

IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH I-2 , NEW DELHI

BEFORE SHRI J. SUDHAKAR REDDY, ACCOUNTANT MEMBER
AND MS. SUCHITRA KAMBLE, JUDICIAL MEMBER

ITA No. 2851 /Del/201 3
A.Y. 2007 -08

New Delhi Television Ltd.
207, Okhla Industrial Estate
Phase III
New Delhi 110 020

vs. ACIT, Circle 13(1)
New Delhi

PAN: AAACN0865D

And

ITA No. 2752/Del/2013
A.Y. 2007 -08

Dy.CIT, Circle 13(1)
New Delhi

vs. M/s New Delhi Television Ltd.
New Delhi

(Appellant)

(Respondent)

Appellant by : Sh. C.S.Aggarwal, Sr.Adv. &
Sh. KM Gupta, Adv.

Respondent by : Sh. Amit Mohan Govil, CIT, D.R.

ORDER

PER J. SUDHAKAR REDDY, ACCOUNTANT MEMBER

These are Cross Appeals filed for the Assessment Year (Assessment Year) 2007 -08 directed against the order of the Ld.CIT(A) -XX, New Delhi dated 6.3.2013.

2. Facts in brief :- The Assessee is a Company and is engaged in the business of Television, News Broadcasting to its two channels namely NDTV 24x7 and NDTV India. It also produced customized software programmes for broadcasters. It filed its return of income on 2.11.2007 declaring loss of

Rs.7,08,80,472 / -. The A.O. completed the assessment u/s 143(3) of the Act on 17.2.2011 determining the total income at Rs.15,01,72,110 / - inter alia making a transfer pricing adjustment of Rs.94,16,785 / - u/s 92CA (3) of the Act, disallowing claim of software expenditure of Rs.3,06,009 / - as revenue expenditure and the claim of expenditure on ESOP of Rs.21,28,41,993 / -.

3. Aggrieved the assessee carried the matter in appeal.

3.1. The First Appellate Authority granted part relief. Both the assessee as well as the Revenue have filed these appeals to the extent they were aggrieved with the order of the Ld.CIT(Appeals).

4. We first take up the assessee's appeal in ITA 2851/Del/ 2013. The grounds of appeal read as follows.

1. That on facts and in law the orders passed by the Assessing Officer (A.O.)/CIT(A) Transfer Pricing Officer (TPO) are bad in law and void ab initio.

2. That on facts and in law the CIT(A)/TPO erred in upholding/making an addition of Rs.94,16,785/ - under Chapter X of the Act.

3. That on facts and in law, as regards appellant's receipts of Rs.4,52,95,590/ - the CIT(A) erred in upholding that the nature of services rendered by the appellant to its AE are in the nature of Management services and not Shareholder services .

3.1. That on facts and in law the CIT(A) erred in holding that the appellant has failed to produce any evidences in support of its claim vis a vis nature of services.

4. That on facts and in law the CIT(A)/TPO erred in not appreciating that appellant's activities of provision of Management Services of Rs.65,01,612/ - to its AE's were at Arm's Length Price (ALP).

5. That on facts and in law the CIT(A)/TPO erred in making/upholding the applicability of a markup of 18.18% to the costs incurred by the appellant on the alleged provision of Management services .
6. That on facts and in law the CIT(A) erred in upholding that for the purposes of benchmarking the international transactions the TPO was justified in using only the current year data.
7. That on facts and in law the CIT(A) erred in upholding a disallowance of Rs.21,28,41,993/ - on account of Employees Stock Option Plan (ESOP) expenses claimed by the appellant on a pro rata basis over the total vesting period.
- 7.1. That without prejudice on facts and in law the CIT(A) erred in not accepting the alternate claim of the appellant in allowing a deduction of Rs.35,51,86,538/ - for ESOP expenses on the basis of exercise of options by the employees.
- 7.2. That on facts and in law the CIT(A) erred in holding that the ESOP expenses claimed by the appellant are notional expenses.

That the appellant prays for leave to add, alter, amend and/or vary the grounds of appeal at or before the time of hearing.

5. The assessee filed an application for modification of ground no.7. The Ld.D.R. did not have any objection to the modification of this ground. Hence we modify this ground as requested by the assessee as follows.

that in view of the decision of Hon ble Tribunal dated December 20, 2013 in appellant s own case on the allowability fo ESOP expenditure for AY 2006 - 07, the Ld.AO ought to have allowed the ESOP expenditure of Rs.4,35,320,484/ - in the year under consideration in accordance with the aforesaid decision as against Rs.12,52,71,933 claimed in A.Y. 2006 -07,

Rs.21,28,41,993/ - claimed in A.Y. 2007 -08 and Rs.17,86,56,690/ - claimed in A.Y. 2008 -09.

6. Ld.Counsel for the assessee Shri C.S.Agarwal submitted that only two issues arise in the assessee's appeal, the first being the challenge to the transfer pricing adjustment made by the A.O. and the second being the disallowance of ESOP expenditure. He submitted that ground no.1 is general in nature. Ground no.2 to 6 deal with transfer pricing issues and ground no.7 is on the issue of ESOP expenditure.

7. On the issue of transfer pricing the Ld.D.R. submitted that the assessee during the year, in order to diversify and expand into various domains, conceptualised, to establish a subsidiary in UK namely NDTV Net Works Plc. After taking us through the various international transactions reflected in 3CEB report in the transfer pricing study he emphasized on page 3 of the executive summary of the Transfer Pricing Report and drew our attention to the following lines in that report.

During the financial year 2006 -07, NDTV has charged the amount incurred by it in rendering management services to NDTV Networks Plc at cost. Further, NDTV has also received consideration from NDTV Networks Plc for shareholder activity even though as per arm's length principle, NDTV is not required to charge any amount to NDTV Networks Plc for the shareholder activity. Hence, having regard to the amount charged by NDTV for management services at cost and further considering the amount received by NDTV for shareholder activity, it is reasonable to conclude that this international transaction appears to be consistent with the arm's length standard from an Indian transfer pricing perspective.

7.1. He further took us through the various findings in the transfer pricing reports, as regards the reimbursement expenditure, the FAR analysis etc. Thereafter he argued as follows.

- (a) The receipt of amount as reimbursement for shareholder activity and reimbursement of expenses, were of identical character. The

expenditure for share holder activity has been incurred by the assessee in order to conceptualise and give effect to an efficient NDTV group structure and that the expenditure has been incurred for dealing with tax, finance and other advisory and it was performed as a promoter share holder .

- (b) That there was no obligation on the part of the NDTV Net Work Plc (UK) to reimburse the expenditure incurred on share holder activity to the NDTV group . Only an amount of 1 ,73,88,214 towards management services is to be reimbursed.
- (c) That there is no risk involved in respect of reimbursement of expenditure or in respect of share holder activity and hence such reimbursement does not require any mark up.
- (d) TNMM is found to be the most appropriate method (MAM) in respect of the transactions entered into by the assessee. As the assessee was not entitled to receive reimbursement of expenditure incurred on share holders activity, but was reimbursed for the same, the assessee charged NDTV Net Works Plc, UK for management services at cost and hence the transaction was done at arm s length .
- (e) He disputed the finding of the TPO that the assessee should have bench marked the transactions of share holder activity under the head management services .
- (f) The TPO had held that the activities performed by the assessee are not share holder activity. He argued that the TPO has erred in not appreciating the nature of expenses incurred in relation to share holding activity which were reimbursed to the assessee company. He submitted that there is a distinction as , expenditure for share holder activity was incurred prior to incorporation of NDTV Net Works Plc in UK, for which the assessee is not entitled for reimbursement and whereas , the expenditure which was entitled to reimbursement , was incurred after incorporation of the company.
- (g) He argued that the mark up of 18.18% made by the TPO on the management services is unjustified. He pointed out that the next year

the TPO accepted 10% of the mark up whereas in the year the rate of mark up is taken at 17%.

- (h) Alternatively and without prejudice, he submitted that if at all an adjustment has to be made, it could not exceed Rs.11,81,994 on Rs.6,55,01,012. He filed a calculation sheet in support of this claim.
- (i) The Ld. Counsel raised a fundamental aspect as to whether the transaction in question i.e. share holder activity can be classified as an international transaction itself. For this proposition he relied on the judgement of Hon'ble Mumbai High Court in the case of Vodafone India Services P.Ltd. 368 ITR 1 (Bom) and submitted that advice given prior to incorporation is not an international transaction and hence such activity is outside the ambit of Transfer Pricing provisions. He submitted that, as a parent company, the assessee was performing its obligation of setting up of a Subsidiary.
- (j) He pointed out that the TPO has not charged any mark up on an amount of Rs.1,68,85,054 and has done so only on an amount of Rs.4,52,95,590 and that there is no logical explanation for doing so.
- (k) He submitted that merely because the Transfer Pricing report shows share holder activity as an international transaction, it cannot be taken as one, when doing so is contrary to law. He submitted that the international transaction as defined in S.92 B means a transaction having a bearing on profits, income, loss or assets and submitted that, share holder activity does not have a bearing on these items.
- (l) He relied on the decision of Hon'ble Delhi High Court in the case of M/s Li & Fung India Pvt.Ltd. vs. CIT (2014) 361 ITR 85 and submitted that, no intangible asset has been created. When the assessee's employees worked for the formation of the assessee's UK Subsidiary and the expenditure reimbursed was nothing but the cost of assessee's employees for the time worked in formation of the UK company.

7.2. On the issue of ESOPs, the second ground in the assessee's appeal, the Ld.Counsel submitted that in the assessee's own case for the A.Y. 2008 - 09, the A.O. applied the propositions laid down by the Special Bench of the

ITAT in the case of Biocon Ltd. 35 Taxman 335 , wherein the assessee was an intervenor for the A.Y.2006 -07 and 2007 -08 and completed the assessments. He submitted that the issue be remanded to the file of the AO for passing necessary orders in consonance with the view taken by the A.O. for the A.Y. 20 08-09.

7.3. The Ld.D.R. Mr.Amit Mohan G ovil, Ld.CIT(A) on the other hand controverted the submissions of the assessee and argued that the mandate given to the TPO is to identify whether there is an international transaction and if so determine its arm s length price. He referred to the transfer pricing study filed by the assessee and specifically took us through executive summary, wherein it is stated that the provision of management services by the assessee to NDTV Net Works PLC was an international transaction. He pointed out that the assessee itself arrived at the ALP margin of 12.29% based on three years data. He argued that each transaction has to be evaluated on a standalone basis and ALP arrived at and that, the transaction of so called share holder activity cannot be clubbed and evaluated with management services activity.

7.4. He referred to page 4 of the transfer pricing study and submitted that the following issues are not in dispute.

- (a) That it is a transaction between two Associated Enterprises .
- (b) That activities were performed
- (c) That consideration was received and
- (d) That the transaction is characterized as of international transaction with the transfer pricing study.

7.5. He further argued that the assessee can not at this stage retract and argue that this is not an international transaction. While submitting that the assessee based its opinion on O ECD commentary , he relied on the very same commentary in paragraph 7.9 to 7.10 to a rgue that this activity is an international transaction. He referred to the examples given at para 7.10 of OECD commentary and argued that it is not the case of the assessee that

the services mentioned in the example were rendered to NDTV Net Works Plc UK. He drew the attention of the Bench to the order of the TPO at page 6 to demonstrate that the nature of services rendered by the assessee are identical, though the assessee tried to classify them into two parts (a) provision of management services and (b) provision of share holder services.

7.6. He submitted that there are no share holder services as such and it was nothing but management services. He vehemently contended that transactions cannot be clubbed. He found fault with the arguments that, just because cost of share holder activity was reimbursed, there is no requirement of charging a mark up on provision of management services and that such cross subsidisation is not permitted under Transfer Pricing provisions. He relied on the order of the TPO and submitted that no new fact was brought before the Ld.CIT(A). He pointed out that note no.2 to form no.3CEB, which is at page 82, what is recorded was , the opinion of the assessee and not the auditor. On the arguments of the assessee that it was acting as a father to promote the son, he submitted that both the entities are separate jurisdictional entities. He distinguished the decision of the Hon ble Delhi High Court in the case of M/s Li & Fung India P.Ltd. vs. CIT 361 ITR 85 by submitting that it was a case relating to creation of intangible assets. Regarding Mumbai High Court decision in Vodafone , 368 ITR 1, it was submitted that this decision was rendered in the context of attribution of income and hence not relevant to the case on hand.

7.7. On the issue of disallowance of ESOPs he made elaborate oral and written submissions. On a query from the Bench he submitted that the issue has been considered by the Special Bench of the Tribunal in the case of Bioco n (supra) but as the revenue has not accepted the order of the Special Bench, he wants the contentions made by him to be taken on record.

8. The Ld.Counsel for the assessee on the other hand submitted that on ESOP the assessee s own case is pending before the Hon ble High Court and

hence the question of considering the arguments against the propositions laid down by the Special Bench of the Tribunal on this issue does not arise.

9. On the issue of transfer pricing he submitted that the assessee is not in the business of providing managerial services. He emphasized that the expenditure was incurred prior to incorporation of the Associated Enterprises. He rebutted the contentions of the Ld.D.R.

10. Rival contentions heard. On a careful consideration of the facts and circumstances of the case and perusal of material on record and orders of lower authorities, case laws cited, we hold as follows.

10.1. For ready reference we extract some portions of the Transfer Pricing Study presented by the assessee.

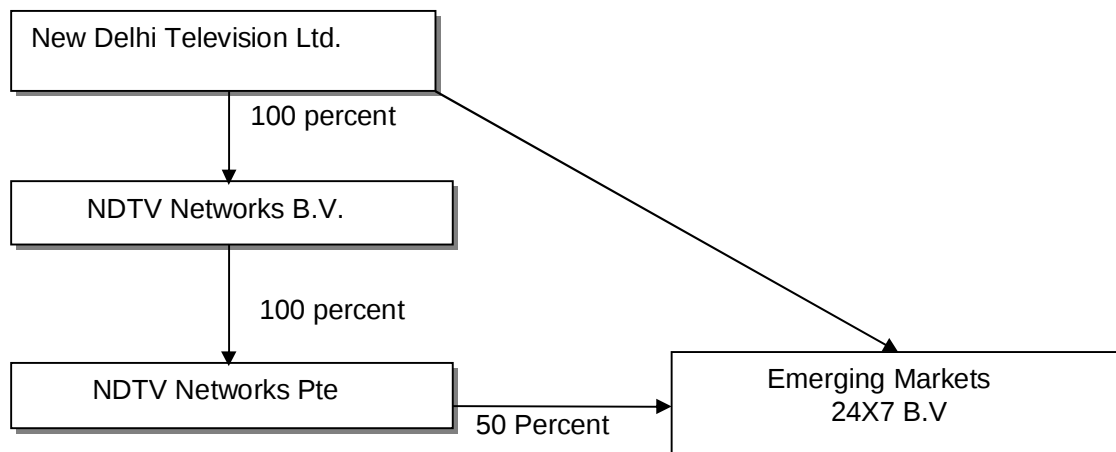
2.1 New Delhi Television Limited

New Delhi Television Ltd. ("NDTV" or "the Company"), founded in 1988. is private producer of news, current affairs and entertainment television. The company has 23 offices and studios across India which host modern and sophisticated production and newsgathering facilities.

The Company's growth can be categorized into three phases. In the first phase, the Company was "content producer" supplying programming to others. Four years ago, the Company transformed into a 'News Broadcaster'. Now in the third phase, the Company is morphing into a full-fledged media network.

To achieve its goal of moving beyond news into a full-fledged media company as well as turning global - a new company called NDTV Networks Plc was incorporated in the UK during financial year 2006-07.

During the financial year 2006-07, NDTV has entered into international transactions with NDTV Networks B.Y. (Netherlands), NDTV Networks Plc (UK) and Emerging Markets 24X7 B.Y. (Netherlands). The relationship between NDTV, NDTV Networks B.Y. and NDTV Network Plc is depicted in the following diagram:



2.2 NDTV Networks B. V.

NDTV Networks B.V. was incorporated in the Netherlands vide incorporation deed executed on 28 December 2006. The company has been incorporated to create the corporate structure for the global media and non-news media related businesses of NDTV.

2.3 NDTV Networks Plc

NDTV Networks Plc was incorporated in United Kingdom on 30 November 2006 under the laws of England and Wales. The company has been incorporated to create a presence for NDTV in the global media market and to develop new avenues of businesses around the world. NDTV Networks Plc has a total of four subsidiaries and two Joint Ventures, each focused on a different genre of media : Entertainment; Internet and Convergence ; Lifestyle channels; technology innovation and integration services; Media Process Outsourcing; and establishing news channels in other countries.

The subsidiaries of NDTV Networks Plc are :

NDTV Imagine Ltd - The company has been established with the aim of launching a Hindi general mass entertainment channel in the near future. In addition, NDTV Imagine Ltd will enter the movie business as well as several other areas in the field of entertainment.

NDTV Lifestyle Ltd .:- The company is aimed at the media space that generates lifestyle programming and channels such as travel, fashion. food. health and fitness. luxury , environment and other similarly targeted channels. The aim of these channels will be to capture the growing retail market in India and to tap the aspirations of the new urban Indian . The first of these lifestyle channels under NDTV Lifestyle Ltd is a 'composite' lifestyle channel coveting a wide range of programming ideas and concepts.

NDTV Labs :- - NDTV Labs is engaged in developing technology and software solutions for television broadcasting, software development, and sale of this software in domestic and international markets.

3. Functions, Assets and Risk Analysis

3.1. Provision of Management Services

3.1.1. Functions

During the financial year 2006 -07, NDTV has rendered management services to NDTV Networks Plc pursuant to the incorporation of NDTV Networks Plc. NDTV has rendered the management services to assist NDTV Networks Plc commence its operations. The management services rendered by NDTV include:

- Facilitation of business development;
- Assistance in negotiations with other persons and in the drafting and finalization of potential agreements with them;
- Formulation and implementation of accounting policies and guidelines customized for local requirements;
- Assistance in obtaining regulatory compliances;
- Assistance in obtaining finances;
- Negotiations with financial and tax consultants to conceptualise an efficient business model of NDTV Networks Plc; and
- Provision of other services that may be deemed necessary to enable NDTV Networks Plc to commence and efficiently run its operations.

3.1.2 Assets

NDTV has employed its human resources for the provision of management services to NDTV Networks Plc. NDTV has the manpower which has experience and knowledge to provide management services to NDTV Networks Plc.

3.1.3 Risk Analysis

There are no inherent external risks associated with this transaction except foreign exchange fluctuation risk, which is borne by NDTV Networks Plc as the payment for management services has been made in Indian currency.

3.2 Grant and Repayment of Loan

3.2.1 Functions

During the financial year 2006 -07, NDTV has advanced loan of Euros 7,62,000 to NDTV Networks B.Y. Further, the loan was repaid by NDTV Networks B.Y. to NDTV during the financial year 2006 -07.

3.2.2 Risk Analysis

There are no inherent external risks in respect of the above international transaction except for foreign exchange fluctuation risk, which is borne by NDTV as the loan was advanced in a currency which is different from the domestic currency of NDTV.

3.3 Receipt of Interest on Loan

3.3.1 Functions

During the financial year 2006 -07, NDTV has received interest amounting to Euros 6,514 on the loan advanced to NDTV Networks B.Y. as per the agreement entered between NDTV and NDTV Networks B.Y.

3.4 Receipt for Shareholder Activity

3.4.1 Functions

During the financial year 2006 -07, NDTV has performed functions to diversify into various domains of media. As part of this diversification and expansion process, NDTV has established a subsidiary NDTV Networks Plc in the United Kingdom. NDTV Networks Plc has further established subsidiaries to enable

NDTV become a full-fledged media group, in order to conceptualise and give effect to an efficient NDTV group structure. the management of NDTV has performed activities prior to the incorporation of NDTV Networks Plc. The activities include making decisions regarding the subsidiaries to be established and the business activities to be performed by those subsidiaries, and dealing with tax, financial and other advisers. The activities performed by NDTV are in the nature of shareholder activity which have been performed in the capacity as the ultimate parent of the NDTV group. NDTV has recharged the salary and other expenses of the managerial personnel of NDTV, who were engaged in performing functions to conceptualise and give effect to an efficient group structure, to NDTV Networks Plc.

3.4.2 Risk Analysis

There are no inherent external risks in respect of the above international transactions.

3.5 Subscription of Shares

3.5.1 Functions

During the financial year 2006-07, NDTV has subscribed to the share capital of NDTV Networks B.Y. and Emerging Markets 24X7 B.Y. NDTV has subscribed to 980 equity shares of Euro 100 each of NDTV Networks B.Y. and 90 shares of Euro 100 each of Emerging Markets 24X7 B.Y.

3.5.2. Risk Analysis

There are no inherent external risks in respect of the above international transactions except for foreign exchange fluctuation risk, which is borne by NDTV as the shares have been subscribed in a currency which is different from the domestic currency of NDTV.

10.2. As per the 3CEP report to international transactions are as follows.

Sl.No.	Name and address of the Associated Enterprise with whom the international transaction has been entered into	Description of transaction	Amount received or receivable in the transaction: As per books of accounts	As computed by the assessee having regard to the arm's length price (Rs.)	Method used for determining the arm's length price S.92C(1)
	Clause 13(a)	Clause 13(b)	Clause 13(c)		Clause 13(d)
1.	NDTV Networks B.V. Martinus Nijhoflan 2,264 ES Delft, Amsterdam, The Netherlands	Reimbursement of courier expenses	3,460	3,460	Refer Note 1 below
2.	NDTV Networks Plc 90, High Holborn, London WC V 6XX	Reimbursement of expenses in the nature of legal and consultancy, hotel, tour and travel	6,501,612	6,501,612	Refer Note 1 below
3.	NDTV Networks Plc 90, High Holborn, London WC V 6XX	Reimbursement of costs	62,180,644	62,180,644	Refer Note 2 below
4.	NDTV Networks B.V. Martinus Nijhoflan 2,264 ES Delft, Amsterdam, The Netherlands	Subscription of shares	5,745,960	5,745,960	Refer Note 3 below
5.	Emerging Markets 24x7 B.V. Martinus Nijhoflan 2,264 ES Delft, Amsterdam, The Netherlands	Subscription of shares	517,500	517,500	Refer Note 3 below
6.	NDTV Networks B.V. Martinus Nijhoflan 2,264 ES Delft, Amsterdam, The Netherlands	Bank charges recoverable from NDTV Networks B.V.	5,922	5,922	Refer Note 4 below
7.	Emerging Markets 24x7 B.V. Martinus Nijhoflan 2,264 ES Delft, Amsterdam, The Netherlands	Bank charges recoverable from Emerging Markets 24x7 B.V.	2,875	2,875	Refer Note 4 below

Note 1: In the opinion of the assessee, these reimbursements do not include
provision of any services and the actual cost incurred is recovered without

any mark up. Based thereon, the assessee considers that the amount received/receivable in respect of the above transactions is at arm's length as provided u/s 92C of the Act.

2. Out of the above, Rs.45,295,590 represents amount received for certain shareholder activities performed by the assessee. As per paragraph 7.9, 7.10 of OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 1995, the aforesaid amount was not required to be charged from the Associated Enterprise, however, the same has been recovered on a conservative basis.

3. The assessee had subscribed to the share capital of this company during the year. Pursuant to such subscription of shares the company became an associated enterprise of the assessee. Further, this transaction does not have an impact on the incomes/expenses of the assessee and thus does not warrant the computation of arm's length price.

4. The above transaction represents misc. Amount recoverable from the company. Since this does not have an impact on the incomes or expenses of the assessee, the said transaction does not warrant the computation of arm's length price. (Emphasis ours).

10.3. OECD transfer pricing guidelines for multinational enterprises and tax administrators states as follows.

Share holder activity: - An activity which is performed by a Member of a MNE group (usually the parent Coordinating Regional Holding Company) solely because of its ownership interest in one or more of other group members i.e. in its capacity as share holder.

In Chapter VII under the head Special consideration for inter group services at para 7.9 it was stated as follows.

7.9: A more complex analysis is necessary wherein Associated Enterprise undertakes activities that relate to more than one member of the group or to

the group as a whole. In a narrow range of such cases, an intra group activity may be performed relating to group members even though those group members do not need the activity (and would not be willing to pay for it were they independent enterprises). Such an activity would be one that a group member (usually the parent company or a regional holding company) performs solely because of its ownership interest in one or more other group members, i.e. in its capacity as shareholder. This type of activity would not justify a charge to the recipient companies. It may be referred to as a shareholder activity , distinguishable from the broader term stewardship activity used in the 1979 report. Stewardship activities covered a range of activities by a shareholder that may include the provision of services to other group members, for example services that would be provided by a coordinating centre. These latter types of non -shareholder activities could include detailed planning services for particular operations, emergency management or technical advice (trouble shooting), or in some cases assistance in day to day management. (Emphasis ours).

10.4. We would now examine the nature of activities that the assessee has undertaken. During the F.Y. 2006 -07, the assessee has rendered management services to NDTV Net Works Plc , prior to its incorporation. It also assisted NDTV Network Plc to commence its operations. The assessee employed its human resources for provision of these management services . It has performed functions to diversify various domains of the media. In order to conceptualise and give effect to an efficient NDTV Group structure, the management of NDTV had also performed various other activities prior to the incorporation of NDTV Network Plc.

NDTV has charged the salary and other expenses incurred on its managerial personnel who were engaged in performing such functions, to conceptualise and give effect to an efficient group structure of NDTV Network Plc and got reimbursement of Rs. 4,52,95,590.

10.5. The management services rendered by NDTV are listed out by the assessee as follows:

1. Facilitation of business development;
2. Assistance in negotiation with the other persons and in drafting and finalisation of potential agreements with them ;
3. Formulation and implementation of accounting policies and guidelines customised for local requirement;
4. Assistance in obtaining regulatory compliances ;
5. Assistance in obtaining finances;
6. Negotiations with financial and tax consultants to conceptualise an efficient business model of NDTV Networks Plc
7. Provision of other services that may be deemed necessary to enable NDTV Network Plc to commence and efficiently run its operations;
8. The activities include making decisions regarding the subsidiaries to be established and the business activities to be performed by those subsidiaries, and dealing with tax finance and other advisories.

The shareholder activities are defined in the OECD Transfer Pricing Guidelines as : an activity which is performed by a Member of an MNE group(usually the parent company or a regional holding company) solely because of its ownership interest in one or more other group members i.e. in its capacity as a shareholder .

10.6. The expenditure in question is listed below .

Details of reimbursement of expenses

Transaction Date	Journal No.	Description	Base Amount Rs.
12/31/2006	80002	Tour & travel expenses, meeting & conferences, legal & professional charges, mobile phone charges	6,048,240
12/31/2006	80005	Consultancy & Professional	

		fees, entertainment, tour & travel, vehicle running & maintenance, salary cost, transfer	22,340,600
12/31/2006	80006	Employee Compensation expenses	16,963,470
12/31/2006	84249	Salary Cost	99,682
12/31/2006	84249	Employee Compensation expenses	(152,099)
12/31/2006	84249	Travel Cost	51,008
12/31/2006	84249	Mobile Phone Charges	(55,310)
		Total :	45,295,590

10.7 . In our view the expenditure incurred prior to incorporation of the U.K. Company i.e. NDTV Network Plc UK can be classified as incurred for share holder activity. This subsidiary company has not come into existence on the date of incurring of this expenditure. The assessee company has incurred the expenditure solely because of its ownership interest. The pre incorporation expenses incurred of the type and nature incurred by the assessee prior to incorporation of its subsidiary NDTV Network Plc UK, in our view, is a different transaction from the one of provision of managerial services after incorporation. Expenditure incurred when an A.E. was not in existence, cannot in our view be classified as an International transaction as per S.92B of the Act. Just because the assessee has classified such expenditure incurred as an international transaction in the T.P.study, we cannot classify the same as such in view of the wordings of Sec.92B of the Act.

10.8 . The expenditure incurred by the assessee, when the A.E. of the assessee was not in existence cannot in our view be taken as a factor for determining the A.L.P. of an international transaction that took place between the assessee and its A.E. post incorporation. Just because, post incorporation NDTV Network Plc UK has reimbursed the employee cost incurred by the assessee prior to incorporation, to the assessee, it does not

lead us to a conclusion that on other managerial services provided by the assessee to the A.E. , no mark up should be charged while reimbursing the expenditure . The assessee in this case has itself worked out 12.29% as the ALP margin , in its Transfer Pricing Report. It is not controverted by the Ld.Counsel for the assessee that in the subsequent Assessment Years , the assessee itself has admitted a mark up on reimbursement of expenditure on these management services . In view of the above discussion, we are of the considered opinion that the TPO is right in making a mark up of managerial services post incorporation of the A.E.

10.9 . Thus we hold that :

- (a) There can be no mark -up on reimbursement of expenses incurred by the assessee prior to incorporation of NDTV Network Plc UK.
- (b) The action of the A.O. in charging a mark -up on reimbursement of expenses incurred by the assessee on management services after incorporation is upheld.

Though the Ld.Counsel for the assessee raised arguments on percentage of mark -up, in view of the percentage of mark -up adopted by the assessee in the subsequent years, we do not see any reason to interfere with the rate of mark -up adopted by the Ld.Transfer Pricing Officer.

11. In the result ground on transfer pricing is allowed in part.

12. On the issue of ESOP, as already stated the Ld.D.R. has submitted his detailed arguments.

12.1. Ld.D.R. arguments are as follows.

Legal perspective

1.1 The allowability of ESOP cost has been a matter of scrutiny by the tribunal and diverse views have been expressed by different benches. In the case of Ranbaxy Laboratories v DC1T [2009 TIOL 632 ITAT DEL], the tribunal has upheld the action of the AO of denial of allowability of the claim of ESOP cost in the profit and loss account and has held that since the receipt of share premium is not taxable, any short receipt of such premium on issuing option to the employees will be notional loss and not actual loss for which any liability

is incurred. However, Hon ble Delhi High Court has admitted further appeal against the decision of Delhi Bench of the Tribunal in the above referred case, which is pending before the Hon ble Court for decision. It is pertinent to mention here that Hon ble Delhi High Court has admitted following questions of law: -

- (i) Whether on the facts and in the circumstances of the case, the tribunal erred in law in holding that the difference between the price at which stock options were offered to the employees of the appellant company under the ESOP Scheme and the prevailing market price of the stock on the date of grant of such options was not allowable expenditure under Section 37(1) of the Act?
- (ii) Whether on the facts and in the circumstances of the case, the tribunal erred in law in not holding that the difference between the prevailing market price of the stock and the price at which stock options were offered to the employees under the ESOP Scheme, resulting in benefit to the employees and thus constituting remuneration of the employees was, allowable deduction under Section 37 of the Act?

1.2 Since issue of claim of deduction of ESOP cost u/s 37(1) of the Act which is actually discounted premium is pending before Hon ble Delhi High Court for adjudication in the case of R anbaxy Laboratorie s v DCIT [2009 TIOL 632 ITAT DEL], the decision of the ITAT allowing claim of the assessee that the ESOP cost was allowable as deduction u/s 37(1) of the Act following decision of Special Bench of the ITAT in case of DCIT Vs. Biocon Ltd. (Supra) is not acceptable.

1.3 The Special Bench of Bangalore in the case of DCIT V Biocon Ltd. [Supra] has considered the identical issue and has held that the ESOP cost is deductible u/s 37(1) of the Act to the profit and loss account. The Special Bench laid down following principles:

"Discounted premium on the ESOP is neither a short capital receipt nor is a capital expenditure but it is employees cost incurred by the company.

"Discounted premium on the ESOP cannot be held as contingent liability.

" Legislature has already considered such discounted premium to the employee as a fringe benefit accordingly, the discount on share under ESOP is an allowable deduction. The amount of discount at the stage on granting of

option with reference to the market price of the shares at the time of grant of options is always a tentative employee cost because the impossibility of correctly visualizing the likely market price of shares at the time of exercise of option by the employees which, in turn, would reflect correct employee cost.

" Since definite liability is incurred during the vesting period, it has to be quantified on some logical basis. Since the actual amount of employee cost can be precisely determined only at the time of the exercise of option by employee, the provisional amount of discount availed as deduction during vesting period needs to be adjusted in the light of actual discount on the basis of market price of the shares at the time of exercise of option. It can be done by making suitable upward and downward adjustment of the provision at the time of exercise of option.

1.4 Whether guidelines of the SEBI on ESOP stipulate discounted premium on share as employee compensation and an allowable deduction u/s 37(1) of the Act?

1.4.1 Securities and Exchange Board of India (SEBI) has issued guidelines on employee stock option scheme (ESOP) which is known as Securities and Exchange Board of India Employee Stock Option Scheme and Employee Stock Purchase Scheme Guidelines 1999 up to dated September 3, 2009 (the SEBI Guidelines). The silent features of the guidelines are as under:

1.4.2 Employee compensation does not include ESOP. For the sake of clarity, definition of employee compensation as stipulated under the SEBI guidelines is extracted as under:

"(2) employee compensation means the total cost incurred by the company toward employee compensation including basic salary, dearness allowance, other allowances, bonus and commissions including the value of all perquisites provided, but does not include

(a) the fair value of the option granted under an Employee Stock Option Scheme; and

(b) the discount at which shares are issued under the Employee Stock Purchase Scheme. (2A) Employee Stock Option means the option given to the

whole-time Directors, Officers or employees of a company which gives such Directors, Officers or employees, the benefit or right to purchase or subscribe at a future date, the securities offered by the company at a predetermined price.]

1.4.3 Accounting policies of the ESOP have been provided in Schedule 1 to SEBI Guidelines 1999. For the sake of convenience, the relevant part of accounting policies is extracted as under: -

(a) In respect of options granted during any accounting period, the accounting value of the options shall be treated as another form of employee compensation in the financial statements of the company.

[(b)] The accounting value of options shall be equal to the aggregate, over all employee stock options granted during the accounting period, of the intrinsic value of the option or, if the company so chooses, the fair value of the option.]

[(c) Where the accounting value is accounted for as employee compensation in accordance with clause(b), the amount shall be amortized as under:

(i) Where the scheme does not provide for graded vesting, the amount shall be amortized on a straight-line basis over the vesting period.

(ii) Where the scheme provides for graded vesting -

(1) the vesting period shall be determined separately for each separate vesting portion of the option, as if the option was, in substance, multiple option and the amount of employee compensation cost shall be accounted for and amortized accordingly on a straight-line basis over the vesting period;

Or

(2) the amount of employee compensation cost shall be accounted for and amortized on a straight-line basis over the aggregate vesting period of the entire option (that is, over the vesting period of the last separately vesting portion of the option):

Provided that the amount of employee compensation cost recognized at any date at least equals the fair value or the intrinsic value, as the case may be, of the vested portion of the option at that date.]

(d) When an unvested option lapses by virtue of the employee not conforming to the vesting conditions after the accounting value of the option has already been accounted for as employee compensation, the accounting

treatment shall be reversed by a credit to employee compensation expense equal to the amortized portion of the accounting value of the lapsed options and a credit to deferred employee compensation expense equal to the unamortized portion.

(e) When a vested option lapses on expiry of the exercise period, after the fair value of the option has already been accounted for as employee compensation, this accounting treatment shall be reversed by a credit to employee compensation expense .

1.4.4 Schedule 3 to the SEBI Guidelines provides methodology to determine fair market value of stock options.

1.4.5 The careful perusal of the SEBI guidelines on ESOP (relevant part of which have extracted above) has revealed that the conclusion of Special Bench of the Tribunal that the SEBI guidelines stipulate ESOP cost as employee compensation is contrary to clause

(2) (a)(b) of the SEBI guidelines which clarifies that discounts at which share are issued to employee under ESOP is not employee compensation. The guidelines of SEBI on accounting policies as contained in Schedule 1 to SEBI guidelines has not laid down any principle that ESOP cost is revenue expenditure and is deductible in the Profit & Loss A/c of the assessee. It is evident from clause (f) of the Schedule 1 of the SEBI guidelines that ESOP cost has been classified as balance sheet item not an item of Profit & Loss A/c for the sake of clarity the relevant part of the guideline is reproduced as under: -

Employee Stock Options Outstanding will appear in the Balance Sheet as part of Net Worth or Shareholders Equity. Deferred Employee Compensation will appear in the Balance Sheet as a negative item as part of Net Worth or Shareholders Equity.

1.4.6 In view of above, the claim of the assessee that the entry in Profit & Loss A/c was made on the recommendation of the SEBI is not correct proposition and contrary to the SEBI guidelines. Even otherwise deduction u/s 37(1) will not be guided by the recommendation of the SEBI. A conjoint reading of provisions of section 78 of the Companies Act, 1956 along with the SEBI guidelines on accounting treatment of ESOP cost has revealed that

discounted premium on shares under the ESOP could be met out of premium reserve of the company if any i.e. the ESOP cost which is discounted premium on shares is a balance sheet item which is capital in nature and can only be adjusted against the reserve. The analysis of SEBI guidelines clearly proves that ITAT has mis-directed itself in reaching a conclusion that the SEBI guidelines stipulates that ESOP cost is employee compensation and that the ESOP cost is deductible to Profit & Loss A/c as revenue expenditure on the ground that the SEBI guidelines do not laid down above referred to principles. Without prejudice to above, the provisions of the SEBI guidelines which have been framed for different purpose and intend are not pari materia with the provisions of Income Tax Act cannot be used to interpret scope of provisions of section 37(1) of the Act.

1.5 Whether share premium is a capital receipt?

1.5.1 Section 78 of the Company Act 1956 which is relevant for the assessment year under consideration provide that whether the company issue shares at premium, whether for cash for otherwise, a sum equal to the aggregate amount or value of the premiums on those shares shall be transferred to an account to be called the share premium account ; and the provisions of this Act relating to the reduction of share capital of the company shall, except as provided in this section, apply as if the share premium account were paid up share capital of the company. For the sake of clarity provisions of section 78 of the Companies Act 1956 have been extracted below: -

78. Application of premiums received on issue of shares.

- (1) Where a company issues shares at a premium, whether for cash or otherwise, a sum equal to the aggregate amount or value of the premiums on those shares shall be transferred to an account, to be called the share premium account ; and the provisions of this Act relating to the reduction of the share capital of a company shall, except as provided in this section, apply as if the share premium account were paid up share capital of the company.
- (2) The share premium account may, notwithstanding anything in sub-section (1), be applied by the company -

- (a) in paying up unissued shares of the company to be issued to members of the company as fully paid bonus shares;
 - (b) in writing off the preliminary expenses of the company;
 - (c) in writing off the expenses of or the commission paid or discount allowed on, any issue of shares or debentures of the company; or
 - (d) in providing for the premium payable on the redemption of any redeemable preference shares or of any debentures of the company.
- (3) Where a company has, before the commencement of this Act, issued any shares at a premium, this section shall apply as if the shares had been issued after the commencement of this Act: Provided that any part of the premiums which has been so applied that it does not at the commencement of this Act form an identifiable part of the company's reserves within the meaning of Schedule VI, shall be disregarded in determining the sum to be included in the share premium account.

(Emphasis supplied)

1.5.2 The Indian Accounting Standards stipulate presentation of financial statement of assets and liabilities. It further provides disclosure of each class of share capital on the liability side of the balance sheet. The standard provides that share capital includes additional paid up capital which includes share premium. It is amply clear from the provisions of the Companies Act and the Indian Accounting Standards that share premium or security premium is considered a capital receipt, has to be shown in Reserves and Surplus as an item on liabilities side of the balance sheet and these reserves can be used only in a limited manner permitted by the law. The permitted use of such reserves generally result into increase in share capital or reduction of some specified liabilities on capital account including payments of discount allowed as stipulated under section 78(2)(c) of the Companies Act which covers discounted premium on allotment of share under ESOP. The amount standing in securities premium is either converted into capital or reduces liabilities. Therefore, share premium including discounted share premium cannot be considered revenue receipt or expense at any stage like at the time of receipt or at the time of use. Hon'ble 1TAT Mumbai Bench examining the nature of share premium receipt on issue of shares in case of Green Infra Ltd. Versus

Income-tax Officer 2013 (12) TMI 949 -ITAT Mumbai have held that share premium realised from issue of shares is capital in nature and form part of share capital of the company. In this case the assessee issued equity shares to the employees which resulted in increase in paid up capital by equivalent amount, accordingly, discounted premium on share was capital in nature. It is also a settled proposition of law that any expenditure incurred for the expansion of the capital base of a company is to be treated as a capital expenditure as has been held by the Supreme Court in the cases of Punjab State Industrial Corporation Ltd v. CIT [1997] 225 ITR 792 (SC) and Brooke Bond India Ltd. v. CIT [1997] 225 ITR 798 (SC). Thus the expenditure and the receipts directly relating to the share capital of a company are of capital in nature and therefore, cannot be taxed under the Act save for certain exceptions.

1.5.3 Till assessment year 2012 -13 share premium received by any company was not deemed as income. Even from AY 2013 -14 share premium received by a listed company and some other specified companies is not deemed as income. Deeming provision as per Section 56 (vii b) (inserted w.e.f. 01.04.2013) is applicable only in case of shares issued at price higher than fair market price by closely held companies (subject to some exceptions). And this is not applicable to a company which is listed on a recognized stock exchange and some other companies, which are also considered as company in which public is substantially interested. In case of issue of shares at premium by listed companies, share premium is not considered as income. However, in case of un-listed companies premium can be considered as income in case the price charged is more than face value (that is at premium) and is also higher than fair market value. In such case, excess of issue price above the fair market value will be considered as income of issuing price. In case a company issues shares at face value, though market value is lower than face value, the difference between price charged that is issue price and fair market value will not be considered as income. It is evident from above that the above referred to deeming provisions only provide taxation on extra price which may be share premium or value more than the book value even though the receipt was in capital in nature. Since the provisions provide taxation of capital receipt it

was brought to tax under the head Income from Other Sources . However, the character of receipt would still remain capital and would not change since the difference was charged to tax under section 56 of the Act.

1.5.4 It is pertinent to mention here that Hon ble IT AT in case of Biocon Ltd. Vs DC IT (Supra) ignoring the provisions of the Companies Act, Indian Accounting Standards and Legal Precedents on the issues by following erstwhile provisions of Fringe Benefit Tax (FBT) has held that once legislature has treated the very same ESOP as expenditure while taxing it under FBT, it cannot be argued that ESOP cost is not expenditure. Fringe Benefits Tax was introduced as part of the Income Tax Act in Chapter XII-H as a self contained code which included complete scheme of levy of tax and its recovery with effect from A.Y. 2006 - 07 only to be abandoned with effect from A.Y. 2010 - 2011, so that it was in force for a brief period of four years being 2006 -2007, 2007 -08, 2008 -09 and 2009 -2010. The object was to ensure that fringe benefits given by the employer to employees disguised in expenditure is best taxed in the hands of the employer. With the abolition of this Act, the liability on the employees under Rule 3 on all benefits excluding benefit from ESOP was restored. It is evident from above that the FBT was introduced to tax benefits disguised in expenditure and for a limited period which is now repealed. Since provision of FBT were introduced for different intend and purchase the provisions of FBT cannot be used to interpret existing provisions of Section 37 (1) of the Act. The words and expressions defined in one statute as judicially interpreted do not afford a guide to the construction of the same words or expressions in another statute unless both the statutes are pari materia legislations or it is specifically provided in one statute to give the same meaning to the words as defined in another statute. In view of above referred to settled legal position on the issue of interpretation of statute, it is respectfully stated that the tribunal has misdirected itself in relying on the provisions of the FBT while examining the nature of share premium u/s 37(1) of the Act.

1.5.5 Since the legislature considers discounted premium to the employees as Fringe Benefit accordingly discounted premium is an expenditure and cannot be treated as short capital receipt.

1.6 As discussed above, the FBT was in force w.e.f assessment year 2006 -07 to 2009 -10 and the object of FBT was to ensure that fringe benefits given by the employer to employees disguised in expenditure is best taxed in hand of employer i.e., to tackle the issues of taxation of benefits which were treated as expenditure by the tax payers. For these reasons, employer was required to pay Fringe Benefit Tax on benefit derived by employee from ESOP. The employer was also allowed to recover such FBT from the employees. It is amply clear from the intent and purpose of the FBT provisions that it was meant to tax benefits including capital benefits disguised as expenditure. In other words, the FBT was applicable both on capital and revenue expenditure accordingly, the provisions of FBT in no way support the conclusion of the Tribunal that ESOP cost cannot be treated as short capital receipt. The provisions do not also support a conclusion of the Tribunal that ESOP cost was expenditure deductible u/s 37(1) of the Act. It is important to highlight here that the assessee as an employer did not pay FBT on ESOP benefit, but had claimed deduction of discounted premium in the grab of expenditure allowable deduction u/s 37(1) of the Act. Since the amount was taxable in hand of employer it could not be taxed in hand of employees. Without paying any tax, the assessee claimed deduction of discounted premium to the Profit & loss A/c. This lead to an irresistible conclusion that the assessee in its return under the FBT did consider ESOP cost as benefit or employee compensation and had not paid taxes on it but had claimed deduction of ESOP cost u/s 37(1) of the Act. In view of above, the conclusion of ITAT that ESOP cost was allowable as deduction u/s 37(1) on the basis of provisions of FBT is without any legal basis and against the rule of construction of the statute.

1.7 In view of above analysis the conclusion of Special Bench that discounted premium on share is neither a short capital receipt or a capital expenditure it is nothing but employee cost incurred by the company and is allowable u/s 37(1) is contrary to the relevant provisions of Income Tax Act, the Companies Act and legal principles as laid by Hon'ble Apex Court on the similar issues. In view of above, it is not logical to plead that premium on share is capital receipt where as discounted premium on share is revenue expenditure. The discounted premium is capital cost or expenditure which

could not be claimed as deduction u/s 37(1) of the Act. Without prejudice to above that ESOP cost is capital in nature, the other part of judgment of special bench has been discussed in succeeding paragraphs.

1.8 Whether discounted premium on share issued under ESOP is expenditure u/s 37(1) of the Act.

1.8.1 The term Expenditure has been judicially interpreted by various Courts including Supreme Court of India. In case of Indian Molasses Company Private Limited Vs. Commissioner of Income Tax, West Bengal [1959] 37 ITR 66, Hon ble Apex court has held the Spending in the sense of paying out or away of money is the primary amounting of expenditure . The term Expenditure is what is paid out or away and is something which is given irretrievably. For the sake of clarity the relevant part of judgment is reproduced as under : -

"Expenditure' is equal to expense: and expense" is money laid out by calculation and intention though in many uses of the word this element may not be present, as when we speak of a joke at another s expense. But the idea of spending in the sense of paying out or away money is the primary meaning and it is with that meaning that we are concerned. Expenditure is thus what is paid out or away and is something which is gone irretrievably.

12.2. He further relied on certain other case laws, which we do not feel it necessary to deal with, as the Special Bench of the ITAT has dealt with the same.

13. In any event, in view of the decision of the Special Bench of the Tribunal in the case of Bioco n Ltd. which is binding on us this issue is set aside to the file of the Assessing Officer for fresh adjudication. The A.O. for the A.Y. 2008 -09 in an order passed u/s 250/143(3) of the Act on 14.9.2015, on the directions of the Ld.CIT(A) and allowed the claim of ESOPs expenditure by following the decision of the Special Bench after verification. Hence the issue in this year should also be decided by him afresh.

14. In the result this ground is allowed for statistical purposes.

15. In the result assessee's appeal is allowed in part.

16. We now take up the Revenue's appeal i.e. ITA 2752/Del/13, which is on the issue of allowability of software expenditure.

17. The A.O. in this case disallowed the expenses incurred on upgradation of accounting software on the ground that it is capital in nature.

17.1. Ld.CIT(A) has allowed this expenditure as revenue in nature. While doing so he observed that the assessee itself has characterised certain software purchase on its own as capital assets. He observed that certain software needs regular upgradation or change as per the requirement of fast changing broadcasting industry and that his predecessor has allowed similar expenditure on upgradation of software as revenue in nature. We find no infirmity in this finding of the Ld.CIT(A).

18. In the result we uphold the order of the Ld.CIT(A) and dismiss this appeal of the Revenue.

19. In the result the appeal of the assessee is allowed in part and the appeal of the Revenue is dismissed.

Order pronounced in the Open Court on 17th August, 2016.

Sd/ -
(SUCHITRA KAMBLE)
JUDICIAL MEMBER

Sd/ -
(J. SUDHAKAR REDDY)
ACCOUNTANT MEMBER

Dated: the 17th August, 2016

Manga

Copy forwarded to: -

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2. Respondent
3. CIT
4. CIT(A)
5. DR, ITAT

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By Order,

ASSISTANT REGISTRAR