HIGH COURT OF DELHI

Commissioner of Income-tax
v.
Sauer Danfoss (P.) Ltd.*

Sanjiv Khanna and R.V. Easwar, JJ.

IT Appeal No. 1367 of 2010

March 26, 2012

ORDER

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1. This appeal by the Revenue under Section 260A of the Income Tax Act, 1961 (Act, for short) in the case of Sauer Danfoss (P.) Limited relates to Assessment Year 2002-03.

2. At the outset, we may notice that the learned counsel for the Revenue has not pressed question No. (h) regarding interest under Section 234D of the Act and submits that this question may be left open with liberty to the Revenue to file an application under Section 254(2) of the Act before the tribunal in case the proposed amendment is enacted and the Finance Bill is passed. We accept the said statement and clarify that we have not expressed any opinion and gone into the said question and the doctrine of merger will, therefore, not apply on the said issue/question.

3. There are four other issues raised in the present appeal. The first issue relates to the date on which the business of the respondent assessee was set up. The Assessing Officer has held that the business of the respondent assessee was set up on 1st June, 2001. The Assessing Officer, therefore, disallowed expenses to the extent of Rs. 19,37,773/-, which include salaries, wages, bonus, staff welfare expenses, recruitment and training etc. for the period prior to 1st June, 2001. Similar expenses have been also disallowed on power and fuel, i.e., electricity and water.

4. On the said aspect/question, we find that the tribunal has dealt with the issue in depth and has recorded several factual findings. We would like to reproduce here paragraph 6 of the order passed by the tribunal, which reads as under:

" We have considered the rival contentions and found from the record that the assessee company was duly incorporated on 5.2.2001 under the Companies Act, 1956. It has also applied for approval to FIPB, and FIPB vide approval dated 24.1.2001 allowed for setting up of business in India for various activities. The assessee set up its business from 1st April, 2001 and was ready to commence its business operation. First director was appointed on 5.2.2001 on the date of incorporation and additional directors were appointed on 10.2.2001. It has taken premises on lease w.e.f. 1.4.2001, the physical possession of which was already taken w.e.f. 15.2.2001. It opened its bank account with Dutche Bank in March first week wherein first remittance was received on 9.2.2001. It is quite clear from these activities of the assessee company that it has set up its business and was ready to commence on 1.4.2001. There is no dispute to the well settled legal proposition that at the point of time, the assessee is in a complete state of readiness to undertake its activity, it can be said that it has set up its business, the actual commencement of business may be at a later date. The trading business of the assessee was ready to commence upon set up of requisite infrastructure i.e. acquisition of place of business, commencement of hiring of suitable

personnel, identifying clients, opening bank account etc. which enabled the assessee to carry out its object clause. ITAT Delhi Bench in the case of Whirlpool of India Ltd.- 19 SOT 293 observed that there may be integregrum(sic) between setting up of business and date of commercial commencement of business, but under the Income Tax Act, all the expenses incurred after the date of setting up of business are to be allowed as a deduction while computing the income u/s 28. The Hon'ble Bench in this case held that where the assessee company has appointed branch manager and regional manager in 1995, paid salaries including PF contribution etc. beginning from November, 1995, its business can be said to be set up from 1.11.1995 i.e. the date on which the company was in a position to commence its business, and not on 1.2.1996 when its bank account was opened. The instant case before us is at a more sound footing where even a bank account was opened prior to 1.4.2001 and the assessee has claimed the expenditure only after it has set up its business which was ready for commencement. Merely because assessee entered into agreement with DHL on 21.5.2001 which was to be operative from 1.6.2001 date on which assessee took over the running business of DHL, it cannot be said that it has set up its business only on 1.6.2001 and not from 1.4.2001. Accordingly, we do not find any merit in the action of the lower authorities for not allowing the expenditure incurred after 1st April, 2001. The AO is at a liberty to verify that the expenditure to be allowed should be restricted to revenue expenditure. We direct accordingly."

5. In view of the aforesaid factual findings, we do not think any substantial question of law arises and it cannot be said that the business had commenced only from 1st June, 2001, when the assessee acquired the rights under the agreement dated 21st May, 2001. The tribunal has rightly kept in mind the difference between setting up of business and commencement of business and by applying the said principle to the factual aspects in the present case has reached the said finding. The factual finding recorded by the tribunal is reasonable and fair. It is not perverse.

6. The second issue raised in the appeal pertains to capitalization of expenses to the extent of Rs. 47,38,979/- and consultancy of Rs. 15,89,625/- paid to the architects. The Assessing Officer in this connection referred to Explanation 1 to Section 32(1) of the Act and held that the said expenditure was capital expenditure and on the said expenditure depreciation as per law could be claimed. The CIT(Appeals) has affirmed the said finding. The tribunal in the impugned order after recording the contentions raised has held and given the following reasoning to allow the appeal:-

"9. We have considered the rival contentions and found from the record that expenditure was incurred in respect of leasehold premises on account of electrical work, wooden partitions, laying down of cables, false flooring etc. There was no addition of extension of the premises taken by the assessee on lease. The expenditure was incurred by the assessee company for optimum use of the business premises taken on lease and the same were incurred to facilitate business operation. Nothing was added to the profit making apparatus of the assessee. Accordingly, we do not find any merit in the action of the AO for treating all such expenditure incurred to improvement of architectural work carried out in the leasehold premises as capital in nature. Similarly, consultancy charges paid for architectural work is also required to be allowed as revenue expenditure. In the result, ground Nos. 3 & 4 of the assessee's appeal stand allowed."

7. The third aspect raised in the present appeal pertain to legal and professional charges of Rs. 6,18,690/-. The findings recorded by the tribunal in this connection with regard to the said expenses are that professional charges were paid in connection with compliance of legal formalities for execution of the agreement with the foreign party. The exact reasoning of the tribunal reads:-

"11. We have considered the rival contentions and found that assessee has paid professional charges to KPMG in relation to legal formalities to be undertaken with regard to execution of agreement with DHL. The legal expenditure so incurred are essentially revenue in nature in view of the decision of Hon'ble Bombay High Court in the case of Bombay Dyeing & Manufacturing Co. - 219 ITR 521. Accordingly, we do not find any merit for the disallowance of professional charges paid to a legal consulting firm, on plea of same being capital in nature."

8. Having heard learned counsel for the parties, we frame the following substantial question of law with regard to the second and third aspect:

"Whether the order of the Income Tax Appellate Tribunal reversing the findings given by the Assessing Officer and the CIT(Appeals) that the expenses of Rs. 47,38,979/- Rs. 15,89,625/- and Rs. 6,18,960/- were capital expenditure is correct and as per law?"

9. A reading of the aforesaid findings recorded by the tribunal would show that it has not discussed the exact nature and character of the expenses. We may note that the expenses involved are substantial, i.e., Rs. 47,38,979/- and Rs. 15,89,625/-. We have also noticed that the assessee had taken premises on rent with effect from 1st April, 2001 (possession of the property was taken on 5th February, 2001). We do not know what was position with regard to fixture, fittings etc. provided by the landlord in the said premises, why and for what reasons expenses of more than Rs. 60 lacs were incurred. We do not know the details of expenditure. Break up and particulars regarding the expenditure is not available and referred to. We do not know whether the said expenditure was towards purchase and installation of air conditioners/air conditioning plant, furniture etc. These factual details have not been considered by the tribunal. The Explanation 1 to Section 32(1), which has been relied upon by the Revenue, has also not been specifically dealt with and examined. In these circumstances, we set aside the findings recorded by the tribunal in respect of the second aspect and pass an order of remand for fresh decision after ascertaining the factual aspects. It is clarified that we are not expressing any view whether or not Explanation 1 to Section 32(1) is applicable as at the first instance factual aspects have to be ascertained.

10. With regard to payment of professional charges, the tribunal has merely recorded that a professional firm had been engaged for the legal formalities regarding execution of the agreement with Dantal Hydraulics Limited. Thereafter, reference is made to a decision of the Bombay High Court. There is no discussion whatsoever by the tribunal on the factual aspects, which have been considered by the Assessing Officer and then by the CIT(Appeals). The CIT(Appeals) has in fact stated that this expenditure was in connection with the transfer of assets and liabilities from Dantal Hydraulics Limited and, therefore, should be treated as a part of cost of acquisition of the business/asset. We accordingly pass an order of remit with a direction to first examine and decide the factual aspects. The question of law mentioned above is accordingly answered in negative, i.e., in favour of the Revenue and against the assessee.

11. The fourth issue raised by the Revenue pertains to software, which was purchased vide invoice of the 20th March, 2002. The Assessing Officer held that the invoice was purchased at the end of the accounting period and, therefore, the asset might not have been put to use. The tribunal, on the other hand, has accepted the contention of the assessee that the software did not require complex installation procedure and could be installed on the hardware with the help of the CD. The aforesaid finding is a finding of fact and does not require interference in this appeal on substantial question of law.

The appeal is partly allowed and is disposed of. No costs.