



\* IN THE HIGH COURT OF DELHI AT NEW DELHI

+ ITA No. 640 of 2009

% Decided on : September 11, 2009

Commissioner of Income Tax . . . Appellant

through : Ms. Prem Lata Bansal, Advocate

*VERSUS*

Aspentech India Pvt. Ltd. . . . Respondent

through : NEMO

CORAM :-

THE HON'BLE MR. JUSTICE A.K. SIKRI

THE HON'BLE MR. JUSTICE VALMIKI J. MEHTA

1. Whether Reporters of Local newspapers may be allowed to see the Judgment?
2. To be referred to the Reporter or not?
3. Whether the Judgment should be reported in the Digest?

A.K. SIKRI, J. (ORAL)

1. For the relevant assessment year, i.e. assessment year 2003-04, the respondent/assessee had filed the return declaring a loss of Rs.2.48 crores. The Assessing Officer (AO) found that the assessee had claimed expenditure of Rs.2.53 crores against a meagre income of Rs.4,93,343/-. He, thus, raised certain queries to the assessee but was not satisfied with the explanation and, therefore, disallowed the aforesaid expenditure of Rs.2.53 crores.

2. We may note at the outset that this expenditure included salary paid to the employees in the sum of Rs.1.72 crores, travelling cost of



Rs.30.61 lacs and administrative and other operating expense  
tune of Rs.39.65 lacs.

3. Perusal of the assessment order passed by the AO would reveal that the main consideration by which the AO was swayed was that against the aforesaid huge expenses incurred by the assessee, he hardly generated any revenue. On this basis, he opined that the said expenses could not be justified and allowable as revenue expenditure. It is clear from the aforesaid order of the AO that the AO had not doubted that the expenditure was, in fact, incurred. However, from the huge expenditure against minimal income, only an inference was drawn that the business of the assessee had not commenced during the year as no revenue earning project had started. On this basis, the expenditure was treated as pre-operative expenditure and, therefore, according to the AO, it should have been, at best, be capitalized as pre-operative expenses.
4. The Commissioner of Income Tax (Appeal) {hereinafter referred to as 'CIT(A)'}, however, reversed the finding of the AO and which finding has been confirmed by the Income Tax Appellate Tribunal (ITAT) in further appeal preferred by the Revenue. The ITAT has reproduced the relevant portion of the discussion contained in the order of the CIT (A), which would indicate that the assessee is in the business of development of software for various industries and as a policy decision it had decided to pursue only prestigious companies in India



personnel. According to the CIT (A), the only objection of that since the assessee company had not obtained any orders to start revenue generation activities, its business could not have been said to have been set up.

5. This was clearly a wrong approach, as rightly observed by the CIT(A), who opined that in an industry like software development business activities start with pursuing of the companies to get orders and all activities carried out to get such orders, being incidental to the business activities, would be regarded as for the purpose of business and not for setting up of the business. The CIT (A) also recorded the reasons, on the basis of which it arrived at the finding that the business had, in fact, started. As to when the activity is deemed to be undertaken as part of business activity and the expenses incurred are to be allowed as business expenses, the CIT (A) referred to and relied upon the judgment of the Gujarat High Court in the case of *CIT v. Saurashtra Cement & Chemical Industries Ltd.* (1973) 91 ITR 170 and that of the Calcutta High Court in *Tetron Commercial Ltd. v. CIT*, 261 ITR 422. Referring to *Saurashtra Cement & Chemical Industries Ltd.* (supra), the CIT(A) stated that following tests were laid down by the Gujarat High Court in that case to determine the commencement of business activities. It reads as under :-

“A business activity consists of three stages: the first stage relates to the activity necessary for the purpose of acquiring the



thereof. The first in point of time lays the foundation for second activity and the second activity when completed the foundation for the third activity. Therefore, the expenditure incurred for carrying on any of these activities including the first activity is also deductible in computing the profits and gains of the assessee for the relevant year when the activity is undertaken. In *Sarabhai Management Corporation Ltd., v. CIT*, (1976) 102 ITR 25, the Gujarat High court took the same view and held that the business commences with the first activity for acquiring by purchase or otherwise, immovable property. There may be an interval between the setting up of the business and the commencement of the business. All expenses incurred during that interval are also permissible for deduction. In *CIT v. Sarabhai Management Corporation Ltd.*, (1991) 192 ITR 151 SC the decision of the Gujarat High Court was affirmed and went a step ahead that even the activities at a preparatory stage is also admissible.”

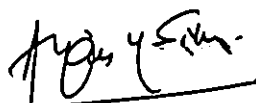
6. Taking note of the aforesaid facts and also referring to the judgment of the Supreme Court in *CIT v. Rajendra Prasad Moody*, 1978 CTR (SC) 141 and of this Court in *CIT v. LG Electronics (India) Ltd.*, 282 ITR 545, the Tribunal made the following pertinent observations while confirming the finding of fact that the business activities of the assessee had, in fact, commenced :-

“6. We have duly considered the rival contentions and gone through the record carefully. From the perusal of the asstt. order it reveals that Ld. AO has disallowed the expenses claimed by the assessee for the reason that it has not shown resultant income in the accounting year. It appears that Ld. AO has swayed away with an impression that whenever any expenses are incurred by the assessee then resultant income should have arisen. However it is well settled that for the purpose of allowance of any expenses u/s 37(1) of the Act as expenses it is not necessary that assessee should have earned income out of such activity. Whatever has required to be seen is that whether the expenses are incurred for the purpose of business or not and such expenses are of not capital nature and not expressly disallowable under the other provisions in the act. It also emerges out from the record that in the succeeding year the assessee has achieved turnover to the tune of Rs.4 crores with the help of seven employees only which clearly indicates that their efforts made in the year under



expenses have been incurred after setting up of the business. Assessee has already filed the return for the earlier year wherein losses declared by it has been accepted. This is not the first year of the business. It is irrelevant to say that assessee should show income if it wants to claim expenses as business expenses. In view of the above, we do not find any merit in this appeal it is dismissed."

7. Learned counsel for the Revenue submits that when the expenses were huge, such expenses need to have been amortized under the provisions of Section 35D of the Income Tax Act, 1961. However, this is clearly a misconceived and erroneous argument inasmuch as it predicates on the premise that the expenditure in question is incurred before the commencement of the business. When a finding of fact is recorded in the instant case that in the relevant assessment year business had already commenced, the provisions of Section 35D would not get attracted at all.
8. We, therefore, find that no question of law arises and dismiss the appeal.

  
(A.K. SIKRI)  
JUDGE

  
(VALMIKI J. MEHTA)  
JUDGE

September 11, 2009  
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