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

\+ ITA 474/2024

THE PR. COMMISSIONER OF INCOME TAX -7

.....Appellant

Through: Mr. Ruchir Bhatia, SSC with Mr. Anant Mann, Mr. Pratyaksh Gupta, Advs.

versus

RELIGARE SECURITIES LTD. .....Respondent

Through: Mr. Rohit Jain, Mr. Aniket Agrawal, Mr. Abhishek Singhvi, Advs.

CORAM:
HON'BLE MR. JUSTICE YASHWANT VARMA
HON'BLE MR. JUSTICE RAVINDER DUDEJA

O R D E R

% 02.09.2024

CM APPL. 50667/2024 (819 Days Delay in Refiling)

1. Bearing in mind the disclosures made, the delay in refiling the appeal is condoned.

2. The application shall stand disposed of.

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3. A request is orally made by Mr. Bhatia, learned counsel appearing for the appellant, to amend the cause title in light of M/s Religare Securities Ltd. having subsequently amalgamated. The prayer as made is granted. Let appropriate steps be taken within a period of 24 hours and an amended memo of parties placed on the record.

4. The Principal Commissioner impugns the order of the **Income Tax Appellate Tribunal**[1] dated 13 December 2019 and has posited the following questions of law for our consideration:-

[1] Tribunal

> "2.1 Whether ld. ITAT erred on facts and in law in deleting the disallowance of Rs.2,04,87,736/- confirmed by the ld. CIT(A) on account of the difference between purchase price of Stock Appreciation Right (SAR) and the sale price of such SAR at the time of exercise by the employees, holding the same to be revenue loss allowable as business deduction?
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> 2.2 Whether ld. ITAT erred on facts and in law not appreciating the fact that it is a general practice of the companies to form a Trust, which acts merely as a custodian of the shares, during the lock-in period in order to prevent the employees from leaving the company after exercising the option whereas in the present case, the assessee has been writing off its loan given to trust ' behind the canopy of SAR granted to employees?
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> 2.3 Whether ld. ITAT erred on facts and in law in not appreciating the fact that merchant banking license is a capital asset having enduring benefit which has been transferred by the assessee company to its sister concern without any consideration, which leads to an irrefutable conclusion that the transaction was not at Arm's Length?
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> 2.4 Whether ld. ITAT erred on facts and in law in not appreciating the fact that transaction of transfer of merchant banking license, which was not at arm's length had helped the assessee in avoiding the capital the capital gain tax, which would otherwise had payable had the transaction been entered into with any other unrelated entity?"

5. We note that insofar as the aspects of disallowance on account of stock appreciation and merchant banking license transfer are concerned, the same admittedly stands concluded and answered in favour of the assessee by the Court inter partes in **Principal Commissioner of Income Tax – 7 vs. M/s Religare Securities Ltd.** [ITA 311/2018 decided on 19 March 2018].

6. The aforesaid appeal had come to be dismissed on 19 March 2018 in the following terms:-

> "The Revenue's appeal under Section 260A of the Income Tax Act alleges that the Income Tax Appellate Tribunal (ITAT) erred in allowing ₹ 2,09,63,780/- as a capital expense. That amount was the quantum of discount given in respect of the SAR (Stock Appreciation Rights) – similar to Employee Stock Option (ESO) offered by the employer to the work force. The ITAT followed its previous decision and also cited a judgment of this Court in

Commissioner of Income Tax vs. Lemon Tree Hotels Ltd, (ITA 107/2015 decided on18.08.2015). The ITAT also relied upon the judgment of Madras High Court in *Commissioner of Income Tax-III, Chennai vs. PVP Ventures Ltd.*, TC(A) 1023 of 2005.

In *PVP Ventures Ltd. (supra),* Madras High Court discussed the relevant issues in the following manner :

> *"7. On the issue of Staff Welfare expenditure, the Commissioner pointed out that the assessee had debited a sum of Rs.66.82 lakhs under the head of Staff Welfare expenditure. The said sum was incurred by the assessee in respect of Employees Staff Option Plan and Employees Staff Purchase Scheme Guidelines. As per SEBI guidelines, the difference between the market value of the shares and the value at which the shares were allotted to the employee is allowable as an expenditure. The Commissioner of Income Tax revised this claim accepted by the Officer and held that the accounting treatment prescribed by SEBI, nowhere suggests that it was a revenue expenditure to be debited to the Profit and Loss Account as it was only a notional and contingent expenditure. In the circumstances, the Commissioner of Income Tax held that the shares allotted under Employees Staff Option Plan and Employee Staff Purchase Scheme Guidelines, 1999, having not stated anything about the manner of treatment to this expenditure, the difference in the value at which the shares were allotted and the market value of the shares did not warrant any allowance as expenditure. Ultimately, the Commissioner of Income Tax passed an order directing the Assessing Officer to revise the assessment. Thus, holding that the revision proceedings were validly initiated, the income received on account of exchange fluctuation was held as a revenue receipt and be taxed as such and the Staff Welfare expenditure was to be disallowed.*
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> *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*

Account as an expenditure. The Tribunal pointed out that what had been adopted was not notional or contingent as had been submitted by the Revenue. Pointing out to the Employees Stock Option Plan, the 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 recognised 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."

In view of the above reasoning, the Court is of the opinion that there is no infirmity with the approach or order of the Tribunal. No question of law arises. The appeal is consequently dismissed."

7. Insofar as whether notional income can be taken into consideration for the purposes of taxation, we had in a recent judgment rendered in **Ravi Kumar Sinha vs. Commissioner of Income Tax**[2] observed as follows:-

"**15.** We also bear in mind the well-settled position in law of the Act not contemplating a tax being levied on notional income. We deem it apposite to extract the following passages from the decision of the Supreme Court **in Commissioner of Income Tax v. Excel Industries Ltd**:

"24. <u>This Court did not accept the view taken by the High Court on facts. Reference was made in this context to Commissioner of Income Tax v. Birla Gwalior (P.) Ltd., [1973] 89 ITR 266 (SC) wherein it was held, after referring to Morvi Industries that real accrual of income and not a hypothetical accrual of income ought to be taken into consideration.</u> For a similar conclusion, reference was made to Poona Electric Supply Co. Ltd. v. Commissioner of

[2] 2024:DHC:6076-DB

Income Tax, [1965] 57 ITR 521 (SC) wherein it was held that income tax is a tax on real income.

25. Finally a reference was made to State Bank of Travancore v. Commissioner of Income Tax, [1986] 158 ITR 102 (SC) wherein the majority view was that accrual of income must be real, taking into account the actuality of the situation; whether the accrual had taken place or not must, in appropriate cases, be judged on the principles of real income theory. The majority opinion went on to say:

> "What has really accrued to the assessee has to be found out and what has accrued must be considered from the point of view of real income taking the probability or improbability of realisation in a realistic manner and dovetailing of these factors together but once the accrual takes place, on the conduct of the parties subsequent to the year of closing an income which has accrued cannot be made "no income".

26. This Court then considered the facts of the case and came to the conclusion (in Godhra Electricity) that no real income had accrued to the assessee in respect of the enhanced charges for a variety of reasons. One of the reasons so considered was a letter addressed by the Under Secretary to the Government of Gujarat, to the assessee whereby the assessee was "advised" to maintain status quo in respect of enhanced charges for at least six months. This Court took the view that though the letter had no legal binding effect but "one has to look at things from a practical point of view." (See R.B. Jodha Mal Kuthiala v. Commissioner of Income Tax, [1971] 82 ITR 570 (SC)). This Court took the view that the probability or improbability of realisation has to be considered in a realistic manner and it was held that there was no real accrual of income to the assessee in respect of the disputed enhanced charges for supply of electricity. The decision of the High Court was, accordingly, set aside.

27. Applying the three tests laid down by various decisions of this Court, namely, whether the income accrued to the assessee is real or hypothetical; 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 the probability or improbability of realisation of the benefits by the assessee considered from a realistic and practical point of view (the assessee may not have made imports), it is quite clear that in fact no real income but only hypothetical income had

> accrued to the assessee and Section 28(iv) of the Act would be inapplicable to the facts and circumstances of the case. Essentially, the Assessing Officer is required to be pragmatic and not pedantic."
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> **16.** In our considered opinion, in light of the restriction with respect to marketability and tradeability of the stock in question, the FMV could not have been recognized to exceed the face value of the shares and thus the determinative being INR 15/-. The Valuation Report, as noted above, was at best a medium adopted by the employer in order to broadly ascertain its obligations for the purposes of withholding tax. The same could not have consequently been taken into consideration for the purposes of FMV. The position which was advocated by the respondents, namely, for the quoted price or the Valuation Report being taken into consideration is clearly untenable, since the same could have had no application to a share which was subject to a lock-in stipulation and could not be sold in the open market owing to a complete embargo on the sale of those shares."

8. Consequently, and for all the aforesaid reasons, we find no ground to interfere with the view expressed by the Tribunal. The appeal consequently fails and stands dismissed.

YASHWANT VARMA, J.

RAVINDER DUDEJA, J.

SEPTEMBER 02, 2024/*neha*