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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

% **Decision delivered on: 12.04.2021**

\+ **ITA 17/2021**

MARUTI INSURANCE BROKING PVT LTD .....Appellant

Through: Mr. Ajay Vohra, Senior Advocate with Mr. Rohit Jain and Mr. Vaibhav Kulkarni Advocates.

versus

DEPUTY COMMISSIONER OF INCOME TAX .....Respondent

Through: Mr. Ruchir Bhatia, Senior Standing Counsel.

CORAM:
HON'BLE MR. JUSTICE RAJIV SHAKDHER
HON'BLE MR. JUSTICE TALWANT SINGH

[Court hearing convened *via* video-conferencing on account of COVID-19]

RAJIV SHAKDHER, J. (ORAL):

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Preface: -

1. The present appeal under Section 260A of the Income Tax Act, 1961 [in short 'the Act'] is directed against the order dated 10.02.2020, passed by the Income Tax Appellate Tribunal [in short 'Tribunal'], in ITA No. 6442/Del/2016. The appeal concerns the assessment year [in short 'AY'] 2012-2013. The appeal was admitted on 08.02.2021 when the following questions of law were framed by the Court: -

> *A. Whether on the facts and circumstances of the case, the Tribunal erred in holding that the business of the Appellant was not set up during the previous year relevant to [the] assessment year 2012-13 and consequently deduction for expenditure incurred was not allowable?*
>
> *B. Whether on the facts and circumstances of the case, the Tribunal erred in law in holding that the business of the Appellant was set up only in February 2012 on grant of license by the Insurance Regulatory Development Authority?*

1.1. It is required to be noticed that the said questions of law were framed in the background of the arguments advanced on behalf of the assessee that the findings of the Tribunal were "perverse and contrary to the proviso appended to Section 3 of the Act". Therefore, we would like to frame, at this juncture, the third question of law, so that the controversy involved is, clearly, etched out.

> *C. Whether in the facts and circumstances of the case, the Tribunal's finding that the assessee set up its business on 02.02.2012, that is, when it was granted a license by the Insurance Regulatory Development Authority (IRDA), was perverse?*

Background Facts:

2. For us to adjudicate upon the aforementioned questions of law, the following facts are required to be noticed: -

2.1. The assessee was incorporated on 24.11.2010. The first meeting of its board of directors was held on 29.11.2010 when certain decisions were taken including, according to the assessee, setting-up of its business; appointment of the Chief Executive Officer and the Principal Officer; approval of the draft application for obtaining a broker's license in the prescribed form under Regulation 6 of IRDA (Insurance Brokers) Regulations, 2002 [in short '2002 Regulations'] (this application had to be filed for obtaining the license); a decision as to the registered office of the assessee; and a decision concerning the opening of a current account with HDFC bank at Surya Kiran Building, 19, K.G. Marg, New Delhi - 110001.

2.2. The assessee claims that, on 29.11.2010 itself, an agreement was executed between the assessee and Maruti Suzuki India Limited (MSIL). *Via* this agreement, the persons, who were employees of MSIL, were sent on deputation to the assessee, and to meet its objective, were made to undergo a minimum of 100 hours of mandatory training as insurance brokers.

2.3. These steps were a precursor to the application preferred by the assessee with IRDA for issuance of a direct-broker license. The application was lodged with the IRDA on 01.12.2010.

2.4. While this application was being processed, presumably, by IRDA, the assessee took certain other steps in furtherance of its business. Accordingly, on 01.06.2011, the assessee executed operating lease agreements for conducting insurance business from various locations across the country. Against these leases, the assessee is said to have paid rent as well. According to the assessee, it set up 29 offices in 29 different locations

across the country for carrying on its insurance business.

2.5. The assessee was, finally, issued a direct broker's license by IRDA on 02.02.2012.

2.6. In the interregnum, the assessee filed its return of income for the preceding AY, i.e., 2011-2012. This return was filed on 30.09.2011. *Via* this return, the assessee declared a business loss amounting to Rs.57,582/-. Likewise, insofar as the subject AY is concerned, i.e., AY 2012-2013, the return of income was filed on 29.09.2012. In this AY, the assessee claimed the impugned deduction, i.e., business expenses amounting to Rs.2,77,99,046/-. The assessee, for A.Y. 2012-2013, declared a net loss amounting to Rs.2,78, 22,376/-. The assessee claims that in between it sold a policy in April 2012 *qua* which an invoice was raised on 31.05.2012.

2.7. Insofar as the subject AY is concerned, i.e., AY 2012-2013, the same was selected for scrutiny and the assessment order was framed under Section 143(3) of the Act. The order framing the assessment was passed on 31.12.2014. The Assessing Officer [in short 'AO'], while framing the assessment concluded that since the license was issued by IRDA on 02.02.2012, the assessee's business could not have been set up prior to that date, and therefore, the entire business expenditure amounting to Rs.2,78,22,376/- was required to be disallowed, and capitalized as pre-operative expenses.

2.8. Being aggrieved, the assessee preferred an appeal with the Commissioner of Income Tax (Appeals) [in short 'CIT (A)']. The CIT (A) *vide* order dated 18.10.2016 sustained the order passed by the AO. The assessee carried the matter further and lodged an appeal with the Tribunal. The appeal preferred by the assessee with the Tribunal met the same fate. The Tribunal sustained the view taken by both CIT (A) as well as the AO.

2.9. It is in this backdrop that the assessee preferred the instant appeal.

Submissions on behalf of the assessee:

3. Mr. Ajay Vohra, learned senior counsel, who appears for the assessee, has submitted that the findings returned by the Tribunal, that the business of the assessee was set up on 02.02.2012 when it was issued the direct-broker's license, was perverse. According to Mr. Vohra, the Tribunal lost sight of the fact that there was a difference between the setting-up and the commencement of the business. Mr. Vohra contended that the reliance placed on the judgment of the Supreme Court rendered in ***CWT vs. Ramaraju Surgical Cotton Mills Ltd., AIR 1967 SC 509*** [in short "***Ramaraju*** Case"] was misplaced. According to him, apart from anything else, the said judgment was rendered under the Wealth Tax Act, 1957 [in short "W.T.A."], and did not pertain to the Act-in-issue. Mr. Vohra went on to submit that there are several judgments in which Courts had distinguished the judgement rendered in the ***Ramaraju*** Case in the context of the Act-in-issue (i.e., Income Tax Act, 1961). In this context, in particular, Mr. Vohra relied upon the judgment of this Court rendered in ***CIT vs. Whirlpool of India* Ltd.*, 318 ITR 347 (Del)*.** Mr. Vohra also relied upon the decisions rendered in ***CIT v. Dhoomketu Builders & Development (P.) Ltd.*, *[2014] 368 ITR 680 (Del)*** **and** ***Western India Vegetable Products Ltd. v. CIT [1954] 26 ITR 151 (Bom).***

3.1. In addition to the aforesaid, Mr. Vohra also drew our attention to the fact [something which we have already noticed hereinabove while capturing the backdrop of the case], that in the earlier AY, i.e., A.Y. 2011-2012, the assessee had filed a loss return, which was accepted by the revenue. It is Mr. Vohra's argument that, since in the earlier AY, the loss return was accepted, the fact that the assessee had already set up his business, logically,

should also be accepted. It was Mr. Vohra's contention that the revenue cannot be allowed to take inconsistent stands. In this context, Mr. Vohra relies upon the judgment of the Supreme Court rendered in ***Shasun Chemicals and Drugs Ltd. vs. Commissioner of Income Tax-II, Chennai, [2016] 388 ITR 1 (SC).***

Submissions on behalf of the revenue:

3.2. On the other hand, Mr. Ruchir Bhatia, who appears on behalf of the revenue, submitted that the common thread which passes through the judgments cited by Mr. Vohra is that a business is set up when the assessee is in a position to carry on its business. It is Mr. Bhatia's contention that, since the object of the assessee's business was to carry on insurance work; it could not have carried on the said business unless it had been issued a license by the IRDA. Furthermore, in support of his submission, Mr. Bhatia says that under Regulations 8 and 17 of 2002 Regulations, IRDA was empowered to reject the application of the assessee for grant of a license.

3.3. In support of his plea, Mr. Bhatia relied upon the judgement rendered by the Supreme Court in the ***Ramaraju*** Case and the judgment of the Division Bench of this Court rendered in ***Marvel Polymers (P.) Ltd. vs. Commissioner of income-tax***, [2007] 165 TAXMAN 618 (DELHI) [in short "***Marvel Polymers (P.) Ltd.*** Case"].

Analysis and reasons:

4. We have heard the learned counsel for the parties and perused the record. The facts, noted by us hereinabove, are not in dispute. What comes through, upon a perusal of the record, is as follow: -

(i) The assessee was incorporated on 24.11.2010 as the joint venture of the following entities, i.e., MSIL, Track Component Ltd., Sunbeam Auto

Pvt. Ltd. and IFB Automotive Pvt Ltd.

(ii) The object and purpose for which the assessee was set up, was to conduct the business of soliciting and procuring life and/or general insurance business.

(iii) Within days of its incorporation, the assessee held its first board of directors meeting on 29.11.2010 whereat various decisions were taken, which included, approval of the draft application for obtaining broker's license and submission of the same to the IRDA and conferring authority on its CEO to sign the same. A decision was also taken to open a current account with the HDFC bank to facilitate its business. It appears that, on the same date, i.e., 29.11.2010, the assessee also had employees of one of its shareholders i.e., MSIL, deputed to it; as noticed above. The employees, who were deputed to the assessee, were made to undergo mandatory training as insurance brokers for the stipulated minimum period of 100 hours. The assessee, followed this up, by preferring an application with the IRDA for issuance of a direct broker's license. This application was filed on 01.12.2010.

(iv). In furtherance of its business, the assessee also entered into operating lease agreements for conducting insurance broking business. These lease agreements were executed on 01.06.2011. The assessee established offices in 29 locations across the country.

(v). In the background of these events, the assessee filed its return of income for the first AY, since its incorporation, on 30.09.2011. As alluded to hereinabove, the assessee declared a loss of Rs.57.582/-. This return, though, was accepted by the revenue as it is and not subjected to scrutiny. The assessee was issued a direct brokers' license by IRDA only on 02.02.2012.

5. Given these facts, we are required, essentially, to determine whether the business expenditure incurred by the assessee could have been disallowed. In other words, in the context of the facts obtaining in the present case, can it be said, that the business was set up by the assessee only when it was issued a license by IRDA.

5.1 However, before we reach a conclusion, one way or the other, concerning the said issue, there are a couple of aspects that are required to be noticed. The first aspect which requires to be noticed is that the Act does not define the expression "setting up of business". This expression finds mention though in Section 3 of the Act; which defines "previous year". A perusal of Section 3 of the Act would show that the "previous year" has been defined as the financial year [in short 'FY'] immediately preceding the AY. However, insofar as a newly set up business or profession is concerned, or *qua* a source of income newly coming into existence, the FY, as per the proviso to Section 3 of the Act, is the period spanning between the date of setting up of the business or profession [or as the case may be, the date on which the source of income newly comes into existence] and the date when the financial year ends. Therefore, if a newly set up business is set up in the financial year, the previous year begins from the date when it is set up and ends with the date on which the financial year ends.

5.2. Thus, the previous year gets tied in with Section 4 of the Act, which is, the charging section. In brief, Section 4, *inter alia*, provides that income arising in the previous year is chargeable to tax in the relevant AY. Thus, income from business and profession, which is carried out in the previous year, can be brought to tax under Section 28 of the Act. This income, in terms of Section 29 of the Act, is required to be computed in accordance with the provisions contained in Sections 30 to 43D of the Act. The fact

that, in the instant case, the assessee took the stand that it had set up its business when it filed its return of income for AY 2011-2012 attains significance. When this was put to Mr. Bhatia, he did submit that since the return was not put to scrutiny it would not have much relevance. While this may be true insofar as the assessment of income is concerned, to our minds, it is an indicator that insofar as the assessee is concerned, it had taken a stand that it was ready to do its business.

5.3. The judgments cited above, both on behalf of the assessee as well as the revenue, have a common thread running through them. The common thread, according to us, is that: Firstly, there is a difference between setting up and commencement of business. Secondly, when the expression "setting up of business" is used, it, merely, means that the concerned assessee is ready to commence business and not that it has actually commenced its business. Therefore, when, the commencement of business is spoken of, in contradiction to the expression "setting up of business", it only refers to a point in time when the assessee actually conducts its business; a stage, which, it necessarily reaches after the business is put into a state of readiness. This distinction has been drawn in a series of judgments starting with the judgement rendered by the Bombay High Court in ***Western India Vegetable Products Ltd.*** Case. The judgment of the Supreme Court in the ***Ramaraju*** Case cites with approval the dicta laid down in ***Western India Vegetable Products Ltd.*** Case.

5.4. It is important to note that in the ***Ramaraju*** Case, the Supreme Court was called upon to interpret a provision of the W.T.A. and, in this context, deal with the interplay between Section 5(1)(xxi) and the second proviso appended to it. The assessee, in that case, had sought deduction of expenditure incurred by it in setting up a new spinning unit. The revenue

disallowed the deduction on the ground that the unit was **set up before 01.04.1957 i.e., the date when W.T.A. came into force**. The facts which obtained on record showed that certain activities were undertaken before 01.04.1957 while some other activities such as completion of the factory building, erection of plant and machinery, and securing a license from the Factory Inspector occurred after 01.04.1957. The assessee had failed not only before the assessing officer but also before the first and the second appellate authority, i.e., the Tribunal. It was only when the assessee reached the High Court that it was able to put forth its case successfully that it had set up its business after 01.04.1957. The Supreme Court, while adjudicating upon the appeal filed by the revenue, applied the dicta obtaining in ***Western India Vegetable Products Ltd.*** Case. The Supreme Court did not permit the revenue to argue that although the operations for establishment of the new unit had commenced prior to 01.04.1957, the unit was set up thereafter. The Supreme Court observed that since all along, the case projected by the revenue was that assessee had not set up its unit before 01.04.1957, it would have to be concluded that the unit was set up at the same time when the operation for its establishments commenced. The important point to be noticed is the difference in the language which appears in proviso to Section 3 of the Act [i.e., the Income Tax Act, 1961] and that which obtained in the provisions of the W.T.A. considered in ***Ramaraju*** Case. Pertinently, the deduction was available under the W.T.A. to that portion of the net wealth of a company/assessee, [which was established with the object of carrying on industrial undertaking in India] – as was employed by it, in a new and separate undertaking that was set up after the commencement of the said Act by way of substantial expansion of its undertaking. The deduction was, however, available only for five successive assessment years commencing

with the assessment year next following **"the date on which the company commences operations for the establishment of such unit"**. As noticed by the Supreme Court, the word "set up" was found only in the principal clause. The Supreme Court was thus, called upon to *inter alia* determine as to whether operations for establishment of the new unit had commenced, as claimed by the assessee. Having found so, it sustained the view of the High Court.

5.5. Likewise, in our view, the judgement rendered in ***Marvel Polymers (P.) Ltd.*** Case is distinguishable from the facts obtaining in the instant case. The assessee, in that case, was said to be in the business of manufacturing and trading in footwear. The assessment year under consideration was 1998-1999. A finding of fact was returned that the assessee had carried out a singular trading activity only to obtain sales tax registration and had employed labour only on 01.04.1998. Based on these facts, the Court concluded and, thus, agreed with the Tribunal, that the assessee's business was not set up, i.e., it was not ready to commence either trading or manufacturing activity in the period under consideration.

6. As noticed above, the assessee did all that, which was necessary, to set up the insurance broking business. Only to recapitulate, the assessee, after its incorporation opened a bank account, entered into an agreement for deputing employees (who were to further its insurance business), gave necessary training to the employees, executed operating lease agreements, and resultantly, set up offices at 29 different locations across the country. Besides this, as noticed above, the application for obtaining a license from IRDA was also filed on 01.12.2010. In the instant case, IRDA took more than a year in dealing with the assessee's application for issuance of a license. The license was issued only on 02.02.2012 although the assessee

was all primed up, i.e., ready to commence its business, if not earlier, since 01.06.2011.

7. Given this position, we are of the view that the finding recorded by the Tribunal that the assessee set up its business only on 02.02.2012 was perverse and erroneous in law. The assessee, having acquired the necessary wherewithal and physical infrastructure for carrying on its business - it was only waiting for the approval of its application for commencement. The Tribunal failed to appreciate the difference between the assessee being ready to commence business and the date from which it conducts business or, as in this, allowed to conduct. It has to be understood that business does not conform to, metaphorically speaking, the "cold start" doctrine. There is, in most cases, hiatus between the time a person or entity is ready to do business and when business is conducted. During this period, expenses are incurred towards keeping the business primed up. These expenses cannot be capitalized as suggested by the authorities below.

8. We are of the view that if Mr. Bhatia's submission was to be accepted, then, it is quite likely that if, in a given situation, the statutory authority, which is required to grant the approval, delays the issuance of the license, the expenses incurred, in the interregnum, would not be allowed as business expenditure. As noticed above, in this case, the AO, based on the facts noted above, has concluded that the expenses incurred by the assessee are preoperative and have to be capitalised. This approach destroys business efficacy and is not countenanced by the law.

Conclusion: -

9. In our view, the authorities below have misdirected themselves on facts, and therefore, the questions of law framed hereinabove are answered in favour of the assessee and against the revenue. The impugned order

passed by the Tribunal is set aside.

10. The appeal is allowed in the aforesaid terms.

RAJIV SHAKDHER, J

TALWANT SINGH, J

APRIL 12, 2021
mr

Click here to check corrigendum, if any