

**IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH “J”, MUMBAI**

**BEFORE AMIT SHUKLA (JUDICIAL MEMBER)
AND
MS. PADMAVATHY S. (ACCOUNTANT MEMBER)**

**I.T.A. No.2107/Mum/2022 - A.Y. 2018-19
I.T.A. No.2108/Mum/2022 - A.Y. 2017-18**

Unilever India Exports Limited Unilever House, B D Sawant Marg Chakala, Andheri East, Sahar P & T Colony S.O., Mumbai PAN : AAACI099ID	vs	ACIT, CC.5(3) Room o.1906, 19 th Floor , Air India Building, Nariman Point, Mumbai- 400 021
ASSESSEE		RESPONDENT

Assessee represented by	Ms. Karishma Phatarphekar, shri Harsh Shah
Department represented by	Shri Samuel Pitta

Date of hearing	20-04-2023
Date of pronouncement	11-05-2023

ORDER

PER BENCH

These appeals of the assessee are directed against the order of the Assistant Commissioner of Income-tax, Central Circle-5(3), Mumbai passed under section 143(3) read with section 144C(13) dated 28/06/2022 and 28/07/2022 for the Assessment Years 2017-18 and 2018-19, respectively. Since identical issues are agitated in these appeals, both the appeals are disposed of by way of this common order.

2. The assessee, Unilever India Exports Limited (UIEL) is a wholly owned subsidiary of Hindustan Unilever Limited (HUL). The fast moving consumer goods (FMCG) exports business of HUL was transferred to UIEL under a court approved scheme of arrangement with the appointed date of April 1, 2011.

3. The assessee company is engaged in the manufacturing of branded FMCG products, namely Foods and Beverages and Home and Personal Care (HPC) products. These brands are owned either by Unilever Plc / Unilever NV, the ultimate parent companies of the Unilever Group of HUL.

I.T.A. No.2108/Mum/2022 for AY 2017-18

4. The assessee has e-filed its return of income for A.Y. 2017-18 declaring total income of Rs.156,38,060/- on 30/11/2017 Statutory notices along with questionnaire were issued by the Assessing Officer which have been complied with by the assessee by electronically submitting the details called for from time to time. Since the assessee had international transactions with its AE a reference was made to the Transfer Pricing Officer (TPO) for determination of Arms Length Price (ALP) of such transactions. The TPO made the following adjustments:-

- | | |
|---|-------------------|
| 1. Payment of royalty for technical documentation, information and technical know | Rs. 6,54,03,000/- |
| 2. Payment of royalty for central services | Rs.11,65,31,532/- |
| 3. Purchase of raw material and the sale/
Export of HPC & P&B | Rs.40,11,63,635/- |

5. The Assessing Officer passed the draft assessment order incorporating the above adjustment. Besides, the Assessing Officer also made a disallowance under section 14A for Rs.83,83,273/- and also disallowance of ESOP expenses to the

tune of Rs.1,47,50,000/-. Aggrieved, the assessee filed its objection before the DRP. The Ld.DRP gave relief to the assessee with respect to the TP adjustment made towards payment of royalty for technical documentation and towards purchase of raw material and sale / export of HPC & F&D. With regard to the disallowance made by the Assessing Officer, the Ld.DRP upheld the same. The Assessing Officer passed the final assessment order in accordance with the directions of the DRP against which the assessee is in appeal before the Tribunal.

6. The issues contended through various grounds are as under –

Ground 1 : General

Ground 2 :Final order of assessment is bad in law as the same is issued without DIN.

Grounds 3 to 7: Transfer pricing adjustment for payment of central fees

Grounds 8 & 9 : Disallowance under section 14A

Grounds 10-13: Disallowance of ESOP expenses.

Ground 14 : Excess levy of interest under section 234B & 234D

Ground 15 : Initiation of penalty under section 270A

7. TP adjustment towards payment of central services (Ground No.3 to 7)

7.1 The brief facts are that the assessee company has made payment to its AE, viz. Unilever Plc towards central service charge. The Central Service Charge consists of the following services:-

- Corporate Services;
- Category Services;
- Global Market Leadership Services; and

•Other Services

8. Unilever PLC has granted a non-exclusive license to Unilever India Exports Ltd. i.e. assessee; firstly for using technical documentation, information, technical knowhow and improvements; and secondly, for central services vide common-technology, trade mark license and simple service agreement, effective from 01/02/2013. The copy of agreements has been filed before us in the paper book. In so far as payment made by the assessee to Unilever PLC for using technical documentation, information, technical knowhow and improvements, the ld. DRP deleted the adjustment made by the ld. TPO in both the assessment years. Accordingly, this is not the issue in dispute. However, the only issue is with regard to central services flowing from the aforesaid agreement. Admittedly, the same agreement was in operation for both the assessment years and therefore, the nature of services rendered in terms of the agreement was also same. The Assessee company has paid Central Services Charge @ 1% of estimated turnover and it has paid Total Central Service Fees of Rs.11,65,31,532/-. The assessee company has chosen external CUP method as MAM for determination of ALP for underlying transaction. In Transfer Pricing Study Report (TPSR), the Assessee company has compared royalty rate as available from Royalty Stat Database @ 5.75% (pg 119 of paper book), with the rate of 1 % (pg 107 of paper book) charged by the AE to the Assessee-company and accordingly, concluded that since the rate charged by the AE is less than the aforementioned rate available from Royalty Stat, the transaction concluded to be arm's length. The Ld.TPO, on perusal of the TPSR and benchmarking of the assessee, observed that there is a need to furnish details relating to nature of services received and also justify the payment(s) made by undertaking cost benefit analysis. Accordingly assessee was asked to furnish details relating to nature of services received justify the payment(s) made by

undertaking cost benefit analysis and also show as to why the method adopted as well as the ALP of the transactions as determined by the assessee should not be rejected, and the same should not be determined afresh as was done in earlier years, mutatis mutandis, facts remaining substantially the same. The assessee submitted a detailed reply explaining the nature of services as has been done as part of transfer pricing study including benefit test. The Ld. TPO, rejected the submissions of the assessee and also the comparables chosen by the the assessee. The TPO held that the assessee failed to clear the benefit test and therefore applied 'Other Method', for determination of ALP of payment of Royalty for Central Services and determined the same at Zero (Nil) by holding that the whole value of international transaction not satisfy the ALP principle. Therefore, the entire amount of Rs.11,65,31,532/- is considered for adjustment in relation to the impugned transaction. The Ld.DRP, finding that the facts of the case remain the same during the year under consideration, chose to follow the decision arrived at for the preceding years.

9. During the course of hearing the ld. AR drew our attention to the various documents filed in the paper book to examine the redemption of central services by giving over PLC to the assessee and commensurate benefits desired from such services. These were highlighted in the following manner vis-à-vis the documents given in the paper book.

Services	PB reference 2017-18	PB reference 2018-19
<p>Finance Kit (FKIT) – Finance Kit is the Treasury Management System used by Unilever Treasury Team for Risk management and treasury operations. Finance Kit is developed by Wall Street System (a global leader in providing treasury management solutions) and offers immediate visibility, control and simplified compliance throughout the enterprise). The solution combines depth of functionality with seamless integration by enabling all cash management, trading, funding and investment activities to be automated, audited, consolidated, and accounted for, instantaneously and globally. UIEL has been using Finance Kit for the following purposes:</p> <p><u>Forex Risk Management</u> – Tracking exposures at a company and unit level and corresponding foreign exchange contracts with banks. This enables UIEL to manage the foreign exchange risk efficiently and effectively and ensure compliance with the approved forex policy.</p> <p><u>Accounting</u> – The accounting entries for forex transactions are generated from the finance kit. This is then posted in UIEL's SAP ERP. It similarly automates the accounting for investment transactions thereby eliminating manual accounting and tracking. Finance Kit also has direct feeds from information service providers such as Reuters and market information such as MTM can be directly accessed from Finance Kit. It also helps generate various accounting reports.</p> <p><u>Reporting and MIS</u> – The System provides management with various reports on forex and investment transactions and help the management to have a bird's eye view of the status of the forex exposure and corresponding hedge against the same. Cash flows, investment positions etc. can be directly obtained from the</p>	<p><i>PB Pg. 392</i></p> <p><i>PB Pg. 393 to 394</i></p> <p><i>PB Pg. 392 to 394</i></p>	<p><i>PB Pg. 347</i></p> <p><i>PB Pg. 348</i></p> <p><i>PB Pg. 347 to 349</i></p> <p><i>PB Pg. 347 to 349</i></p>

Services	PB reference 2017-18	PB reference 2018-19
<p>FinanceKit.</p> <p><u>Counterparty Risk Management</u> – UIEL investments and foreign exchange transactions are subject to overall counterparty risks, hence there is an approved counterparty limit for each bank that UIEL deals with. All transactions with the bank are recorded in Finance Kit and compliance against approved limits is tracked on a real-time basis using FinanceKit.</p>	<p><i>PB Pg. 392 to 394</i></p>	
<p>Environmental sustainability – Given the industry and regulatory focus on environmental sustainability, UIEL is following very high standards to ensure minimum impact on the environment through constant improvement in processes and technologies. Unilever's global operations help UIEL to understand the latest trends in environmental sustainability and adopt such technologies.</p>	<p><i>PB Pg. 395 to 398</i></p>	<p><i>PB Pg. 350 to 353</i></p>
<p>Issue management tools – Due to widespread information available through social media and other mediums, any issue can flare up with lightning speed. To manage such crises, guidelines are provided by Unilever to provide necessary protocols for crisis management and to prevent any mishaps. There are various templates and training documents about risk and issue management. This tool also helps in understanding the best practices to be adopted. Further, there are constant improvements to improve the usability and functionality of logging issues. There is guidance available depending on the priority of issues eg. critical, high, low, etc.</p>	<p><i>PB Pg. 399 to 400</i></p>	<p><i>PB Pg. 354 to 355</i></p>
<p>Personal Care Identity Toolkit – To increase the awareness and position of UIEL's products in a more unique, authentic and different way than its competitors. Unilever has created a special tool which is adopted by UIEL to ensure consistency in the visibility of the products both internally and externally in the market. The</p>	<p><i>PB Pg. 401 to 402</i></p>	<p><i>PB Pg. 356 to 357</i></p>

Services	PB reference 2017-18	PB reference 2018-19
toolkit uses techniques like visual identity, photography, graphic styling, etc.		
<p>Human Resources (HR) services – UIEL has a large workforce, thereby making the HR function extremely important. To help in managing its employees efficiently, Unilever’s Global HR team has provided various tools and applications to UIEL, which helps UIEL in the automation of its HR functions. Following are some of the tools and applications used by UIEL:</p> <p><u>HR Online</u> - An Oracle tool used for managing employee lifecycle actions, like moves/ transfers etc. This helps the line managers to initiate such requests for their team. Employees manage their personal information through this application. The home page of the website HR Online is accessed by the employees. Further, it provides various tabs to the employees according to the information to be accessed by the employees.</p> <p><u>Peoplesoft</u> – An Oracle ERP application which manages employee data and their position-related details. A specific requirement is through the request service page and the request status page.</p> <p><u>Learning Hub</u> – It is a learning application, of different types i.e. web-based, virtual and blended learning modules. This is used for learning and development and capability agendas. The home page, guidelines for the Learning Hub application and the learning calendar.</p> <p><u>Unify</u> – It is a leave management Module. The employee uses this application to manage their assigned annual leaves. Homepage, request for encashment and the email from Unify Team for leave approval request.</p> <p><u>Sparkle</u> – It is a tool to manage Blue-collar employees’ capability and</p>	<p><i>PB Pg. 403 to 405</i></p> <p><i>PB Pg. 406 to 408</i></p> <p><i>PB Pg. 409</i></p> <p><i>PB Pg. 410 to 429</i></p> <p><i>PB Pg. 430 to 432</i></p>	<p><i>PB Pg. 358</i></p> <p><i>PB Pg. 359 to 361</i></p> <p><i>PB Pg. 362 to 364</i></p> <p><i>PB Pg. 365 to 384</i></p> <p><i>PB Pg. 385 to 387</i></p>

Services	PB reference 2017-18	PB reference 2018-19
<p>performancemanagement. The Sparkle quick reference guide and the screenshot of the Sparkle home page displaying various tabs such as assessment and identification of skill gaps and priority areas for training, track progress and map primary and secondary skills based on standardized jobs. Also, the screenshot of various documents such as sparkle key activities, sparkle training decks, sparkle support model etc</p> <p><u>TalentPlusOnline</u>–UnileverhasprovidedanonlinetoolwhichisusedbyUIEL as a recruitment, talent and performance management system for keeping track of one's individual performance development. It allows UIEL employees to manage their Talent Profile, set goals, create Individual Development Plans and conduct mid-year and annual reviews for self-developmentpurposes.</p>	<p><i>PB Pg. 433 to 434</i></p> <p><i>PB Pg. 435 to 457</i></p>	<p><i>PB Pg. 388 to 389</i></p> <p><i>PB Pg. 390 to 412</i></p>
<p>Assistance by Unilever for undertaking various businessprocesses:</p> <p><u>Specification management</u> – UIEL also receives process-related support from the globalteam.Forexample,the‘specificationmanagementtool’isacommunication tool between the R&D team and the supply chain team. This tool contains the detailed specification of products including the formulation and manufacturing process (with flow diagrams). The same is used to support the raw material purchasing decision for the procurement team and the manufacturing of a product for the manufacturing team. The tool for creating a specification to display the entire formulation process.</p> <p><u>Logistic support</u> – Unilever has provided Ultralogistik software (Oracle</p>	<p><i>PB Pg. 458 to 460</i></p>	<p><i>PB Pg. 413 to 415</i></p>

Services	PB reference 2017-18	PB reference 2018-19
<p>Transport Management system) to India for tracking its supply chain of products, etc. The software focuses to track the movement of supplies which are transported by sea/ road.</p> <p><u>Procurement support</u> – The Global Procurement Team helps UIEL Procurement Team by giving timely advice and guidelines by providing market intelligence on Global markets and guidance on commodity pricing to enable UIEL to take timely decisions.</p>		
<p>Quality management guidelines:-</p> <p>UIEL has access to the Unilever Global Quality Management System (QMS) which is a one-stop-shop for global quality standards, processes and tools and is accessible to everyone within Unilever. It covers all the business critical quality processes needed to design, manufacture and distribute safe products for use by consumers.</p> <p>Some of the recent quality standard documents issued by the Global QMS Team are on Good Manufacturing Practice (GMP) for the Foods Category, HPC, Refreshments, etc., Cleaning and Disinfection, Consumer relevant quality standards, Disposal of non-conforming products, Foreign matter management and control, Integrated Pest Management, Personnel Hygiene & Employee facilities, Prevention of Cross Contamination, Quality Sampling, Monitoring & Testing, Guidelines on Warehouse and Transport, etc. The home page displays various documents such as Supplier Assurance and Audit, microbiological and hygiene issues, customer services, complaint handling and management of errors etc.</p> <p>UIEL gets significant inputs on consumer-relevant quality standards (CRQS) from the global teams, and in addition, there is significant value addition by</p>	<p>PB Pg. 461 to 462</p>	<p>PB Pg. 416 to 417</p>

Services	PB reference 2017-18	PB reference 2018-19
doing category-specific deep dives, recommending solutions based on experiences in other Unilever countries and educating UIEL team on quality standards for new product innovations.		
<p>Safety – UIEL gets expert advice from a global centre of excellence in the UK called the Safety & Environmental Assurance Centre (SEAC). They advise on the design of new projects and facilities, safety incident investigation, discussions with internal and external consultants without any cost to UIEL and provide in-depth advice.</p> <p><u>Process Safety</u> – UIEL Team gets training on specialist subjects from Subject matter experts.</p> <p><u>Group Security</u> – It provides specialized security training via web and face-to-face in addition to site assessments. They also guide security strategy & hardware standards for access control & security surveillance that help UIEL get the right hardware at the right cost without bringing in external consultants.</p>	<i>PB Pg. 463 to 464</i>	<i>PB Pg. 418 to 419</i>
<p>Risk Management – UIEL believes that effective risk management is fundamental to good business management and that the success of an organization like UIEL depends on its ability to identify and then exploit the key risks and opportunities for the business. Successful businesses take/manage risks and opportunities in a considered, structured, controlled and effective way. Unilever shares a lot of information on risk management with UIEL, which helps UIEL in framing its risk management policies. The risk management homepage displays the principles of risk management, the embedded risk management approach, the risk management policy, global physical security procedures guidance document incorporating the scope and structure. The Unilever Principles of</p>	<i>PB Pg. 465 to 471</i>	<i>PB Pg. 420 to 426</i>

Services	PB reference 2017-18	PB reference 2018-19
Risk Management are to be implemented by all the managers.		

10. Besides the Ld.AR also submitted a detailed written submission which has been taken on record for the purpose of adjudication. The summary of the submissions of the ld AR is as under

- The assessee has rightly benchmarked the payment of intra-group services based on CUP, which is one of the prescribed methods, and has also provided documentation in support of the rendition of services in both the impugned years.
- Though the TPO states he has followed the ‘Other method’, no comparable transaction has been brought on record, and the TPO has merely resorted to *ad-hoc* benchmarking of the transaction which is contrary to the mandate of section 92C of the Act. The Hon’ble Bombay High Court has repeatedly held in various decisions that ad-hoc transfer pricing additions, without following any one of the prescribed methods, are not sustainable in law.
- In AY 2012-13 and AY 2013-14, the Tribunal has deleted the transfer pricing addition arising from TPO’s identical determination of ALP. The facts of the impugned are the same accordingly, the findings of the said decision ought to apply *mutatis-mutandis* to the impugned assessment years.
- In AY 2015-16 and AY 2016-17, the Tribunal has deleted the transfer pricing addition arising from TPO’s identical determination of ALP. The facts of the impugned are the same accordingly the findings of the said decision ought to apply *mutatis-mutandis* to the impugned assessment years.

11. The ld AR also submitted that the scientific CUP analysis done by the assessee ought to be upheld, instead of the ad-hoc nil determination of ALP by the

TPO. The summary of the economic analysis undertaken by the assessee in AY 2017-18 is as under:

Particulars	AY 2017-18
FAR and benchmarking discussion in TPSR	PB Pg. 104
No. of Comparable instances	4 PB Pg.118 to 123
Nature of services	Various advisories, management advisory, strategic planning, business administration, marketing etc
Mean	5.75% PB Pg. 119
Payment by Ld AR	1% PB Pg. 107
Conclusion	At ALP

12. The Ld.DR, on the other hand submitted that the assessee has failed to substantiate that the services are indeed rendered, what benefit is derived and what is the need for availing the services from AE instead of locally etc. The ld DR further submitted that the evidences submitted by the assessee are only screenshots from the software and are inadequate. The ld DR also argued that what is the overall cost incurred by the AE for the services is not provided in order to understand that the amount paid is reasonable as compared to uncontrolled transactions. With regard to the contention that the TPO has not done any bench marking, the ld DR submitted that the TPO has adopted “other Method” for bench marking and had determined the ALP at NIL. The ld DR placed reliance on the decision of the Hon’ ble Delhi High Court in the case of Akzonobel India (P) Ltd vs ACIT (2022) 145 taxmann.com 468 (Delhi) to submit that when the assessee fails to furnish evidences to demonstrate that the services are rendered the TPO is justified in determining the ALP at NIL.

13. The Id AR in rebuttal submitted that the assessee has done a proper bench marking using CUP method and has chosen external comparables having agreements for intergroup services and accordingly concluded that the price paid by the assessee is within arms length. The Id AR further submitted that the price paid is not based on cost allocation considering the complexity and the size of the parent company, the price is determined as a percentage of the turnover, since the benefit derived by the assessee from the inter group services are directly linked to the turnover. With regard to the determination of ALP at NIL the Id AR argued that while applying the “other method” the TPO should have chosen something uncontrolled which he has not done in the present case and therefore determination of ALP at NIL is not correct. The Id AR drew our attention to the various documentary evidences submitted as part of paper book to submit that the assessee has discharged the onus by providing the necessary evidences for having received the services and therefore the decision of the Hon’ ble Delhi High relied on by the Id DR is not applicable in assessee’ s case.

14. We heard the parties and perused the material on record. We notice that the coordinate bench of the Tribunal has been consistently holding the impugned issue in favour of the assessee. The coordinate bench in assessee’ s own case (supra) while considering the issue of payment of inter group services has held that –

16.It has been further submitted that the Tribunal in assessee’s own case for A.Y.2012-13 and 2013-14 have decided this issue in favour of the assessee. The relevant observation of the Tribunal reads as under:-

“30. We have considered rival submissions and perused the material on record. Undisputedly, the assessee has benchmarked the payment of royalty under central service agreement by applying CUP method. Whereas, the Transfer Pricing Officer has determined the arm's length price of the royalty payment at nil on purely conjecture and surmises without following any prescribed method.

In fact, the observations of the Transfer Pricing Officer on the issue are very cryptic and non-speaking. Therefore, simply for the reason that the determination of arm's length price by the Transfer Pricing Officer is not in accordance with the statutory provisions, the adjustment made deserves to be deleted. In any case of the matter, it is noticed by us that under the very same agreement, the AE is paid royalty by Hindustan Unilever Ltd. for domestic sales and by the assessee in respect of export sales. While examining the royalty payment in case of Hindustan Unilever Ltd. in assessment year 2013-14, the Transfer Pricing Officer has accepted royalty paid to the AE to be at arm's length. Similarly, in the order passed under section 92CA(3) of the Act in respect of AE, the Transfer Pricing Officer has accepted the royalty payment to be at arm's length. That being the case, the arm's length price of royalty payment at the hands of the assessee cannot be determined at nil. In any case of the matter, it is not disputed that the assessee is remunerated by the AE on cost plus mark-up basis. That being the case, royalty paid to the AE forms part of the cost base of the assessee on which it has charged mark-up @ 9%. In the aforesaid circumstances, if the payment of royalty to the AE is disallowed by determining the arm's length price at nil, then logically the income of the assessee also should be reduced. This is the view expressed by the Co-ordinate Bench in Mercer Consulting Pvt. Ltd. (supra). Thus, considering the overall facts and circumstances of the case and keeping in view the ratio laid down in the decisions cited before us, we are of the view that the adjustment made by determining the arm's length price of royalty payment at nil deserves to be deleted. Accordingly, we do so. Grounds are allowed."

17. Thus, in sum and substance, the observation of the Tribunal is summarized as under:-

- *The Assessee had benchmarked this transaction using CUP method, whereas the TPO has determined the ALP as Nil on purely conjectures and surmises without following any prescribed method*
- *Under the very same agreement, Hindustan Unilever Ltd. pays royalty on domestic sales and the Assessee pays for export sales. In HUL's case for AY 2013-14, the TPO had accepted the payment to be at ALP.*
- *Even in the case of Unilever Plc, the TPO had accepted the transaction to be at ALP for AY 2013-14*
- *The Assessee is remunerated by the AE on cost-plus and the royalty paid to the AE forms part of the cost base of the Assessee on which it has charged mark-up. In such a case, disallowance of royalty would reduce the income of the Assessee, which is not given the overall facts and circumstances, the Tribunal deleted the adjustment.*

18. *After considering the facts and material on record and the relevant finding given in the impugned order as well as the order of the Tribunal in earlier years, we find*

that before the authorities below, the assessee has given all the detailed submission and analysis not only demonstrating the rendition of central services but also commensurate benefits derived from such services to the assessee. This is evident from the details discussed above has called upon by us during the course of hearing. Accordingly, it cannot be held that either there was no rendition or no benefit as observed by the ld. TPO. Apart from that the CUP analysis done by the assessee by taking four comparables in both the assessment years in providing advisories, management advisory, strategic planning, business administration services, marketing plan, protocols, procedures, etc., wherein mean margin determined was 2.75% in A.Y.2015-16 and 5.75% in A.Y.2016-17; whereas the assessee has made payment at 0.50% in A.Y.2015-16 and 0.75% in 2016-17. Thus, the payment made by the assessee for Central services are at ALP and the adjustments made by the ld. TPO is deleted.

15. For the year under consideration, on perusal of records, we notice that the assessee has submitted evidences not only demonstrating the rendition of central services but also commensurate benefits derived from such services to the assessee. Further the assessee has done the bench marking analysis similar to AY 2015-16 and 2016-17 for the year under consideration also and therefore the impugned issue is squarely covered by the above decision of the coordinate bench and therefore respectfully following the same we direct the AO/TPO to delete the addition made towards inter group services.

16. Disallowance u/s 14A (Grounds 8 & 9)

16.1 The assessing officer noticed from the financial of the assessee that the assessee had made substantial investment where from the income shall not form part of the total income for the year. The total investment in such assets at the beginning of the year was Rs.9,98,138 Lakh and at the end of year was Rs. 26,91,746/-. Beside that the assessee had received exempt income in the nature of dividend amounting to Rs.3,05,76,650/- The assessing office also noticed that the assessee has determined the disallowance to be made u/s 14A r.w. Rule 8D on

account of expenses related to such investment the income from which is not includible in the total income at Rs.66,150/-. The assessing officer was of the view that the said disallowance was not in conformity with the method provided in rule 8D and called on the assessee to provide the requisite details and basis of the calculation of disallowance. The assessee has vide its submission dated 22.04.2021 submitted that it has computed disallowance u/s14A on the basis of estimated time spent by treasury team on investment activities income which is exempt. Further, pursuance to the show cause notice assessee has recomputed the disallowance u/s14A in accordance in accordance with method provided in rule 8D and accordingly on such basis the average investment is Rs.49,02,45,834/- and 1% thereon is Rs.49,02,458/- is disallowed by the assessee.

16.2 The Assessing Officer, however, did not accept the contention of the assessee. The AO observed that

“7.3 It is seen that the assessee has suo-moto disallowed an amount of Rs. 66.150/- under u/s 14A of the Act in respect of Expenditure incurred in relation to Income not includible in total income in A.Y 2017-18 at the time of filing income tax return. In this connection, it is submitted that the expenses disallowable u/s 14A of the Act do not limit only to the proportionate salaries of one or two persons. There is a larger environment consisting of Board Directors, senior officials, maintenance costs to keeping these people operational and a host of other indirect expenses. Further during the scrutiny assessment the assessee has re-computed disallowance u/s 14A and accordingly on the basis average investment is Rs.49,02,45,834/- and 1% thereon is Rs.49,02,458/- is disallowed. In this regard it is seen that the annual average of monthly average of the opening and closing investments has been computed only based on investment wise monthly summery for four month instead of twelfth month.

7,4 Furthermore, the assessee state that for the purpose of computing monthly average of investment for Rule 8D, have been ignored and investment like Growth Scheme of Liquid Funds, Hindustan Unilever Foundation and Pond Exports Limited are not capable of yielding exempt income. However, the said contention of the assessee is not acceptable as the Act and relevant rules does not provide for such selective exclusion and what has to be considered is the investment wherein income

received or receivable including in future is not includible in the total income. The Hon'ble Supreme Court had in the case of Maxopp Investment asserted that whether dividend income is earned or not is immaterial for the attracting of the provisions of Section 14A. Moreover, the CBDT Circular No. 5/2014 dated 11.12.2014 provides a clarification in this regard that the provisions of Rule 8D and Section 14A are applicable even when no exempt income is received.

7.5 In view of the said facts it is held that the contention of the assessee is not tenable and the disallowance of expenses related to the activity from which the income shall not form part of the total income is made as per the provisions of Rule 8D of the Income Tax Rules by considering the average investment wherein the income shall be not includible in the total income irrespective whether it is earned during the year or not. The disallowance is to be made as per Rule 8D(2)(ii) at 1% of the annual average of monthly average of the opening and closing investments, income from which shall not form part of the total income. In absence of detailed summary of investment, the annual average of monthly average of the opening and closing investments have been computed on the basis of financial statement provided by the assessee vide submission dated 16.03.2013. Accordingly annual average of monthly average of the opening and closing investments comes to 184,49,42,324/-(99,81,38,451+2,69,17,46,197/2) and 1% thereto is Rs.1,84,49,423/- which is accordingly disallowable out of the expenses claimed for the year as related to the activity income from which is exempt from tax. However, the assessee has on its own disallowed an amount of Rs.66,150/- on such account and accordingly the balance of Rs.1,83,83,273/-(1,84,49,423-66,150) is disallowed.”

16.3 The ld. DRP upheld the ld. AO's action.

16.4 The Ld AR submitted that the assessee's *suo-moto* disallowance is appropriate and scientific. The AO has not recorded any cogent satisfaction for rejecting the said calculation. The AO has proceeded on conjectures and surmises by observing that “*there is a large environment consisting of Board of Directors, senior officials, maintenance costs to keeping these People operational and a host of other indirect expenses*”. Both AO and the Hon'ble DRP failed to appreciate that the treasury team of the Assessee was capable and authorized(**AY 2017-18 PB Pg. 502**) to carry out the investment activities and the proportionate cost was already disallowed(**AY 2017-18 PB Pg. 475**). No specific defects were found by

either of the authorities in the said work. It is further submitted that the AO has proceeded to invoke Rule 8D mechanically, without any cogent satisfaction to reject the Ld AR's *suo-moto* disallowance, which manifests from the facts that:

- The AO has not applied his mind at all, despite submission from the Ld AR on the aspect that investments that yielded taxable capital gains ought to be removed from the calculation.
- The AO has not applied the amended Rule 8D(2)(ii), which required the calculation of “annual average of the monthly average” and instead had computed the disallowance based on an unamended provision wherein average investment is calculated based on “*the first day and last day of the previous year*”.

16.5 Accordingly, the Ld AR prayed that the disallowance made by the AO and upheld by the DRP ought to be deleted following the Hon'ble Tribunal's decision for AY 2015-16 and AY 2016-17 (*LPB Pg. 71 to 72, Para 23*).

16.6 We notice that the similar issue has been considered and decided by the coordinate bench in assessee's own case (supra) in A.Ys 2015-16 & 2016-17 where it is held that:-

23. After considering the aforesaid submissions, we are in tandem with the contentions of the ld. Counsel, because in so far as investment made in A.Y.2015-16 is concerned, these are mostly growth options of UTI mutual funds which does not yield any dividend income but are taxable as capital gains, hence, the same cannot be taken up for computing the disallowance under section 14A. If the average investment of Rs.0.29 Crores is taken into consideration, then disallowance would work out under Rule 8D(2)(iii) would be only Rs.1.45 lakhs which is much less than the suo-moto disallowance made by the assessee. Similarly, in A.Y.2016-17 also the investment in Kotak Mahindra Mutual Fund-Direct Growth and Reliance Mutual Fund-Direct Plan Grown which yields taxable income and therefore, same cannot be taken as part of computation for the purpose of disallowance. Once, these are excluded from the disallowance, then according to Rule 8D(2)(iii), the disallowance in A.Y.2016-17 would be Rs.1.45 lakhs. In any case, the ld. AO has mechanically applied Rule 8D without having recorded his satisfaction or examining the nature

of investments whether they have yielded any exempt income or not, thus, such disallowance made by the ld. AO are to be deleted. Accordingly, these grounds are allowed.

16.7 For the year under consideration also the assessee has investments the details of which has already been furnished before the AO (page 472 to 479 of paper book). Further it is noticed that that AO has applied Rule 8D without having recorded his satisfaction or examining the nature of investments whether they have yielded any exempt income or not. Therefore respectfully following the above decision of the coordinate bench in assessee ' s own case we delete the disallowance made by the assessing officer.

17. Disallowance of ESOP expenditure (Grounds 10 to 13)

17.1 The assessing officer during the course of assessment noticed that the assessee has debited a sum of Rs.147.50 lakhs towards benefit provided to employees of the company in respect of “Employees Share Option Scheme (ESOP)” The assessee made a detailed submission before the assessing officer explaining the nature of the ESOP and the reasons why the same is allowable u/s.37(1). However the assessing officer did not accept the contentions of the assessee by stating that the ESOP expenses has not crystallised and that the same is capital in nature. Accordingly the AO disallowed the ESOP expenditure. The DRP upheld the disallowance.

17.2 We heard the parties. We notice that the issue is covered by the decision of the coordinate bench in assessee ' s own case for AY 2015-16 & 206-17 where it is held that –

29. This issue again is covered by the decision of the Tribunal in the case of Unilever Industries Pvt. Ltd. *supra* where the Tribunal has followed the decision of the Hon'ble Karnataka High Court in the case of M/s. Biocon Ltd, the relevant observation of the Tribunal reads as under:-

10. The Ld. AR has made elaborate submissions on the ESOP scheme & expenditure and provisions of law on the allowability of claim. We found that the Honble High Court of Karnataka in the case of CIT(LTU) VS M/S Biocon Ltd in ITA.No.653 of 2013 dated 11-11- 2020 has observed as under:

9. In the instant case, the ESOPs vest in an employee over a period of four years i.e., at the rate of 25%, which means at the end of first year, the employee has a definite right to 25% of the shares and the assessee is bound to allow the vesting of 25% of the options. It is well settled in law that if a business liability has arisen in the accounting year, the same is permissible as deduction, even though, liability may have to quantify and discharged at a future date. On exercise of option by an employee, the actual amount of benefit has to be determined is only a quantification of liability, which takes place at a future date. The tribunal has therefore, rightly placed reliance on decisions of the Supreme Court in Bharat Movers *supra* and Rotork Controls India P. Ltd., *supra* and has recorded a finding that discount on issue of ESOPS is not a contingent liability but is an ascertained liability.

10. From perusal of Section 37(1), which has been referred to *supra*, it is evident that an assessee is entitled to claim deduction under the aforesaid provision if the expenditure has been incurred. The expression 'expenditure' will also include a loss and therefore, Issuance of shares at a discount where the assessee absorbs the difference between the price at which it is issued and the market value of the shares would also be expenditure incurred for the purposes of Section 37(1) of the Act. The primary object of the aforesaid exercise is securing consistent services of the employees and not to waste capital but to earn profits by therefore, the same cannot be construed as short receipt of capital. The tribunal therefore, in paragraph 9.2.7 and 9.2.8 has rightly held that incurring of the expenditure by the assessee entitles him for deduction under Section 37(1) of the Act subject to fulfillment of the condition.

11. The deduction of discount on ESOP over the vesting period is in accordance with the accounting in the books of accounts, which has been prepared in accordance with Securities And Exchange Board of India

(Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999.

12. *So far as reliance place by the revenue in the case of CIT VS. INFOSYS TECHNOLOGIES LTD. is concerned, it is noteworthy that in the aforesaid decision, the Supreme Court was dealing with a proceeding under Section 201 of the Act for non deduction of tax at source and it was held that there was no cash inflow to the employees. The aforesaid decision is of no assistance to decide the issue of allowability of expenses in the hands of the employer. It is also pertinent to mention here that in the decision rendered by the Supreme Court in the aforesaid case, the Assessment Year in question was 1997-98 to 1999-2000 and at that time, the Act did not contain any specific provisions to tax the benefits on ESOPs. Section 17(2)(ita) was inserted by Finance Act, 1999 with effect from 01.04.2000. Therefore, it is evident that law recognizes a real benefit in the hands of the employees. For the aforementioned reasons, the decision rendered in the case of Infosys Technologies is of no assistance to the revenue. The decisions relied upon by the revenue in Gajapathy Naidu, Morvi Industries and Keshav Mills Ltd. supra support the case of assessee as the assessee has incurred a definite legal liability and on following the mercantile system of accounting, the discount on ESOPS has rightly been debited as expenditure in the books of accounts. We are in respectful agreement with the view taken in PVP Ventures Ltd. And Lemon Tree Hotels Ltd. Supra.*

13. *It is also pertinent to mention here that for Assessment Year 2009-10 onwards the Assessing Officer has permitted the deduction of ESOP expenses and in view of law laid down by Supreme Court in Radhasoami Satsang vs. CIT. (1992) 193 ITR 321 (SC), the revenue cannot be permitted to take a different stand with regard to the Assessment Year in question*

In view of preceding analysis, the substantial questions of law framed by a bench of this court are answered against the revenue and in favour of the assessee. In the result, we do not find any merit in this appeal, the same fails and is hereby dismissed.

11. *We find the facts of the present case are similar respect of claim of ESOP Expenses and we follow ratio of judicial decision and direct the assessing officer to delete the addition and allow the grounds of appeal in favour of the assessee.*

32. *Accordingly, following the aforesaid decision in assessee's own case, this addition stands deleted.*

17.3 The facts being identical for the year under consideration, respectfully following the above decision we hold that the addition made by the AO towards ESOP expenses be deleted.

18. Excess Levy of interest u/s.234B and D (Ground No.14)

18.1 In this regard we direct the assessing officer to consider the facts afresh and rectify the errors in the calculation interest u/s.234B and 234D after giving a reasonable opportunity of being heard.

19. Ground 1 is general and Ground No.15 is consequential and these grounds do not warrant a separate adjudication.

20. The assessee also raised a legal issue through Ground No.2 with respect to the assessment order being issued without Department Identification Number (DIN). The ld AR during the course of hearing submitted that if the issues are considered on merits and held in favour of the assessee the ground no.1 will not be pressed. In view of our decision as given in this order, the legal issue contended has become academic and accordingly left open.

I.T.A. No.2107/Mum/2022 for A.Y. 2018-19

21. Ground No.1 is general and Ground No.8 is consequential and these grounds do not warrant a separate adjudication.

22. Through Ground No.2, the assessee is contending the TP adjustment made towards Central Services. For the year under consideration the Id AR and Ld DR made similar submissions. We have in the earlier part of this order, have considered the same issued and have held that the TP adjustment be deleted. The facts for AY 2018-19 being identical, we hold that the TP adjustment made towards central services for this year also be deleted.

23. Ground No.7 pertains to excess levy of interest u/s.234B. In this regard we direct the assessing officer to consider the calculation of interest afresh in accordance with law and rectify the errors in the computation of interest.

24. In the result, appeal of the assessee for AY 2017-18 and 2018-19 are allowed.

Order pronounced in the open court on 11/05/2023.

Sd/-

sd/-

(AMIT SHUKLA)	(PADMAVATHY S)
JUDICIAL MEMBER	ACCOUNTANT MEMBER

Mumbai, Dt : 11th May, 2023

Pavanan

प्रतिलिपि अग्रेषितCopy of the Order forwarded to :

1. अपीलार्थी/The Assessee ,
2. प्रतिवादी/ The Respondent.
3. आयकर आयुक्त CIT
4. विभागीय प्रतिनिधि, आय.अपी.अधि., मुंबई/DR, ITAT,
Mumbai
6. गार्ड फाइल/Guard file.

BY ORDER,

//True Copy//

Asstt. Registrar / Senior Private Secretary
ITAT, Mumbai