THE INCOME TAX APPELLATE TRIBUNAL
"K" Bench, Mumbai
Before Shri Shamim Yahya (AM) & Shri Pawan Singh (JM)

I.T.A. (TP) No. 2059/Mum/2017 (Assessment Year 2012-13)

AGC Networks Limited Equinox Business Park Tower No. 1 (Peninsula Techno Park) Off Bandra Kurla Complex LBS Marg, Kurla West Mumbai-400 070. PAN : AAACT3992M	Vs.	DCIT Circle-14(1)(2) Room No. 470 Aayakar Bhavan M.K. Road Mumbai-400 020.
(Appellant)		(Respondent)

Assessee by	Shri Nitesh Joshi & Shri Ketan Ved
Department by	Shri Anand Mohan
Date of Hearing	07.11.2019
Date of Pronouncement	14.01.2020

O R D E R

Per Shamim Yahya (AM) :-

This appeal by the assessee is directed against the order of the Assessing Officer dated 31.1.2017 passed u/s. 143(3) read with section 144C of the Act pursuant to the direction the of learned Dispute Resolution Panel (DRP) dated 29.1.2016.

2. Issue arising out of the grounds of appeal read as under :-

(i) Transfer pricing adjustment of Rs. 93,6,00,000/-
(ii) disallowance of provisions for expenditure Rs. 2,16,73,001/-.
(iii) disallowance of renovation expenses Rs. 1,38,50,107/-.
(iv) depreciation not allowed on renovation expenses assessed as capital in nature in A.Y. 2005-06 to 2011-12.
(v) addition on account of change in revenue recognition policy.
(vi) disallowance of expenses claimed under employee separation scheme.
(vii) short credit of tax deducted at source.

3. The assessee company in this case in the business of providing telecommunication equipment, services and solutions. The Transfer Pricing Officer (TPO) in this case made an adjustment of Rs. 12.97 crores. Thereafter the Assessing Officer incorporated TPO's order and issued draft order dated 15.3.2016. Subsequently, the assessee filed objections before the DRP.

Transfer Pricing adjustment

4. The Transfer Pricing officer asked for the detail of international transaction of reimbursement of expenses amounting to Rs. 6,52,58,171/-. The TPO was not satisfied that the same was reimbursement of expenses. After further examination the TPO came to the following conclusion :-

> I. Assessee does not dispute service and support rendered to AE across the verticals of Sales, Pre-Sales, Supply Chain, Marketing, Finance and Legal in all his submissions. Assessee's only contention is that they are on a cost to cost basis and in the nature of reimbursement.
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> II. Cost reimbursement cannot be only of salary cost. All other costs incurred by Assessee towards such support services have to factored in.
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> III. Assessee itself has accepted that the service rendered spreads on to Sales, Pre-sales, Supply Chain, Marketing, role of CEO& CSO , Finance and Legal Assistance to AE. After offering wide and complete business and sales support to AE. Assessee can by stretch of imagination call it a stewardship activity.
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> IV. Assessee has changed its allocation key from order sales ratio to employee ratio without any reason and substantiating documents. There's no proof to substantiate the claim of the Assessee that only 51 employees are involved in rendering services to AE. Neither AE books nor AE s employee profile was furnished to substantiate the veracity of claim of the Assesssee. The fresh claim of assessee to consider employee ratio is clearly an afterthought in nature. Moreover, obtaining a ratio of Assessee's employees of 51 of 1124 is incorrect as the assessee's employee profile is spread across two segments and the support services rendered to AE cannot be benchmarked on the ratio of Employee of the Assessee. The same is illogical as it does not capture the role played by Assessee in AE's business. 1124 is the entire employee strength of service and goods segment. This base will lead to absurd results when used. Using the employee ratio of Assessee in NO WAY CAPTURES the benefit flowing to AE. Hence, employee ratio is rejected.
>
> V. Assessee failed to furnish any documents pertaining to AE to show why the cost allocation be not made on the basis of Sales revenue.

Mere explanation without substantiating documents cannot be a ground to reject sales revenue as ratio to determine costs.

VI. The very bifurcation furnished by assessee clearly displays the fact that the Assessee is providing support services to its AE.

VII. It is observed that the costs allocated by the Assessee are in the nature of sales related costs which cannot be considered to be in the nature of shareholders costs by any stretch of imagination. It is purely in the nature of service provided by the Assessee to the AE. Hence, assesse's own allocation key of sales order ratio of 12.5% is relied upon to be the cost driver for the support services rendered by Assessee to its AE.

8.6 In view of the above defects and others which are evident from the discussion above, the price paid in the international transaction has not been determined in accordance with sub-section (1) and (2) of 92C and the information as well as the data used in computation of the arms length price is. not, reliable and correct. The provisions of Sec. 92C(3)(a) & (c) are invoked and the TP documentation is rejected.

The Transfer Pricing officer made further observed that based on the above and the profit and loss account, costs for the traded goods segment have been derived at as follows:

Head of expenses	Rs. in Crores	Less (expenditure pertaining to services)	Total
Employee's Benefit Expenses	107.00	44.7	62.30
Other Expenses	154.80	97.7	57.10
Exceptional items	0.90		0.90
Depreciation and amortization expenses	8.20		8.20
Finance cost	6.30		6.30
Total product sales expenditure			134.80
Cost allocated on the basis of 12.5%			16.85

5. Finally the transfer pricing officer computed on adjustment of Rs. 12.97 crore as under :-

10. In view of the above discussion, final comparables in Marketing Support Services is as under:-

Sr.No.	Name of the company	Margin(%) OP /OC
1	Apitco Limited	24.45%
2	Killick Agencies and Marketing Limited	9.04%

3	BVG India Limited	24.22%
4	Axis Integrated Systems Limited	10.27%
5	Marketing Consultants & Agencies Limited	10.32%
	Grand Average	15.66%

10.2 Even at any point the comparables are rejected, it is brought on record that the Assessee has claimed 9.87% as industry average for marketing support services.

10.3 ADJUSTMENT WORKING

Based on the working in para 9 above, the cost allocated to this segment works out to	Rs.16.85 crores.
Add : Mark up of 15.66% as per above benchmarking	Rs.2.64 crores
Total	**Rs. 19.49**
Less: Remuneration already offered by the Assessee as cost to cost recovery	Rs.6.52 crores
Adjustment to ALP (Rs. 19.49 crores - 6.52 crores)	= Rs. 12.97 crores

11 In view of the above discussion after considering the submissions of the assessee and facts of the case, an adjustment of Rs.12.97 crores is made to the Assessee case.

6. Upon assessee objection the dispute resolution panel gave the following direction :-

"We have considered the submission of the assessee. The claim of the assessee that few of the employees of the assessee were involved in monitoring and guidance to AGC Singapore team while performing the sales activities in system and that the assessee merely monitored such activities and did not render any service with respect to AE's trading activity is contrary to facts mentioned in the transfer pricing report, the submission dated 2/12/2015 and working of the 'cost to be recovered' filed by the assessee alongwith the submission dated 2/12/2015. Similarly, the claim of the assessee that only 51 employees were involved in such activities is also contrary to the submission made before the TPO vide letter dated 2/12/2015. It is clearly an afterthought because if this was the actual position then the assessee had no business to allocate cost on the basis of products sales order ratio over the entire sales team, pre sales team, supply chain team and marketing team. However, in principle we are in agreement with the claim of the assessee that costs which are directly attributable to trading activity being conducted by the assessee should not be allocated to the AE. The AO/TPO shall exclude the expenses which are directly linked

with the trading business of the assessee on furnishing of necessary supporting evidences. Prima facie such expenses are as under:-

a) Exceptional Item (INR 9 millions)
b) Consumption of stores and spares (INR 1 million)
c) Rates and taxes (INR 15 millions)
d) legal and professional fees (INR 13 millions) to the extent they are for assessee's business
e) Advertisement and sales promotion (INR 13 millions)
f) Outward freight, clearing and forwarding charges (INR 34 millions)
g) Commission to others (INR 9 millions)
h) Payment to auditor (INR 5 millions) to the extent they are for assessee's business
i) Exchange differences net (INR 30 millions)
j) Provision for doubtful debts and advances (INR 68 millions)
k) Bank Charges (INR 31 millions}
l) interest so far it relates to fixed assets

Pro rata allocation of following expenses is upheld because possibility of them being related to sales team, pre-sales team and supply chain team cannot be ruled out :-

a) Travelling and conveyance (INR 124 millions)
b) Other expenses (INR 37 millions)
c) interest so far it relates to working capital."

7. In the final assessment order the assessing officer however made the addition of Rs. 12, 97, 00,000/- as per the TPO's order.

8. Against this order assessee is in appeal before us. We have heard both the Counsel and perused the records. The submission of learned Counsel of the assessee is as under :-

"This ground relates to transfer pricing adjustment in respect of reimbursement of expenses received from Aegis Network Pte Limited, associated enterprise in Singapore. The appellant's brief submissions, each of which are in the alternative and without prejudice to any others, are as under:

a. The final assessment order dated 31 January 2017 passed by the AO is not in conformity with the directions of the DRP in its order dated 29 November 2016 as cost relatable to the manufacturing segment as directed to be excluded by the DRP in para 12.2 at pages 36-37 has not been given effect to. The working as per the Appellant and that as done by the AO/TPO in the final assessment order has been handed over at the time of hearing. As per the ITAT order in the case of M/s July Systems & Technologies Private Limited dated 31 October 2018, final assessment order which is not in conformity with

directions of the DRP is illegal and bad in law and hence needs to be quashed and set aside."

b. As per section 92 of the Income tax Act, 1961 ('the Act'), income has to be computed having regard to the arm's length price when-

i. There is an international transaction; and
ii. Income arises from an international transaction.

In the present case, no income arises from any international transaction as the receipt is in the nature of reimbursement. It is an undisputed position that there is no mark-up charged. In this regards relevance is placed on A. P. Moller Maersk A S (2017) 392 ITR 186 (SC) in para 11, page no. 192. Further, the appellant is the parent company of Aegis Network Pte Limited. With a view to guide its subsidiary as well as monitor its functioning, the appellant's CEO, CSO, marketing personnel, finance & legal personnel, supply chain employees, sales executives etc. have spent certain time for its subsidiary. In view thereof, reimbursement of their proportionate salary has been claimed by the appellant. This was purely a shareholder's function. The expenditure has been incurred for the benefit of the appellant and not the subsidiary. Hence, there could not be any mark-up in this transaction.

c. Apart from the salary cost as allocated by the appellant, the TPO has also proportionately allocated the other expenses comprising of power and water charges, rent, repair and maintenance, travelling, telephone, printing and stationery etc. depreciation and amortization cost and finance cost (see para 9 at page i 1 of the TPO's order)

As explained at the time of hearing, these expenses have not been incurred for the subsidiary but relates to the appellant's business. Most glaring amongst this is the finance cost. This cost has been incurred to meet the appellant's requirement of funds for carrying on its business in India. There is not even a remote use of these borrowed funds for the business of the subsidiary. Hence, the TPO erred in allocating expenses other than salary cost to the subsidiary.

d. For arriving at the mark-up to be charged by the appellant on the reimbursement of cost, the TPO identified the following comparables considering the appellant as providing sales support services working out the mark-up as 15.66 % (see para 10.1 at page 15 of the TPO's order).

Sr. No.	Name of Company	Margin (%) OP/OC
1	Apitco Limited	24.45%
2	BVG India Limited	24.22%
3	Killick Agencies & Marketing Limited	9.04%
4	Axis Integrated Systems Limited	10.27%

5	Marketing Consultants and Agencies Limited	10.32%
	Arithmetic mean of companies considered comparable	15.66%

Of the above, the DRP has directed deletion of BVG India Ltd. resulting into arm's length mark-up of 13.53 %. The appellant submits that Apitco Ltd. is not comparable as it is a Government company. See CIT v. Thyssen Krupp Industries India Private Limited. (2016) 385 ITR 612.

In any event, the business of the said entity is also not functionally comparable as they are carrying business in capacity as a government enterprise. Further, this company is engaged in providing services such as asset reconstruction and management, cluster allotment for mega footmarks and environment services, energy related services, infrastructure planning and development, energy audit etc. and undoubtedly this company is a high-end consultancy service provider. In this regard, reliance is placed on Philip Morris Services India SA ruling by the Hon'ble Delhi Court, decision dated 18 December 2018 (Income Tax Appeal No. 1468/2018. If Apitco Ltd. is excluded the arm's length mark-up would work out to 9.88%."

9. Per contra, learned Departmental Representative relied upon the orders of the authorities below.

10. As regards submission of learned Counsel of the assessee that since the Assessing Officer has not followed the direction of learned DRP for the transfer pricing adjustment in our considered opinion the same cannot be said to be fatal. In this regard we note that Hon'ble Apex Court in the case of Kapurchand Shrimal Vs. CIT (131 ITR 451) has expounded that it is the duty of the appellate authority to correct the errors in the orders of the authorities below and remit the matter for their reconsideration with or without direction unless prohibited by law. In our considered opinion ratio from the said Apex Court decision is squarely applicable on the facts of the case here. Hence, in our considered opinion the decision from Hon'ble Apex Court as above is applicable. Hence, we hold that the matter can be remitted for fresh adjudication with necessary directions.

11. As regards the issue of comparables we note that the DRP has itself directed that the BVG India Ltd. should be removed from the list of comparables.

12. As regards comparable APITCO Ltd., we agree with the submission of learned Counsel of the assessee that this is a Government company and needs to be excluded from the list of comparables on the touchstone of Hon'ble Jurisdictional High Court decision in the case of CIT Vs. Thyssen Krupp Industries India Pvt. Ltd. (385 ITR 612).

13. As regards expenses which have been subjected to allocation we find that the DRP has accepted in principle the assessee's plea that costs which are directly attributable to the trading activity conducted by the assessee, should not be allocated to the AE. Thereafter DRP has given certain direction for computation of attributable expenses. In our considered opinion the direction of the DRP in this regard doesn't contain any infirmity. Assessee's contention that the assessee's function is a shareholder function and no allocation and markup is required is totally misplaced. It is abundantly clear from the facts that the assessee is providing services to the AE. The assessee has itself accepted that assessee is guiding and monitoring the functions of the AE and for this purpose assessee CEO CSO, marketing personnel finance and legal personnel supply chain employees, sales executives etc. CSO are all spending times. In this view of the matter the services provided by the assessee to its AE fall under the realm of international transaction and hence determination of arm length price is required. Assessee cannot seek the refuge under the nomenclature that these are shareholder function, and thus avoid benchmarking the international transaction. The decision referred by the learned counsel of the assessee above is in a totally different context. In the said case honourable Supreme Court has held that cost reimbursed by Indian agents for utilising global telecommunication facility cannot be treated as fee for technical services and therefore not taxable. In our considered opinion this case law doesn't fortify the case of the assessee.

14. In the present case instead of making submissions against DRP's direction learned counsel of the assessee has referred to TPO’s selection and allocation of expenses. In our considered opinion we are concerned with the

allocation of expenses as per direction of DRP and not allocation of expenses as per TPO's computation. This is so when the DRP has not entirely upheld the TPO's action. In our considered opinion the DRP direction is cogent and we do not find any infirmity in the same. The learned counsel of the assessee submission about inclusion of finance cost has been taken care of by the DRP when it is mentioning that interest so far as it relates to working capital only need to be considered. It is not the entire finance cost which is being considered by the DRP. Hence we uphold the DRP's direction.

15. Accordingly we direct that Transfer Pricing officer assured compute the ALV keeping in mind our directions as above.

16. Next issue relates to disallowance of provision for expenditure. A sum of Rs. 2,16,73,001/- was disallowed by the Assessing Officer holding them to be contingent. The DRP direction in this regard is as under :-

> "We have considered the submission of the assessee. There is no doubt that provisions for expenses will have to be allowed if they have been actually incurred but bills are yet to be received and corresponding income has been offered for taxation during the year or the work under consideration is a part of the closing stock. The assessee has not demonstrated the same. It is also seen that year after year, the provision made by the assessee is on the higher side only and by doing this, the assessee is postponing its tax liability. Accordingly, the AO is directed to allow the expenditure to the extent of the bills the next year and disallow the balance amount provided the assessee furnishes evidence to show that the responding income has been offered during the previous year under consideration or the corresponding work is part of the closing stock shown by the assessee."

17. At the outset, learned Counsel of the assessee stated that this issue has been decided in assessee's favour by the ITAT, Mumbai "A" Bench in assessee's own case vide order dated 31.8.2019 for A.Y. 2005-06 to 2009-10. On similar disallowance the Tribunal in the above said order has elaborately considered the issue and has held as under :-

> "12. We have considered rival submissions and perused the material on record. We have also applied our mind to the decisions relied upon by the parties. There is no dispute between the parties with regard to the basic facts relating to the disputed addition. The core issue, which is required to be examined is, whether the provision for expenditure made by the assessee is in accordance with Accounting Standards and legal provisions. It is a fact on

record that in respect of some goods/services received/availed by the assessee towards the end of the financial year, the bills/invoices were not raised by the concerned parties within the financial year but were raised in the subsequent year. However, since the assessee is following mercantile system of account, the expenditures incurred during the year have to be accounted for in the books of account. Therefore, in absence of bills/invoices raised by the vendors, the assessee made provision for such expenditure in its books of account. There is no dispute that the provision made by the assessee is on estimate basis. Therefore, it has to be seen whether such estimate of provision made by the assessee is on reasonable and scientific basis and in accordance with business prudence. As could be seen from the facts discussed earlier, the assessee had made provision for expenditure under three distinct heads. While the Assessing Officer has added back the difference between the provision made and actual expenditure incurred under all the three heads, learned Commissioner(Appeals) has restricted such disallowance only in respect of provision made for sundry creditors relating to sales commission, promotion, advertisement, etc. Therefore, it requires consideration whether the provision made can be stated to be in accordance with AS-1 r/w section 145(2) of the Act. In this context, learned Authorised Representative has specifically referred to Para-16 and 17 of AS-1. For ease of reference, we reproduce the aforesaid paragraph herein below:-

> "Considerations in the Selection of Accounting Policies
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> 16. The primary consideration in the selection of accounting policies by an enterprise is that the financial statements prepared and presented on the basis of such accounting policies should represent a true and fair view of the state of affairs of the enterprise as at the balance sheet date and of the profit or loss for the period ended on that date.
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> 17. For this purpose, the major considerations governing the selection and application of accounting policies are:--
>
> a. Prudence
> In view of the uncertainty attached to future events, profits are not anticipated but recognised only when realised though not necessarily in cash. Provision is made for all known liabilities and losses even though the amount cannot be determined with certainty and represents only a best estimate in the light of available information.
>
> b. Substance over
> Form The accounting treatment and presentation in financial statements of transactions and events should be governed by their substance and not merely by the legal form.
>
> c. Materiality
> Financial statements should disclose all "material" items, i.e. items the knowledge of which might influence the decisions of the user of the financial statements."

> 13. A careful reading of the aforesaid paragraphs would reveal that as per Para-16 of AS-1, the Accounting Policy to be selected by the enterprise should represent a true and fair view of the state-of-affair of the enterprise as at the Balance Sheet date and of the profit. Para-17(a) provides that for all known liabilities and losses, which cannot be determined or quantified with certainty, the enterprise by using business prudence can make provision in the light of available information on the basis of a best estimate. Thus, a reading of AS-1 makes it clear that the liability for expenditure incurred during the year if cannot be determined with certainty, the assessee can make a provision for such liability on best estimate on the basis of available information. Thus, though, there cannot be any doubt that for expenditure incurred during the year which cannot be determined with certainty, since the vendors have not raised bills/invoices, the assessee is entitled to make provision on estimate basis, however, such estimate has to be a best estimate. It transpires from record, the assessee is following the aforesaid method of accounting in respect of unbilled expenditure from past years and it has never been disputed by the Department. Additionally, AS-1 provides for creating provision for expenditure on estimate basis keeping in view business prudence and information available. In fact, learned Commissioner (Appeals) also not only recognizes the necessity of making provision for expenditure but has also allowed provision for expenditure not exceeding 10% of the actual expenditure. In our view, there is no such thumb rule either in Accounting Standards or elsewhere to restrict the provision to within the range of 10% of the actual expenditure. It is worth mentioning; the assessee has reversed the provision in the subsequent year and offered to tax. This fact has not been disputed by the Department. Therefore, the ratio laid down in case of CIT V/s Excel Industries Ltd. would apply. More so, when the assessee is consistently following this accounting method from past years. In view of the aforesaid, we hold that the part disallowance sustained by learned Commissioner (Appeals) also deserves to be deleted. Therefore, learned Commissioner (Appeals) direction to grant consequential relief in subsequent assessment year becomes infructuous. This ground is allowed."

18. We find that the facts are same. Accordingly, following the above said Tribunal decision, we direct that this disallowance be deleted.

19. Apropos issue of disallowance of renovation expenses. This issue relates to disallowance of a sum of Rs. 1,38,50,107/- on leasehold premises on the ground the same is capital in nature. Learned Counsel of the assessee states that this issue is also covered in favour of the assessee by the above said ITAT decision. We note that in the above ITAT decision the Tribunal had adjudicated the issue as under :-

> "20. We have considered rival submissions and perused the material on record. We have also applied our mind to the decisions relied upon. The issue before us is, whether the expenditure incurred by the assessee towards

> repair/renovation of leased premise is of capital or revenue nature. On a perusal of the details of expenditure incurred, as submitted in the paper book, we are of the view that by incurring such expenditure, the assessee has not brought into existence any capital asset of enduring nature. A reference to Explanation-1 to section 32(1) of the Act, would reveal that it speaks of capital expenditure incurred towards construction of any structure or renovation or extension or improvement to the building. Thus, on a reading of the aforesaid provisions, it becomes clear that if any expenditure is incurred for construction of any structure or extension or improvement of the building taken on lease would be treated as capital expenditure. The nature of expenditure incurred by the assessee in respect of the leased premises and more particularly the premises at Hyderabad and Bangalore are not of the nature of constructing new structure, extension or improvement of building. Therefore, Explanation-1 to section 32(1) of the Act would not be applicable to the facts of the present case. Though, there cannot be any quarrel with regard to the proposition laid down in the decisions cited before us, however, the nature of expenditure incurred by the assessee with reference to facts of each case would decide whether it is capital or revenue in nature. In the facts of the present case, after examining the details of expenditure incurred by the assessee, we are of the view that it is of revenue nature, hence, has to be allowed. Accordingly, we do so. The decision of learned Commissioner (Appeals) on this issue is, therefore, set aside. Ground raised is allowed.

20. We hold that the issue needs to be examined by the Assessing Officer in accordance with the ITAT decision as above. If the nature of expenditure is same as the one dealt by the ITAT the assessee deserves to succeed. We direct accordingly.

21. Apropos issue of depreciation not allowed on renovation expenses assessed as capital in nature in A.Y. 2005-06 to 2011-12. On this issue learned Counsel of the assessee's submission are as under :-

> This ground is consequential on the basis of the adjudication made for allowability of renovation expenses in the earlier years. The status of the earlier years is as under:
>
> - Renovation expenses have been held by the ITAT to be revenue in nature in the above order passed for assessment years 2005-06 to 2009-10;
> - Assessment year 2010-11 is pending before the Commissioner of Income Tax (Appeals): and
> - Assessment year 201 1-12 is pending before the ITAT.

22. Apropos issue of addition on account of change in revenue recognition policy. On this issue learned Counsel of the assessee states that this issue

has been restored by the ITAT to the file of the Assessing Officer in the above said order. We note that in the above said order the ITAT by dealing with the issue has considered the issue elaborately in para 41 to 45. The Tribunal had remitted the issue to the file of the Assessing Officer with certain directions. We have gainfully refer to the Tribunal order as under :-

> "41. We have considered rival submissions and perused the material on record. We have also carefully applied our mind to the decisions relied upon before us by both the parties. The factual matrix clearly reveals that the assessee has not changed mercantile system of accounting consistently followed by it from the past years. However, it has changed its revenue recognition policy in the impugned assessment year. It is evident, in the past years, the assessee was recognising revenue on the basis of invoices raised for sales effected and service rendered. However, in the impugned assessment year, the assessee has adopted a new system under which it recognizes revenue on the basis of completion of project and on receiving completion certificate from the customers. Undisputedly, due to the change in revenue recognition policy as aforesaid, quite a substantial part of the revenue, which otherwise would have been shown in the impugned assessment year as per the revenue recognition policy consistently followed, has been deferred to subsequent assessment years which resulted in less profit shown of Rs. 22.83 crore. To justify the change in revenue recognition policy, it is the contention of the assessee that in the year under consideration it has shifted its focus from providing specific voice equipment solutions to converged communication solutions as per the business strategy adopted by its Head Office in USA. It is also submitted that the new revenue recognition policy adopted by the assessee is in tune with similar policy adopted by the Head Office and which is also followed by various other reputed organizations/entities. As per section 145(1) of the Act, income chargeable under the head profits and gains of business and profession has to be computed by employing either cash or mercantile system of accounting regularly employed by the assessee. Of course, sub-section (2) of section 145 of the Act prescribes the Accounting Standards to be followed by any class of assessee or any class of income has to be notified by the Central Government. Whereas, sub- section (3) of section 145 of the Act prescribes that if the Assessing Officer is not satisfied with the correctness or completeness of the accounts of the assessee or where the method of accounting provided in sub-section (1) has not been regularly followed by the assessee or income has not been computed in accordance with Accounting Standard notified under sub-section (2), he may proceed to make an assessment to the best of his judgment as provided under section 144 of the Act.
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> 42. It is evident, after examining the factual aspect and the submissions of the assessee the Assessing Officer has observed in the assessment order, though, the assessee to justify with valid reasons the change in revenue recognition policy, however, it was not able to furnish any satisfactory reason

for such change except stating that accounts are to be prepared as per global standard. Further, he has observed that the assessee has not produced any documentary evidence regarding the global standards allegedly followed by it and how it is relevant in the context of Indian Accounting Standard. It is also crucial to bear in mind, as regards Sales Tax and Service Tax the assessee is complying to the statutory requirement in terms with the earlier practice followed by it. In other words, it is paying Sales Tax and Service Tax on the basis of invoices raised towards sales and services.

43. In the aforesaid factual background, it requires to be examined whether the revenue recognition policy followed by the assessee is acceptable. No doubt, the assessee has contended that the change in revenue recognition policy is due to shift in business strategy and as per global standards followed by the Head Office. However, this cannot simply be a reason to change the revenue recognition policy consistently followed over the years. The assessee must furnish cogent material and explanation to justify the change in revenue recognition policy. More so, when such revenue recognition policy has substantially reduced the profit shown by the assessee in the impugned assessment year. The assessee must establish on record why the change in revenue recognition policy, claimed to be in accordance with the alleged global standards, is relevant for chargeability of assessee's income to tax in India, as, such income has to be computed in terms with the provisions of the Indian Income Tax Act and Accounting Standards notified therein. Further, as per the new revenue recognition policy revenue is to be recognized on completion of project and that too on receipt of completion certificate from the customer. It is relevant to observe, the assessee continues to raise bills/invoices on customers on standalone basis as it was consistently doing in the preceding assessment years. However, it is recognising revenue only in respect of completed projects, whereas, showing the rest of the revenue in the Balance Sheet as unearned revenue. In this process, the assessee though is following mercantile system of accounting but it is effectively deferring substantial part of its revenue and profit to future assessment years. Therefore, the onus is all the more on the assessee to justify the change in revenue recognition policy through cogent material and explanation. Though, the assessee may be correct in saying that provisions of Sales Tax and Service Tax laws cannot be imported to determine assessee's tax liability under the Income Tax Act, however, it is also equally true that in the preceding assessment years, the assessee was recognising revenue for income tax purpose on the basis invoices raised towards sales and services. Therefore, when the assessee was following a consistent method over years, it has to demonstrate the compelling circumstances which necessitated change in revenue recognition policy. Therefore, the decisions relied upon by learned Authorised Representative cannot be applied uniformly to assessee's case without examining the factual aspect. Similarly, though, project completion method has been accepted as a recognized method for revenue recognition, however, the assessee must establish on record that the change in revenue recognition policy from invoice based to project completion method is for bona fide reasons.

44. As regards assessee's contention that there is only a timing difference relating to the income offered due to change in revenue recognition policy, we

must observe, though it may be a fact that the assessee might have offered or may be offering the income on completion of projects in future years, however, as per assessee's own contention, it is completely dependent upon the completion certificate to be issued by the customers. As regards the decision of the Hon'ble Supreme Court in Excel Industries Ltd. (supra), as could be seen from the facts involved in the aforesaid decision, the income which the revenue wanted to assessee is benefit of duty entitlement to be received by the assessee on certain imports which has not taken place in the relevant assessment year but took place in the subsequent assessment years. The Hon'ble Supreme Court while dealing with the issue of accrual income laid down the following three tests:-

i) Whether the income accrued to the assessee is real or hypothetical;

ii) Whether there is a corresponding liability of the other party to pass on the benefits of duty free import to the assessee even without any imports having been made; and

iii) The probability or improbability of realization of the benefits by the assessee considered from a realistic and practical point of view.

45. In the facts of the said case, admittedly, the assessee had not imported the goods in the relevant assessment year. Therefore, the question of availing benefits relating to duty entitlement did not arise. Whereas, in the facts of assessee's case, the assessee has not only raised invoices relating to sales and services rendered but it has also paid Sales Tax/Service Tax on such sales/services. Therefore, the facts in assessee's case cannot be equated with the facts involved in Excel Industries Ltd. (supra). Since, the other decisions cited before us do not squarely fit in to the facts of assessee's case, we do not intend to deliberate much on such decisions. Therefore, on over all consideration of facts and material on record, we are of the view that the issue requires further examination by the Assessing Officer as the assessee needs to establish with cogent material and evidence that the change in revenue recognition policy is for bona fide reasons and necessary for carrying on its business activities in a more efficient manner. Further, the assessee has to establish that the change in revenue recognition policy is in conformity with the provisions contained under section 145(1) and (2) of the Act. With the aforesaid observations, we are inclined to restore the issue to the Assessing Officer for de novo adjudication after due and sufficient opportunity of being heard to the assessee. It is made clear, the Assessing Officer must decide the issue independently and strictly in accordance with law and judicial precedents to be cited before him without being influenced by any of the observations made by learned Commissioner (Appeals). If the assessee can establish that the change in revenue recognition policy is for bonafide and valid reasons, occasion for any addition on this count would not arise. The Ground raised is allowed for statistical purposes."

23. Following the aforesaid decision we remit this issue to the file of the Assessing Officer.

24. Apropos issue of disallowance of expenses claimed under employee separation scheme.

25. On this issue the Assessing Officer noted that the assessee has claimed 90,00,000/- towards employee separation scheme. The Assessing Officer referred to the auditor's remarks and opined that the ESS scheme is akin to voluntary retirement scheme and the assessee was asked to give detail of ESS and also explain why disallowance should not be made u/s. 35DDA in this case as the scheme is similar to VRS. The assessee responded as under :-

1. In order to right size the work force the company has announced a Employee Separation Scheme (ESS) on 01 august 2011. The scheme was open till 31 March 2012. 22 workmen opted for ESS aggregating expenditure of Rs 9 million, charged to the statement of profit and loss for the year ended 31 March 2012.

2. 22 employees have been separated and the total cost incurred was Rs 94,35,297/-.

3. The company has claimed this as a deduction as it is a separation scheme and it is the absolute discretion of the management to accept or reject the application of any employee made under the scheme without assigning any reason.

4. It was a separation of the employees as decided by the management for cost cutting and to maintain cost effectiveness.

26. The Assessing Officer considered the same and he was not convinced and disallowed a sum of Rs. 94,35,297/- u/s. 35DD. However, he held that the assessee has allowed to amortize the said expenses over a period of five years with Rs. 18,87,060/- to be allowed as 1/5th deduction in the current year.

27. Against this order the assessee is in appeal before us.

28. We note that this addition was rejected by the Assessing Officer in draft assessment order. But the assessee has not objected to the same before DRP. Hence, the Assessing Officer has confirmed the same. Since the assessee had

no grievance against the Assessing Officer's order, now before the ITAT, this ground is not tenable. Hence this ground is dismissed.

29. In the result, assessee appeal stands partly allowed.

Order has been pronounced in the Court on 14.1.2020.

Sd/-	Sd/-
(PAWAN SINGH)	(SHAMIM YAHYA)
JUDICIAL MEMBER	ACCOUNTANT MEMBER

Mumbai; Dated : 14/01/2020

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent
3. The CIT(A)
4. CIT
5. DR, ITAT, Mumbai
6. Guard File.

BY ORDER,

//True Copy//

(Assistant Registrar)

PS ITAT, Mumbai