

INCOME TAX APPELLATE TRIBUNAL  
DELHI BENCH "F": NEW DELHI  
BEFORE SHRI SUDHANSHU SRIVASTAVA, JUDICIAL MEMBER  
AND  
SHRI PRASHANT MAHARISHI, ACCOUNTANT MEMBER

ITA No. 2396/Del/2013  
(Assessment Year: 2008-09)

M/s. Religare Macquarie Wealth Management Ltd,  
D-3, P-3B, District Centre,  
Saket, New Delhi  
PAN:AADCR5677C  
(Appellant)

Vs. ACIT,  
Circle-15(1),  
New Delhi  
  
(Respondent)

Assessee by :

Shri Ajay Vohra, Sr. Adv  
Shri Gaurav Jain, Adv  
Ms. Tejasvi Jain, CA

Revenue by:

Shri Atiq Ahmad, Sr. DR

Date of Hearing

03/08/2017

Date of pronouncement

09/10/2017

O R D E R

PER PRASHANT MAHARISHI, A. M.

1. This is an appeal filed by the assessee against the order of the Id CIT (A)-XVIII, New Delhi dated 28.02.2013 for the Assessment Year 2008-09.
2. The assessee has raised the following grounds of appeal:-
  - "1. That the Commissioner of Income tax (Appeals) erred on facts and in law in sustaining disallowance of Rs.6,69,626 (as against correct amount of Rs.7,51,482) made by the assessing officer on account of the difference between purchase price of Stock Appreciation Right ('SAFA') and the sale price of such SAR at the time of its exercise by the employees of the appellant holding the same to be capital loss not allowable business deduction.
  - 1.1. That the Commissioner of Income tax (Appeals) erred on facts and in law in not appreciating that the above differential amount actually represents the loan granted by the appellant to Religare Enterprises Ltd. Employees SAR Trust ('the Trust') for the purpose of administering Employee Stock Appreciation Right Scheme ('SAR

scheme'), which was not meant to be and, in fact, not recovered from the latter in accordance with the SAR scheme.

- 1.2. That the Commissioner of Income tax (Appeals) erred on facts and in law in not appreciating that the above SAR scheme was implemented to motivate, reward and retain key employees whereby each SAR granted to the employees of the appellant stood equivalent to one share of Religare Enterprises Ltd. ('REL') and the aforesaid differential amount was, thus, in the nature of employee benefit allowable under section 37(1) of the Income Tax Act, 1961 ('the Act').
- 1.3 Without prejudice, the Commissioner of Income tax (Appeals) erred on facts and in law in not allowing deduction of the aforesaid amount of loan written off as loss incidental to business under section 28 of the Act.
2. That the Commissioner of Income tax (Appeals) erred on facts and in law in enhancing the income of the appellant by directing further disallowance of Rs. 15,99,306 on account of difference between the sale price of SAR and the exercise price of SAR (prefixed at Rs. 140 per SAR) paid to the employees of the appellant, holding the same to be capital expenditure incurred in relation to issue of shares to employees.
  - 2.1 That the Commissioner of Income tax (Appeals) erred on facts and in law in not appreciating that the above differential amount of Rs. 15,99,306 was in the nature of employee compensation allowable as deduction under section 37(1) of the Act.
  - 2.2 Without prejudice, and in alternative, the Commissioner of Income tax (Appeals) erred on facts and in law in not allowing deduction of the above differential amount of Rs. 15,99,306 under section 36(l)(ii) of the Act alleging that the same was not in accordance with the provisions of the Payment of Bonus Act, 1965.
3. That the Commissioner of Income tax (Appeals) erred on facts and in law in confirming the disallowance of Rs. 93,89,552 made by the assessing officer in respect of the expenditure incurred by the appellant during the period from April'2007 to June 2007 holding the same to be in the nature of pre operative expenses, on the basis that the business was set up only on 30.06.2007 when the first invoice was raised by the appellant.
4. That the Commissioner of Income tax (Appeals) erred on facts and in law in upholding disallowance of Rs. 1,96,524 made by the assessing officer under section 14A of the Act by applying Rule 8D of the Income Tax Rules, 1962 ('the Rules').
  - 4.1 That the Commissioner of Income tax (Appeals) erred on facts in upholding the observation of the assessing officer that the loan

given by the appellant to the Trust would constitute investment for the purposes of making disallowance under section 14A of the Act.

- 4.2 That the Commissioner of Income tax (Appeals) erred in not appreciating that Rule 8D of the Rules would not apply, per se, inasmuch as no investments were appearing either on the opening or closing date of the audited annual accounts of the appellant.
5. That the Commissioner of Income tax (Appeals) erred on facts and in law in upholding the disallowance of Rs.34,34,000 made by the assessing officer under section 40(a)(ia) of the Act alleging that tax was not deducted at source.
- 5.1 That the Commissioner of Income tax (Appeals) erred in not appreciating that the above sum of Rs.34,34,000 were paid to the group companies towards reimbursements of actual expenditure and thus, there was no requirement to deduct tax at source on such payments.”

#### Brief facts

3. The assessee is a company which is engaged in the business of wealth management services including portfolio management services. It filed its return of income on 26/09/2008 declaring loss of Rs. 3.73 crores.

#### Assessment proceedings

4. During the assessment proceedings it was observed by the Ld. assessing officer that the assessee company has introduced the scheme of stock appreciation rights for its employees. The company has invested in a trust who buys the shares of Religare Enterprise Ltd at an average price of Rs. 503/- per share and the grant price of shares to employees was Rs. 140/- per share. The difference between the grant price and cost price is treated as a bonus to the employees in the books of the company and the difference between the sale price of the share and the cost of shares is taken as a 'loan written off' by the company in books of the company. Therefore, during the year the difference between the sale price of the

share and the purchase price was debited of Rs. 6 69626/- in the books of accounts of the company and same was claimed as allowable expenditure. The Ld. assessing officer held that loss on sale of investment claimed by the assessee of this sum is not allowable as it is deduction on account of loan written off and apparently under section 37 same is not allowable.

5. Further, the assessee has incurred expenditure from the period of April 2007 to June 2007 of Rs. 9389552/- and claimed the same as an allowable expenditure. The Ld. assessing officer was of the view that assessee has commenced its business from July 2007. Therefore, all the expenditure incurred prior to that period are treated as pre commencement expenses and are not allowable.
6. Further as the stock appreciation right in holding investment in shares of company through trust, The Ld. AO held that it will attract the provisions of section 14 A of the income tax act and therefore applying provisions of rule 8D of the income tax rules, 1962 he disallowed a sum of Rs. 196524/- under section 14 A of the income tax act.
7. The assessee further shown reimbursement of certain expenditure to its group entities amounting to Rs. 65.37 lakhs , Ld. assessing officer held that the provisions of section 40 (a)(ia) of the income tax act applies as tax should have been deducted thereon and therefore out of that some on reimbursement amount of Rs. 3103000 on which tax has been deducted is allowed and on the balance on which no tax is deducted of Rs. 3434000/- was disallowed.

8. Consequently, assessment under section 143 (3) of the income tax act 1961 was passed on 31/12/2010 determining net loss of Rs. 2364 4815/- against the returned loss of Rs. 3 733 4517/-.

Appellate proceedings

9. Assessee aggrieved with the order of the Ld. assessing officer preferred an appeal before the Ld. CIT (A), who vide order dated 28/02/2013 disposed off the appeal of the assessee. He confirmed the disallowance of Rs. 669626/- on account of the difference between the purchase price of stock appreciation rights and the sale price of such stock appreciation right at the time of exercise by its employees holding the same to be capital loss not allowable as business deduction. He also confirmed the disallowance on account of pre-commencement expenditure of Rs. 9389552/- as pre-commencement expenditure holding that the business of the assessee was setup only on 30/06/2007 when the 1<sup>st</sup> invoice was raised by the appellant. He also confirmed the disallowance under section 14 A of the income tax act of Rs. 196524/- and disallowance under section 40(a)(ia) of the act.
10. The Ld. CIT appeal further enhanced the assessment of the assessee on account of loss on sale of shares difference between the purchase price of the SAR of Rs 503/- per share and SAR value of RS 140/- per share being Rs. 363/- per share which is claimed by the assessee as loss on sale of shares . According to Id CIT (A) assessee has claimed total

expenses of Rs. 2268932/- whereas the Id AO has disallowed only Rs. 669626/- therefore the balance amount was also disallowed for the same reasons after issue on notice of enhancement by him.

11. Therefore the assessee aggrieved with the order of the Ld. CIT (A) preferred an appeal before us contesting all the disallowances confirmed by the Ld. CIT appeal as well as the enhancement made by him.

Arguments of the Assessee

12. On the 1<sup>st</sup> issue of the disallowance of stock appreciation right and further on the enhancement made by the Ld. CIT (A), The Ld. authorised representative submitted that now the issue is squarely covered in favour of the assessee by the decision of the coordinate bench in case of Religare commodities Ltd in ITA No. 2283/del/2013 for assessment year 2008 – 09. He further referred to para No. 7 of that decision stating that coordinate benches allowed the claim of the assessee following the special bench decision in case of Biocon Ltd versus DCIT, Bangalore 144 ITD 21. He therefore submitted that ground No. 1 and 2 of the appeal of the assessee is covered in favour of the assessee by the decision.
13. With respect to ground No. 3 on account of the pre-commencement expenditure, he submitted that as soon as the activity which is essential in the course of carrying on business started the businesses is said to be set up. Therefore he submitted that the business of the assessee was not set up on 30/6/2007 when the invoices were raised but when the activities essential in course of carrying on such businesses started. He further stated that the bank account of the assessee was open on

27/04/2007 at the share capital was allotted on 11/05/2007. He further submitted that merely because the 1<sup>st</sup> debit note was issued on 30/06/2007, it cannot be said that the business have been set up on that particular date because before that date, the assessee has already rendered the services and for which various activities commenced in the month of April 2007 only. He further referred to the copy of the salary Ledger account showing payment of salary on 30/04/2007 plus various other memorandum of understanding dated 01/04/2007 to show that the businesses already set up on that particular date. He further referred to the resolution dated 10/03/2007 of the assessee with the appointment of the auditors were made. He further relied upon the decision of the Hon'ble Delhi High Court in case of the Omniglobe information tech India (P) Ltd versus CIT 68 Taxmann.com 112 (Delhi) (369 ITR 1) to support his contentions.

14. With respect to ground No. 4 of the appeal of the assessee with respect to disallowance under section 14 A of the income tax act he submitted that there is no exempt income earned by the assessee during the year and when there is no exempt income, no disallowance can be made. He further referred to the decision of the Hon'ble Delhi High Court in case of Cheminvest limited versus CIT, wherein identical issue was considered in para No. 23 of that order.
15. With respect to ground No. 5 of the appeal of the assessee against the confirmation of disallowance under section 40 (a)(ia) of the act of Rs. 3434000/-. He submitted that the above amount of the expenditure is a

reimbursement of expenditure on which no disallowance can be made. He further referred to the para No. 6 of the Ld. assessing officer wherein the above disallowance was made. He submitted that the total payment was of Rs. 65.37 lakhs and the Ld. assessing officer has already allowed Rs. 31.03 lakhs and made the disallowance of the balance of Rs. 34.34 Lacs. He submitted that the Ld. CIT-A has wrongly stated that the amount of reimbursement is for actual services rendered by this group entities to the assessee. He submitted that these are the expenditure of reimbursement of salary, travelling, conveyance, insurance etc made by the appellant without deduction of the tax at source. He further referred to MOU with Religare securities Ltd for reimbursement of rent and maintenance charges placed at page No. 170 – 175 of the paper book. He further referred to the memorandum of understanding between the assessee and other company for reimbursement of rent and maintenance charges and MoUs dated 01/11/2007 with Religare Group entities for reimbursement of rent and maintenance charges. He further referred to the copy of debit note raised by the Religare group companies on the appellant at page No. 189 to 250 stating that these are all the reimbursement of the expenditure and they are not in the nature of rendition of any services to the assessee. For that reason he submitted that there is no requirement of tax deduction at source on the above payment and hence disallowance made by the Ld. assessing officer as well as by confirmed by the Ld. CIT (A) is erroneous. He further referred

to decision of Honourable Delhi high court in case of Fortis Healthcare Limited .

Arguments of the revenue

16. The Ld. departmental representative vehemently contested the grounds raised by the assessee relying on the order of the Ld. assessing officer as well as the Ld. CIT (A). He further submitted that stock appreciation right expenditure incurred by the assessee are in relation to the issue of capital of the assessee and therefore they are capital in nature cannot be allowed as deduction under section 37 (1) of the income tax act. Further with respect to the provisions of section 14 A of the income tax act, He submitted that merely because the income has not been earned during the year, it cannot be said that the disallowance under section 14 A of the act cannot be made. He further referred that the provisions of section 14 A does not provide that the year in which no income is earned disallowances not to be made. He further referred that the expenditure incurred by the assessee with respect to the sister concern is not in the nature of reimbursement of expenditure as already held by the Ld. CIT (A) but in the nature of rendition of the services. Therefore, the tax would have been deducted thereon on these payments made by the assessee to the sister concern and hence disallowance has been correctly confirmed by the Ld. CIT (A).

Decision and reasons

17. We have carefully considered the rival contention as well as perused the orders of the lower authorities on the various issues and grounds of appeal raised by the assessee. Our decision and reasons for the same on each of the ground are as follows.
18. The 1<sup>st</sup> and 2<sup>nd</sup> ground of appeal of the assessee is with respect to the disallowance of expenditure on stock appreciation right being the difference between the purchase price of stock appreciation right and the sale price of stock appreciation right at the time of the exercise by the employees holding the same to be capital loss and not allowable as business deduction. With respect to the enhancement made by the CIT – A of Rs. 1 599306/- on account of difference between the sale price of stock appreciation right and the exercise price of stock appreciation right holding the same to be capital expenditure incurred in relation to the issue of share issued to the employees. The assessee has submitted that Religare enterprise Ltd has introduced Employee stock appreciation rights scheme 2007 for Religare group of entities to reward and retained the employees for higher-level of individual performance and to attract the best talent and provide motivation for better performance of the employees. According to that non assignable shares equivalent were granted to the employees. Pursuant to clause No. 7 of the scheme which entitles them to receive stock appreciation rights compensation under the scheme provided the participant satisfy the requirement of that particular scheme, the compensation is paid by the company to the participant in respect of this surrendered vested stock appreciation rights according to

the scheme. According to the particular scheme the grant price was paid by the Granti who is an employee eligible to participate under the scheme. According to that scheme the 10 employees of the assessee company opted for the scheme and all of them exercised their stock appreciation rights. According to that Rs. 2505946 was sale proceeds of the stocks of the company, resulting into the loss of Rs. 1599362 which was claimed by the assessee as an employee compensation. Further, the company has purchased the shares of Religare enterprise Ltd, through a trust under that particular scheme at an average price of Rs. 503/- per share whereas the grant price of shared to the employees was Rs. 140/- per share. Therefore, the difference between the sale price of the share and the purchase price of the share was claimed by the assessee as deduction as employee compensation. In the identical circumstances. With respect to one of the group companies, Religare commodities Ltd for assessment year 2008 – 09 identical issue arose before the coordinate bench, which decided this issue in ITA No. 2283/Del/2013 by order dated 04/01/2017 wherein relying upon the decision of the special bench in 144 ITD 21 claim of the assessee with respect to both the above items were allowed vide para No. 7 of that order. The coordinate bench in para No. 8 also held that the issue is also squarely covered by the decision of the Hon'ble Madras High Court in 211 Taxmann 554 wherein it has been held that the above expenditure on account of employee stock option scheme is an ascertained liability for deduction and further the Hon'ble Delhi High Court in CIT versus Lemon tree hotels Ltd in ITA No. 107/2015 has also

held that the expenses debited is cost of employee stock option plan in the profit and loss account is an allowable expenditure. The Ld. departmental representative also could not point out any other judicial precedent against the above judicial precedents cited by the Ld. authorised representative. In view of this ground No. 1 and 2 of the appeal of the assessee is allowed reversing the decision of the Ld. CIT – A and directing the assessing officer to allow the sum of Rs. 6 69626/- on account of the difference between the purchase price of stock appreciation right in the sale price of such stock appreciation right on exercise by the employees of the appellant as these are revenue expenditure in nature. Further the Ld. CIT (A) has also erred in making the disallowance by enhancing the assessment of Rs. 1 599306/- on account of difference between the sale price of the stock appreciation right and the exercise price of stock appreciation right paid to the employees of the appellant as it has already been held to be the revenue expenditure in relation to the stock appreciation rights scheme of the assessee to appreciate the performance of the employees holding the same as revenue expenditure. Therefore ground no 1 & 2 of the appeal of the assessee is allowed.

19. The 3<sup>rd</sup> ground of appeal is with respect to the issue that whether the assessee is eligible for deduction of expenditure incurred by it from April 2007 to June 2007. The Ld. assessing officer as well as the Ld. CIT (A) has held that the business was set up only on 30/06/2007 when the 1<sup>st</sup> invoice was raised by the appellant and therefore the expenditure

incurred after that date would be deductible. The claim of the assessee is that the business has been set up in April 2007 when the 1<sup>st</sup> salary was paid and the employees of the assessee were taken on board. It was further stated that w.e.f. that date, the assessee is incurring expenditure for the lease of the premises as well as all other incidental expenditure are incurred. Merely because the invoices were raised on 30/06/2007 cannot be said that the business has been set up on that particular date, because without the employees as well as without proper infrastructure the assessee could not have rendered these services which assessee has started putting in place w.e.f. 01/04/2007. At page No. 148 of the paper book assessee has given the detail of the salary for the month of April 2007. Hon'ble Bombay High Court in western India vegetable products private limited versus CIT in 26 ITR 151 has held that that businesses held to be set up when it is established and ready to commence the business. Therefore, all expenditure incurred when the businesses set up till the time it commences the business are also deductible as revenue expenditure. The final distinction has been made by the courts that when the businesses are set up all the expenditure incurred by the assessee are deductible. In the present case the business of the assessee was set up by employment of the employees as well as by hiring the requisite infrastructure which happened in the month of April 2007. The courts have held that there is a clear distinction between a person 'commencing a business' and a person 'setting up a business' and for the purposes of the Indian Income-tax Act the 'setting up of the business' and not the

'commencement of the business' that is to be considered for cut off of deductibility of expenditure. It is only after the business is set up that the previous year of that business commences and any expense incurred prior to the setting up of a business would not be permissible deduction. When a business is established and is ready to commence business then it can be said of that business that it is set up; but before it is ready to commence business it is not set up. There may however be an interval between the setting up of the business and the commencement of the business and all expenses incurred during that interval would be permissible deductions. We also draw support from the decision of Hon'ble Bombay High Court in case of CIT versus Axis Equity private limited in ITA No . 1204 of 2017 dated 30/01/2017 wherein on identical facts, issue has been decided that the expenditure are allowable to the assessee after the businesses are set up. Therefore in view of this we are of the opinion that the assessee must be allowed the deduction of expenditure incurred w.e.f. 01/04/2007 when the employees were hired and the expenditure With respect to infrastructure was incurred by the assessee. In the result we reverse the finding of the lower authorities and direct the assessee officer to allow the expenditure of Rs. 9389552/- incurred by the assessee for the period from April 2007 to June 2007. In the result ground No. 3 of the appeal of the assessee is allowed.

20. Ground No. 4 of the assessee's appeal is with respect to upholding the disallowance of Rs. 196524/- under section 14 A of the income tax act applying the provisions of rule 8D of the income tax rules, 1962 even in

the absence of any exempt income earned by the assessee. Hon'ble Delhi High Court has decided the identical issue in Cheminvest Ltd versus CIT [378 ITR 33], wherein in para No. 23, it is been held that where the assessee has not earned any exempt income during the year there cannot be any disallowance under section 14 A of the income tax act. Undisputedly there is no exempt income during the year, earned by the assessee, therefore there cannot be any disallowance under section 14 A of the income tax act. Therefore, respectfully following the decision of the Hon'ble Delhi High Court, we reverse the finding of the lower authorities and direct the assessing officer to delete the disallowance of Rs. 196524/- under section 14 A of the income tax act . In the result ground No. 4 of the appeal of the assessee is allowed.

21. With respect to ground No. 5 of the appeal of the assessee, the assessee has submitted that that expenditure has been incurred by the assessee towards reimbursement of expenses by the other group concern and it is sharing of cost of common services utilised by those companies. The claim of the assessee is that for the purpose of reimbursement of expenses these debit notes are raised and therefore no tax is required to be deducted there on. The Hon'ble Delhi High Court in case of CIT versus Fortis healthcare Ltd in 181 Taxmann 257[Delhi] has held that no tax is required to be deducted on the reimbursement of the expenses. The revenue could not point out any fact that these expenses are not reimbursement of the expenses but for the purpose of rendering specific services to the assessee. In view of this respectfully following the decision

of the Hon'ble Delhi High Court in 181 Taxmann 257, we direct the Ld. assessing officer to delete the disallowance of Rs. 3 434000/- made by the assessing officer under section 40(a) (ia) of the act. In the result ground No. 5 of the appeal of the assessee is allowed.

22. In the result appeal of the assessee is allowed.

Order pronounced in the open court on 09/10/2017.

-Sd/-

(SUDHANSHU SRIVASTAVA)  
JUDICIAL MEMBER

-Sd/-

(PRASHANT MAHARISHI)  
ACCOUNTANT MEMBER

Dated:09/10/2017  
A K Keot

Copy forwarded to

1. Applicant
2. Respondent
3. CIT
4. CIT (A)
5. DR:ITAT

ASSISTANT REGISTRAR  
ITAT, New Delhi