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

+ ITA 107/2017

PR COMMISSIONER OF INCOME TAX-6 Appellant
Through: : Sh. Rahul Chaudhary and Sh. Anurag
Vijay, Advocates.

Versus

NEW DELHI TELEVISION LIMITED Respondent
Through: Sh. Sachit Jolly, Advocate.

CORAM:

HON'BLE MR. JUSTICE S. RAVINDRA BHAT

HON'BLE MR. JUSTICE NAJMI WAZIRI

ORDER

% **27.02.2017**

1. The Revenue's appeal contends that the expenditure reported by the assessee for which it claims benefit under Section 37 was taxable for AY 2007-08. The assessee succeeded before the Income Tax Appellate Tribunal (ITAT) which followed its Special Bench ruling in *Biocon Limited v. DCIT* [2013] 144 ITD 21 (Bang) (SB). The assessee's like expenditure for the previous AY 2006-07 was the subject matter of an appeal by the Revenue. This Court, by its order dated 12.07.2016 (in ITA 366/2016 and connected matter), refused to entertain the appeal. Learned counsel for the Revenue contends that a substantial question of law arises because the reliance placed upon *CIT v. Lemon Tree Hotels* (ITA 107/2015) by the previous order of

this Court is not strictly justified. It was submitted that more importantly, the appeal was rejected on the ground of delay and the observations made by the Court cannot be treated as conclusive.

2. Learned counsel for the assessee appearing on advance notice, on the other hand, urges that there is no infirmity with the approach of the ITAT and that this Court had on 12.07.2016 given reasons for not entertaining the appeal which was not dismissed merely on the ground of delay. The previous order of the Court records *inter alia* as follows:

“7. As far as this issue is concerned, it is pointed out by the learned counsel for the Assessee that the issue stands covered in favour of the Assessee and against the Revenue by the order of this Court dated 18th August, 2015 in ITA No.107/2015 (Commissioner of Income Tax v. Lemon Tree Hotels). The Court had affirmed the order of the ITAT deciding the issue in favour of the Assessee in the said case where the addition made by the AO by way of disallowance of the expenses debited as cost of ESOP in profit and loss account was deleted by the ITAT.

8. In the present case, the ITAT has by the impugned order restored the matter to the file of the AO for re-adjudication. The impugned order of the ITAT is consistent with what has been held by this Court in Commissioner of Income Tax v. Lemon Tree Hotels (supra). Consequently, no substantial question of law arises as far as this issue is concerned.”

3. In *Lemon Tree* (referred to by the previous order), the Court had relied upon a ruling of the Division Bench of the Madras High Court in *CIT Chennai v. PVP Ventures Ltd.* [TC(A) 1023/2005,

decided on 19.06.2012]. In *PVP (supra)*, the Madras High Court, after considering the SEBI's claim held as follows:

“11. As regards the second issue which is now canvassed before this Court, viz. On the issue of expenditure of 66.82 lakhs towards the issue of shares to the Employees Stock Option is concerned, the Tribunal pointed out that the shares were issued to the employees only for the interest of the business of the assessee to induce employees to work in the best interest of the assessee. The allotment of shares was done by the assessee in strict compliance of SEBI regulations, which mandate that the difference between the market prices and the price at which the option is exercised by the employees is to be debited to the Profit and Loss. Tribunal in its order stated that it was a benefit conferred on the employee. So far as the company is concerned, once the option was given and exercised by the employee, the liability in this behalf got ascertained. This was recognized by SEBI and the entire Employees Stock Option Plan was governed by guidelines issued by SEBI. On the facts thus found, the Tribunal held that it was not a case of contingent liability depending on the various factors on which the assessee had no control. The expenditure in this behalf was an ascertained liability, thus the expenditure incurred being on lines of the SEBI guidelines, there could be no interference in the relief granted by the Assessing Authority for the expenditure arising on account of Employees Stock Option Plan. This expenditure incurred as per SEBI guidelines and granted by the Officer could not be considered as erroneous one calling for exercise of jurisdiction under Section 263 of the Act.”

4. The Special Bench ruling in *Biocon (supra)* considered the matter rather elaborately and also examined all the previous decisions.

It scrutinized different accounts of ESOPs and the points of time when they could have vested. The observations of the Special Bench in this regard, *inter alia*, are as follows:

“9.3.5 When we consider the facts of the present case in the backdrop of the ratio laid down by the Hon’ble Supreme Court in Bharat Earth Movers (supra) and Rotork Controls India (P) Ltd.(supra), it becomes vivid that the mandate of these cases is applicable with full force to the deductibility of the discount on incurring of liability on the rendition of service by the employees. The factum of the employees becoming entitled to exercise options at the end of the vesting period and it is only then that the actual amount of discount would be determined, is akin to the quantification of the precise liability taking place at a future date, thereby not disturbing the otherwise liability which stood incurred at the end of the each year on availing the services.

9.3.6 As regards the contention of the ld. DR. about the contingent liability arising on account of the options lapsing during the vesting period or the employees not choosing to exercise the option, we find that normally it is provided in the schemes of ESOP that the vested options that lapse due to non-exercise and/or unvested options that get cancelled due to resignation of the employees or otherwise, would be available for grant at a future date or would be available for being re-granted at a future date. If we consider it at micro level qua each individual employee, it may sound contingent, but if view it at macro level qua the group of employees as a whole, it loses the tag of ‘contingent’ because such lapsing options are up for grabs to the other eligible employees. In any case, if some of the options remain unvested or are not exercised, the discount hitherto claimed as deduction is required to be reversed and offered for taxation in such later year. We, therefore, hold that the

discount in relation to options vesting during the year cannot be held as a contingent liability.

C. Fringe benefit

Act 2005 w.e.f. 1.4.2006. Memorandum explaining the provisions of the Finance Bill, 2005 highlights the details of the Fringe Benefits Tax. It provides that : 'Fringe benefits as outlined in section 115WB, mean any privilege, service, facility or amenity directly or indirectly provided by an employer to his employees (including former employees) by reason of their employment. Charging section 115WA of this Chapter provides that: "In addition to the income tax charged under this Act, there shall be charged for every assessment year.....fringe benefit tax in respect of fringe benefits provided or deemed to have been provided by an employee to his employees during the previous year....."'. Section 115WB gives meaning to the expression "Fringe Benefits. Sub-section (1) provides that for the purposes of this Chapter, 'fringe benefits' means any consideration for employment as provided under clauses (a) to (d). Clause (d) which is relevant for our purpose, states that: any specified security or sweat equity shares allotted or transferred, directly or indirectly, by the employer free of cost or at concessional rate to his employees (including former employee or employees) shall be taken as fringe benefit. Explanation to this clause clarifies that for the purposes of this clause, - (i) "specified security" means the securities as defined in clause (h) of Section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956) and, where employees' stock option has been granted under any plan or scheme thereof, includes the securities offered under such plan or scheme. Thus it is discernible from the above provisions of the Act that the legislature itself contemplates the discount on premium under ESOP as a benefit provided by the employer or its employees during

the course of service. If the legislature considers such discounted premium to the employees as a fringe benefit or any consideration for employment, it is not open to argue contrary. Once it is held as a consideration for employment, the natural corollary which follows is that such discount (i) is an expenditure; (ii) such expenditure is on account of an ascertained (not contingent) liability; and (iii) it cannot be treated as a short capital receipt. In view of the foregoing discussion, we are of the considered opinion that discount on shares under the ESOP is an allowable deduction.

11. IF YES, THEN WHEN AND HOW MUCH?

10.1 Having seen that the discount under ESOP is a deductible expenditure under Section 37(1), the next question is that 'when' and for 'how much' amount should the deduction be granted?

10.2 The assessee is a limited company and hence it is obliged to maintain its accounts on mercantile basis. Under such system of accounting, an item of income becomes taxable when a right to receive it is finally acquired notwithstanding the fact that when such incomes is actually received. Even if such income is actually received in a later year, its taxability would not be evaded for the year in which right to receive was finally acquired. In the same manner, an expense becomes deductible when liability to pay arises irrespective of its actual discharge. The incurring of liability and the resultant deduction cannot be marred by mere reason of some difficulty in proper quantification of such liability at that stage. The very point of incurring the liability enables the assessee to claim deduction under mercantile system of accounting. We have noticed the mandate of the Hon'ble Supreme Court in Bharat Earth Movers (supra) that if a business liability has definitely arisen in an accounting year, then the deduction should be allowed in that year itself

notwithstanding the fact that such liability is incapable of proper quantification at that stage and is dischargeable at a future date. It follows that the deduction for an expense is allowable on incurring of liability and the same cannot be disturbed simply because of some difficulty in the proper quantification. A line of distinction needs to be drawn between a situation in which a liability is not incurred and a situation in which the liability is incurred but its quantification is not possible at the material time. Whereas in the first case, there cannot be any question of allowing deduction, in the second case, deduction has to be allowed for a sum determined on some rational basis representing the amount of liability incurred.”

5. Having regard to the above discussion, especially that the previous order dated 12.07.2016 in ITA 366/2016 had considered the same items of expenditure, under Section 34, we are of the opinion that no question of law arises. The appeal is accordingly dismissed.

S. RAVINDRA BHAT, J.

NAJMI WAZIRI, J.

FEBRUARY 27, 2017/ajk