

IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH "A" NEW DELHI
BEFORE SHRI R.P. TOLANI AND SHRI SHAMIM YAHYA

ITA No. 2302/Del/2010

Asstt. Yrs: 2004-05

Abhiram Seth
C/0 Gupra Ranjan K & Co. CAs
208, Ansal's Laxmi Deep,
Laxmi Nagar Distt. Centre,
Delhi-110092.
PAN/GIR NO. AASPS0522R

Vs. JCIT Range-47,
New Delhi.

(Appellant)

(Respondent)

Appellant by : Dr. Rakesh Gupta; Sh. Ashwani Taneja &
Ms. Rani Kiyala Advocates
Respondent by: Dr. V.R.R. Kumar Sr. DR

ORDER

PER R.P. TOLANI, J.M :

This is assessee's appeal against CIT(A)'s order dated 17-3-2010 relating to A.Y. 2004-05. Following grounds are raised:

"1. That having regard to the facts and circumstances of the case Ld. CIT(A) has erred in law and on facts in confirming the action of Ld. AO in reopening of the case u/s 147 as per law and the reason recorded were valid in the eyes of law and has further erred in not quashing the assessment order on the ground that order passed u/s 147 red with section 143(3) was framed without complying with the mandatory conditions as prescribed under section 147 to 151 of the Income Tax Act, 1961.

2. That in any case and in any view of the matter, action of Ld. CIT(A) in confirming the action of Ld. AO in reopening the

impugned assessment is bad in law and against the facts and circumstances of the case.

3. That having regard to the facts and circumstances of the case, Ld. CIT(A) has erred in law and on facts in confirming the action of Ld. AO in treating the long term capital gain as shown by the assessee in the return as “short term capital gain” and accordingly made the addition.

4. That in any case and in any view of the matter action of Ld. CIT(A) in not reversing the action of Ld. AO in making the impugned addition and framing the impugned assessment order is bad in law and against the facts and circumstances of the case, void ab initio, beyond jurisdiction, by recording incorrect facts and findings and the same is not sustainable on various legal and factual grounds.

5. That having regard to the facts and circumstances of the case, Ld. CIT(A) has erred in law and on facts in not reversing the action of Ld. AO in charging interest u/s 234B of the Income Tax Act, 1961.”

6. That the appellant craves the leave to add, modify, amend or delete any of the grounds of appeal at the time of hearing and all the above grounds as without prejudice to each other.

2. At the time of hearing, ground nos. 1 & 2 regarding reopening of assessment were not pressed, accordingly both the grounds stand rejected accordingly.

3. In ground nos. 3 the assessee has challenged the order of CIT(A) in confirming the action of AO in treating the capital gains on account of ESOPs shares as “short term capital gains” as against “long term capital gains” claimed by the assessee.

4. Brief facts are that assessee individual, was an employee of M/s Pepsico India Holdings (P) Ltd. in executive position. The said M/s PepsiCo India Holdings (P) Ltd. (PIHL) is a part of Pepsico Inc. Consequent to this employment with PIHL, assessee was granted valuable rights in shares of Pepsico Inc ESOP stock held with Barry group of Merrill Lynch USA. The rights were conferred on various dates i.e. 27-7-1995; 25-7-1996; 23-9-1999 & 27-1-2000. The assessee sold these shares on 25-2-2004 relevant to F.Y. 2003-04 i.e. A.Y. 2004-05. Consequent to the sales, assessee claimed the gains as long term capital gains, relevant details are as under:

Option date	Nos	Cost \$	Sale/ Executive Date	Sale Rate\$	Gain \$	INR (Rs.)
27-7-1995	2783	21.54	25-02-2004	52.00	84701	3853896
25-7-1996	2514	29.84	25-2-2004	52.00	95593	4349482
23-9-1999	5056	32.25	25-2-2004	52.00	55560	2527980
27-1-2000	4963	34.00	25-2-2004	52.00	89076	4052958
						14966315

27-7-1995	2783	21.54	59946
25-7-1996	2514	29.84	75018
23-9-1999	5056	32.25	163056
27-01-2000	4963	34.00	168742

- Sale of Shares
(valuable right) on 25-2-2004 15316 USD \$ 796432
- Cost of shares sold (as per chart above) USD \$ 466742
- Gain USD \$ 328930

- Gain converted @ 45.50 per USD (\$) INR Rs. 14966315
The gains were claimed as Long term capital gains as the assessee held the rights for a period of more than three years by the assessee.

Besides, assessee claimed deduction u/s 54F against these gains by way of investment in residential house.

4.1. The return was accepted u/s 143(1)(a). Thereafter notice u/s 147 was issued on 10-2-2009 as AO was of the view that the shares were never transferred to the assessee. The shares were actually held by a trustee i.e. Barry Group at USA. The assessee actually received the differential amount between gross sale consideration and the cost price. In reassessment AO held that the issue date or date of grant was immaterial in this case. The shares were allotted to the assessee and sold by him on the same date, therefore, they were liable to tax as short term capital gains. Since they were held to be short term capital gains, no further deduction u/s 54F was allowed to the assessee.

4.2. Aggrieved, assessee preferred first appeal to the CIT(A), before whom it was submitted as under:

- (i) The reliance placed by the AO on the cases, Infosys Technologies Ltd. Vs. CIT, Garric D'Silv Vs. JCIT (2006) 105 TJ 445 (T del T) and Gridhar Krishan Vs. ACIT (2008) 117 TTJ (Bang) 965 was misplaced because facts of appellant's case are materially different.

- (ii) The ESOP scheme and especially the terms stock and option has not been correctly appreciated by the AO
- (iii) The AO has not appreciated that what was transferred was valuable right and not tangible shares because distinctive shares were not allotted to the assessee.
- (iv) The capital asset i.e. a valuable right to exercise an option to sell 'stock' was a long term capital asset because it was created on the date of acceptance i.e. 27-7-1995 and other dates.
- (v) The calculation of capital gains made by the AO was based upon sale and purchase dates, which is exercise date and sale date. Difference between sale and exercise date would not arise as the sale price and purchase (cost. Price of Pepsico Inc share would be same on both dates being instantaneously same). This cannot result in any gain or loss therefore question of taxation of capital gain would not arise.
- (vi) The AO has on the one hand accepted the price paid by the assessee on the dates of acceptances of offer as the cost but had not accepted them to be dates as the dates of respective of acquisitions.

4.3. CIT(A), however, upheld the order of AO on this issue by following observation:

“I have given a careful consideration to the above points made by the appellant and I am also aware that there are conflicting decisions of the ITAT on this issue, e.g.

1. 2009-TIOL-573-Mum Mr. Bomi S Billimoria vs. AC Mumbai
2. ACIT vs. Dr. Dhurjati Gupta ITAT Hyderabad B Bench (2010) 33 DTR (Hyd) (Trib) 287
3. ACIT Vs. Shri Jaswinder Singh Ahuja ITA no. 185 & 186 Del/2009

However, as far as the present appeal is concerned, this issue is decided against the assessee by the ITAT in the case of ACIT Vs. Shri Jaswinder Singh Ahuja in ITA no. 185 & 186.Del/2009 where it has been held as under:-

“We have heard the rival submissions and have gone through the material available and the judgments cited by both sides. We find that the issue in the present case is squarely covered by the Tribunal decision rendered in the case of Alok Kumar (supra). In that case also, the employer company was the same company i.e. Cadence Design Systems (India) Pvt. Ltd. and the ESOP shares were of the same USA company. In that case, it was held by the Tribunal that when the option is exercised by the employee that date will be the date of acquisition of shares for the purpose of determining whether the shares were long term or short term capital asset. After holding so matter was restored back by the Tribunal to the files of the assessing officer in that case for a fresh decision after examining the date of acquisition. In the present case the date of exercising of option is not in dispute as the option was exercised in the present case on the date of sale of shares and hence as per Tribunal decision, the capital gain in question is short term capital gain only. It is the claim of the assessee that this Tribunal decision put in by RBI for not making payment for

purchase of shares from India. We are of the considered opinion that for this reason alone, it cannot be said that the shares were acquired by the assessee before the date of exercise of option. After going through the ESOP scheme in the present case, we find that the assessee was given an option for purchase of shares at a fixed price at any point of time within 10 years but until and unless the assessee exercises his option, the assessee does not become the owner of shares because if the assessee becomes the owner of anything he is entitled for gain on that account and he is liable to suffer the loss for the same. But in the present case, if the market price of shares is more than the offer price, the assessee is entitled for the gain but if the market price of the shares falls below the offer price, the assessee is not bound to suffer such loss on those shares because in that situation the assessee will not simply exercise his option and as a result, the assessee will not suffer any loss. This goes to show that the assessee was not having any ownership of the shares till he exercised the option. Unless the assessee becomes the owner being liable for loss also on price fall, it cannot be said that shares are acquired and this period prior to acquisition date cannot be considered.”

Therefore, respectfully following the above decision of the jurisdictional ITAT, I hold that the short term capital gains had arisen on account of sale of shares of a foreign company and since no STT had been paid, the entire STCG of Rs. 1,49,66,315/- is liable to normal rates of tax. The addition of Rs. 1,49,66,315/- made by the AO is therefore confirmed.”

Aggrieved, assessee is before us.

5. Learned counsel for the assessee contends as under:

(i) In the case of Pepsico ESOP the shares are held in stock by an appointed trustee e.g. Barry group of Merrill Lynch, who hold them in stock. This group is official representative of the various employees of Pepsico Inc all over the world and as a group policy, holds shares with them in stock on their behalf and the employer. This arrangement suits both employee and employer. The employer would not like to transfer shares directly to employee unless they performs as per expectation. The employees also would not like to totally trust the employer till the time of commitment date arrives. Hence the employees are allowed to become the owners (by way their written agreement also known as filling up and signing agreement for eligible shares ‘Options’) with the company and the official ESOP trustees viz Barry group of Merrill Lynch. Reasons for separate agreements and signing of these agreements on various dates was to ensure firm commitments on these dates from employees and also ensure equity of purchase price of share amongst these employees on respective date of their eligibility at prevailing market rates.

(ii) Appellant entered into various agreements and accepted following offers and prices for ESOP stock, which was commensurate to US markets:

Date of offer	Nos.	Issue price
27-7-1995	2783	21.54
25-7-1996	2514	29.84
23-9-1999	5056	32.25
27-01-2000	4963	34.00

(iii) These shares as per scheme were offered on the dates mentioned above and were encashable in a period of ten years after elapse of

initial period of three years from the date of acceptance of ESOP stock offer.

- (iv) All employees were given the option on the date of their eligibility to sign and own it on the date they are eligible and keep the same till they reach their optimum time in the eyes of employee to sell/liquidate. It is important to note that shares are never issued by Pepsico Inc in the name of the employee but in the name of designated trust or acquired by this trust from market and stored in their stock also called “capital stock” for the employees of worldwide Pepsico. Thus, the employee became the owner of the stock on the day when he signed the agreement and could redeem or encash his rights(part of stock) any time after lock in period of three years. No transfer of shares took place from company to employee but were held by this trust Barry group in its stock on behalf of the employee. They allocated and sold them as and when asked for by assessee. The Barry group of Merrill Lynch acted as the custodian of these shares for and on behalf of the Pepsico Inc and employees world wide.
- (v) After a lock in period of three years the shares would be transferable i.e. employee can sell them. This was done to ensure minimum retention of employee for a period of three years so that he would not leave before that period.
- (vi) The assessee acquired the rights in indistinctive shares as mentioned above, at the prevailing market price only.
- (vii) The only benefit by ESOP scheme was that the consideration for purchase was deferred i.e. assessee could pay the purchase price when he opts to sell them. This could constitute an important

incentive. Thus it was only postponement of payment of purchase price.

- (viii) After option became exercisable, the Trustees had the sole discretion and without the assessee's consent could sale such option and pay the difference between the option price and the prevalent fair market value of the shares by giving written notice called as the "Buy out notice". Payments of such buy out amounts pursuant to this provision was to be effected by Pepsico and could be paid in cash, in shares of capital stock or partly in cash and partly in capital stock, as the Trust deemed advisable.
- (ix) Clause no. 4 of Pepsico ESOP agreement stipulates availability of a valuable right in ESOP stock (existing on the date of signing of options) with the appellant as it lays down transferability in case of death etc. from the employee to his legal heirs i.e. something valuable exists.
- (x) Clause 9 recognizes existence of this valuable right i.e. buy out option (what can be bought and sold is applicant/ appellant's right to shares in ESOP stock). Thus Pepsico recognized existence of valuable rights of holding of these undistinctive shares in the hands of the employee.

5.1. Learned counsel contends that CIT(A) has not disputed these facts on page 44 of his order has appreciated only the conflicting decisions of the ITAT on this issue. This clearly indicates that there are cases which are in favour of the assessee also. CIT(A) ignoring the favourable decision has

preferred to rely on the case of ACIT Vs. Shri Jaswinder Singh Ahuja (ITA no. 185 & 186.Del/09), whose facts are clearly distinguishable.

5.2. Learned counsel then relied on ITAT judgment in the case of ACIT Vs. Dr. Dhurjati Gupta (2010) 127 TTJ (Hyd) 356. It is pleaded that in the similar facts and circumstances Hyderabad Bench of the ITAT, after considering various ITAT and High Courts judgments in a group of cases, held as under:

“With regard to the question as to the nature of the capital gains, viz., long-term or short-term capital gains, we are of the considered opinion that it is the date of grant of the stock option in favour of the assessee that is material for determining the period of holding the asset in question, and not the date on which the option was exercised and stock option were converted into shares. As already noted above, Mumbai Benches of this Tribunal in the cases cited above, specifically considered this issue also and decided the same in favour of the assessee following the decisions of the Bombay High Court in CIT vs. Sterling Investment Corporation Ltd. (1979) 12 CTR (Bom) 263; (1980) 123 ITR 441 (Bom) and CIT vs. Tata Services Ltd. (1979) 13 CTR (Bom) 227; (1980) 122 ITR 394.

At this juncture, we may also notice that there was a significant change in the position on account of amendment to cl. (ba) under s. 115wC(1) of the Act whereby, the date of liability for fringe benefit tax (FBT) on such concessions under ESOP scheme, has been shifted from the date of exercise of option by the employees to the date on which option vests on them. The nature of explanation was a clarificatory one. Option has been defined in the Explanation to this new clause to mean “a right but not an obligation granted to an employee to apply for the specified security or sweat equity shares at a predetermined price”. Vesting of such right would be date of liability for that

purpose. This Explanation also fortifies our view that date of vesting the options on the employee shall be the date of acquisition for the purpose of capital gain computation. In the case under consideration, there is no dispute regarding the date on which the ESOPs were vested on the assessee by WLC.

As for the decision of the Calcutta High Court in the case of Mrs. A. Ghosh Vs. CIT (supra), relied on by the learned Departmental Representative, it relates to conversion of debentures into equity shares and date of acquisition of shares in that context, as against holding of ESOPs by the assessee in the present case, date of acquisition of shares, in respect of which relates back to the date of grant of ESOPs and not exercise of option. Similarly, in the case of Dr. V.V. Mody (supra) before the Karnataka High Court, the issue relates to capital gains in relation to an immovable property held by the assessee in dual position both as tenant as well as landlord at the same time and in relation to the same property. Facts of that case are distinguishable and the ratio laid down therein has no application to the facts of the present case.

Further, sequence of events commencing from the grant of option to the sale of the shares, as seen from the copies of the option letters from WLC, acceptance letters by way of declaration of the assessee, approval letter from RBI and such other material placed on record in the paper book establish that the assessee becomes the owner of the shares pursuant to the acceptance of the ESOP from the WOC and subsequent sale of shares giving rise to long-term capital gains. Our considered view is that once the grant of option is conferred, such right becomes a right in the nature of the property. And such stock option grants given to the assessee by WLC represented such property which were valuable and inheritable and hence were capital asset. Our view is fortified by the decision of the Delhi Bench of the Punjab High Court in the case of Hari Bros. (P) Ltd. Vs. ITO (1964) 52 ITR 399 (Punj), wherein it was held that right to subscribe for shares of a company is also a capital assets. On exercising the option, the assessee gets shares, which is only conversion of one capital asset into another capital asset. It is evident from the details of the date of acquisition of such

right by the assessee, as submitted in the paper book, the shares were held by the assessee for a period more than twelve months and hence the resultant gains must be computed as long-term capital gains.”

5.3. It is pleaded that this case clinches the issue and unequivocally holds that ESOP account allotted to assessee at a market value when sold after a period of one year ought to be held as long term capital gains.

5.4. Adverting to the order of the ITAT in the case of Mr. Bomi S. Billimoria Vs. ACIT (2009) 124 TTJ (Mumbai) 960, learned counsel contends that this case lays down following propositions:

- (i) In case of cashless ESOPs the cost of acquisition was unascertainable and therefore relying on the ratio of decision of Hon’ble Supreme Court in the case of CIT Vs. B.C. Srinivasa Setty (1981) 128 ITR 294 (SC) it has been held that cost of acquisition being unascertainable, the long term capital gains cannot be computed. The fact remains that even in case of cashless ESOPs it has been held that it constituted a valuable right and was a capital asset and on transfer, liable to be treated short term or long term on the basis of holding period.
- (ii) It has been further held that if the revenue treats the date of acquisition and sale to be same in that case market value of acquisition will be same as sale price and resulting gain will be ‘nil’, thus giving rise to no capital gains.

5.5. The ITAT concluded the case of Bomi S. Billimoria (supra), as under:

“16. We have carefully considered the rival submissions and perused the record. As could be noticed from the stock option plan and the terms of RBI, no payment was made by the assessee nor exercised the right to purchase shares before 13th Aug., 1992 and thus, so far as the assessee is concerned, there is no cost of acquisition to the assessee in which event, by applying the decision of B.C. Srinivasa Setty (supra), the amount received is not liable to tax under the head “Income from capital gains”. Even if it is assumed that the market value of the share is not benefit given to the assessee, such benefit can be said to accrue to the assessee only on the date of exercise of the option. In the instant case, the date of exercise of option as well as the date of sale is same and thus there is no difference between the deemed cost of acquisition and the actual price realized by the assessee and thus the learned CIT(A) was not justified in directing the AO to bring to tax the amount of Rs. 5,44,925 as short-term capital gain. Under these circumstances we set aside the orders passed by the tax authorities and direct the AO to exclude the impugned amount from the computation of income.”

5.6. Learned counsel thus contends that in assessee’s case it is admitted that there was an ascertained value to the allotment of ESOPs as per prevalent US market. The price was thus definite and ascertainable; only non-payment of purchase consideration by assessee cannot deny the fact of acquisition of rights. The assessee has rightly offered the gains as long term capital gains. The ITAT Mumbai Bench in the case of Bomi S. Billimoria (supra) has held the cost of acquisition to be unascertainable as the ESOPs were allotted on the basis of a cashless scheme whereas in assessee’s case

there is a corresponding cost of undistinctive but ascertained quantity of shares allotted in 1995-96 to 1999-2000 as per the US market value. Therefore, the assessee is not raising the plea of unascertainable cost. Since the cost of acquisition is apparent and not disputed the gains are liable as long term capital gains.

5.7. If the logic adopted by lower authorities is taken, then the assessee's right to distinctive shares was acquired on the same day when it is sold, then there will be no capital gains as the right on such shares accrued on the same day and the cost will be same.

6. Learned DR is heard who supports the order of lower authorities.

7. We have heard rival submissions and gone through the entire material available on record. The facts have been narrated in details above. A perusal of the clauses of allotment clearly reveals that the particular numbers of shares were allotted to assessee in different years at different prices; only distinctive numbers were not allotted which has not been disputed by department. The apparent benefit to assessee out of ESOPs scheme was that it had not to pay the purchase price immediately at the time of allotment but the same was to be deducted at the time of sale or redemption of shares. Since there was an apparent fixed consideration of ESOPs shares, the right to allotment of particular quantity of shares accrued to the assessee

at relevant time. The benefit of deferment of purchase price cannot lead to an inference that no right accrued to assessee. The sales of such valuable rights after three years are liable to be taxed under the head “long term capital gains” and not ‘short term capital gains’. CIT(A) out of conflicting ITAT judgments has preferred to rely on only favourable to revenue i.e. Jaswinder Singh Ahuja (supra), overlooking others and without commenting about the relevant facts. It has not been dealt on that acquisition of valuable rights in a property amounts to a capital asset. In the case of Jaswinder Singh (supra), the shares were of the same company, whereas in this case there are group companies held through trustee and there were certain RBI guidelines about nonpayment of price of shares and the option being exercised by assessee on the date of sale of shares. There was no trustee whereas in assessee’s case there was a fixed price of allotment of right to fixed quantity of shares and the indistinctive shares were held by a trust on behalf of assessee. Non-allotment of distinctive number of shares by trust cannot be detrimental to the proposition that assessee’s valuable right of claiming shares was held in trust and stood sold by Pepsico. Therefore, there was a definite, valuable and transferable right which can be termed as a capital asset in favour of the assessee.

7.1. In our view, the assessee's claim of taxability of gains on the transfer of such rights under the head "long term capital gains" is justified and deserves to be accepted. If we accept AO's stand, then there will be no capital gain; if the date of allotment of share and sale thereof is the same, the price of purchase of shares cannot be the price paid for right which is not held as purchase, which becomes unascertainable. According to AO, the earlier right of allotment does not constitute a purchase of shares and thus leads to a presumptive situation. In that case, as rightly observed by the ITAT in the case of Bomi S. Billimoria (supra), the purchase price will be unascertainable. If we apply the case of Dhurjati Gupta (supra), then allotment constitutes new right of purchase and the price will be same as the sale consideration. In both situations there will be no taxability.

7.2. In our view, these propositions are of no avail insofar as we have held that the assessee acquired a valuable and transferable right on these shares as on the respective dates in 1995-96 to 1999-2000, as mentioned above. The cases of Bomi S. Billimoria (supra) and Dhurjati Gupta (supra), are squarely applicable in favour of assessee. The right of shares constitute capital assets and the gains should be taxed as "Long Term Capital Gains" as the holding period is more than 3 years. We reverse the orders of lower

authorities on this issue, treating the gains as short term capital gains. The ground is allowed.

8. Next issue raised in ground no. 5 is regarding charging of interest u/s 234B of the I.T. Act. The charging of interest u/s 234B is consequential in nature. The AO shall recalculate the interest u/s 234B, if any, while giving effect to appellate order.

9. Ground no. 6 is general in nature and requires no adjudication.

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

Order pronounced in open court on 30-09-2011.

Sd/-
(SHAMIM YAHYA)
ACCOUNTANT MEMBER
Dated: 30-09-2011.

Sd/-
(R.P. TOLANI)
JUDICIAL MEMBER

MP

Copy to :

1. Assessee
2. AO
3. CIT
4. CIT(A)
5. DR

