INCOME TAX APPELLATE TRIBUNAL

DELHI BENCH "A": NEW DELHI

BEFORE

SHRI ANIL CHATURVEDI, ACCOUNTANT MEMBER
AND
MS. ASTHA CHANDRA, JUDICIAL MEMBER

ITA No. 3161/Del/2019
Assessment Year: 2015-16

M/s. Bigfoot Retail Solution Pvt. Ltd., 81A/41, Punjabi Bagh West, New Delhi – 110 028 PAN AAECB7131Q	Vs.	ACIT, Circle 5(1) Room No. 102, Ayakar Bhawan, New Delhi.
(Appellant)		**(Respondent)**

Assessee by:	Shri R.M. Mehta, CA
Department by :	Shri Rajinder Jha, Sr. DR
Date of Hearing	28.04.2022
Date of pronouncement	18.07.2022

O R D E R

PER ASTHA CHANDRA

The appeal by the assessee is directed against the order dated 27.02.2019 of the Ld. Commissioner of Income Tax (Appeals)- 2, New Delhi **("CIT(A)")** pertaining to the assessment year **("AY")** 2015-16.

2. The assessee is a company engaged in the business of providing IT enabled and BPO services. It filed its return for AY 2015-16 on 15.09.2015 declaring loss of Rs. 2,20,29,872/-. The case was selected for scrutiny through CASS. The assessment was completed on 11.09.2017 under section 143(3) of the Income Tax Act, 1961 **("the Act")** on net loss of Rs. 39,03,530/- resulting in addition of Rs. 9,95,086/- under section 56(2)(viib); addition of Rs. 6,82,055/- due to difference in TDS between ITR and 26AS;

security deposit of Rs. 1,53,20,438/- shown by the assessee; company international system expenses of Rs. 8,89,844/- and telephone and internet expenses of Rs. 2,38,919/-. On appeal, the Ld. CIT(A) allowed part relief. The assessee is in further appeal against sustaining the addition of Rs. 9,95,086/- on account of excess share premium received by the assessee; disallowance of Rs. 8,89,844/- being company international system expense and disallowance of Rs. 1,19,460/- out of telephone and internet expenses and all the four grounds of appeal relate thereto.

3. Ground No. 1 is of general nature.

4. Ground No. 2 relates to addition of Rs. 9,95,086/- on account of excess share premium received by the assessee. During assessment proceedings the Ld. AO raised a query in this regard to which the assessee vide letter dated 24.08.2017 replied that:

> *"1. 3180 shares have been issued to Nirvana Digital Investment Holding Co. Ltd. which is foreign company and the provisions of section 56(2)(viib) are applicable to the shares issued to resident persons only. Since Nirvana Digital Investment Holding Co. Ltd. is a foreign company, therefore, the provisions of see. 56(2)(viib) are not applicable to the shares allotted to this company.*
>
> *2. 3180 shares were issued to Nirvana Digital India Fund which is a venture capital fund and as per the first proviso to sec. 56(2)(viib) premium received by a venture capita! undertaking from venture capital company or venture capital fund has been excluded from the rigours of sec. 56 (2)(viib). The assessee submitted a letter dated 27.9.2011 addressed-to DGM, Division of Funds to prove that Nirvana Digital India Fund is a venture capital fund, The body of the letter is reproduced as below:*
>
> *"We, IL&FS Trust Company Ltd, (ITCL) are acting as trustee to the Patni New Age Trust (the trust), a registered Venture Capital Fund with SEB! having Registration no. IN/VCF/11-12-0216.*

In capacity as Trustee to the aforesaid Trust, we are submitting a copy of the Private Placement Memorandum of Nirvana Digital India Fund, which is a scheme of Patni New Age Trust, It is clarified that Nirvana Digital India Fund is the first scheme of Patni New Age Trust."

The Ld. AO observed that it is clear from the above that the Patni New Age Trust is a Venture Capital Fund **("VCF")** but nowhere it has been mentioned that Nirvana Digital India Fund is a VCF. The assessee has not proved that first proviso to section 56(2)(viib) is applicable. According to him the allowable premium as per Rule 11UA is Rs. 10.07 per share whereas the assessee has received premium of Rs. 322.99 per share. He therefore added excess premium of Rs. 9,95,086/- (3180 x 312.99) to the income of the assessee.

4.1 Before the Ld. CIT(A) the assessee contended that as per section 56(2)(viib) of the Act taxability arises when a company receives consideration exceeding fair market value of shares from resident. As per first proviso to section 56(2)(viib), exclusion has been provided where the consideration of shares is received by Venture Capital Undertaking **("VCU")** from Venture Capital Fund or Venture Capital Company. In the case of the assessee, the share premium was received by Venture Capital Undertaking (VCU) i.e. Bigfoot Retail Solutions Pvt. Ltd. from Venture Capital Fund (VCF) i.e. Nirvana Digital India Fund which is first scheme of Patni New Age Trust. Following documents were produced to substantiate that Nirvana Digital India Fund is Venture Capital Fund:

1) Certificate of registration as Venture Capital Fund issued by SEBI vide No. 11-12/0216 in the name of Patni New Age Trust. Nirvana Digital India Fund is a first scheme of Patni New Age Trust.
2) Letter filed by IL&FS Trust Company Ltd. (Trustee to Patni New Age Trust) with SEBI.
3) Copy of Income Tax return filed by Nirvana Digital India Fund for AY 2015-16 showing that it is registered with No. INVCF 11-12/0216 and claimed exemption under section 10(23FB) of the Act.

4) The financial statement of Nirvana Digital India Fund for the year ended March 2015.

It was contended on the basis of above evidence that Nirvana Digital Fund qualified as Venture Capital Fund, and as per first proviso to section 56(2)(viib) exclusion is provided to Venture Capital Funds, the impugned addition made by the Ld. AO is not correct.

4.2 The contentions of the assessee were not acceptable to the Ld. CIT(A). According to him, the share floating company has to be a Venture Capital Undertaking (VCU) and the purchaser company has to be a VCF. The assessee is not a VCU. It has only received consideration from a VCF. Since the assessee is not a VCU it is not covered by first proviso to section 56(2)(viib) of the Act. Relying on Kerala High Court decision in Sunrise Academy of Medical Specialties (I) (P) Ltd., the Ld. CIT(A) confirmed the impugned addition.

4.3 Aggrieved, the assessee is in appeal before the Tribunal.

4.4 The Ld. AR submitted that the investor in this case was an unconnected party at the point of time when the shares in question were issued. The issue of shares at the same premium i.e. Rs. 322.99 was accepted in the case of Nirvana Digital Holding Co. Ltd. , a foreign company which apparently did not attract the provisions of section 56(2)(viib) of the Act. It was further submitted that the assessee was a "Venture Capital Undertaking" as defined in clause (n) of definitions clause of the (Venture Capital Funds) Regulations, 1996 issued by SEBI. It was emphasized that the Ld. CIT(A) has held the investor to be a Venture Capital Fund, the requirements of the first proviso to section 56(2)(viib) stood satisfied. Hence, the assessee was entitled to be excluded from the applicability of section 56(2)(viib) of the Act.

4.5 The Ld. DR relied on the order of the Ld. AO/CIT(A).

4.6 We have given our careful thought to the rival contentions and perused the material on record. Section 56(2)(viib) inserted by the Finance Act, 2012 w.e.f 01.04.2013 provides that where a closely held company receives, in any previous year, from any person being a resident, any consideration for issue of shares that exceeds the face value of such shares, the aggregate consideration received for such shares as exceeds the fair market value of the shares shall be chargeable to income tax under the head "Income from other sources". However, this provision shall not apply where the consideration for issue of shares is received by a Venture Capital Undertaking from a Venture Capital Company or a Venture Capital Fund. Explanation (b) there-under provides that "Venture Capital Company", "Venture Capital Fund" and "Venture Capital Undertaking" shall have the meanings respectively assigned to them in clause (a), clause (b) and clause (c) of Explanation to clause (23FB) of section 10.

4.6.1 Clause (a) of Explanation to section 10(23FB) defines "Venture Capital Company" to mean a company which has been granted a certificate of registration, before the 21st day of May, 2012, as a Venture Capital Fund and is regulated under SEBI (Venture Capital Funds) Regulations, 1996 made under the SEBI Act, 1992.

4.6.2 Clause (b) of Explanation to section 10(23FB) defines "Venture Capital Fund" to mean a fund operating under a trust deed registered under the provisions of the Registration Act, 1908 which has been granted a certificate of registration, before the 21st day of May, 2012, as a Venture Capital Fund and is regulated under the Venture Capital Funds Regulations.

4.6.3 Clause (c) of Explanation to section 10(23FB) defines "Venture Capital Undertaking" to mean a Venture Capital Undertaking as defined in clause (n) of Regulation 2 of the Venture Capital Funds Regulations.

4.6.4 Clause (n) of Regulation 2 of the Venture Capital Funds Regulations defines "Venture Capital Undertaking" to mean a domestic company –

(i) whose shares are not listed on a recognized stock exchange in India;

(ii) which is engaged in the business for providing services, production or manufacture of article or things or does not include such activities or sectors which are specified in the negative list by the Board with the approval of the Central Government by notification in the Official Gazette in this behalf.

4.6.5 The negative list as per the Third Schedule of SEBI (Venture Capital Funds) Regulations, 1996 comprises of non-banking financial services with certain exclusions stated therein, gold financing with certain exclusions stated therein, activities not permitted under Industrial Policy of Govt. of India and any other activities which may be specified by the Board in consultation with Govt. of India from time to time.

5. The issue for consideration before us is whether or not the case of the assessee is covered by the exception to clause (viib) of sub-section (2) of section 56 of the Act.

5.1 The assessee vide letter dated 24.08.2017 to the Ld. AO submitted that the assessee received share premium from the following parties :-

Name of the Party	Number of Equity shares	Per share premium (Rs.)	Total (Rs.)	Remarks
Nirvana Digital Investment Holding Co. Ltd.	3180	322.99	10,27,108	Foreign company
Nirvana Digital India Fund	3180	322.99	10,27,108	Venture Capital Fund
Total	6360		20,54,216	

It was pointed out that Nirvana Digital Investment Holding Co. Ltd. is Mauritius based Company and therefore, the provisions of section 56(2)(viib) are not attracted. It was submitted that the assessee company falls under the category of Venture Capital Undertaking and that it has received the money from Venture Capital Fund i.e. Nirvana Digital India Fund. Therefore, section 56 is not applicable. The assessee submitted documentary evidence before the Ld. AO/CIT(A) to prove that Nirvana Digital India Fund comes

under the category of Venture Capital Fund. Though Ld. AO did not agree with the contention of the assesee that Nirvana Digital India Fund was a VCF, the Ld. CIT(A), in our opinion rightly, on appreciation of the documentary evidence on record, came to the conclusion that the assesee received consideration from a Venture Capital Fund. However, the Ld. CIT(A) was of the view that the assessee is not a VCU. The case of the assessee before the Ld. AO/CIT(A) was that the assessee is a VCU. We have perused the definition of Venture Capital Undertaking given in clause (c) of Explanation to section 10 (23FB) as also its (VCU) definition in clause (n) under the head definitions contained in the SEBI (Venture Capital Funds) Regulations, 1996 issued by the SEBI. The assessee is a private limited company engaged in the business of IT enabled and BPO services. The assessee thus satisfies the twin conditions prescribed under clause (n) of Regulation 2 of the Venture Capital Funds Regulations. Moreover, the assessee company does not fall in the negative list of the Third Schedule of SEBI (Venture Capital Funds) Regulations, 1996 in view of the nature of business carried on by it. We are of the considered view that the assessee fulfils the requisite conditions of being a Venture Capital Undertaking. Therefore, the case of the assessee falls within the ambit of the exclusionary provision contained in first proviso to clause (viib) of section 56(2) of the Act.

5.2 The Ld. CIT(A) referred to the decision of Kerala High Court in Sunrise Academy of Medical Specialities (India) (P) Ltd. This decision is rendered in the context of first proviso to section 68 inserted by the Finance Act, 2012 w.e.f. 1.04.2013. The Hon'ble Court held that section 56(2)(viib) is not controlled by section 68. The Ld. CIT(A) lost sight of the second proviso to section 68 which carves out an exception to the first proviso which says that first proviso shall not apply if the person, in whose name the sum referred to therein is recorded, is a Venture Capital Fund or a Venture Capital Company as referred to in clause (23FB) of section 10. Hence, reliance by the Ld. CIT(A) on the decision (supra) is misplaced. Accordingly, we hold that the first proviso to section 56(2)(viib) is applicable to the case of the assessee and decide ground No. 2 in favour of the assessee.

6. Ground No. 3 relates to disallowance of Rs. 8,89,844/- on account of company international system expense by treating it as capital expenditure which has been upheld by the Ld. CIT(A). In para 7 of his order the Ld. AO observed that the expenses appeared to be of capital in nature. On query the assessee submitted that payment has been made to various parties for subscription services etc. and that expenditure is of recurring nature. The Ld. AO, however, made the impugned disallowance in the absence of any evidence to prove that the expenditure is revenue in nature and that it does not provide enduring benefit.

6.1 Before the Ld. CIT(A) the assessee submitted that the assessee has made payment for subscription services, application usage and payroll software access charges to various parties which require renewals and its benefit is consumed within same financial year. It was the contention of the assessee is that no case was made out by the Ld. AO that the periodic payments made by the assessee for software services were for acquisition of such software and the payment was not for mere usage of software. It was also submitted that payment for usage of software services did not have the effect of any enduring benefit for holding the same as capital in nature. Since the payment made for usage of software did not provide any enduring benefit to the assessee, it did not bring into existence an asset or advantage of enduring nature. In support of the proposition that when expenditure is not incurred for acquiring or bringing into existence an asset or advantage of enduring nature, it cannot be treated as capital expenditure. Following decisions were cited:-

(1) Assam Bengal Cement Co. Ltd. vs. CIT (1965) 27 ITR 34 (SC)

(2) Bombay Steam Navigation Co. (P) Ltd. vs. CIT (1965) 56 ITR 52 (SC)

(3) Hilton Roulunds Ltd. vs. CIT (2018) 92 taxmann.com 368 (Delhi)

(4) CIT vs. J K Synthetics Ltd. (2009) 309 ITR 371 (Delhi)

(5) ACIT vs. M/s. GE Capital Business Process Management Services 64 taxmann.com 156 (Delhi ITAT)

6.2 The Ld. CIT(A) confirmed the disallowance observing that since the software was an integral and essential part of computer, the expenditure on software services was rightly treated as capital expenditure. He mentioned the decision of Delhi Tribunal in Maruti Udyog 92 ITD 119 (Del).

6.3 Aggrieved, the assessee is before the Tribunal.

6.4 The Ld. AR reiterated the same arguments which were advanced before the Ld. AO/CIT(A). The Ld. DR supported the orders of the Revenue authorities.

6.5 We have given our careful thought to the rival submissions and perused the material on record. It is well settled that if the expenditure is not incurred for acquiring or bringing into existence an asset or advantage for the enduring benefit of the business but for running of the business of the assessee more efficiently, it partakes the character of revenue expenditure. The case of the assessee has all along been that it made payment for getting access to pay roll services, subscription services etc. in software wherein the assessee does not get any right to exploit the software for commercial purposes as the ownership remains with the vendor itself. The invoices available on record support the contention of the assessee that payment was made for subscription services and use of software and not for any outright purchase.

6.6 The reliance by the Ld. CIT(A) on the decision of Maruti Udyog (supra) is misplaced as in that case the software was acquired by the assessee which was held to be capital asset and hence expenditure incurred on acquiring the software was held to be capital expenditure. In the case of the assesee before us there is no acquisition of software. The payment was made for mere usage of software. The ownership remained with the vendor.

6.7 We, therefore, hold that the impugned expenditure is of revenue nature and is an allowable deduction. Accordingly, we set aside the order of the Ld. CIT(A) and allow ground No. 3 of the assessee.

7. Ground No. 4 relates to ad-hoc disallowance of Rs. 1,19,460/- out of telephone and internet expenses account. The Ld. AO disallowed 20% of the expenses claimed at Rs. 11,94,595/- amounting to Rs. 2,38,919/- observing that utilisation of the services of telephone and internet for purposes other than business of the assessee cannot be denied. On appeal, the Ld CIT(A) reduced disallowance to 10% of the expenses resulting in upholding of the impugned disallowance of Rs. 1,19,460/- against which the assessee is in appeal before us.

7.1 We have heard the Ld. Representative of the parties and perused the material on record.

7.2 It is observed that the assessee submitted before the Ld. AO/CIT(A) that all telephones are either installed at office premises or used by officers and the employees of the assessee company and that usage of telephone/internet is done by employees for official purposes only. It was also submitted that the impugned expenses were incurred in the course of business of the assessee company and that it was not in the nature of personal expenditure. We agree with the above contentions of the assessee. The Ld. AO/CIT(A) made the observation that there was twelve times increase in the expenditure as compared to the preceding year which is disproportionate but that alone cannot be the basis of disallowance. Genuineness of the expenditure has not been doubted. Moreover, the increase in revenue from Rs. 1,21,78,271/- in the last year to Rs. 5,64,16,108/- in this year has been overlooked by both Ld. AO and Ld. CIT(A).

7.3 We, therefore, hold that the impugned disallowance is not justified at all. Accordingly, the order of the Ld. CIT(A) is set aside. The Ld. AO is directed to delete the disallowance in toto and modify the assessment. Ground No. 4 is thus allowed.

8. In the result, the appeal of the assessee is allowed.

Order pronounced in the open court on 18th July, 2022.

sd/-	**sd/-**
(ANIL CHATURVEDI)	**(ASTHA CHANDRA)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Dated: 18/07/2022

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1. Applicant
2. Respondent
3. CIT
4. CIT (A)
5. DR:ITAT

ASSISTANT REGISTRAR
ITAT, New Delhi

Date of dictation	
Date on which the typed draft is placed before the dictating Member	
Date on which the typed draft is placed before the Other Member	
Date on which the approved draft comes to the Sr. PS/PS	
Date on which the fair order is placed before the Dictating Member for pronouncement	
Date on which the fair order comes back to the Sr. PS/PS	
Date on which the final order is uploaded on the website of ITAT	
Date on which the file goes to the Bench Clerk	
Date on which the file goes to the Head Clerk	
The date on which the file goes to the Assistant Registrar for signature on the order	
Date of dispatch of the Order	