



Global Business Tax Alert Sharp Insights

Revenue expenditure is deductible from the date of 'set-up of business' and not from the date of 'commencement of business'.

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Synopsis

The Delhi High Court recently in the case of Jcdecaux Advertising India Pvt. Ltd. has held that the deduction of revenue expenditure is allowed from the date of the 'set up of the business' and not the 'commencement of business'.

Facts

- The assessee was incorporated in April 2005 to carry on the business of out of home advertisement, consisting of street furniture (such as advertising on bus shelters, public utilities, parking lots, etc.) bill boards and transportation (such as advertisement in airports, railway stations etc.).
- The assessee was awarded its first contract by NDMC in March 2006 for construction of Bus Queue Shelters (BQs) on Build-Operate-Transfer (BOT) basis according to which the assessee was required to undertake preliminary investigations, study, design, finance, construct, operate and maintain BQs at its own cost. In consideration, the assessee was allowed to commercially exploit the space allotted in these BQs by means of display of advertisement etc. for a period of 15 years.
- On 30th March 2006, the assessee entered into a manufacturing agreement with Uttam Sucrotech International Pvt. Ltd. for manufacture and installation of BQs and also made advance payment.
- The assessee claimed deduction of certain amount as business expenditure.
- The Assessing Officer ('AO') held the said expenses to be revenue in nature, however disallowed the same stating that the business of the assessee had not commenced. While concluding, the AO held that the business would commence when the BQs would be ready for providing space for advertisement.
- The Commissioner of Income-tax (Appeals) upheld the order of the AO. The Tribunal reversed the Order of the CIT(A) against which the Revenue filed an appeal to the High Court.

Issue before the High court

- Whether the Tribunal is correct in holding that the assessee is entitled to claim deduction for the business expenses in the year in which it entered into agreement with NDMC in March 2006?

Ruling of the Delhi High Court

- The Delhi High Court observed that the Tribunal while ruling in favour of the assessee relied upon the Delhi High Court decisions in the case of ESPN Software¹ and Samsung India Electronics².
- The Delhi High Court referred to its own decision in the case of Carefour WC&C³ in which it relied on the decision of ESPN Software and Samsung India Electronics (supra) and observed that that activity or exercise which is a prerequisite to the commencement or proposed set up would be treated as that connected with commencement of business.
- After quoting the observations in ESPN Software (supra), the Delhi High Court (in Carefour's case) held that on the facts of that case, nothing barred the assessee from making the first purchase (that was a case of wholesale business) after necessary legal approvals but the fact that the appellant wanted to commence actual trading after negotiations with other parties would not postpone the date when the business was set up.
- The Delhi High Court in the present case also noted that the Tribunal relied upon the decision of Bombay High Court in the case of Western India Vegetables⁴ which has held that 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.

¹ CIT v/s. ESPN Software India Pvt. Ltd. (2009) 184 Taxman 452 (Delhi),

² CIT v/s. Samsung India Electronics Ltd. (2013) 356 ITR 354 (Delhi)

³ Carefour WC & C India Pvt. Ltd. v/s. DCIT (2015) 53 taxmann.com 289 (Delhi)

⁴ Western India Vegetables Products Ltd. v/s. CIT (1954) 26 ITR 151 (Bom.)

- In view of the above, the Delhi High Court held that the ruling of Tribunal in assessee's own case does not call for any interference and upheld the same.
- The Tribunal had held that the business of the assessee was set-up in the year 2005-06 on the basis of following:
 - The assessee had started the execution of the contract in the preceding year itself by taking steps such as entering into manufacturing agreement with a third person for manufacture and installation of BQs on making advance payment.
 - The assessee's business was set up when it prepared itself for undertaking the activity of building BQs on receipt of contract from NDMC. It cannot be in relation to the completion of construction of BQs.
 - The project of NDMC for construction of BQs was not set up but insofar as the assessee is concerned, it had certainly commenced its business with the execution of contract awarded by NDMC.
 - The authorities below have tagged the setting up of business with the provision of space for advertisement by NDMC. This is certainly a post commencement business stage of the assessee. Such an event would mark the generation of actual income on commencement of business and cannot be construed as the setting up of business.
 - As the setting up of the business was over in the preceding year, at the maximum, on entering into manufacturing agreement for manufacture and installation of BQs on 30th March, 2006, it was held that not only the business of the assessee was set up but had also commenced in the instant year.

Comments

The setting-up of business is contentious issue and there have been several judgements pronounced on this subject. However, the tax authorities are typically taking a position that the business is set-up when there is commencement of business or when the revenue generating activities begun.

The Delhi High Court in the present case has clearly accepted the position that the deduction of revenue expenses is allowable the business is set up and ready to commence while the actual commencement of business can be later.

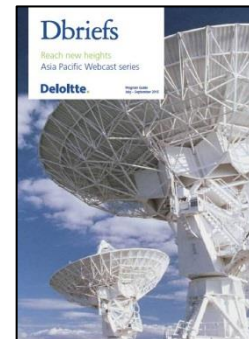
Source: Delhi High Court decision dated 23 April 2015, in the case of CIT v/s. Jcdecaux Advertising India (P.) Ltd. (ITA No. 241/2015)

Upcoming Dbriefs - Register

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Contacts

Ahmedabad

Heritage, 3rd Floor,
Near Gujarat Vidyapith,
Off Ashram Road,
Ahmedabad – 380 014.
Tel: + 91 (079) 2758 2542
Fax: + 91 (079) 2758 2551

Coimbatore

Shanmugha Manram
41, Race Course,
Coimbatore
Tamil Nadu - 641018
Tel: + 91 (0422) 439 2801
Fax: +91 (0422) 222 3615

Kolkata

Bengal Intelligent Park Building Alpha,
1st floor, Block EP and GP Sector V,
Salt Lake Electronics Complex,
Kolkata - 700 091.
Tel : + 91 (033) 6612 1000
Fax : + 91 (033) 6612 1001

Bangalore

Deloitte Centre, Anchorage II,
100/2, Richmond Road,
Bangalore 560 025.
Tel: +91 (080) 6627 6000
Fax: +91 (080) 6627 6010

Delhi/Gurgaon

Building 10,
Tower B, 7th Floor,
DLF Cyber City,
Gurgaon 122 002
Tel : +91 (0124) 679 2000
Fax : + 91 (0124) 679 2012

Mumbai

Indiabulls Finance Centre,
Tower 3, 28th Floor,
Elphinstone Mill Compound,
Senapati Bapat Marg, Elphinstone (W),
Mumbai – 400013
Tel: + 91 (022) 6185 4000
Fax: + 91 (022) 6185 4101

Chennai

No.52, Venkatanarayana Road,
7th Floor, ASV N Ramana Tower,
T-Nagar,
Chennai 600 017.
Tel: +91 (044) 6688 5000
Fax: +91 (044) 6688 5050

Hyderabad

1-8-384 and 385, 3rd Floor,
Gowra Grand S.P.Road,
Begumpet,
Secunderabad – 500 003.
Tel: +91 (040) 6603 2600
Fax: +91 (040) 6603 2714

Pune

106, B-Wing, 7th Floor,
ICC Trade Tower,
Senapati Bapat Road,
Pune – 411 016.
Tel: + 91 (020) 6624 4600
Fax: +91 (020) 6624 4605

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