 28th July, 1994 with M/s. Hughes Network Systems, USA for the purchase of the VSAT equipment. This purchase order was placed consequent upon the Bank of America, by its letter dated 3rd June, 1994 addressed to the Assessee expressing interest in purchasing and installing four VSAT PES modules in their branches to be located at Mumbai, Chennai, Delhi and Kolkata.

4. In its return for the assessment year in question, that is 1995-96, the Assessee claimed an expenditure of Rs.28,96,269. The Assessee considered its business as having commenced in the month of March, 1995 and therefore, capitalized the expenses. However, in a revised return it claimed the said expense as revenue expense and therefore, claimed as a deduction. The Assessee explained this change by pointing out that it had placed a purchase order on M/s. Hughes Network Systems, USA on 28th July, 1994 for purchase the VSAT equipments and therefore, it was this date that should be reckoned as date of which the business has been set up. Any expenditure incurred thereafter must therefore, be considered as revenue expenditure that did not require to be capitalized. On the other hand, the Revenue contended that the Assessee had begun receiving the satellite signals only in the month of February 1995 and Further since the installation was complete only on 15th March, 1995 it could be said that the business of the Assessee had been set up only on 5th March, 1995.

5. The Assessing Officer rejected the explanation of the Assessee and held that the claim for deduction of Rs.28,96,269/- as revenue expenses cannot be permitted. However, the Commissioner of Income Tax (Appeals) [‘CIT(A)’] disposed of the appeal filed by the Assessee by holding that the formal order by the Bank of America on the Assessee was placed only on 6th October, 1994 and therefore, this was the date on which the Assessee had set up its business.

6. Aggrieved by the decision of the CIT(A), the Revenue and the Assessee both filed appeals before the Tribunal. Relying on the judgment of M/s. Western India



Vegetable Products Limited v. Commissioner of Income Tax [1954] 26 IT (Bombay) and other judgments including the judgment of this Court in Commissioner of Income Tax v. L.G. Electronic (India) Limited [2005] 149 TAXMAN 166 (Del), the Tribunal held that the setting up of business and commencement of the business can be on two different dates. On facts it was held that the business was set up on 28th July, 1974 on which date the Assessee had placed a purchase order on M/s. Hughes Network Systems, USA. Accordingly, the Revenue's appeal was dismissed and the Assessee's appeal allowed. That is how the Revenue is before us in these appeals.

7. it is contended by Ms. Prem Lata Bansal, learned senior standing counsel appeared on behalf of the Revenue that the business of the Assessee obviously could not be said to have commenced till such time the satellite signals were not available to its customers. This required the Assessee to have a licence from the DOT. The installation of equipment was completed only in the month of March 1995. In the circumstances, the Assessing Officer was right in concluding that the business of the Assessee could be held to have been set up only in March 1995. Consequently all the expenses incurred prior to this date were required to be capitalized and could not have been allowed to be deducted as revenue expenditure.

8. Appearing for the Assessee, Mr. Ajay Vohra, learned counsel referred to the proviso to Section 3(1) of the Act to contend that it only refers to the date of setting up of the business. He then referred to the date of setting up of the business in the present case was even earlier to the actual commencement of the business and therefore the Tribunal's conclusion required no interference.

9. Section 2(34) of the Act which defines 'previous year', in turn refers to Section 3(1) which reads as under:

Section 3(1) "Previous year" defined- (1) Save as otherwise provided in this section, 'previous year' for the purposes of this Act, means the financial year immediately preceding the assessment year:

Provided that, in the case of a business of profession newly set up, or a source of income newly coming into existence in the said financial year, the previous year shall be the period beginning with the date of setting up of the business or profession, as the case may be, the date on which the source of income newly comes into existence and ending with the said financial year."

10. A plain reading of the above provision shows that for a new business the previous year is the period beginning with the date of setting up of the business. As



explained by the Bombay High Court in *M/s. Western India Vegetable Products Limited* once it is known what the business of an Assessee is:

“the important question that has got to be considered is from which date are the expenses of this business to be considered permissible deductions and for that purpose the section that we have got to look to is Section 2(11) and that section defines the “previous year” and for the purpose of a business the previous year begins from the date of setting up of the business. Therefore it is only after the business is set up that the previous year of that business commences and in that previous year the expenses incurred in the business can be claimed as permissible deductions. Any expenses incurred prior to setting up of a business would obviously not be permissible deductions because those expenses would be incurred at a point of time when the previous year of the business would not have commenced.” (ITA, p.157)

11. The Bombay High Court, which was in this case dealing with the corresponding provision of the Indian Income Tax Act, 1922, then explained the distinction between the concepts of “commencement” and “setting up” of a business (ITR, pp. 158-159):

“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 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).”

The above decision has been followed in a large number of decisions including this Court in *L.G. Electronic (India) Limited*.

12. Turning the facts of the present case, it is clear that the business of the Assessee involved different activities in which the first step was the purchase of the VSAT equipment. There was no question of Assessee having to place a purchase order with *M/s. Hughes Network Systems, USA* for a purpose other than that of its business. The said purchase order was placed on 28th July, 1994. The application to DOT for licence and the receipt of the satellite signals were the consequential stages. The signals were to be received after the VSAT equipment was installed in the premises of the customer. In the circumstances, we are of the view that the business of the Assessee should be held to have been set up on 28th July, 1994. This is the



relevant date for determining the nature of the expenses incurred thereafter expenses incurred in the previous year, prior to the commencement of the business but after the setting up its business, which two dates need not be the same, would be deductible as revenue expenses.

13. No ground for interference with the judgment of the Tribunal is made out. No substantial question of law arises in these appeals. Accordingly, the appeals are dismissed.

Sd/-
S. MURALIDHAR, J

Sd/-
MADAN B. LOKUR, J