

**IN THE INCOME TAX APPELLATE TRIBUNAL
COCHIN BENCH, COCHIN**

Before Shri Sanjay Arora, Accountant Member and
Shri Sandeep Gosain, Judicial Member

ITA No. 63/Coch/2022
(Assessment Year: 2016-17)

V-Guard Industries Ltd.
42/962, Vennala High School
Road, Vennala,
Ernakulam 682028
[PAN: AAACV5492Q]

(Appellant)

Principal CIT-1,
C R Building, I S Press Road,
vs. Kochi 682018

(Respondent)

Appellant by: Shri Anil D. Nair, Advocate
Respondent by: Shri Prashant V.K., CIT-DR

Date of Hearing: 01.02.2023
Date of Pronouncement: 20.03.2023

ORDER

Per: Bench

This is an Appeal by the Assessee challenging the revision of it's assessment under section 143(3) of the Income Tax Act, 1961 ('the Act' hereinafter) dated 28/12/2018 for Assessment Year (AY) 2016-17 by the Principal Commissioner of Income Tax-1, Kochi ('Pr. CIT' for short) vide order u/s. 263 dated 22/03/2021.

2. The appeal, filed on 08/03/2022, though delayed by 256 days, was admitted in view of the blanket condonation by the Apex Court in *Suo Motu* WP(C) No.3/2020, dated 10/01/2022, excluding the period from 15/3/2020 to 28/02/2022 in reckoning the delay in computing limitation under law, and the hearing accordingly proceeded with. The assessee is a company manufacturing electrical cables, pumps, solar water heaters, etc., and trading in electrical and electronic goods. Revision of it's impugned assessment is on several issues on which the revisionary authority found an absence or lack of enquiry by the Assessing Officer

(AO), necessitating restoration back to his file for the said verification and examination, holding as:

‘6.4 From the above discussion, it is clear that the Assessing Officer in the impugned assessment order has incorrectly assumed the facts of the case and has incorrectly applied the law as applicable to the issues at hand. He has failed to take note of the salient aspects of the case and has passed the assessment order without application of mind and without making any enquiry whatsoever and in my view has committed an error in the assessment which is also prejudicial to the interests of the revenue. Therefore, I hold that the AO has passed an erroneous order which is prejudicial to the interests of the revenue.’

3. At the outset, Shri Nair, the ld. counsel for the assessee, would submit that he would proceed *qua* each of the 07 issues raised vide the impugned order for verification by the AO in the set aside proceedings, demonstrating of the same having been in fact already considered by the AO in assessment, so that the revision was impermissible in law in the facts and circumstances of the case. We consider this as apposite, and adopt the same manner for adjudication purposes; the assessee having raised corresponding Grounds of Appeal. Gd. 1, though is general in nature, making an omnibus claim as to the various issues raised by the Pr. CIT as having been already enquired into by the AO. The same, even as remarked by the Bench during hearing, would necessarily require us to visit each of the issues separately. Shri Nair would for the purpose take us in the main through the assessee’s reply during assessment proceedings (PB-4, pgs.21-22, 23-36); the show-cause notice u/s. 263 dated 03/02/2021 (PB-2, pgs.328-329); and the assessee’s reply dated 22/02/2021 (PB-2, pgs.330-358).

4.1 Issue # 1: Difference in stock reporting

The issue stands delineated by the ld. Pr. CIT, thus:

‘In the ITR, part A-QD-Quantitative Units given for different products are identical, i.e., 107 units, 102 kgs, etc. AO has omitted to notice this. He has also not noticed that there is excess stock reported for raw materials Copper and PVC.’

With reference to the assessee’s tax audit report in Form 3CD (PB-2, pgs.370- 371,

413), reflecting the quantitative details as to consumption, production, and yield, it was shown to us by Sh. Nair that there is no inconsistency in, nor any excess, stock. There is, on the contrary, loss in manufacturing, which, at 1%, was normal and minimal. Further, while the raw materials, i.e., copper and PVC, are measured by weight (in kg.), the finished product, viz. stabilizers, pumps, water heaters, electrical fans, Digital UPS, are in individualized units, i.e., in numbers. The assessee's reply (PB-2, pgs.333-334) stands perused for the purpose. It's case is clearly borne out by it's return of income for the year, of which Form 3CD is a part. We find no substance in the Revenue's claim, nor any case for revision; the Id. Pr. CIT in his final observation only reiterates what stands stated by the assessee (para 6.1 of the impugned order).

4.2 Issue #2: Claim for Additional Depreciation

The issue stands delineated by the Id. Pr. CIT thus:

'In the Notes to the Form No.3CD/Clause No.18 - regarding depreciation - refer Note 7 & 8: This note informs that company has considered additional depreciation on certain assets put to use for less than 180 days during the earlier AY 2015-16, which is prima-facie not permissible. AO has omitted to notice this aspect of the case.'

With reference to clause 18 of Form 3CD, the assessee-company had claimed additional depreciation for AY 2015-16 on assets put to use for less than 180 days. The assessee's claims to have furnished all the relevant details in assessment, taking us through the same, and of it being in order; rather, consistent with the decision by the Apex Court in *Brakes India Pvt. Ltd.* SLP(C) No. 033755/2017 (PB-2, pgs.334, 402, 415, 431-432/PB-4, pg. 23). Depreciation had been correctly claimed at 50% of the normal depreciation for the assets put to use for less than 180 days. The confusion arose as, due to large number of additions in the second half of the year, these were stated as made and, accordingly, put to use, on one date (31/3/2016). The matter stands looked into by the AO. Now, the difference in depreciation, if any, for AY 2015-16, could in our view be rectified, pursuing a remedial course, only for that year, even if by

way of rectification u/s. 154. The depreciation claimed and allowed for that year would be irrespective of the extent unabsorbed entitled to be carry-forward for this year, forming part of the current year's depreciation, reducing the open written down value (WDV) thereby. No issue therefore, in our view, arises for being considered by the AO. The Revenue has no case, with the Id. Pr. CIT having himself not made any adverse comment in the matter (para 6.1)

4.3 Issue #3: *Non-consideration of expenses disallowed, u/s. 115-JB*

'Perusal of the assessment order reveals that additions have been made towards (i) disallowance of reimbursement Rs.1.15 crores, (ii) disallowance of year-end provision Rs. 7.14 crores, (iii) 35 (2AB) claim disallowed Rs.13.57 crores, (iv) 14A disallow Rs.16.84 lakhs, (v) club expenses disallow Rs.12.77 lakhs and (vi) penalties, fines for late payment of taxes disallowed Rs.43,189 have been made. However, applicability of such additions with reference to provisions of Section 115JB has not been considered by the AO, which is a mistake prejudicial to the interest of revenue.'

That is, non-consideration of certain claims of expenditure for computation of book-profit. The assessee, in reply, admits to the said deficiency, though claims that it would be of no consequence as the tax liability u/s. 115JB, even after considering all the adjustments referred to (aggregating to Rs. 2217.15 lacs), would be at Rs. 3908.31 lacs, while that under the normal provisions of the Act is at Rs. 5877.14 lacs, and toward which Shri Nair would take use through the relevant working (PB-1, pg.238). In other words, the assessee's stand is that the impugned order, even if erroneous on that account, is not prejudicial and, therefore, not liable to be subject to revision on that score. We agree, both in principle as well as on facts. This is as even if the assessee agitates the said additions/disallowance made in regular assessment, the tax liability u/s. 115JB would be lower than that on the returned income. Again, we observe no adverse remark by the Pr. CIT in the matter (para 6.1).

4.4 Issue # 4: *Non-charge of interest to MSME units*

'In the notes forming part of the financial statements, note no.9, assessee has reported 'dues to MSME units'. Reference may also be made to note no.26.2. As per MSME Act, mandatory interest has to be charged for delay in payments to MSME

units. The interest paid for such delay in payments to be disallowed u/s 37 (Board's Circular No. 651 dated 11.06.1993).'

We have pursued note 26.2 of the Notes to the Account (NTA) (PB-2, pgs.544). The same determines an amount of Rs. 2413.52 lacs as interest payable to Micro, Small and Medium Enterprises, in terms of the MSMED Act, 2006. The assessee has explained that no claim *qua* this interest has been preferred; having in fact been not debited in it's accounts, so that the question of disallowance thereof for tax purposes does not arise. Reference stands also made to the Guidance Note (para 39.10) by ICAI. The Id. Pr. CIT, while recording this clarification by the assessee, states it to have not clarified the position (para 6.2). What, pray, we wonder, does that mean, and what further clarification the Revenue seeks we are unable to understand. Once the expenditure has not been claimed, the question of it's disallowance for the relevant year cannot arise, so that there is no prejudice per the impugned order to the Revenue. Sure, there is non-observance of the said Act, but that is outside the domain of the Act. No case for revision is made out.

4.5 Issue # 5: Provision for warranty expenses

'In the notes forming part of the financial statements, note no.25-other expenses, assessee has debited Rs.2975.98 lakhs towards warranty expenses. In note no.7, provision for warranty is reported at Rs.546.29 lakhs. It can be seen that for FY 2014-15, against the provision made Rs.1537.69 lakhs, on Rs.1382.72 lakhs has been utilized. Therefore, the company appears to charge higher figures for provision notwithstanding its claim that it is scientific, etc. (historical figures). *Auditor's qualification in clause no.21(g) w.r.t Form 3CD is that 'provision for warranty at Rs.20,73,68,178 is not considered as a contingent liability'*. AO has not considered this issue in the proper perspective and in the light of the SC decision in the case of *Rotork Controls vs. CIT*.'

The issue raised by the Id. Pr. CIT, as we were given to understand by Sh. Nair, is to seek clarification on the provision for warranty. The same cannot *per se* be an infirmity in the assessment order. The Id. Pr. CIT has merely raised a doubt, which would assume validity only where there is a conflict or inconsistency in the figures reported by the assessee, and which may, again, be only apparently so, and not survive as where abundantly clarified by the assessee in the revision proceedings.

This is as it may well be that the doubt expressed by the revisionary authority arises on account of an improper understanding or inference drawn from the reported figures. The provision is made, in keeping with the earlier years, on estimates based on historical trend of such claims, as further modified by the management estimates regarding future incidence based on corrective actions on product failures, even as stated in the notes to the annual accounts (Note 2.1(s)), which reads as under (PB-2, pg.527):

‘The estimated liability for the product warranties is recorded when the products are sold. These estimates are established using historical information on the nature, frequency and average cost of warranty claims and management estimates regarding possible future incidence based on corrective actions on product failures. The timing of outflows will vary as and when warranty claim will arise. *The estimate of such warranty related costs is revised annually.* (emphasis, ours)

The assessee has furnished a detailed reply in the revisionary proceedings, clarifying of providing for warranty ranging from 1 to 4 years on different products, on a scientific basis. We were during hearing taken through the relevant schedules to the balance-sheet, as well as the assessee’s reply in the revision proceedings (PB-2, pgs.349-351, 531-532), including a tabulation of the provision movement, as under: (Rs. in lakhs)

Opening Provision as on April 1, 2015	Additional provision made	Provision reversed	Closing Provision as on March 31, 2016
1,944.37 (1,311.31)	1,522.03 (1,537.69)	1,392.72 (904.63)	2,073.68 (1,944.37)

The adverse remarks by the Id. Pr. CIT (para 6.2), denoting the infirmity observed in the assessee’s claim, clearly not verified by the AO, reads as under:

‘6.2 As regards huge provision for warranty shown in the books, assessee has replied that such provision for warranty created is reversed in the subsequent years and such reversal offered as income in those subsequent years and there is no prejudice caused to the revenue. This submission of the assessee is misplaced as *it is the bounden duty of the AO to compute the correct total income for the impugned AY* and he cannot permit excess claims or postponement of income, deliberate or otherwise, in the hope that such excess claims/postponed income will be subject to tax somewhere in the future.’ (emphasis, ours)

4.6 It may at this stage be relevant to visit the law in the matter, i.e., insofar as it relates to absence or lack of inquiry in the matter, which at heart is the charge by the revisionary authority in the instant case. Non-application of mind, as explained by the Apex Court in *Malabar Industrial Co. Ltd. v. CIT* [2000] 243 ITR 83 (SC), is one of the ingredients that renders an order as prejudicial and erroneous to the interest of the Revenue. Absence or lack of enquiry is an attribute, a manifestation, of this non-application, so that an order imbued therewith would be liable to revision. This represents trite law, since co-opted on the Statute itself vide *Explanation 2(a)* to s. 263(1). As explained therein, where the AO accepts the assessee's version in absence of any supporting material and without making any enquiry, his order would be erroneous and exercise of jurisdiction u/s. 263(1) justified. As an example, it, citing its earlier decisions in *Rampyari Devi Saraogi v. CIT* [1968] 67 ITR 84 (SC) and *Tara Devi Aggarwal v. CIT* [1973] 88 ITR 323 (SC), held that where a sum not earned by a person is assessed as income in his hands on his so offering, the order passed by the AO accepting the same would be subject to sec. 263. The decision by the Hon'ble jurisdictional High Court, reported at [1992] 198 ITR 611 (Ker), holding the assessment as without application of mind, was, accordingly, affirmed. In *Gee Vee Enterprises v. Addl. CIT* [1975] 99 ITR 375 (Del), again with reference to judicial precedents, it stands explained that the order of the AO becomes erroneous on a failure to make enquiry where the circumstances call for it. This is not because there is anything wrong in the order if all the facts stated therein are assumed to be correct. However, the AO is not only an adjudicator but also an investigator and, therefore, cannot remain passive in the face of a return which is apparently in order but calls for further enquiry. It is his duty to ascertain the truth of the facts stated in the return when the circumstances of the case are such as to provoke an enquiry. In *Toyota Motor Corporation v. CIT* [2008] 306 ITR 52 (SC), confirming the decision by the Hon'ble High Court reported at [2008] 306 ITR 49 (Del), it was explained that the Tribunal could not

have substituted its own reasons which were required to be recorded by the AO, and ought to have remanded the matter to the latter. Sure, there must thus be circumstances which would make the enquiry prudent, and not *de hors* the same, even as explained in *CIT v. Gabriel India Ltd.* [1993] 203 ITR 108 (Bom), the same being an objective fact which must be satisfied on the basis of the material on record. This in fact is captured by the words: 'which should have been made' occurring in *Explanation 2(a)* to s. 263(1) with reference to any inquiry or verification by the AO.

4.7 We may next discuss the case on merits. In the facts of the case, as noted by the Id. Pr. CIT, the assessee has claimed an expenditure of Rs. 2975.98 lacs as warranty expenses.

Our first observation is that the assessee's explanation only outlines the manner in which the warranty expense is accounted for, and is *sans* any facts. Why, it does not even state if the expenditure stood examined and, if so, what was the rate/s on different products, stated to be reviewed annually and, further, vis-a-vis that obtaining in the past. Further, the Pr. CIT has made a factual observation, which remains unaddressed. The Auditor, who had access to the details, states that the expenditure of Rs. 2073.68, which in fact works to 70% of the total expenditure claimed, has not been regarded as contingent. A strong statement indeed, even as in our view he ought to have been more explicit and, in fact, expressed his clear opinion if he regarded it as so, rather than putting it obliquely. We say so as there was no question of observing thus if he also did not regard it as a contingent expenditure. Further, where, one may ask, is the question of it being regarded as contingent if it is, as claimed, based on a scientific model and, w.r.t. past experience. Two, as we observe, the tabular chart forming part of the assessee's submissions before him (para 4.5); which in fact forms Note 27.8 of Disclosure under Accounting Standards, exhibits a net additional provision made during the year at Rs. 129.31 lacs (1522.03 – 1392.72). The difference between the two, i.e., the amount claimed (Rs. 2975.98 lacs) and provided for (Rs. 129.31

lacs), for the relevant year, could perhaps be in respect of the products sold during the year warranty on which had lapsed, which again is highly improbable. The same remains unexplained before the competent authority, much less the AO. Couple this with the fact that the AO has not examined the said expenditure at all, and the irresistible conclusion is of the objection by the revisionary authority as valid. In fact, in column 3 of the Table, the assessee has correctly stated the fact position inasmuch as at Note 27.8, the heading of this column appears as: 'provision reverse/utilised'. As explained in revisionary proceedings, *there has been in fact no utilisation*, but only a reversal of the provision for earlier years. In other words, there is an admission of the provision outstanding as at the beginning of the year, i.e., Rs. 1944.37 lacs, being in excess by Rs. 1392.72 lacs, i.e., at nearly 72% thereof. This makes it particularly pertinent to verify the assessee's claim; it admittedly reversing the excess provision ostensibly based on actual data, initiating correctives, each year. This explanation, along with others, may have been furnished before him had the AO enquired in the matter, and place the observations by the Id. Pr. CIT in context.

The matter being factual, reference to the decision in *Rotork Controls v. CIT* [2009] 314 ITR 62 (SC), also relied upon by the Revenue, would be of no consequence; the instant being rather a case of application of the principles laid down therein. The basis for the provision of warranty, claimed to be on empirical evidence, generated by past data, would have to be examined by him, even if on a test-check basis, arriving at a satisfaction before accepting the same, as explained in *Malabar Industrial Co. Ltd.* (supra). The invocation of s. 263 in its respect is thus valid. We decide accordingly.

4.8 Issue # 6: Claim in respect of 'employee stock option scheme'

'Assessee has shown 'employee stock option scheme' expenses at Rs.357.88 lakhs (refer note 23). It has also reported this amount towards 'amortisation' during the year. In the significant accounting policies (refer para no.2.1-item O), assessee has stated that expenses or credit recognized in the statement of P&L for a period represents the movement in cumulative expense recognized as at the beginning and end of that period and is recognized in employee benefits expense. *In other words*

there is no consistent policy of 'amortisation' regarding ESOP and as admitted by the assessee, it may either be an expense or an income. AO has failed to probe the correctness of such claim in the light of available details.'

The final observations by the Id. Pr. CIT are to the same effect (para 6.3). Though Sh. Nair would during hearing, with reference to Note 2.1(o), explaining share-based remuneration to senior employees, as also the assessee's submissions before the Id. Pr. CIT (PB-4, pgs.351-356), seek to explain the accounting of the equity settled transactions, as indeed deductibility thereof u/s. 37(1), making out a case therefor, it is clear, and was an admitted position before us, that there was no enquiry by the AO in the matter in assessment, which was restricted only to the increase in share capital. The Revenue's charge of non-verification by the AO in its respect is thus valid, with there being nothing on record to exhibit it. The revision is upheld in principle. The AO shall in the set aside proceedings make full enquiry in the matter with regard to the amortization of the ESOP expenditure from the stand-point of the correctness of the assessee's claim. We also consider it relevant to bring forth certain aspects of the matter for his consideration, particularly in view of the reliance by the assessee on several decisions by the Tribunal, as indeed the Hon'ble High Courts, as follows.

4.9 The assessee's reply, which is only in the revision proceedings, is along the following lines:

- a) Stock options have been granted to employees under the Employees Stock Option Scheme (ESOS), 2013. The options stand granted as Grant I and Grant II, which can be exercised by the concerned employee within a period of three years. The grant under the scheme is on the basis of the length of service of the concerned employee, over which period of time the provision in its respect is amortised and claimed.
- b) The accounting of the ESOP expenditure is in accordance with the SEBI Regulations, 2014 and Guidance Note on accounting for employees share based payment (the same though don't form part of the record);
- c) The Tribunal and the Hon'ble Courts have held the same as an expenditure deductible u/s. 37(1).

There has admittedly been no examination in the matter by the AO, whose enquiry was limited to an increase in the share capital, which is at Rs. 11.21 lacs, as against ESOP expenditure at Rs. 357.88 lacs. Though interrelated, they operate differently; the latter being claimed as expenditure, while the former is against receipt of cash, even as both find reflection under the grouping 'Reserves & Surplus' (i.e., Schedule-4) to the Balance-Sheet. The actual amount of options exercised during the year is at Rs. 232.47 lacs (PB-2, pgs.529).

The rationale of the expenditure, as explained, is the difference between the market price of the share as on the date/s of the grant of the option by the Company (stated as July 2013 and May 2015, for Grant I & II respectively), and the price charged to the employee in its respect, which is at par value of Rs. 10. This difference, which forms the basis of the 'expenditure', is amortised over the period of service of the concerned employee with the company inasmuch as the same forms the basis of his eligibility under the scheme. The options can though be exercised within a period of three years of the Grant. The market price of the shares (being at Rs. 485.35 & Rs. 999 for the two dates respectively) may well be different on the date of the exercise of the option, resulting in either an additional or lower expenditure being booked. It is this expenditure or credit, being in addition to or in retraction of that provided earlier, that the assessee refers to in Note 2.1(o) (PB-2, pg. 526). There is, however, no reversal of the expenditure and the entire amount of Rs. 232.47 lacs is transferred to the securities premium account. *It may be that the expenditure finally booked for the relevant year accounts for this difference, as it appears from a reading of Note 2.1(o).*

Further, the valuation of the options unexercised as at the end of the account period, inasmuch as it would only be with reference to the extant market price of the share, the provision would need to be visited at each year-end. The assessee, however, states that the cost of option is valued not at the market price, but using intrinsic value method, which we understand to be the book-value of the share, in which case it is this book-value as at the year-end (or at the relevant time), at

which the outstanding stock options stand to be valued. Two, the deductibility of the expenditure is justified on the ground of securing dedicated efforts of the employees, besides of course attracting new talent. As a corollary, the employees are motivated to work over the qualifying period, if not beyond. For the employees leaving the organisation, they may yet be entitled to the stock options, granted for, and based on, past services, i.e., prior to the date of grant.

What stands thus stated, is only to emphasize the various aspects involved, requiring verification, even if on a sample basis, and nothing more. It could also be that our understanding, which is based on a combined reading of Note 2.1(o); Notes 23, 27.5; and the assessee's submissions before the revisionary authority, may well bear some difference/s. We may though highlight certain aspects of the matter that come readily to mind, for being examined in the set aside proceedings.

Firstly, without doubt, the employees stand to be benefited by the excess of market (or book) value of the shares allotted (in exercise of the option/s) over their purchase price thereto, stated to be at face value of Rs. 10; in lieu of their services, and surely in pursuance to a business decision by the employer-company to allow benefit to its employees in the interest of its business. It is thus decidedly an income in their hands. There is, however, no corresponding cost incurred by the assessee-company, whether the accounting of the ESOP expenditure is based on the market value of the shares or their book (intrinsic) value, at which the equity settled transactions are stated as measured in the instant case (Note 2.1(o)). The book, or the net asset value, is surely more realistic and conservative vis-a-vis the market value, even as the employee stands to be benefited on the basis of the market value thereof. The question however is if this value (i.e., BV/NAV) (in excess of the purchase cost of shares to the employees) could be regarded as a cost to or expenditure incurred by the company or even as a loss to it. By issuing shares at lower than the book-value, it is the general body of the shareholders that suffers a decline in the value of its share-holding, as in the case of bonus shares or even rights shares, where issued at a discount. This is as the same is only a

capitalization of its profits by the company, securitizing it. The only difference is that in this case the allottees, as a class, are employees (or ex-employees), who had worked for the company for a definite period of time.

In other words, it is the existing shareholders, as opposed to the company, that suffers the loss in the value of their shareholding on a pro-rata basis. That is to say that neither any expenditure is incurred nor any loss suffered by the company issuing the shares on the exercise of the stock option by an employee, even as admittedly, as also afore-noted, a benefit is passed to him, and being in lieu of his services to the company, an income in his hands; the said benefit being at the expense of the shareholder's wealth. It would be a different matter, we may add, where shares of another company, even if a group company, are allotted, even though it would technically not be under ESOP. Yes, it could be for shares in the employer-company itself, where the same are acquired through trading operations under the buyback route, since allowed under the company law, i.e., where not cancelled. This is as in either case there is a release/write-off of the assets of the company in favour of the concerned employee on the exercise of the options and the corresponding allotment of shares, so that there is an expenditure by definition. A share, it may be appreciated, represents a share, to that extent, in the net assets of the company. The issue of a share, whether against value received in cash or in kind, and incurring expenditure, are mutually exclusive.

Our second observation in the matter is that, considered in proper perspective, a stock option denotes conferring a benefit to an employee by way of shares in the employer-company against value received in kind, i.e., by way of services in the past. There does not therefore appear to be any basis for debiting the profit and loss account for the current or the subsequent years on the grant of the stock options or their exercise by the concerned employee; each year being an independent and separate unit of assessment. Further, the same implies that the services received by the issuer-company in the past were undervalued or, in any case, the profits of the earlier year/s overstated, to that extent. Per contra, it is the

books of the earlier year/s which ought to, in case of a continuing stock option scheme, and on the basis that the benefit thereunder would be accepted and eventually availed of, bear the charge or the cost to that extent, by being provided for, as in the case of leave encashment, gratuity, etc., based on empirical evidence. Yes, a fraction of the employees may leave the organisation without qualifying under the scheme, i.e., prior to the threshold period of service. These parameters could, as in the case of other provisions, be though incorporated in estimating the provision. Further, any changes in the cost booked vis-a-vis that obtaining at the time of exercise of option, could be adjusted in accounts. In other words, there is no scope for charge or claim of expenditure on the grant of options or their exercise, which could only be in the year of rendering services against which the same are allowed, where the accounts are maintained on accrual basis, mandatory under the governing law and that adopted under the Act (s. 145).

There is yet another aspect of the matter, i.e., the point of time at which the rights in the shares inure to the employee. That is, upon the employee accepting the stock option or on exercising it. This is as the benefit can be said to be allowed by the company to the employee only on the right being acquired by him. The Tribunal in *Asst. CIT v. Pramod H. Lele* [2012] 66 DTR 134 (Mum), and again in *Asst. CIT v. Pramod H. Lele* [2016] 156 ITD 571 (Mum), held that the said right passes only on the exercise of the option by the employee. Prior thereto, an employee signifying his willingness to take the shares, only promises to accept the offer of the company in future. Promise to offer or to accept is not an 'offer' or 'acceptance' *per se*. This becomes relevant as the expenditure can be said to have accrued only on the vesting of the right on the exercise of the option, and not prior thereto. There is, it may be appreciated, no legal obligation on the employer prior to the said date. As explained in *CIT v. Kharwar (B.M.)* [1969] 72 ITR 603 (SC), it is not permissible to ignore the legal character of the transaction on the ground of 'substance of the transaction'. Reference in this regard may also made to the

decision by the Apex Court in *CIT v. Infosys Technologies Ltd.* [2008] 297 ITR 167 (SC), as well as in *Addl. CIT vs. Bharat V. Patel* [2018] 404 ITR 37 (SC).

4.10 Our observations are without prejudice to each other, as, for example, the time of expenditure assumes relevance only where it is, firstly, regarded as so; and only seek to highlight the different issues arising for determination. They may accordingly not be construed as our final findings, though shall be taken into account, and the assessee required to meet the same, by the assessing authority, before whom the matter is at large. The assessee has also relied on the decision in *Radhasoami Satsang v. CIT* [1992] 193 ITR 321 (SC). We may though clarify that the same has to in any case satisfy the test of s. 37(1) (*Ram Bahadur Thakur Ltd. v. CIT* [2003] 261 ITR 390 (Ker)(FB)), and that the same cannot be compromised on the ground of consistency (refer *CIT v. British Paints India Ltd.* [1991] 188 ITR 44 (SC)), *qua* which there is though no finding by the AO. Why, such a contention could be raised only where there is a finding in assessment in an earlier year, even as the principle of *res judicata* is not applicable to the proceedings under the Act. The AO shall decide on merits in accordance with law, issuing definite findings of fact, per a speaking order after hearing the assessee. We decide accordingly.

4.11 Issue # 7: Non-verification of huge claims for expenditure

‘Assessee has claimed huge expenses against 'salaries and wages and bonus: Rs.9847.32 lacs, consumption of packing materials: Rs.1232.69 lacs, repairs and maintenance: Rs.786.39 lacs, travelling and conveyance: Rs.1464.85 lacs, freight and forwarding charges: Rs.1942.50 lacs, cash discount: Rs.1738.97 lacs, advertisement and business promotion expenses: Rs.8031.40 lacs, loss on foreign currency transaction (nett): Rs.105.82 lacs, outsourced manpower cost: Rs.1574.66 lacs, misc. expenses: Rs.1335.02 lacs - the nature, genuineness and reasonableness of which the AO has not enquired into.’ (emphasis, by underlining, ours)

The assessee has, per it's reply in the revisionary proceedings, clarified that the details of various expenses were submitted to the AO during assessment proceedings vide replies dated 13/11/2018 & 26/12/2018, with he in fact making disallowance/addition/s on several of them, at an aggregate of Rs. 2217.15 lacs,

referred to by the Id. Pr. CIT in Issue #3, so that the AO cannot be said to have not enquired into the nature, genuineness and reasonableness of the said expenditure. There is, however, nothing on record to indicate any enquiry, much less verification, made by the AO in the matter, which was also the admitted position before us. The same would *per se* render the order erroneous and prejudicial to the interests of the Revenue. It is well settled that once the AO assumes jurisdiction to assess or reassess, he is duty bound to assess the total income for the relevant assessment year. Each of the expenditure referred to by the Id. Pr. CIT is material in relation to the returned income of Rs. 16314 lacs, with the AO having not made an iota of enquiry on the relevant aspects. *Explanation 2(a)* is clearly attracted under the circumstances. We find no reason to interfere.

5. In view of the foregoing, revision per the impugned order is upheld *qua* issues 5, 6 & 7 supra raised by the Pr. CIT, corresponding to Gds. 6, 7 & 8 r/w Gd. 1 before us, and revoked on other Grounds. We decide accordingly.

6. In the result, the assessee's appeal is partly allowed.

*Order pronounced under Rule 34(4) of the Income Tax (Appellate Tribunal)
Rules, 1963*

Sd/-
(Sandeep Gosain)
Judicial Member

Sd/-
(Sanjay Arora)
Accountant Member

Cochin, Dated: March 20, 2023

vr/-

Copy to:

1. The Appellant
2. The Respondent
3. The Pr. CIT-1, Kochi
4. The CIT-DR, ITAT, Cochin
5. Guard File