

IN THE INCOME TAX APPELLATE TRIBUNAL “B” BENCH : KOLKATA

[Before Hon’ble Shri S.S.Godara, JM & Hon’ble Shri M.Balaganesh, AM]

I.T.A No. 946/Kol/2017

Assessment Year : 2013-14

DCIT,Circle-8(1), Kolkata
(Appellant)

-vs- M/s Magma Fincorp Ltd.
[PAN: AABCM 9445 K]
(Respondent)

For the Appellant : Shri Robin Chowdhury, Addl. CIT Sr. DR

For the Respondent : Smt. A. Chatterjee, AR

Date of Hearing : 04.12.2018

Date of Pronouncement : 07.12.2018

ORDER

Per M.Balaganesh, AM

1. This appeal by the Revenue arises out of the order of the Learned Commissioner of Income Tax(Appeals)-3, Kolkata [in short the Id CIT(A)] in Appeal No.2210/CIT(A)-3/C-8(1)/2015-16 dated 20.02.2017 against the order passed by DCIT, Circle-8(1), Kolkata [in short the Id AO] under section 143(3) of the Income Tax Act, 1961 (in short “the Act”) dated 29.03.2016 for the Assessment Year 2013-14.

2. The adjournment petition preferred by the Id AR was rejected as the issues involved in this appeal are already covered by various decisions of Special Benches of Tribunal

and Hon'ble Supreme Court. Accordingly, we proceed to hear this appeal on hearing the ld DR and based on materials available on record.

3. The first issue to be decided in this appeal is as to whether the ld CITA was justified in granting relief to the assessee in the sum of Rs 33,18,575/- u/s 14A of the Act read with Rule 8D of the Rules in the computation of book profits u/s 115JB of the Act.

3.1. The ld AO observed that the assessee had non-current non-taxable investments having opening value of Rs. 3332.05lakhs and closing value of Rs. 11934.05 lakhs. The average value of investment during the year under consideration was Rs. 7633.15/ lakhs. The assessee was requested to furnish details of expenses incurred on such investments, income from which is not includible in the total income of the assessee. The assessee stated that there was no amount was incurred for earning exempt income and an amount of Rs. 4.98 lakhs was offered for disallowance / s 14A of the Act. The submission of the assessee is considered but found not tenable. It has been clarified by Hon'ble CBDT vide Circular no. 05/2014 dated 11.02.2014 that the legislative intent is to allow only that expenditure which is relatable to earning of income and it therefore follows that the expenses which are relatable to earning of exempt income have to be considered for disallowance, irrespective of the fact whether any such income has been earned during the financial-year or not. As the assessee did not maintain any separate books of accounts for accounting for expenses incurred in relation to income not includible in its total income, the amount of expenses actually incurred cannot be ascertained from the assessee's books of accounts satisfactorily. Accordingly, the provisions of section 14A r. w. rule 8Dd of the Act are attracted in the case of the assessee. Therefore, the disallowance u/ s 14A of the Act comes to 0.5% of Rs. 7633.15 lakhs i. e. Rs. 38,16,575/ -. Accordingly, an amount of Rs. 33,18,575/-(38,16,575-4,98,000) is disallowed and added back to the total income of the assessee.

3.2. The Id CITA deleted the disallowance u/s 14A of the Act read with Rule 8D of the Income Tax Rules under normal provisions of the Act as well as in the computation of book profits u/s 115JB of the Act. Aggrieved, the revenue had preferred an appeal before us only on the aspect of disallowance u/s 14A of the Act read with Rule 8D of the Rules in the computation of book profits u/s 115JB of the Act alone.

3.3. We have heard the Id DR. We note that the Special Bench of ITAT Delhi Bench in ACIT vs Vireet Investment (P) Ltd (2017) 82 taxmann.com 415 (Delhi.Trib.)(SB) has held as under:-

“6.22. In view of above discussion, we answer the question referred to us in favour of assessee by holding that the computation under clause (f) Explanation 1 to section 115JB(2) is to be made without resorting to the computation as contemplated u/s 14A read with Rule 8D of the Income-Tax Rules, 1962.”

Respectfully following the judicial precedent relied upon hereinabove, we restore the matter to Id AO to calculate the book profit u/s 115JB of the Act after working out the disallowance, if any, in terms of clause (f) to Explanation 1 of Section 115JB of the Act independently after considering the expenses debited in the profit and loss account as mandated under the provisions of law. We would like to state that the disallowances made under the provisions of Sec. 14A r.w.s 8D of the IT Rules, cannot be applied to the provisions of Sec. 115JB of the Act. Accordingly, Ground No. 1 of revenue's appeal is allowed for statistical purposes.

4. The next issue to be decided in this appeal is as to whether the Id CITA was justified in allowing the ESOP expenses of Rs 23,98,000/- in the facts and circumstances of the case.

4.1 . The Id AO observed that assessee in its Income Tax computation claimed Rs.23.98 lakhs on account of ESOP extra allowance. ESOP is a plan wherein an option is provided by the employer to employee to opt for issue of shares in the company at the

end of vesting period on satisfying specific conditions set in by employer at an agreed pre-determined discounted price against a commitment from the employee of provision of uninterrupted services to the company. The ESOP expense of Rs. 23.98 lakhs have not been reflected in the books and is not an allowable expense under the provisions of the Act. Accordingly, an amount of Rs. 23.98 lakhs is disallowed and added back to the total Income of the assessee.

4.2. The assessee argued that the expenditure incurred towards ESOP is an allowable expenditure. Without prejudice to the same, the assessee submitted that ESOP is a scheme under which the Directors, Officers and Employees receive a right to purchase securities or shares of the company at a pre-determined price, lower than the market value. The ESOP discount is a taxable perquisite to the employee at the time of exercise of option, and its valuation is to be done by considering the fair market value of the shares on the date on which the option is exercised. Since the remuneration to the employees under the ESOP is the amount of discount with respect to the market price of shares at the time of exercise of option, the employee cost in the hands of the company should also be respect to the same base. With regard to the Id AO's allegation that the assessee's claim on account of ESOP discount had not been reflected in the books of account, the assessee submitted that during the financial year 2012-13, the assessee had debited Rs 13.05 lacs as Employee Compensation Expenses on account of ESOP under Note 23 of Employee Benefit Expenses in its audited financial statements and had claimed the same as an allowable expenditure. The company has amortised the ESOP expenditure of Rs 13.05 lacs during this year, in the books on the basis that the entire amount has been amortised over the vesting period. However, an amount of Rs 23,98,000/- claimed by the assessee on account of ESOP discount is an additional discount provided to the employees by the assessee which is the amount of discount calculated with reference to the market price at the time of grant of option and the market price at the time of exercise of option. Since the actual amount of employee cost

can be precisely determined only at the time of exercise of option by the employees, the provisional amount of discount availed as deduction during the vesting period needs to be adjusted in the light of the actual discount on the basis of the market price of the shares at the time of exercise of options. Thus it was pleaded that the said expenditure incurred by the assessee is an extra allowance by the assessee to its employees, which is the difference in the amount of discount calculated with reference to the market price at the time of grant of option and the market price at the time of exercise of option and hence cannot be reflected in the books of account. Further it is to be noted that the additional allowance of Rs 23,98,000/- is a taxable perquisite in the hands of the employees, and tax was accordingly deducted on it and hence has been duly offered to tax by the employees.

4.3. The Id CITA placed reliance on the Special Bench decision of Bangalore Tribunal in the case of Biocon Ltd vs DCIT reported in 35 taxmann.com 335 wherein it had considered the allowability of ESOP expenses in detail and had held the discount on ESOP as a part of employee's cost and hence allowable in the hands of the employer. Accordingly, the Id CITA deleted the disallowance of Rs 23,98,000/- . Aggrieved, the revenue is in appeal before us.

4.4. We have heard the Id DR. We find that the issue under dispute is squarely covered by the Special Bench decision of Bangalore Tribunal supra and respectfully following the same, we find no infirmity in the order of the Id CITA granting relief to the assessee. Accordingly, the Ground No. 2 raised by the revenue is dismissed.

5. The last issue to be decided in this appeal is as to whether the Id CITA was justified in deleting the addition made in the sum of Rs 2,83,30,000/- towards exchange loss in the facts and circumstances of the case.

5.1. The brief facts of this issue are that during the relevant A.Y. the assessee has booked Mark to Market profit of Rs. 283.30 lakhs shown as negative figure under Note 24 'finance cost' arising on account of derivative transactions. It is noticed from the computation of income that the same amount has been reduced from the taxable profit in the computation of income. The assessee has referred to the Board's Instruction No. 3/10 dated 23.03.2010. It is noticed that this instruction of the Hon'ble Board is applicable in the case of MTM loss on derivatives. Herein the assessee has not furnished any detail of the underlying assets, meaning thereby whether the transaction is related to the business or not. In the absence of the details of transactions it cannot be denied that the transaction can be related to the business of the assessee. AS-11 deals with giving of accounting treatment for the effects of changes in foreign exchange rates. In case of the revenue items falling under section 37(1), para 9 of AS-11, which deals with recognition of exchange differences, needs to be considered. Under this para, exchange differences arising on foreign currency transactions have to be recognized as income or as expense in the period in which they arise. The important point to be noted is that AS-11 stipulates effect of changes in exchange rate vis-a-vis monetary items denominated in a foreign currency to be taken into account for giving accounting treatment on the balance sheet date. Therefore, an enterprise has to report the outstanding liability relating to import of raw materials using closing rate of exchange. Any difference, loss or gain arising on conversion of the said liability at the closing rate, should be recognized in the profit and loss account for the reporting period. In conclusion, it may be stated that in order to find out if an expenditure is deductible, the following factors have to be taken into account (i) whether the system of accounting followed by the assessee is mercantile system, which brings into debit the expenditure amount for which a legal liability has been incurred before it is actually disbursed and brings into credit what is due, immediately it becomes due and before it is actually received; (ii) whether the same system is followed by the assessee from the very beginning and if there was a change- in the system, whether the change was bona fide; (iii) whether the assessee has

given the same treatment to losses claimed to have accrued and to the gains that may accrue to it; (iv) whether the assessee has been consistent and definite in making entries in the account books in respect of losses and gains; (v) whether the method adopted by the assessee for making entries in the books both in respect of losses and gains as per nationally accepted Accounting Standards; (vi) whether the system adopted by the assessee is fair and reasonable or is adopted only with a view to reduce the incidence of taxation. In view of the above, deduction of Rs. 2,83,30,000/- claimed by the assessee in its computation of income is disallowed and added back to the total income of the assessee.

5.2. The Id CITA deleted the addition by observing as under:-

“I have carefully considered the facts of the case, assessment order, the remand report and the other material brought on record. The assessing officer had disallowed an amount of Rs. 283.30 lacs shown as negative figure under note 24 as finance cost arriving out of derivative transactions. The reason given for disallowance was that in absence of details for transactions, it could not be denied that the transactions were related to the business of the assessee. However the appellant has explained that the amount reduced this year was actually related to the reversal of entry in the previous year. During the year ended on 31.03.20 12 the assessee had a MTM loss on reinstatement of hedging transactions of Rs. 522.68 lacs which had been claimed in the books of accounts. At the time of filing of return for A.Y 2012-13 the said amount was added back while computing returned income. As on 01.04.2012 in the books the said loss of Rs. 522.68 lacs had been reversed and therefore appeared an income side. Also as on 31.03.2013 there was MTM loss of Rs. 239.38 which appeared as expenditure in the books. While filing of return for the year, the appellant reversed both the entries resulting in net reduction of Rs. 283.30 lacs. The appellant has produced copy of computation of income for both the years to support its contention. Thus it can be seen that the deduction is on 'account of reversal of entry which had been considered as part of income in A.Y 2012-13. Considering this, there is no justification in adding back the amount of Rs. 283.30 lacs. The addition of Rs. 283.30 lacs is accordingly deleted.”

5.3. Aggrieved, the revenue is in appeal before us.

5.4. We have heard the Id DR. We find that the issue under dispute had been dealt elaborately by the Id CITA supra which, in our considered opinion, does not call for any interference. Accordingly, the Ground No. 3 raised by the revenue is dismissed.

6. In the result, the appeal of the revenue is partly allowed for statistical purposes.

Order pronounced in the Court on 07.12.2018

Sd/-

[S.S. Godara]
Judicial Member

Sd/-

[M.Balaganesh]
Accountant Member

Dated : 07.12.2018

SB, Sr. PS

Copy of the order forwarded to:

1. DCIT, Circle-8(1), Kolkata, Aayakar Bhawan, 5th Floor, P-7, Chowringhee Square, Kolkata-700069.
2. M/s Magma Fincorp Ltd, 24, Park Street, Kolkata-700016
- 3..C.I.T.(A)-
4. C.I.T.- Kolkata.
5. CIT(DR), Kolkata Benches, Kolkata.

True copy

By Order

Assistant Registrar
ITAT, Kolkata Benches