IN THE INCOME TAX APPELLATE TRIBUNAL, 'E' BENCH MUMBAI

BEFORE: SHRI AMIT SHUKLA, JUDICIAL MEMBER
&
SHRI GAGAN GOYAL, ACCOUNTANT MEMBER

ITA No.3468/Mum/2016
(**Assessment Year :2009-10**)

M/s. Tata Sons Limited 24, Bombay House Homi Mody Street Fort, Mumbai-400 001	Vs.	Commissioner of Income Tax-2, Mumbai 344, Aaykar Bhavan M.K.Road Mumbai – 400 020
PAN/GIR No.AAACT4060A		
(Appellant)	..	**(Respondent)**

Assessee by	Shri J.D. Mistri / Shri Rohit Adalji & Ms. Aastha Dhowan
Revenue by	Shri Ujjwalkumar Chavhan
Date of Hearing	**10/11/2023**
Date of Pronouncement	**23/01/2024**

आदेश / O R D E R

PER AMIT SHUKLA (J.M):

The aforesaid appeal has been filed by the assessee against order dated 28/03/2016 passed by ld. PCIT-2, Mumbai in his revisionary jurisdiction u/s.263 for the A.Y.2009-10.

2. In the grounds of appeal, assessee has raised the following grounds:-

1.Proceedings u/s.263 Bad in Law:

a) The Principal Commissioner of Income-tax 2 ('CIT') erred in disregarding the specific inquiry on the Computation of Capital Gains undertaken by the Assessing Officer during assessment proceedings, upon which the claim was allowed by the AO consciously, advisedly and upon application of mind.

b) The CIT further erred in treating the Assessment Order dated 9 May 2013 as erroneous and prejudicial to the interests of the Revenue, based upon a different opinion formed by him.

c) The CIT failed to confirm, though raised by the appellant, that the proceedings u/s 263 were not based on a suggestion from audit and hence the Order is bad in law and requires to be quashed.

2) <u>Computation of Income from Capital Gains</u>

a) The CIT erred in concluding that the Scheme of Arrangement and Reconstruction was not a case of Reduction of Capital.

b) The CIT erred in concluding that the computation mechanism under section 48 fails by holding that to compute capital gains there must be an element of consideration received or accruing to the assessee. The CIT erred in ignoring that the Supreme Court in CIT v D. P. Sandu Bros. Chembur P Ltd 273 ITR 1 has held that, for S 48 to apply, consideration should be capable of being determined.

3) Cost of Acquisition of remaining shares. The CIT erred in failing to note the provisions of S 55(2)(v)(b) and in not confirming that the cost of remaining shares would include the cost of the shares cancelled on Reduction."

2. The assessee has also raised an additional ground which is reproduced as under:-

"The Order passed under Section 263 of the Income Tax Act, 1961 (the Act) dated 28 March, 2016 by the Principal Commissioner of Income Tax -2 (PCIT) is bad-in-law and illegal and therefore, should be quashed, since having given an opportunity of being heard to the appellant, the PCIT ought not to have expressed any final opinion as regards the merits of the case, (as held by a Co-ordinate Bench of the Honourable Tribunal in the case of Ved

Prakash Contractors vs. CIT ITA No. 573/2015, dated 3/11/2015)."

3. The entire controversy involved in the present case is, *firstly*, whether the ld. AO was correct in allowing long term capital loss of Rs.20,46,97,54,090/- on account of reduction of capital; and *secondly*, whether ld. PCIT's order is correct in law and facts in cancelling the assessment order holding that ld. AO has committed a mistake in allowing set off of long term capital loss of Rs. 20,46,97,54,090/- in the computation of total income of the assessee company and to direct the ld. AO to disallow the long term capital loss after giving assessee an opportunity of being heard.

4. The brief facts qua the issue involved are that, as on 01/04/2008 the assessee was holder of 288,13,17,286 equity shares in Tata Tele-Services Company Ltd. (TTSL) acquired at various points of time. TTSL is an Indian company engaged in business of providing telecom services. In the assessment years prior to the assessment year in question, TTSL had incurred substantial losses in the course of its business which had resulted in a large part of the paid-up share capital of TTSL being utilized so as to finance / bear the said loss. In view of such losses the 'Scheme of Arrangement and Re-structuring' between TTSL and its shareholders was entered whereby as per the scheme:

(a) the paid-up equity share capital of TTSL was to be reduced by way of reduction of the number of equity shares of the company of Rs. 10/- each from 634,71,52,316 shares to 317,35,76,158 shares;

(b) the said reduction of paid-up equity share capital of 3173,57,61,580 was to be given effect to by reducing the said amount from the accumulated debit balance in the Profit & Loss Account and by reduction from Share Premium Account;

(c) the said reduction of capital was effected as part of the Scheme u/s. 100 to 103 of the Companies Act, 1956;

(d) the Scheme was to become effective on the happening of the events set out in para 7.2 of the Scheme. The Effective Date of the reduction of capital was 04-12- 2008;

(e) in terms of this particular Scheme, no consideration was payable to the shareholders in respect of the shares which were to be cancelled.

5. Thus, as a result, assessee's shareholding of 288,13,17,286 equity shares in TTSL was reduced to half, i.e., 144,06,58,643, that is, equity shares were cancelled as a result of reduction of capital pursuant to the scheme of arrangement u/s.100 and 391 of the then Companies Act, 1956. The said scheme was approved by the Hon'ble Delhi High Court vide judgment and order dated 07/11/2008 and this resulted in cancellation of *interalia* certain shares of TTLS as specified in the scheme. The scheme of arrangement and restructuring has been placed before us during the course of the hearing. The relevant portion of the said scheme duly approved by the Hon'ble High Court reads as under:-

4.1.2 The paid up equity share capital of TTSL be reduced by way of reduction in the number of equity shares of Rs 10/- each from 634,71,52,316 shares to 317,35,76,158 shares resulting in the total reduction of the paid up equity share capital of TTSL from. Rs. 6347,15,23,160/- comprising of 634,71,52,316 equity shares of Rs. 10 each to 317,35,76,158 equity shares of Rs. 10 each to Rs. 3173,57,61,580/-. However, due to the above reduction, when the shareholding of a shareholder holding odd number of shares results in fraction of a share, then it would be rounded off to lower multiple of one. Therefore, an amount Rs. 3173,57,61,580/- would be reduced from the accumulated debit balance in Profit & Loss Account and unabsorbed depreciation of TTSL from the amount remaining after the deduction mentioned in Clause 4.1.1 above in the following manner.

Amount available from extinguishment of Share Capital	*Rs. 3173,57,61,580/-*
Less: Write off against book losses	*Rs. 1586,78,80,790/-*
Less: Write off against unabsorbed depreciation	*Rs.1586,78,80,790/-*
Balance available	***NIL***

The said reduction of capital shall be effected as a part of this Scheme only in accordance with Sections 100-103 of the Act. As the same does not involve either diminution of liability in respect of unpaid share capital or payment to any shareholder of any paid up share capital, the provision of Section 101(2) shall not be applicable. However the order of the Hon'ble High Court of Judicature at New Delhi, sanctioning the Scheme shall be deemed to be an order under Section 102 of the Act confirming such reduction.

Thus, in view of the scheme, the paid up equity share capital of TTSL was reduced by way of reduction in the number of equity shares of Rs 10/- each from 634,71,52,316 shares to 317,35,76,158 shares, resulting in the total reduction of the paid up equity share capital of TTSL from Rs. 6347,15,23,160/- to Rs. 3173,57,61,580/-. Consequently the assessee's share was reduced to half.

6. In the return of income for the A.Y. 2009-10 filed on 30/09/2009, assessee had shown long term capital loss on reduction on the shares of TTSL. In the computation of income for capital gain, assessee had shown capital gains / losses arisen as a result of various transfer of capital assets held by it and one of the components of capital gains / loss was long term capital loss of Rs.2046,97,54,090/-. The computation of capital gains filed alongwith return of income was as under:-

Tata Sons Limited												
Assessment Year 2009-10												
Computation of Capital Gains - Long Term - Short Term												
Sr. No.	**Name of Company**	**Number of Shares**	**Date of Purchase**	**Cost per Share Rs.**	**Cost of Purchase Rs.**	**Indexed Cost Rs.**	**Date of Sale**	**Sale Proceeds Rs.**	**Gains / (Loss) Rs.**	**Gains / (Loss) Rs.**	**Gains / (Loss) Rs.**	**Gains / (Loss) Rs.**
	<u>Long Term Capital Gain:</u>								As per book	As per Indexed Cost	As per Book Cost	
									Exempt u/s.10(38)	Taxable @22.66%	Taxable @11.22%	
1	Tata Consultancy Services	2040500	Jun-00	1.55	3162775		Jun-08	1914871078	1911708303			
		10321324	Jun-00	1.55	15998052		Sep-08	6983819989			6967821937	
		40000	Jun-00	1.55	62000		Sep-08	27065600			27003600	
									1911708303		**6994825537**	**6994825537**
2	Tata Teleservices Co. Ltd	171500000	Apl: 02 Mar 03	10	1715000000	2232953020		0		2232953020		
	(Note 1)	525500000	Apl 03 Mar 04	10	5255000000	6605637149		0		-6605637149		
		419047593	Apl.04 Mar 05	10	4190475930	5080952065		0		-6080952065		
		238767977	Apt 05 Mar 06	15	3581519655	4194053198		0		4194053198		
		10000000	Apl.06 Mar 07	25.8	258000000	289317019		0		289317919		
		75843073	Apl.07-Mar 08	25.8	1956751283	2066840739		0		2066840730		
		1440658643				**20469753190**		0		-20489754090		20469754090
3	Tata Teleservices Co. Ltd	60600438	Dec-02	10	606004380	789025837	Mar-09	7035104847		6246079010		
		10000000	Dec-06	25.8	258000000	289317919	Mar-09	1160900000		871582081		
		70343073	Sep-07	25.8	1814851283	1916957254	Mar-09	8166127345		6249170091		
		1264361	Sep-07	25.8	32620514	34455788	Mar-09	146779668		112323881		
		142207872				**3029756798**		**16508911860**		**13479155063**		13479155063
	Short Term Capital Loss											
1	Indian Hotels Co. Ltd	55571216	May-08	100	5557121600		May-08	5026316459		-530805141		-530805141
2	Tata Power Co. Ltd.	10389000	Jul-07	58.71	609938190		Dec-08	0		-609938190		-609938190
	(Note 2)											
	Net Long Term Cap Gains/Loss								**1911708303**	**-6990599027**	**5854082206**	**-1136516821**

Note

1) The shareholding of the Company in Tata Teleservices Co. Ltd. (TTSL) aggregating to 144,06, 56,643 equity shares acquired over a period above, has been transferred within the meaning of Sec. 2(47) of the Income Tax Act, upon a reduction of Capital carried out by TTSL during the year. The Supreme Court. in 228/TR/103 and 236/TR/327 have held that a reduction of Capital constitutes transfer Accordingly, the capital gains have been computed in the mariner prescribed in Sec 48 following the Supreme Court decision in 273/ITR/1

2) The Company had subscribed subscribed 1,03,89,000 warrants issued by Tata Power Co. Ltd entitling it to acquire 1,03,89,000 shares @1351.63 per share. Since the payment for acquiring of the Tata Power Co. Ltd shares was not made by the Company upto 17/12/08, the warrants stood forfieted, resulting in extinguishment of rights therein. Reliance is placed on the Supreme Court decisions cited in Note 1

7. This computation of capital gain was filed before the ld. AO in response to his notice u/s. 142(1) dated 04/06/2011. It has been pointed out before us that during the course of assessment proceedings u/s. 143(3), AO has specifically raised this issue in connection with the assessee's claim for allowability of long term capital loss of Rs.2046.97 Crores. It has been stated that in

response to the specific query raised in the notices by the ld. AO assessee has given the details, the computation of income and working of its capital gain providing necessary details before the ld. AO and also how the claim of the assessee for long term capital losses is allowable in view of the decision of the **Hon'ble Supreme Court** in the case of **Kartikeya Sarabhai** reported in **228 ITR 163 (SC); CIT vs. G. Narasimhan** reported in **236 ITR 327** and also the judgement of **Hon'ble Supreme Court** in the case **of D.P. Sandhu Brothers Chembur Pvt. Ltd.** reported in **273 ITR 1(SC).** It was specifically pointed out that reduction of capital, i.e., loss of shares tantamount to transfer u/s. 2(47) of the Act and it was held that computation provision can only be passed only if it was not possible to conceive of any element of cost. After the assessee's reply, ld. AO again issued a show-cause notice dated 13/01/2012 which was on the basis of assessee's contention that long term capital loss arose by virtue of cancellation of Rs.144.06 Crores shares of TTSL was correct however, he asked for further clarification stating as under:-

> *"Why the corresponding cost of shares due to reduction in share capital of Tata Teleservices Ltd. should not be treated as cost of shares of the balance shares of Tata Teleservices Ltd."*

8. Thereafter, ld. AO had asked for other details of capital gain which was again replied by the assessee vide letter dated 11/01/2013. The ld. AO after examining the submissions both factual and legal in respect of long term capital loss of Rs.2046.97 crores in the reduction of capital / cancellation of 144.06 Crores number of shares of TTSL accepted the assessee's

claim for long term capital loss in his order passed u/s.143(3) dated 09/05/2013. The AO treated the amount of long term capital gain arising on sale of shares of TCS Ltd as business income and correspondingly sought to reduce the same from the computation of capital gains. Ultimately, as against the return income of Rs.43,54,03,565 under normal provision of the Act, income was assessed at 776,47,54,038/-.

9. Thereafter, on the receipt of the assessment order, assessee filed rectification application dated 26/08/2013 and 27/08/2013 and rectified certain mistake apparent from record and in pursuance of which ld. AO has rectified the order as u/s.154 dated 16/06/2014.

10. Post the above proceedings and examination of material on record by the AO, ld. PCIT in his revisionary jurisdiction issued a notice u/s. 263 dated 28/12/2015 to revise the assessment order passed by the ld. AO dated 09/12/2013 on the same very issue. In his show-cause notice, he has observed that order passed by the ld. AO is erroneous and prejudicial to the interest of the Revenue in view of the following reasons:-

> *i) The Assessing Officer has failed to take into account the fact that the loss of Rs 20,46,97,54,090/- on account of reduction of capital in computation only and not in the books of account.*
>
> *(ii) The Assessing Officer has failed to consider that the assessee did not receive nor it showed accrual of any such consideration in its books of accounts*
>
> *(iii) The Assessing Officer has failed to consider that assessee had suffered only notional loss on the above transaction and that*

the same should have not been set off against long term capital gains on shares earned.

iv) The Assessing Officer has failed to consider that the Gujarat High Court decision in the case of CIT vs Mohanbhai Pamabhai 1971(9) TMI - wherein the High Court has held that section 45 is the charging section and it undoubtedly provides that any profits or gains arising from the transfer of a capital asset shall be chargeable to income tax under the heading 'Capital Gains". But, section 48 shows that the transfer that is contemplated by Section 45 is a transfer, if consideration is received by the assessee or accrues to the assessee.

(v) The Assessing Officer has failed to consider the decision of Mumbai ITAT Bench, in the case of Bennett Coleman and Co. Ltd. Vs. Addl.CIT 2011(9) TMI-ITAT, Mumbai, Special Branch, wherein the ITAT had considered the judgments given by the Supreme Court in the case of Kartikeya V Sarabhai and CIT vs G. Naralmhan for computation of capital gain on reduction of capital and held that if the earlier shares have been replaced or substituted by new shares then the same would not amount to transfer at all. It would be merely a case of substitution of one kind of share with another kind of share which has been received by the assessee because of the rights of the original shares on the reduction of capital. The transfer of a capital asset, in order to attract the capital gain, must be a transfer as a result of which consideration is received by the assessee accrued to the assessee. If there is no consideration received or accruing to the assessee as a result of the transfer, the machinery section enacted in section 48 would be wholly inapplicable and it would not be possible to compute profits or gains arising from the transfer of the capital asset. Where transfer consists of extinguishment of a right in the capital asset, there must be an element of consideration for such extinguishment, for then only it would be a transfer exigible to capital gains tax. The Tribunal held that if no consideration is received / accrued on account of reduction in capital, then loss arising on account of reduction in

shares capital cannot be subjected to the provisions of Section 45 read with Section 48 and accordingly such loss is not allowable as capital loss. At best such loss can be described as notional loss and it is settled that no notional loss or Income can be subjected to the provisions of Income Tax Act.

(vi) The Assessing Officer has failed to consider that as the distribution of surplus to shareholders as bonus is not taxable, in the same way, losses of the company which have been adjusted by reducing the capital cannot be allowed.

11. Thus, ld. PCIT observed that there has been failure on the part of the ld. AO to work out the correct amount of capital gains and therefore, assessment order dated 09/12/2013 is erroneous and prejudicial to the interest of the Revenue.

12. In response to the show-cause notice, assessee filed its submissions, relevant portion of which has been reproduced in the impugned order which has been incorporated from pages 4-11 of the order. However, the explanation of the assessee has been rejected by the ld. PCIT. The relevant observation and the finding of the ld. PCIT while rejecting the assessee's explanation and cancelling the order reads as under:-

6.0 I have taken into consideration all the arguments of the assessee. But I have arrived at the conclusion that long Term Capital Loss Rs 2046.97 Crores claimed by the assessee in respect to TTSL shares is not allowable. In the Scheme of Arrangement and Restructuring between Tata Teleservices Limited and its Shareholders and creditors that was approved by the Hon Delhi High Court in para 4.1.2 it is mentioned that the paid up equity share capital of TSSL be reduced in the number of equity shares of Rs 10/- each from 634,71,52,316 shares to 317,35,76,158 shares resulting in total reduction of the paid up *equity share capital of TTSL from 6347,15,23,160/- comprising of 634,17,52,316 equity shares of Rs 10/- each to 317,35,76,158 equity shares of Rs 10/- each to Rs 3173,57,61,580. Therefore an amount Rs. 3173,57,61,580 would be reduced from the accumulated debit balance in profit & loss account and unabsorbed depreciation of TTSL from the (of Rs 1967,7161645 tem available balance in Share premium Account) mentioned in clause 4.11 in the following manner.*

Amount available from extinguishment of Share Capital	*Rs 3173,57,61,580/-*
Less: Write off against book loss	*Rs.1586,78,80,790/-*
Less Write off against unabsorbed depreciation	*Rs 1586,78,80,790/-*
Balance available	*Nil*

6.1 Thus amount Rs 3173,57,61,580 available from extinguishment of share capital has been utilized by TTSL for write off of book loss and unabsorbed depreciation to the extent of Rs 3173,57,61,580/-. Section 48 provides for the mode of computation of capital gains by enacting that the Income chargeable to tax as capital gain shall be computed by deducting from the full value of consideration received or accruing as a result of transfer of capital asset, following amounts namely expenditure Incurred wholly and exclusively in connection with such transfer, and the cost of acquisition of capital asset and cost of improvement thereto. If there is no consideration received or accruing to the assessee as a result of transfer, the machinery section enacted in section 48 would be wholly Inapplicable and it would not be possible to compute profits or gains arising from the transfer of capital asset. The transaction in order to attract the *charge of tax as capital gains must, therefore, clearly be such that consideration is received or accrues to the assessee as a result of the transfer of capital asset. Where transfer consists in extinguishment of a right in the capital asset, there must be an element of consideration for such-extinguishment, for then only it would be exigible to capital gains tax. In the case of the assessee transfer of shares is by way of extinguishment of shares of TTSL which the assessee had held. Though the assessee has cited the case law Kartikeya Sarabhal 228 ITR 163 SC, to substantiate it claim that reduction of right in the capital asset would clearly amount to a transfer within the meaning of that expression in section 2(47), but in the case of the assessee it is not mere reduction in the face value of shares. Rather, it is effacement of the shares as well as corresponding capital of the Company. The arrangement itself is called scheme of arrangement and restructuring between TTSL and its shareholders and creditors. It is not called scheme of reduction of capital of TTSL. It Involves depriving the shareholders of rights in the capital, The freed capital then has been used by TTSL to reduce accumulated book loss and unabsorbed depreciation to the extent of freed capital. In my view it is not a case of reduction of capital by reducing the face value of shares to NIL. Rather it is case where the shares have got extinct along with corresponding rights. In case of extinct shares, there is no right in corresponding asset. Where transfer consists in extinguishment of a right in the capital asset there must be an element of consideration for such extinguishment to compute capital gains. But in case the capital asset has been effaced, how there can be rights in it? Once rights cannot be there, there cannot be extinguishment of rights? And further, how there can be consideration on extinguishment of rights? In case of effaced capital asset the consideration received or accrued will be nil (non existing consideration) and not 'zero'. The AO has committed a mistake because in the case of assessee there cannot be two views on the issue of computation of LTCL. There is only one view one can hold in given facts and circumstances of the case and it is that no consideration is received or receivable Since consideration* *is neither received nor receivable as the balance sheet of TTSL is shrunk by reduction of book loss and unabsorbed depreciation on asset side and share capital on the liability side, the assessee cannot expect any consideration on accrual basis on effacement of shares. Therefore, computation provisions u/s 48 of the Act*

6.2 The AO in the case of Tata Power Ltd AY 2009-10 disallowed the loss arising in respect to shares of TTSL for AY 2009-10 but the AO did not consider the same Issue in the case TATA Sons Ltd. It is a mistake the AO has committed in the case of the assessee, which has resulted in loss to revenue.

6.3 The AO has thus committed mistake in allowing set of Long Term Capital Loss (LTCL) of Rs 20,46,97,54,090/- in computation of total income of the assessee Company. Therefore, I direct the AO to determine the total income for AY 2009-10 disallowing LTCL after giving assessee Company an opportunity of being heard. The Assessment order will be modified by the Ad to this extent. The order u/s.263 of the Act is passed accordingly."

13. In sum and substance, the case of the ld. PCIT is that;

- *Firstly,* no consideration has been received or accrued to the assessee as a result of the transfer of 144.06 crore shares of TTSL therefore, Section 48 of the Act would be inapplicable and it would not be possible to compute the profits, gains or losses arising from the transfer of the capital asset. He held that in case where no consideration accrued or received as a result of capital asset, the provision of Section 48 of the Act cannot be applied.
- *Secondly,* he distinguished the decision of the Hon'ble Supreme Court in the case of Kartikeya Sarabhai reported in 228 ITR 163 holding that in that case, it was not a case

of reduction in the face value of the shares but an effacement of the entire shares.

- *Thirdly,* he held that scheme was claimed as scheme of arrangement and restructuring but it is not the scheme of reduction of capital.
- *Fourthly,* he held that there can be no extinguishment of rights in the present case and the consideration received is Rs. Nil and not Rs. Zero. He further held that there is one view which can be held in the facts of the present case that, if no consideration was received or accrued to the assessee, then, the computation provision u/s.148 of the Act fails and
- *Lastly,* he noticed that the AO in another company M/s. Tata Power Ltd had disallowed the capital loss in respect of reduction of share capital / cancellation of shares of TTSL which order was not considered by the present AO.

Accordingly, ld. PCIT directed the AO to determine the total income by disallowing the long term capital loss of Rs. 2046.97 Crores.

14. Before us, ld. Sr. Counsel for the assessee, Mr. J.D. Mistry, first of all, submitted that in this case on the same very issue, the Assessing Officer has raised query and asked for the details which were duly replied and explained before the ld. AO alongwith the details of computation of long term capital gain and also explaining the law in light of various Hon'ble Supreme Court judgments stating that in the case of reduction of the

capital, amounts to transfer and not only that the claim of capital loss is also allowed. Once, the AO after considering these facts and the proposition of law laid down by the various statements of the Hon'ble Supreme Court has accepted the long term capital loss, then ld. PCIT cannot take a different view holding that view of the ld. AO is incorrect. He referred to various judgments on this proposition that if AO has taken one view which is possible view in law then CIT cannot revise or cancel the assessment order within the scope of section 263.

15. Mr. Mistry further submitted that, ld. PCIT has clearly erred and failed to consider that it is possible in law for schemes of reduction of capital, similar to the scheme in the present case, to provide for payment of consideration to the holders of the shares. He has also filed a table giving three examples of cases where reduction of capital had taken place by cancellation of shares and one of them was M/s. Jupiter Capital Private Limited, wherein consideration payable to the holder of the shares was cancelled. In all these cases the Tribunal has held that it is an allowable capital loss would result to the holders of the shares in all the cases whether or not consideration was payable in terms of the scheme. The lists of these details have been given before us which for the sake of ready reference is reproduced hereinbelow:-

Comparisons of Facts between Tata Sons Limited and others:
Extinguishment of rights In Shares vis-a-vis allowabillty of Capital loss

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Sr. No.	Particulars	Tata Sons Limited	Jupiter Capital Pvt Ltd	Ginners & Presses ltd.	Bennett Coleman AND Co. Ltd
		{Assessee Company)	ITA No. 445/Bang/2018	{ITA4133/Mum/2007]_	[12 ITR (Trib) 97]
1	Type of Instrument	Equity shares	Equity shares	Equity shares	Equity shares
2	Underlying Inestee Company	Tata Teleservices Limited	Asianet News Pvt. Limited	Polychem Llmited	TGL
3	Original Capital (in number of shares)	6,34,71,52,316	15,35,05,750	1,61,01, 00	1,79,86,299
4	Original Capital (in Rupees)	63,47,15,23,160	1,53,50,57,500	16,16,18,080	17,98,62,990
5	New Capital (in number of shares)	3,17,35,76,158	10,000	4,04,450	89,93,150
6	New Capital (in Rupees)	31,73,57,61,580	1,00,000	40,40,450	8,99,31.495
7	Method of Reduction of Capital	Cancellation	Cancellation	Cancellation	Reduction of Face value from Rs.10 to
					Rs. 5 Later consolidation of two shares into one. Therefore it is Reorganization and consolidation
8	Consideration	Nil	3,17,83,474	Nil	Nil
9	Date of Decision	NA	29/11/2018	20/1/2010	31-09-2011

16. He further submitted that, from the bare perusal of the order of the ld. PCIT it could be seen that, *firstly*, in the impugned order it is the agreed position that transfer of capital assets being 144.06 crores shares of TTSL has taken place in the hands of the appellant by virtue of the Scheme; *secondly*, the CIT

in the impugned order has set out and based his decision on an entirely incorrect legal principle that the provisions of section 48 fail and therefore no capital loss can be determined in a case where no consideration is received/ accrues to the transferor of the capital asset. No basis has been set out for this erroneous conclusion/assertion of the ld. PCIT. Further, this is contrary to well-settled law laid down by the Supreme Court in the matter of inter alia **Srinivasa Setty (B.C.) 128 ITR 294** and **D. P Sandu Brothers Chembur Pvt. Ltd. 273 ITR 1 (SC),** wherein the correct principle laid down by the courts is that the capital gain computation provisions may be held not to apply, if and only if, any part thereof cannot **<u>conceivably</u>** be attracted. The correct principle is that if it is **<u>impossible to conceive</u>** of consideration as a result of the transfer (here the reduction in the capital under the Scheme), then perhaps, it could be urged that the provisions of section 48 of the Act do not apply. However, in the instant case, although no consideration has been received by or has accrued to the appellant, it is certainly possible to conceive of consideration being received or receivable in such cases.

17. Mr. Mistry further submitted that there is a vast difference between a case where no consideration, i.e., cost or any other element is conceivable in a transaction, as opposed to a case where zero or nil consideration is received in a given case. He further submitted that in respect of ld. PCIT's observation that scheme is not a reduction in capital but an extinguishment / effacement has no significance, because there is no such

distinction that exists in law in view of Section 102 of the Companies Act, 1956 on which he drew our attention. He further submitted that the ld. PCIT accepts that no consideration is received by the assessee and then goes on to make some alleged distinction between "nil" consideration and "zero" consideration which distinction is not understood. The simple question to be considered is, if it is conceivable that consideration can result, that consideration may be "zero" or "nil" or any figure. This is vastly different from no consideration being conceivable in a given case.

18. Further, with respect to the ld. PCIT's findings that there is only one view that can be held in the facts and circumstances of he submitted that only view can be that a capital loss will result on application of the provisions of sections 45 to 48 of the Act, Mr. Mistry submitted that there can be no dispute that assessee had subscribed to the shares and was holding the shares of TTSL and post scheme (which was duly approved by the Hon'ble High Court), the shares held by the assessee has been reduced which has laid to a huge loss to the assessee as share holding has been reduced from 288,13,17,286 shares to 144,06,58,643 equity shares. It is clearly a capital loss to the assessee and it cannot be held that the loss is not allowable. He submitted that, there can be no dispute that-

(a) the reduction of capital effected under the Scheme resulted in 144,06,58,653 equity shares of TTSL held by the assessee being cancelled;

(b) such cancellation and extinguishment of the aforementioned shares would clearly amount to a transfer as defined in section 2(47) of the Act. Section 2(47)(ii) clearly applies to the cancellation of shares under the Scheme and in the alternative, it is possible to contend that section 2(47)(1) may also be applicable. Even in the impugned order, the Ld. PCIT accepts /proceeds on the basis that the transfer of a capital asset/(s) has taken place:

(c) the provisions of section 45 of the Act are clearly attracted as the said number of shares of TTSL being capital assets of the assessee have been transferred.

(d) the provisions of section 48 of the Act are also clearly attracted which prescribe the mode of computation of any income/loss which arises under the head "capital gains by deducting from the full value of the consideration received/accrued as a result of the transfer, the cost of acquisition of the asset so transferred.

(e) On a plain reading of the provisions, it is indisputable that a capital loss of Rs 2046.97 crores has arisen as a result of the transfer of the said shares in TTSL and consequently, allowability of the said capital loss is certainly a possible view and accordingly, the provisions of section 263 of the Act could not be invoked by the ld. PCIT,

(f) That the view of the ld. PCIT that, since in the present case, no consideration was received by the assessee on the reduction of capital under the Scheme, the provisions of sections 45 to 48 could not be applied - cannot be termed to be a correct, irrefutable or definitive view, and the same is not supported by any statutory provision or principle of law or binding judicial precedent.

Accordingly, there is no jurisdiction empowering the CIT to invoke section 263 of the Act. In fact, the decision of the Gujarat High Court in the matter of **CIT Vs. Jaykrishna Harivallabhdas (1997) 231 ITR 108 (Guj)]** holds in favour of the assessee's contention that the capital loss must be computed in cases such as the present one even where no consideration has been received on the transfer of a capital asset.

19. With respect to the ground No. 2(a) raised by the assessee that ld. CIT was erred in concluding that the scheme of arrangement and reconstruction was not a case of reduction of capital,. Mr. Mistry submitted that provisions of the then section 100(1)(b) of the Companies Act, 1956 providing Inter-alia that a reduction in share capital of a company may be effected in inter-alia the following manner:-

(i) Either with or without extinguishing or reducing liability on any of its shares, <u>cancel any paid-up share capital which is lost, or is unrepresented by available asset.</u>

(ii) Either with or without extinguishing or reducing liability on any of its shares, pay off any paid-up share capital which is in excess of the wants of the company.

TTSL followed the mode set out in (i) above. Further, the express provisions of Section 100(1)(c) of the Companies Act, 1956 made it clear that in a reduction of capital as per the provisions of the Companies Act, 1956 it is conceivable (and indeed very possible) that consideration may be payable to the holders of the shares being reduced / cancelled. Order of the Hon. High Court of Delhi dated 07-11-2008 approving the Scheme specifically provided that the Scheme was one of reduction of capital of TTSL.

20. In so far as the conclusion of ld. PCIT that the computation mechanism u/s.48 fails, he submitted that the correct principle as laid down by the courts is that the capital gain computation provisions may be held not to apply if and only if any part thereof cannot conceivably be attracted. In the case of the assessee, although no consideration has been received by or has accrued to the assessee, it is certainly possible to conceive of consideration being received or receivable in such cases and that consideration here is "zero". The Gujarat High Court in the matter of **CIT Vs Jaykrishna Harivallabhdas (1997) 231 ITR 108** has held that a capital loss is sustained by an assessee, when shares of a company which had gone into voluntary liquidation are extinguished and no consideration is received by the assessee. In such a case, a capital loss should have been computed u/s 46(2) r.w.s. 48 of the Act despite the fact that "zero" or no consideration is received or receivable.

21. Further, when there is a reduction by way of cancellation of shares, the same constitutes transfer u/s 2(47) and therefore the consequential capital loss is allowable whether or not any consideration is received /receivable by the shareholder is

supported in the matter of Jupiter Capital Pvt. Ltd Vs. ACIT (Bangalore ITAT) (ITA No. 445/Bang/2018) and Ginners & Pressers Ltd. Vs. ITO (Mumbai Tribunal) (ITA No 398/Mum/2007).

21. In so far as reliance placed by the ld. PCIT on the decision of the ITAT Special Bench in the case of Bennett Coleman & Co. Ltd. reported in (2011) 12 ITR(T) 97, Mr. Mistry submitted that same is not applicable in the following reasons:-

a) the present case is one where section 263 of the Act has been invoked. The provision cannot be applied where a possible view is taken by the AO In the special bench decision of Bennett Coleman there was dissenting order and hence, clearly two views are possible and therefore the same has no application in the present case.

(b) the facts in the Bennett Coleman case was that the assessee was holding investments in equity shares of another company wherein the paid-up capital was reduced to Rs. 5/- from Rs. 10/- per share and subsequently, two equity shares of Rs 5/- each were consolidated into one equity share of Rs. 10/- each. The holders of the original shares received new shares. In the facts of Bennet Coleman's case there was a substitution of shares, which are not the facts in the present case.

This crucial distinction between the facts of the Special Bench decision (Bennett Coleman) have been noticed and dealt with by the Mumbai ITAT in Carestream Health INC vs. DCIT (2020) (ITA

No. 826/Mum/2016) and the Tribunal has allowed capital loss on cancellation of shares while distinguishing Special Bench in Bennett Coleman & Co. Ltd. in view of the fact that the Special Bench was concerned with a case of substitution of one kind of share with other kind of share.

22. *Lastly*, with regard to reliance placed on Srinivasa Shetty (B.C.) 128 ITR 294 as referred by the ld. PCIT, he submitted that the same would not apply to the facts of the present case. On the contrary, judgment of the Hon'ble Supreme Court in the case of D.P. Sandhu Brothers Chembur Pvt. Ltd (supra) wherein the principle laid down is that when some element of the provision cannot conceivably apply be attracted then only it may be contended that computation provision fails. Here it cannot be said that it is not conceivable an only consideration here is 'Nil'.

23. In so far as ground No.3, the ld. PCIT erred in failing to take note of the provisions of Section 55(2)(v)(b) and in not confirming that the cost of remaining shares would include the cost of the shares cancelled on reduction. He submitted that; *firstly*, the said section 55(2)(b)(v) provides for the cost of shares of a company which became the property on happening of the events mentioned therein to mean the cost of acquisition of the shares from which such asset is derived. The said provision <u>does not include the cancellation of shares held consequent to reduction of the capital.</u> Hence, on the interpretation of the ld. PCIT the cost of the cancelled shares if not allowed in the year of cancellation, will never be allowed; *secondly*, it is indisputable

that shares of TTSL which it owned were acquired at a cost. The said shares have now been cancelled and extinguished. It has undoubtedly suffered a loss. The view set out above is also upheld by the Mumbai Tribunal in the case of Carestream (supra).

24. On the other hand, ld. CIT DR submitted that here in this case ld. AO has not examined the correct principle of law on the facts of the case as earlier pointed out by the ld. PCIT in his order at various places. The judgments which have been relied upon by the assessee before the PCIT and by the ld. Sr. Counsel are not applicable in the facts of the case, because none of the case pertains to loss on reduction of capital. Even if it tantamount to transfer u/s. 2(47), then also the computation mechanism fails because there is no cost. Section 48 provides that transfer as contemplated u/s.45 applies only if consideration received by the assessee or accrues to the assessee. Here in this case, ld. AO has failed to consider that assessee did not receive nor it showed accrual of any such consideration in its books of accounts. The transfer of a capital asset, in order to attract the capital gain, must be a transfer as a result of which consideration is received by the assessee accrued to the assessee and if there is no consideration received by the assessee or accruing to the assessee as a result of the transfer, the machinery section enacted in section 48 is inapplicable and it is not possible to compute profits or gains arising from the transfer of the capital asset. This precise issue and law has been

well settled way back by the decision of the Hon'ble Supreme Court in the case of B.C. Srinivasa Shetty (supra).

25. He further submitted that on this very issue, there is a precise judgment of **ITAT Mumbai Special Bench in the case of Bennett Coleman & Co. Ltd. vs. Addl. CIT** (supra) wherein this Tribunal after considering all the judgments of the Hon'ble Supreme Court as cited by the assessee have been duly considered and it has been categorically held that in the case of reduction of capital, if no consideration can be determined then the computation mechanism fails. He also referred to para 17,19,21,23,26,28 & 29 of the Special Bench decision which for the sake of ready reference is reproduced hereunder:-

> ***17.*** *We have considered the rival submissions in the light of material on record as well as the decisions cited by both the parties. Initially the Ld. Counsel argued that share capital of TGL was reduced from Rs. 17,98,62,990/- divided into 17986299 equity shares of face value of Rs. 10/- each to Rs. 8,99,31,495/- divided into 17986299 of Rs. 5/- each paid up. This means basically the capital was reduced by reducing the face value of Rs. 10/- paid up of each share to Rs. 5/- paid up of each share. As a second step such shares (Rs. 5/- per share) were again consolidated into Rs. 10 paid up share and number of shares were reduced to 89,93,149. The Ld. Counsel had argued that basically the original shares got extinguished and, in fact, new shares have been issued by TGL. If the argument is that earlier shares have been replaced or substituted by new shares then the same would not amount to transfer at all. In that case, it would be merely a case of substitution of one kind of share with another kind of share which has been received by the assessee because of its rights to the original shares on the reduction of capital. This position was clarified by the Hon'ble Supreme Court in the case of CIT v. Rasiklal Maneklal (HUF) [1989] 177 ITR 198/ 43 Taxman 259. In that case, the*

assessee was holding 90 shares in one S. company of face value of Rs. 100/- each. Pursuant to the scheme of amalgamation sanctioned by the High Court, the holders of the shares in S. company were to be allotted one share of Rs. 125/- each of NS Company for two shares in S. company and S. Company was to be dissolved. The assessee in that case was allotted 45 shares in N.S company. A question arose, whether this would amount to transfer and the Hon'ble Supreme Court held that there was neither an 'exchange' nor a 'relinquishment' in this transaction. The Hon'ble Supreme Court observed as under:

> *"An "exchange" involves the transfer of property by one person to another and reciprocally the transfer of property by that other to the first person. There must be a mutual transfer of ownership of one thing for the ownership of another.*
>
> *A "relinquishment" takes place when the owner withdraws himself from the property and abandons his rights thereto. It presumes that the property continues to exist after the relinquishment. Where, upon amalgamation, the company in which the assessee holds shares stand dissolved, there is no "relinquishment" by the assessee."*

The apex court had also observed that in case of exchange that one person transfers a property to another person in exchange of another property, the property continues to be in existence. In that case, shares of S. company had ceased to be in existence and therefore the transaction did not involve any transfer. Similarly in the case before us if argument of assessee is accepted then the older shares with different ISIN number ceases to exist and new shares with a different ISNI numbers have been issued and, therefore, it cannot be called a case of extinguishment or relinquishment and it is a mere case of substitution of one kind of share with another. In case before us also assessee got the new shares on the strength of its rights with the old shares and, therefore, same would not amount to transfer.

***18.** ………………………………………………………………………*

***19.** In that case the court was concerned with the issue whether reduction of face value of equity share from Rs. 1000/- each to*

Rs. 210/- each after reduction of share capital which was duly approved by the High Court would amount to transfer. It is important to note that in this case on reduction of capital, certain assets were also given to the shareholders in the form of property, payment of cash and/or adjustment of debit balances. When the matter travelled to Hon'ble Supreme Court, following the decision of Kartikeya V. Sarabhai case (supra) the apex court held that such reduction of capital would constitute transfer and any profit or gain arising from the transfer of capital asset is liable to be taxed u/s.45. In the above mentioned case 90 non-cumulative preference shares, of the face value of Rs. 1000/-, were purchased at a price of Rs. 420/- per share from a company called Sarabhai Limited. In 1965, a sum of Rs. 500/- per preference shares was paid to the assessee upon reduction of share capital and the face value of preference shares was reduced to Rs. 50/- per share and further payment of Rs. 450/- per share was made to the assessee. The ITO was of the opinion that the sum of Rs. 450/- per share which was received now was liable to be taxed under the head 'capital gain'. However, assessee contended that since no transfer had taken place in terms of sec.2 (47), no tax could be imposed. When the matter travelled to Hon'ble Supreme Court it was held that definition of transfer u/s.2 (47) was inclusive and would include relinquishment of an asset or extinguishment of any right therein. It was further observed that even preference shareholders have right to vote on resolutions which would effect the right of preference shareholder u/s. 87(2)(a), 87(2)(b) and 87(2)(c). Therefore the rights of preference shareholders are curtailed to that extent. A careful analysis of the above decision indicates that whenever there is reduction of shares and upon payment by company to compensate the value equivalent to reduction, apart from the effect on shareholders' rights to vote etc., a transfer can be said to have taken place. However, the question is whether the same can still attract sec.45? The answer is given by the Hon'ble Gujarat High Court in the case of Mohanbhai Pamabhai (supra). In this case the issue was whether there is a transfer if a particular partner retired from the firm and his share in the partnership was worked out by taking the proportionate value of his share in the net partnership assets after deduction of liability and prior charges. The ITO was of the opinion that the amount received by the assessee to *the extent which included his proportionate share in the value of the goodwill is liable to be taxed as capital gain. When the matter travelled to the High Court their lordships observed, at pages 404 & 405, as under:*

> *But, even if we are wrong in taking this view and the correct view is that when a partner retires from the partnership his interest in the partnership assets is extinguished and there was, therefore, in the present case, "transfer" of interest of each of the assessees in the goodwill when the assessees retired from the firm, the amount received by each assessee in respect of his share in the value of the goodwill must still be held to be outside the pale of chargeability to capital gains tax. It is not every transfer of a capital asset which attracts the charge of capital gains tax. Section 45 which is the charging section, undoubtedly, provides that any profits or gains arising from the transfer of a capital asset shall be chargeable to income tax under the head "capital gains". But, section 48 shows that the transfer that is contemplated by section 45 is a transfer as a result of which consideration is received by the assessee or accrues to the assessee. Section 48 provides the mode of computation of capital gains by enacting that the income chargeable to tax as capital gain shall be computed by deducting from the "full value of the consideration received or accruing as a result of the transfer of the capital asset" the following amounts, namely: (i) expenditure incurred wholly and exclusively in connection with such transfer ; and (ii) the cost of acquisition of the capital asset and the cost of any improvement thereto. The amounts specified in clauses (i) and (ii) are to be deducted from the " consideration received or accruing as a result of the transfer of the capital asset " for the purpose of determining the profits or gains chargeable to tax. It is, therefore, clear that the transfer of a capital asset, in order to attract the capital gains tax, must be a transfer as a result of which consideration is received by the assessee or accrues to the assessee. If there is no consideration received or accruing to the assessee as a result of the transfer, the machinery section enacted in section 48 would be wholly inapplicable and it would not be possible to compute profits or gains arising from the transfer of the capital asset. The transaction in order to attract the charge of tax as capital*

gains must, therefore, clearly be such that consideration is received by the assessee or accrues to the assessee as a result of the transfer of the capital asset. Where transfer consists in extinguishment of a right in the capital asset, there must be an element of consideration for such extinguishment, for then only it would be a transfer exigible to capital gains tax.

Thus, it becomes absolutely clear that even if a transfer had taken place, unless and until some consideration is received, the transfer of such asset would not attract the provisions of sec.45. The Revenue has challenged this position in appeal before the Hon'ble Supreme Court and the court dismissed the appeal of the Revenue in Addl. CIT v. Mohanbhai & Pamabhai [1987] 165 ITR 166 (SC) in view of the decision of Hon'ble Supreme Court in the case of Sunil Siddharthbhai v. CIT [1985] 156 ITR 509/23 Taxman 14W. Decision of Hon'ble Gujarat High Court was not approved by the Hon'ble Supreme Court, while adjudicating the case of B.C. Srinivasa Setty (supra) on another point i.e. whether building of goodwill in a business which did not cost anything could still be regarded as capital asset for the purpose of charging the same under the head 'capital gains'. However, as far as proposition that a transfer cannot be subjected to provisions of sec.45 in the absence of consideration still remains valid. It may not be out of place to refer to the commentary on Income Tax Law, Fifth Edition, Volume- 2 page 2772, by Chaturvedi & Pithisaria wherein it has been observed as under:

"Transfers not chargeable.—It is not every transfer of a capital asset which attracts the charge of capital gains tax. Although section 45 provides the generality of the charge, it is followed by several sections exonerating the charge under stipulated circumstances. Section 48 provides the mode of computation and in doing so, it excludes expenditure incurred wholly and exclusively in connection with the transfer as also the cost of acquisition of, as well as any improvement to, the capital asset concerned.

The transfer of a capital asset, in order to attract the capital gains tax, must be a transfer as a result of which consideration is received by the assessee or accrues to the assessee. Without the element of consideration, no transfer will attract capital *gains tax [CIT v. Mohanbhai Pamabhai, [1973] 91 ITR 393, 404 (Guj), not approved, on another point, in (1981) 128 ITR 294 (S.C)]"*

In any case, to understand the matter further we shall go through the decision of the Hon'ble Supreme Court in the case of Sunil Siddharthbhai (supra). In this case, the issue involved was whether transfer of personal capital assets to the firm towards contribution of capital, would constitute transfer and whether such transfer would attract capital gain tax? The court held that such contribution of capital asset of a partner into the firm would definitely constitute a transfer because in that case the partner's interest in such asset is reduced from exclusive interest to a shared interest. In respect of taxability of this transfer, three arguments were made before the Hon'ble court which are being extracted from page 515 of the report of the above judgment in the case of Sunil Siddharthbhai (supra) as under:

1. *There must be a "transfer" of a capital asset either under the general law or within the definition in clause (47) of section 2 of the Income-tax Act.*
2. *Consideration must be received or must accrue as a result of the transfer and the consideration must be capable of being determined in monetary terms in order that the computation of capital gains may be made as required by section 48.*
3. *Profits or gains must arise from the transfer and must be embedded in the consideration.*

Since the point raised in the first argument is not material regarding the issue involved before us, therefore, it would suffice to point out that the Hon'ble court held that such contribution of the capital by way of transfer of personal capital assets into the firm would constitute transfer. In respect of the 2nd and 3rd arguments the Hon'ble Supreme Court observed at pages 520 to 522 as under:

"On the basis of that proposition learned counsel for the assessee has urged that s.45 is not attracted in the present case because to compute the profits or gains under s.48 the value of the consideration received by the assessee or accruing to him as a result of the transfer of the capital asset

must be capable of ascertainment in monetary terms. The consideration for the transfer of the personal assets is the right which arises or accrues to the partner during the subsistence of the partnership to get his share of the profits from time to time and, after the dissolution of the partnership or with his retirement from the partnership, to get the value of a share in the net partnership assets as on the date of the dissolution or retirement after a deduction of liabilities and prior charges. The credit entry made in the partner's capital account in the books of the partnership firm does not represent the true value of the consideration. It is notional value only, intended to be taken into account at the time of determining the value of the partner's share in the net partnership assets on the date of dissolution or on his retirement, a share which will depend upon a deduction of the liabilities and prior charges existing on the date of dissolution or retirement. It is not possible to predicate before hand what will be the position in terms of monetary value of a partner's share on that date. At the time when the partner transfers his personal asset to the partnership firm, there can be no reckoning of the liabilities and losses which the firm may suffer in the years to come. All that lies within the womb of the future. It is impossible to conceive of evaluating the consideration acquired by the partner when he brings his personal asset into the partnership firm when neither the date of dissolution or retirement can be envisaged nor can there be any ascertainment of liabilities and prior charges which may not have even arisen yet. In the circumstances, we are unable to hold that the consideration which a partner acquires on making over his personal asset to the partnership firm as his contribution to its capital can fall within the terms of s.48. And as that provision is fundamental to the computation machinery incorporated in the scheme relating to the determination of the charge provided in s.45, such a case must be regarded as falling outside the scope of capital gains taxation altogether.

The third contention of learned counsel for the assessee is that no profit or gain can be said to arise to a partner when he brings his personal asset into a partnership firm as his contribution to its capital. It is urged that the capital gains *chargeable under s.45 are real capital gains computed on the ordinary principles of commercial accounting and that the capital gains must be embedded in the capital asset. In Miss Dhun Dadabhoy Kapadia v. CIT [1967] 63 I.T.R. 651, the appellant held by way of investment some ordinary shares in a limited company. An offer was made by the company to her by which she was entitled to apply for an equal number of new ordinary shares at a premium with an option of either taking the shares or renouncing them in favour of others. The appellant renounced her rights to all the shares and realised Rs. 45,262.50. When this amount was sought to be wholly taxed as a capital gain the appellant claimed that on the issue of the new shares the value of her old shares depreciated and that as a result of the depreciation she suffered a capital loss in the old shares which she was entitled to set off against the capital gain of Rs. 45,262.50. In the alternative she claimed that the right to receive the new shares was a right which was embedded in her old shares and consequently when she realised the sum of Rs. 45,262.50 by selling her right, the capital gain should be computed after deducting from that amount the value of the embedded right which became liquidated. This Court upheld the claim of the appellant that she was entitled to deduct from the sum of Rs. 45,262.50 the loss suffered by way of depreciation in the old shares. The Court proceeded on the basis that in working out capital gain or loss, the principles which had to be applied are those which are a part of commercial practice or which an ordinary man of business would resort to when making computation for his business purposes. It will be noticed that this principle was applied by the Court in a case where a capital gain was sought to be taxed under the Income Tax Act. That profits or gains under the Income Tax Act must be understood in the sense of real profits or gains, that is to say, on the basis of ordinary commercial principles on which actual profits are computed, a sense in which no commercial man would misunderstand, has been regarded as a principle of general application, and there is a catena of cases of this Court which affirms that principle. Reference may be made to Calcutta Co. Ltd. v. CIT [1959] 37 I.T.R. 1 (SC), CIT v. Bai Shirinbai K. Kooka, [1962] 46 I.T.R. 86 (S.C), Poona Electric Supply Co.*

Ltd. v. CIT [1965] 57 I.T.R. 521 (SC), (1973) 89 I.T.R. 266 (SC) and Bafna Textiles v. ITO [1975] 98 I.T.R. 1 (Kar)."

Thus, from the above it is clear that the court relied on the principles laid down in the case of B.C. Srinivasa Setty (supra) and held that unless and until the consideration was present the computation provision of sec.48 would not be workable and, therefore, such transfer could not be subjected to tax. The court further went on to hold that unless and until the profits or losses are real, same cannot be subjected to tax.

20. *..*

21. *Now in the case before us the assessee has not received any consideration for reduction of share capital. What has happened is that ultimately the number of shares held by the assessee has been reduced to 50% and nothing has moved from the side of the company to the assessee. The Ld. Counsel of the assessee submits that the decision of the Hon'ble Gujarat High Court in the case of Mohanbhai Pamabhai (supra) is not applicable because, in the case before us, it was possible to ascertain the consideration by envisaging the same as zero. In this regard he relied on the decision of the Hon'ble Bombay High Court in the case of Cadell Wvg. Mill (P.) Ltd. (supra) and, in particular, referred to the observations at pages 284 and 285 of the report wherein it was observed that whole of the value of the capital asset transferred could not be brought to tax because that would amount to taxing the value of asset and not profit as contemplated in sec.45. In this case the issue involved was whether the compensation received on surrender of statutory tenancy rights is chargeable as casual income u/s.10(3) or it should be charged u/s.45. The court, after examining the issue in detail, held that amount received on such surrender is chargeable only u/s.45. The court observed that whole value of the compensation could not be charged u/s.56 because same was chargeable u/s.45 and the decision of the Hon'ble Supreme Court in the case of B.C. Srinivasa Setty (supra) was applied. It was also noted that, in fact, sec.55 (2)(a) itself was amended by Finance Act, 1994 w.e.f. 1-04-1995 and the cost of acquisition of tenancy rights was to be taken at nil, therefore, this provision could not be applied retrospectively. Thus, it is clear that the* *decision of Hon'ble Supreme Court in the case of B.C. Srinivasa Setty (supra) was followed in principle wherein it has been held that if computation provision of sec.48 fails, then such transaction cannot be brought to tax u/s.45. The court specifically declined to entertain the argument that cost of tenancy right should be taken at zero because that would amount to charging of capital value of the asset and not capital gain. In the case of reduction of capital nothing moves from the coffers of the company and, therefore, it is a simple case of no consideration which cannot be substituted to zero. It is pertinent to note that after the decision of Hon'ble Supreme Court in the case of B.C. Srinivasa Setty (supra), the legislature has introduced specific provision wherein cost of acquisition of goodwill was to be taken at nil. Similar amendments were made to specify the cost with reference to trademark, cost of right to manufacture or produce or process any article or thing etc. Therefore, wherever Legislature intended to substitute the cost of acquisition at zero, specific amendment has been made. In the absence of such amendment it has to be inferred that in the case of reduction of shares, without any apparent consideration, that too in a situation where the reduction has no effect on the right of shareholder with reference to the intrinsic rights on the company, it is always possible to argue that cost of acquisition cannot be ascertained and, therefore, provisions of sec.45 would not be applicable. Since no amendment has been made in respect of consideration, principles laid down by the Hon'ble Gujarat High Court in the case of Mohanbhai Pamabhai (supra)- later confirmed by the Hon'ble Supreme Court in the case of B.C. Srinivasa Setty (supra) and also in the case of Sunil Siddharthbhai (supra)- are applicable, if the consideration cannot be ascertained, then provisions of sec.45 would not apply. No doubt Learned counsel forcefully submitted that the legislature has listed out all transactions which are not regarded as transfer such as gifts etc, (sec.47-iii) and per contra any other transfer even without specific or zero consideration should be considered for taxation U/s 45 but we find no force in it. The situation regarding non ascertainment of any of the element of sec.48 came to light only after the pronouncement of the decision of the Hon'ble Supreme Court in the case of B.C. Srinivasa Setty (supra). Perhaps legislature intended to exempt only gifts from subject matter of capital gains and that is why clause (iii)* *to sec.47 must have been put in the statute. In any case, the decision of the Hon'ble Bombay High Court in the case of The Bombay Burmah Trading Corpn. Ltd. (supra) is directly on the issue wherein third question referred before the Court reads as under:*

> *"3. Whether on the facts and in the circumstances of the case, the Tribunal was right in law in holding that where in a case of compulsory acquisition by Government without compensation no capital loss will ensure?"*
>
> *This question was answered by the Hon'ble court vide para which reads as under:*
>
> *"4. So far as the third question is concerned, the same is covered by the ratio of the decision of the Supreme Court in B.C. Srinivasa Setty [1981] 128 ITR 294. The answer to the question is, therefore, self-evident. Questions Nos. l, 2 and 3 are not preferable questions of law."*

Thus, from the above it is clear that when no consideration is received, no loss can be allowed in view of the principles laid down by the Hon'ble Supreme Court in the case of B. C. Srinivasa Setty (supra) which was followed in above decision. In fact, assessee has not suffered any loss on reduction of share capital which we shall see little later.

22. *...*

23. *As pointed out by Ld. DR, assessee's percentage of share holding, immediately before reduction of share capital and immediately after such reduction, remained the same. Therefore, assessee was holding 74.9% shares of TGL immediately before the reduction of capital and also immediately after the reduction of capital. Such capital has been reduced not only in the case of assessee by TGL but the same has been reduced for all the shareholders of the TGL. Though under the concept of joint stock company, the joint stock company is having independent legal entity but for all practical purposes the company is always owned by the shareholders. Therefore, sum total of 100% shareholders would own the net assets of the company. Now let us say a company started with a capital of Rs. 100/- and had assets of Rs. 100/-, then 75% shareholders would own 75% of* *such assets i.e. Rs. 75. If after few years, this company suffers a loss and the assets are reduced to Rs. 50, then share of the assessee in the assets of the company would be only Rs. 37.50. If the capital of the company is reduced by 50%, even then the share of the assessee would be 75% and it would remain same at Rs. 37.50. Therefore, the effective share of assessee, in the assets of the company, would remain the same immediately before and after reduction of such capital. In other words, the loss suffered by the company would belong to the company and that cannot be allowed to be set off in the hands of the assessee. This position is further supported by another example. If, in the above illustration, after few years, instead of assets becoming Rs. 50/-, it increases to Rs. 200/-, because of profit, and in turn this company issued bonus shares, even then the profit would remain in the books of the company and mere allotment of such bonus shares cannot be subjected to tax. This position was accepted even by the Ld. Counsel of the assessee. Therefore, when the profits of the company which have been distributed to the shareholders by way of bonus shares cannot be assessed, on the same principle losses of the company which have been adjusted by reducing the capital cannot be allowed.*

24. *..*

25. *..*

26. *The Ld. Counsel of the assessee had also relied on the following decisions of the Tribunal-*

(a) *Zyma Laboratories Ltd.'s case (supra)*

(b) *Polychem Ltd.'s case (supra)*

(c) *Ginners & Presser Ltd.'s case (supra)*

But in all these cases the principle laid down by the Hon'ble Supreme Court in the case of B.C. Srinivasa Setty (supra) was neither cited, nor considered and, therefore, these decisions are distinguishable and in any case, not binding on the Special Bench. In fact such profit or loss arising out of issue of bonus shares or reduction of capital is only a notional profit or notional loss and this concept has been approved by the Hon'ble Supreme Court in the case of Miss Dhun Dadabhoy

Kapadia (supra) and further confirmed by the Hon'ble Supreme Court in the case of Sunil Siddharthbhai (supra). In the case of MissDhun Dadabhoy Kapadia (supra) the facts noted by the Hon'ble apex court are as under:

> *The appellant was holding 710 ordinary shares of the Tata Iron and Steel Company Ltd. (hereinafter referred to as "the company"), which she had inherited some tine prior to 1st January, 1954, as an investment. It was admitted that she was not a dealer in shares. Under a special resolution passed at an extraordinary general meeting of the company oil 12th March, 1956, the appellant, as holder of 710 ordinary shares, became entitled to purchase new ordinary shares issued in the ratio of one new ordinary share for one existing ordinary share as held on 26th April, 1956. In pursuance of this resolution, an offer was made to the appellant by the company by its circular letter dated 15th May, 1956, that she was in terms of the resolution, entitled to apply for 710 new ordinary shares to be paid for at the rate of Rs. 105 per new ordinary share. This payment was to represent Rs. 75 as the face value of the share and Rs. 30 as premium. She was also given the option of either taking the shares wholly or partly, or renouncing them either wholly or partly, in favour of any other person or persons. The appellant chose to renounce her right to all the 710 ordinary shares instead of taking the shares herself, and when renouncing the shares, she sold them in the open market on 12th June, 1956, as a result of which she actually realised a sum of Rs. 45,262,50P. It was common ground before the income-tax authorities as well as the Tribunal that this amount received by her was a capital gain and the whole of this amount was sought to be taxed as capital gain received by the appellant. On behalf of the appellant the plea was that, on the issue of the new ordinary shares, the value of her old ordinary shares depreciated, because the assets of the company remained stationary, while the number of shares increased. It was in consideration of this depreciation in her original holdings that she was given the right to purchase these new ordinary shares, or to renounce them in favour of some other person and make up the loss which she would suffer on her original shares. The board of*

> *directors of the Native Stock and Shares Association Ltd. had passed a resolution that the transactions in these shares were to be cum-right up to and including 1st June, 1956, and were to be ex-rights from 4th June, 1956, onwards. The intervening days, 2nd and 3rd June, being official holidays, there were to be no transactions on those days. The market quotation of the old Tata ordinary shares was Rs. 253 per share on 1st June, 1956, and fell to Rs. 198.75nP. On 4th June, 1956. There was, thus, a fall in the market quotation of old shares of Rs. 54.26P. per share. It was claimed by the appellant that, as a result of this depreciation in the price of her old ordinary shares, she suffered a capital loss in those shares to the extent of Rs. 37,630, and she was entitled to set off this loss against the capital gain of Rs. 45,262.50P. which she realised on selling her right to take the new ordinary shares. In the alternative, the case was put forward on the basis that the right to receive these new ordinary shares was a right which was embedded in her old ordinary shares, and, consequently, when she realised the sum of Rs. 45,262,50P by selling her right, the capital gain should be computed after deducting from this amount realised the value of the embedded right which became liquidated. The value of that right, according to the appellant, should be calculated in accordance with the principles of accountancy, as laid down by various authors on the subject to be applied in such Situations. Even if this principle be accepted, the amount taxable as capital gain in her hands would have to be reduced by at least a sum of Rs. 37,630, if not more.*

The contention of the assessee was rejected by the income tax authorities as well as by the Tribunal and the High Court confirmed the decision of the Tribunal. When the matter travelled to Hon'ble Supreme Court, the apex court observed as under:

> *"In order to answer the question referred to the High Court, it appears to us that the nature of the transaction, which resulted in this receipt of Rs. 45,262.50P. by the appellant, must be analysed and properly understood. The amount, it is the agreed case of the parties, was a capital gain. The capital asset which the appellant originally possessed consisted of 710 ordinary shares of the company. There was already a*

provision that, if the company issued any new shares, every holder of old shares would be entitled to such number of ordinary shares as the board may, by resolution, decide. This right was possessed by the appellant because of her ownership of the old 710 ordinary shares, and when the board of directors of the company passed a resolution for issue of new shares, this right of the appellant matured to the extent that she became entitled to receive 710 new shares. This right could be exercised by her by actually purchasing those shares at the shares Plus this right to take 710 new shares. At the time of her transaction, her old shares were valued at Rs. 253 per share, so that the capital asset in her possession can be treated to be the cash value of 710 multiplied by Rs. 253 of the old shares Plus this right to obtain new shares. After she had transferred this right to obtain new shares, the capital assets that came into her hands were the 710 old shares, which became valued at Rs. 198.75P. per share, together with the sum of Rs. 45,262.50P. The net capital gain or loss to the appellant obviously would be the difference between the value of the capital asset and the cash in her hands after she had renounced her right and realised the cash value in respect of it, and the value of the capital asset including the right which she possessed just before these new shares were issued and before she realised any cash in respect of the right by renouncing it in favour of some other person. As we have indicated above, the value of the capital asset, after renouncement, would be 710 multiplied by Rs. 198.75P. Plus the sum of Rs. 45,262.50P while the value of the asset, immediately before the renouncement, would be 710 multiplied by Rs. 253, there being no cash value at that time of the right to be taken into account. Thus, the capital gain or loss would be worked out at Rs. 45,262.50P. after deducting from it the sum worked out at 710 multiplied by the difference between Rs. 253 and Rs. 198.75P. This last amount comes to a little more than the sum of Rs. 37,630 which the appellant claimed should be deducted from Rs. 45,262.50P. in computing her capital gain. The claim made by the appellant was thus clearly justified because the net capital gain by her in the transaction, which consisted of issue of new shares together with her renouncement of the right to receive new *shares and make some money thereby, could only be properly computed in the manner indicated by us above.*

In the alternative, the use can be examined in another aspect. At the time of the issue of new shares, the appellant possessed 710 old shares and she also got the right to obtain 710 new shares. When she sold this right to obtain 710 new shares and realised the sum of Rs. 45,262.50P., she capitalised that right and converted it into money. The value of the right may be measured by setting off against the appreciation in the face value of the new shares the depreciation in the old shares and, consequently, to the extent of the depreciation in the value of her original shares, she must be deemed to have invested money in acquisition of this new right. A concomitant of the acquisition of the new right was the depreciation in the value of the old shares, and the depreciation may, in a commercial sense, be deemed to be the value of the right which she subsequently transferred. The capital gain made by her would, therefore, be represented only by the difference between the money realised on transfer of the right, and the amount which she lost in the form of depreciation of her original shares in order to acquire that right. Looked at in this manner also, it is clear that the net capital gain by her would be represented by the amount realised by her on transferring the right to receive new shares, after deducting therefrom the amount of depreciation in the value of her original shares, being the loss incurred by her in her capital asset in the transaction in which she acquired the right for which she realised the cash. This method of looking at the transaction also leads to the same conclusion which we have indicated in the preceding paragraph."

In the above case, Hon'ble court has made it clear that capital gain on account of sale of rights shares has to be understood similarly as understood in the commercial world. It has to be noted that while stating the facts, the Hon'ble Supreme Court noted and stressed that assets of the company remained stationary and that is why depreciation has accrued in the value of old ordinary shares, because same assets would be represented by old ordinary shares plus the new rights shares. Thus, when there was no change in the value of assets of the company on the date of issuance of rights shares, then such *reduction in the value of new shares has to be reckoned because assets remained the same. Similarly, in the case before us the value of asset of a company immediately before and after reduction of share capital remained the same and therefore by reducing the amount and number of shares the assessee's proportionate share in such assets remained the same. In the case before us also the value of assets even after reduction of capital remained the same and, therefore, loss, if any, at best can be called notional loss which cannot be allowed as observed by the Hon'ble Supreme Court in the case of Sunil Siddharthbhai (supra) at pages 521 & 522 which we have reproduced earlier.*

.. It was noticed that perhaps during the earlier hearing of this case, reliance has been placed by the department on the decision of the Ahmedabad Bench of the Tribunal in the case of Ajay C. Mehta v. Dy.CIT [2008] 305 ITR (AT) 155/ 114 ITD 628. In that case also assessee had claimed short term capital loss. The assessee had applied for 2,00,000 warrants and paid Rs. 2.70 per warrant as upfront payment. Later on, assessee exercised the option only in respect of 40,000 warrants and the right with respect to 1,50,000 warrants was extinguished, which was claimed as short term capital loss. This claim of loss was rejected by the Tribunal because no consideration was received by following the decision of the Hon'ble Supreme Court in the case of B.C. Srinivasa Setty (supra). In any case, in addition to the above detailed discussion, the issue is squarely covered by the decision of the Hon'ble Bombay High Court in the case of The Bombay Burmah Trading Corpn. Ltd. (supra) wherein it is clearly held that if no compensation is received, then capital loss cannot be allowed. It was argued by the Ld. Counsel of the assessee that detailed facts are not available, but we find that the Hon'ble Madhya Pradesh High Court in the case of National Textile Corpn. v. CIT [2008] 171 Taxman 339 has clearly held that a decision of jurisdictional High Court cannot be ignored by the Tribunal simply because it is assumed that certain aspects of the issue might not have been considered by the jurisdictional high court. In the case of National Textiles Corporation, it was observed as under:

> *"It is neither permissible nor legal for any Court and Tribunal to comment upon the decision of Supreme Court/High Court. Similarly, it is also not permissible for the Tribunal to comment upon the manner in which a particular decision was rendered by Supreme Court/High Court. It is also not permissible for Tribunal to sidetrack or/and ignore the decision of High Court on the ground that it did not take into consideration a particular provision of law. If such approach is resorted to by subordinate Courts/Tribunals then it is held to be not in conformity with the law laid down by Supreme Court. It was deprecated by Supreme Court as being improper. When the High Court has no jurisdiction to comment upon any decision of Supreme Court nor High Court has a power to ignore such decision by virtue of mandate contained in Article 141 of Constitution then on the same reasoning, the Tribunal being subordinate to High Court has to follow the decision of jurisdictional High Court without making any comment upon the said decision or/and without ignoring it on any ground except those which are well recognized as indicated hereinbelow. In other words, when law laid down by Supreme Court is binding on all Courts/Tribunals in the country by virtue of Article 141 of Constitution of India then law laid down by High Court is equally binding on Courts/Tribunals they being subordinate to High Court by virtue of powers conferred by Articles 215, 226 and 227 of Constitution of India and by judicial precedents."*

Therefore, in our view, the decision of Hon'ble Bombay High Court is binding and has to be applied.

27. *..*

28. *We also find force in the submissions of the Ld. DR that as per sec.55(v) the cost the cost of acquisition of shares even after conversion etc. has to be taken with reference to the cost of original shares. Therefore, after reduction of share capital the cost of acquisition of the remaining shares would be reckoned with references to the original cost. Though at this stage assessee has not obtained any benefit because loss has been computed with reference to the actual cost, but, in future, if assessee decides to sell its shareholding in TGL then assessee has the right, U/s 55(v), to substitute the cost of acquisition with reference to the original shareholding and in that case it may* *amount to double benefit later on which is not permissible under the law.*

29. *Therefore, in the light of the above discussion, we are of the opinion, that the loss arising on account of reduction in share capital cannot be subjected to provisions of sec.45 r.w.s. 48 and, accordingly, such loss is not allowable as capital loss. At best such loss can be described as notional loss and it is settled principle that no notional loss or income can be subjected to the provisions of the I.T. Act. We hold accordingly.*

26. Thus, in view of the aforesaid judgment of Special Bench, Ld. DR submitted the claim of assessee cannot be upheld, because capital gain / loss cannot be determined. In any case, the ld. AO has not discussed this issue at all in his order nor he has considered this legal aspect and has simply accepted the claim of the assessee. He thus strongly relied upon the order of the ld. PCIT.

DECISION

27. We have heard rival submissions and perused the relevant finding given in the impugned order as well as material placed on record. The main issue which for our adjudication is, *firstly*, whether the ld. AO was correct in allowing long term capital loss of Rs. 2046,97,54,090/- on account of reduction of capital and consequently whether ld. AO was correct in allowing set off of the said amount of long term losses in computation of total income of the assessee company. *Secondly*, whether ld. PCIT was correct in law and facts in holding that assessment order passed by the ld. AO is erroneous and prejudicial to the interest of the Revenue; and lastly, whether the view taken by the ld. AO for

possible view while allowing the claim of the set off of long term capital loss.

28. We have already discussed the facts relating to reduction of capital of asset and claim of long term capital loss. To put in succinct manner, the assessee was holder of 288,13,17,286 equity shares in TTSL acquired at various points of time. Thus, assessee had invested in the shares of TTSL which was a capital asset in the hands of the assessee company. Since, TTSL had incurred substantial loss in the course of its business for providing telecom services, the large part of the paid-up share capital of TTSL was utilized so as to finance / bear the said loss. In view of such losses, a Scheme of Arrangement and Re-structuring between TTSL and its shareholders was entered and one of the major shareholder was the assessee company. The equity shares of TTSL of Rs.10/- each from 634,71,52,316 shares was reduced to 317,35,76,158 shares. The said reduction of capital was effected as part of the scheme provided u/s. 100 to 103 of the Companies Act, 1956. As per the scheme, no consideration was payable to the shareholders in respect of the shares which were to be cancelled. Consequently, the shareholding of the assessee was also reduced to half, i.e., 144,06,58,643 from 288,13,17,286 equity shares. The relevant portion of the scheme has already been incorporated above. Now, such a reduction of capital has been claimed as long term capital loss by the assessee in the computation of capital gain and has been set off against other long term capital gain as per the working incorporated in para 6 of the order. The entire case of

the ld. PCIT hinges upon the fact that, since no consideration has been received or accrued to the assessee by way of reduction of capital and therefore, computation mechanism provided u/s.48 fails and consequently, long term capital loss cannot be worked out. According to him, Section 48 provides mode of computation of capital gains which is computed by deducting from the full value of consideration received or accruing as a result of the transfer of the "capital asset" including expenditure incurred wholly and exclusively in connection with such transfer and the cost of acquisition of the capital asset and if there is no consideration received or accruing to the assessee as a result of the transfer, the machinery section enacted in section 48 becomes wholly inapplicable and it would not be possible to compute profits or gains arising from the transfer of the capital asset. Further, according to him while transfer consists in extinguishment of a right in the capital asset, there must be an element of consideration for such extinguishment, for then only it would be a 'transfer' exigible to capital gains tax. The observation and the finding of the ld. PCIT have already been dealt in the foregoing paragraphs.

29. First of all we have to bear in mind the reduction / cancellation of shares were as per the scheme of arrangement and restructuring between TTSL and its shareholders in terms of Section 100 & 391 under the relevant provisions of the Companies Act, 1956. The assessee had invested in the equity shares and has acquired 288,13,17,286 equity shares at face value of Rs. 10/-. Thus, at the time of the acquisition of the

shares, assessee has paid consideration for acquiring the capital asset. As per the scheme, book loss and unabsorbed depreciation was written off first from the balance available in the share premium account and write-off of book losses remaining after deduction against the balance in the share premium account to the amount available from extinguishment of paid up equity shares. As a result of this, the shares of the assessee were reduced to half and the consideration paid on acquisition of capital asset was also reduced to half which resulted into loss to the assessee. **<u>There can be no dispute that there was a loss on the capital account by way of reduction of capital invested and therefore any loss on capital account, is a capital loss</u>.** The issue is, whether it is a notional loss according to the ld. PCIT and even if it is a capital loss, the same cannot be allowed because of reduction of the capital asset has not received any consideration or any consideration has accrued to the assessee. First of all the reduction of a capital has been provided u/s. 100(1) of the companies Act). It provides the manner in which reduction of capital can be effected. The sub-clause (c) of section also envisaged to pay for any paid up capital which is in excess with the wants of the company. Thus, there is a consideration envisaged in the reduction of capital. There could be a case where consideration is paid on the reduction of capital or consideration is not paid at all. Whether in such circumstances, can two views be taken in the reduction of capital, one where certain consideration is paid and in another where no consideration is paid. For example, if the share capital of the assessee was reduced from 288.13 Crore shares to 144.06 Crore share and if assessee would have received some amount, say Rs.1 Crore, then as per the ld. PCIT, assessee would be entitled to compute long term capital loss of Rs. 2045,97,54,090/-, because there is some consideration received. If assessee has not received the consideration then, whole computation mechanism fails. We are unable to accept such reasoning or view taken by the Ld. PCIT.

30. There cannot any divergent view that a 'capital asset' is subject to tax if there is a 'transfer' within the scope and meaning of Section 2(47) of the Act. Now, whether the reduction of face value of shares amounts to transfer or not, has been settled by the Hon'ble Supreme Court in the case of **Kartikeya Sarabhai reported in 228 ITR 163 (SC)** wherein the issue was whether reduction of face value of the shares will be subject to levy of capital gains, whether reduction of the face value result in extinguishment of assessee's right and is there any transfer within the meaning of Section 2(47). The case of the assessee in that case was, since reduction of face value did not result in extinguishment of assessee's right and therefore, there is no transfer and hence, is not exigible to capital gains tax. The Hon'ble Supreme Court however held that:-

> *" Section 2(47) which is an inclusive definition, inter alia, provides that relinquishment of an asset or extinguishment of any right therein amounts to a transfer of a capital asset. While it is no doubt true that the appellant continues to remain a shareholder of the company even with the reduction of share capital, it is not possible to accept the contention that there has*

> *been no extinguishment of any part of his right as a shareholder qua the company. It is not necessary for a capital gain to arise that there must be a sale of a capital asset. Sale is only one of the modes of transfer envisaged by section 2(47) of the Act. Relinquishment of the asset or the extinguishment of any right in it, which may not amount to a sale, can also be considered as a transfer and any profit or gain which arises from the transfer of a capital asset is liable to be taxed under section 45 of the Act.*

Further, the Hon'ble Supreme Court held that *a company under section 100(1)(c) of the Companies Act, 1956 has a right to reduce the share capital and one of the modes which can be adopted is to reduce the face value of the preference share. Section 87(2)(c) which, inter alia, provides that "Where the holder of any preference share has a right to vote on any resolution in accordance with the provisions of this sub-section, his voting right on a poll, as the holder of such share, shall, subject to the provisions of section 89 and sub-section (2) of section 92, be in the same proportion as the capital paid-up in respect of the preference share bears to the total paid-up equity capital of the company." Hence, when as a result of the reducing of the face value of the share, the share capital is reduced, the right of the preference shareholder to the dividend or his share capital and the right to share in the distribution of the net assets upon liquidation is extinguished proportionately to the extent of reduction in the capital.* ***Such reduction of the right of the capital asset would clearly amount to a transfer within the meaning of that expression in section 2(47) of the Income Tax Act, 1961.*** Thus, reduction of capital has been treated as a transfer within the meaning and expression of Section 2(47).

31. In the case of **DCIT vs. BPL Sanyo Finance Ltd. reported in 312 ITR 63 (KAR),** the Hon'ble Karnataka High Court dealing with the case where loss on account of forfeiture of share application money, amounts to short term capital loss or not. The Hon'ble High Court held that consequent to assessee's default in not paying the balance of money on allotment, its right in the shares stood extinguished on its forfeiture and the loss suffered by the assessee, i.e., non-recovery of share application money is consequent to the forfeiture of its right in the shares and the same is to be understood to be within the scope and ambit of transfer and therefore, the Tribunal was justified in holding that it would amount to short-term capital loss to the assessee. Thus, the loss was allowed even if share application money paid by the assessee was forfeited due to default in payment and balance money of allotment. The relevant observation of the High Court reads as under:-

> ***"10.*** *On account of the aforesaid fact that the binding contract existed between the assessee and the investee company, the irresistible conclusion that can be drawn on the aforesaid facts and circumstances is that as soon as the allotment is made, the assessee would be deemed to have acquired a right in such shares even if the call monies or the full face value of the shares has not been paid. Thus, in a case where only share application money is paid and the balance is yet to be paid on actual allotment of shares, the holder of such allotment would be recognised as a member of the investee company. Thus, it cannot be said that the assessee had not acquired right in such shares on account of its failure to deposit the balance amount for allotment of shares. The aforesaid view would attract the provisions of section 2(47) of the Act. The extinguishment of any*

rights therein as appeared in section 2(47) of the Act, covers every possible transaction resulting in the destruction, annihilation, extinction, termination, cessation or cancellation, by satisfaction or otherwise of all or any of the bundle of rights whether qualitative or quantitative, which the assessee has in a capital asset whether or not such an asset is corporeal or incorporeal.

***11.** In the case on hand consequent to the assessee's default in not paying the balance of money on allotment, its right in the shares stood extinguished on its forfeiture by the investee company. **The loss suffered by the assessee, i.e., non-recovery of share application money is consequent to the forfeiture of its right in the shares and the same is to be understood to be within the scope and ambit of transfer.** In this view of the matter, the Tribunal was justified in holding that it would amount to short-term capital loss to the assessee. No other point was urged before us.*

***12.** With regard to the extinguishment of any rights, we may profitably refer to the judgment of the Supreme Court in the case of CIT v. Mrs. Grace Collis [2001] 248 ITR 323. In the said case, it has been held as under (page 329) :*

> *"It is true that the definition of 'transfer' in section 2(47) of the Act is an 'inclusive' definition and, therefore, extends to events and transactions which may not otherwise be 'transfer' according to its ordinary, popular and natural sense."*

***13.** For the aforesaid reasons, we are of the considered opinion that the questions posed have to be answered in favour of the assessee and against the Revenue. The appeal accordingly stands disposed of."*

32. In case of **CIT vs. Mrs. Grace Collis And Others reported in 248 ITR 323,** Hon'ble Supreme Court had observed and held as under:-

*"**15.** We have given careful thought to the definition of 'transfer' in section 2(47) and to the decision of this Court in Vania Silk Mills (P.) Ltd.'s case (supra). In our view, the definition clearly contemplates the extinguishment of rights in a capital asset distinct and independent of such extinguishment consequent upon the transfer thereof. We do not approve, respectfully, of the limitation of the expression 'extinguishment of any rights therein' to such extinguishment on account of transfers or to the view that the expression 'extinguishment of any rights therein' cannot be extended to mean the extinguishment of rights independent of or otherwise than on account of transfer. To so read, the expression is to render it ineffective and its use meaningless. As we read it, therefore, the expression does include the extinguishment of rights in a capital asset independent of and otherwise than on account of transfer.*

***16.** This being so, the rights of the assessees in the capital asset, being their shares in the amalgamating company, stood extinguished upon the amalgamation of the amalgamating company with the amalgamated company. There was, therefore, a transfer of the shares in the amalgamating company with the meaning of section 2(47). It was, therefore, a transaction to which section 47(vii) applied and, consequently, the cost to the assessees of the acquisition of the shares of the amalgamated company had to be determined in accordance with the provision of section 49(2), that is to say, the cost was deemed to be the cost of the acquisition by the assessees of their shares in the amalgamating company.*

33. **Thus, if the right of the assessee in the capital asset stands extinguished either upon amalgamation or by reduction of shares it amounts to transfer of share within the meaning of 2(47) and therefore, computation of capital gains has to be made.** Ergo, there could be no quarrel that

reduction of equity shares under the scheme of arrangement and restructuring in terms of Section 100, amounts to extinguishment of rights in the shares and hence, it is a transfer within the ambit and scope of Section 2(47) of the Act. This fact has also not been disputed by the ld. CIT DR also that reduction of capital amounts to transfer in the present case.

34. Now whether there could be conceivable consideration or it is a case here where consideration itself is inconceivable. The Hon'ble Supreme Court in the case of **CIT vs. D.P. Sandhu Brothers Chembur Pvt. Ltd.** reported in **273 ITR 1 (SC),** while deciding the issue of surrender of tenancy rights for a consideration, amount to transfer giving rise to capital gains where no cost of acquisition can be computed. The Hon'ble Supreme Court first of all held that tenancy right is a capital asset and the surrender of tenancy right is "transfer" and the consideration received thereof is a capital receipt within the meaning of Section 45 after referring to the judgment of Hon'ble Supreme Court in the case of A. Gasper vs. CIT reported in 192 ITR 382. Thereafter, on the issue of cost of acquisition, the Hon'ble Supreme Court referred to the decision of CIT vs. B. C. Srinivasa Setty (supra) and observed as under:-

"8. *In 1981 this Court in B.C. Srinivasa Setty's case (supra) held that all transactions encompassed by section 45 must fall within the computation provisions of section 48. If the computation as provided under section 48 could not be applied to a particular transaction, it must be regarded as "never intended by section 45 to be the subject of the charge". In that case, the Court was considering whether a firm was liable to pay capital gains on the* *sale of its goodwill to another firm. The Court found that the consideration received for the sale of goodwill could not be subjected to capital gains because the cost of its acquisition was inherently incapable of being determined. Pathak J. as his Lordship then was, speaking for the Court said :*

> *"**What is contemplated is an asset in the acquisition of which it is possible to envisage a cost.** The intent goes to the nature and character of the asset, that it is an asset which possesses the inherent quality of being available on the expenditure of money to a person seeking to acquire it. It is immaterial that although the asset belongs to such a class it may, on the facts of a certain case, be acquired without the payment of money..." (p. 300)*

9. In other words, an asset which is capable of acquisition at a cost would be included within the provisions pertaining to the head 'capital gains' as opposed to assets in the acquisition of which no cost at all can be conceived. *The principle propounded in B.C. Srinivasa Setty's case (supra) has been followed by several High Courts with reference to the consideration received on surrender of tenancy rights. [See Among others Bawa Shiv Charan Singh v. CIT [1984] 149 ITR 29 (Delhi); CIT v. Mangtu Ram Jaipuria [1991] 192 ITR 533 (Cal.); CIT v. Joy Ice Cream (Bang.) (P.) Ltd. [1993] 201 ITR 894 (Kar.); CIT v. Markapakula Agamma [1987] 165 ITR 386 (A.P.); CIT v. Merchandisers (P.) Ltd. [1990] 182 ITR 107 (Ker.)]. In all these decisions the several High Courts held that if the cost of acquisition of tenancy rights cannot be determined, the consideration received by reason of surrender of such tenancy rights could not be subjected to capital gain tax.*

35. From the plain reading of the aforesaid judgment, the sequitur is, whether cost of acquisition is inherently incapable of being determined or not, i.e., whether it is possible to envisage a cost of an asset which is capable of acquisition at a cost. The

distinction has been made by the Hon'ble Supreme Court where the asset which is capable of acquisition at a cost would be included in the provisions pertaining to the head "capital gains" as opposed to assets in the acquisition of which no cost at all can be conceived. If cost can be conceived, then it is chargeable under the head 'capital gains'. In this case, whether sale consideration can be conceived or it cannot be conceived at all?

36. In this case there is no dispute about the cost, because assessee had incurred the cost for acquiring of the shares and therefore, there is no dispute regarding cost of acquisition. Here, the assessee did not receive any consideration due to reduction of capital which has resulted into a loss to the assessee. The issue is whether the price can be conceived or not? The price paid by the assessee for acquiring the asset has been reduced to half of the cost of an asset was waived off / extinguished. For example, assessee acquired 100 shares for Rs.1000/- in a company and after reduction of capital of the company, assessee's share was reduced to 50 shares from 100 and share value reduced to Rs. 500/- from Rs.1000/-. What if for reduction of 50 shares instead of getting Rs.10/- per share had assessee received Rs.1/- per share on reduction, can still be said there was no consideration received or consideration is inconceivable; and if assessee has received 'Zero' consideration, then can it be held that there is no conceivable consideration at all or 'Zero' is not a consideration. This precise issue had been answered by the Hon'ble Gujarat High Court in the case of **CIT vs. Jaykrishna Harivallabhdas reported in 231 ITR 108**. In that case assessee

has claimed loss on shares of particular companies under the head 'capital gains' and the case of the assessee was that the company with respect to whose shares of loss had been claim had gone into voluntary liquidation and nothing was distributed by those companies to its members, therefore, the assessee received 'Nil' consideration for his holdings in the companies. The claim of the assessee was that capital loss should have been computed under section 46(2) read with section 48. The Hon'ble High Court observed as under:-

> *Thus assuming the extinguishment of the shareholder's interest on liquidation in the shares held by him as transfer is a necessary assumption accompanying liquidation of company and computation of "Capital gain" as a result thereof, whether income or loss, is a logical conclusion of operation of section 48 in such state of affairs.*
>
> *Ordinarily operating section 45 to consider any transaction to be a transfer of capital asset by any of the modes referred to in section 2(47) apart from the legal fictions created therein, envisage passing of consideration from one hand to another and passing of rights, notwithstanding extinguishment in the hands of the transferor to the transferee, whether in the form of tangible gain or augmentation of the existing rights of others. It was because of this, on liquidation return of corpus to the shareholders, who were otherwise entitled to the same as a matter of right, was not held to be transfer within the meaning of section 2(47), because on extinguishment of their rights in the shares and their having received cash or assets in the place of rights which they held in the shares, no corresponding rights accrue in any one for that consideration. However, once a legal fiction is created to treat the receipt or assets on distribution of liquidation in the hands of a shareholder, it inheres transfer of assets by extinguishment of rights, by the recipient of*

consideration and once that fiction comes into existence it must lead to its logical conclusion in the computation of capital gains in accordance with the provisions of the Act, whether the ultimate result is found to be a gain or loss.

The section creates not merely the charge but directs the taxable income to be computed under the head "Capital gains". The phraseology used by the Legislature is not that cash or value of the assets received by a shareholder on liquidation is to be charged to tax as a capital gains but makes it chargeable under the head "Capital gains" by further providing for computation under section 48 in respect of what is considered as consideration. Along with the charge the entire computation provisions for charging the capital gains are made applicable to such computation. Therefore, extinguishment, partly or fully of the right of the shareholder to surplus [capital asset for the purpose of section 46(2)] is to be treated as transfer and as and when such extinguishment takes place, treating such extinguishment as transfer, the net result of such transfer has to be worked out or computed as per section 48. If the result of such computation under the head "Capital gains" is a positive balance, it is to be added in the total income chargeable to tax augmenting the same. If the balance is negative, it has to be treated under the Chapter titled, "Set off and carry forward losses" in accordance with the provisions to the extent the same are permissible.

Section 48 provides for the mode of computing income under the head "Capital gain". The mode of computation shorn of all technicalities and other complexities is to deduct from the full value of the consideration received or accruing as a result of the transfer of the capital asset, the cost of acquisition of the asset. It does not envisage that in all cases such computation must result in surplus or gains. Section 4 of the Act makes the income computed in accordance with the provisions of the Act subject to tax. Section 46(2) which has also been held to be the charging section for bringing the result of receipts by member of a *company on its liquidation too provides for computation of capital gains in accordance with section 48, for which receipt or value of asset after deducting sum assessed as dividend under section 2(22)(c), if any, is to be deemed to be the full value of the consideration. Entire receipt or value of asset has not been subjected to charge, but what has been subjected to tax is event of a receipt on liquidation of a company giving rise to capital gain, by treating it to be consideration. Consideration in the ordinary sense means something in lieu of or exchange of. It does not provide, that on computation of capital gain as per section 48, the surplus if any only is to be charged to tax as capital gains. This is how it was suggested to us to read the provision. On the contrary, the provision in question section 46(2) does not provide any such further inhibition against treatment of the balance. Such balance resulting as per computation made in accordance with section 48 has to be subjected to charge of tax as per the provisions of the Act. Section 71 of the Act envisages where computation under any head of income is a loss, the assessee is entitled to set off such loss against computation of income assessable under other head for that year. Section 74 specifically provides that where in respect of any assessment year, the net result of computation under the head "Capital gains" is a loss to the assessee, the same may be carried forward, if it cannot be set off against income of that year. Thus the computation of income under any head, including under the head "Capital gain", envisages a situation where such computation may result in negative balance or loss. In other words, computation of income chargeable to tax includes computation of loss as well, for the purpose of levy of tax in accordance with the provisions of the Act and to be treated accordingly. There is nothing in the provision of section 46(2) which excludes the applicability of other provisions of the Act dealing with set off and carry forward of loss under any head of income to the computation of income chargeable to tax under the head "Capital gains" under it.*

Viewed from the aforesaid angle, one must reach the conclusion that as on the date, the affairs of the company are fully wound up and the entitlement of the shareholder to any return of its capital comes to an end, any disbursement made to a shareholder either by way of cash or asset has to be treated in the hands of the recipient shareholder as the full value of consideration on deemed transfer of his capital asset, as a result of extinguishment of all rights has to be deemed to be resulting in capital gain or loss, as the case may be, as per the result of computation made under section 48 of the Act. Though the value of the asset has to be taken at its market value as on the date of actual receipt as a result of joint reading of section 46(2) and section 55(2)(b)(iii) of the Act which provides for determination of cost of acquisition in the hands of the recipient for determination of capital gains in his hands whenever he transfers such asset after its receipt by him.

The contention that this provision should apply to actual receipts only also cannot be accepted for yet another reason, because acceptance of that would lead to an incongruous and anomalous result as will be seen presently. The acceptance of this view would mean whereas even in a case where a sum is received, howsoever negligible or insignificant it may be, it would result in the computation of capital gains or loss, as the case may be, but in a case where nothing is disbursed on liquidation of a company the extinction of rights, would result in total loss with no consequence. That is to say on receipt of some cost, however insignificant it may be, the entire gamut of computing capital gains for the purpose of computing under the head "Capital gains" is to be gone into, computing income under the head "Capital gains", and loss will be treated under the provisions of Act, but where there is nil receipt of the capital, the entire extinguishment of rights has to be written off, without treating under the Act as a loss resulting from

computation of capital gains. The suggested interpretation leads to such incongruous result and ought to be avoided, if it does not militate in any manner against object of the provision and unless it is not reasonably possible to reach that conclusion. As discussed above, once a conclusion is reached that extinguishment of rights in shares on liquidation of a company is deemed to be transfer for operation of section 46(2) read with section 48, it is reasonable to carry that legal fiction to its logical conclusion to make it applicable in all cases of extinguishment of such rights, whether as a result of some receipt or nil receipt, so as to treat the subjects without discrimination. Where there does not appear to be ground for such different treatment the Legislature cannot be presumed to have made deeming provision to bring about such anomalous result.

37. Ergo, the Hon'ble High Court had rejected the contention of the Revenue that the provision of capital gain should apply to actual receipts only cannot be accepted because it would result into incongruous and anomalous results because in case even where negligible or insignificant sum received, it would result in computation of capital gain or loss but in case where nothing was disbursed or received on extinguishment of rights will not result in loss cannot be upheld. The Hon'ble High Court even held that even where there is a 'nil' receipt of the capital, the entire extinguishment of rights has to be written off as a loss resulting from computation of capital gains. Thus, once a conclusion is reached that extinguishment of rights in shares is deemed to be transferred for operation of section 46(2) read with section 48, it is reasonable to carry that legal fiction to its logical

conclusion to make it applicable in all cases of extinguishment of such rights, whether as a result of some receipt or nil receipt. The said ratio of the Hon'ble Gujarat High Court is clearly applicable on the facts of the present case also because there could be no distinction where assessee receives some negligible or insignificant consideration and where assessee had received 'Nil' consideration. This judgment and the ratio clearly clinch the issue in favour of the assessee.

38. Thus, in view of the ratio and principle laid down in the aforesaid judgments, we hold that:

- *firstly*, in this case the reduction of capital is extinguishment of right on the shares and it amounts to transfer within the meaning and scope of section 2(47);
- *secondly*, the loss on reduction of shares is a capital loss and not notional loss; and
- *lastly*, even when assessee has not received any consideration on reduction of capital but its investment has reduced to loss resulting into capital loss and while computing the capital gain, capital loss has to be allowed or set-off against any other capital gain.

39. The entire case of the Revenue is hinges upon the judgment of ITAT Special Bench in the case of **Bennett Coleman & Co. Ltd. (supra)**. In the facts of that case assessee was holding investments in equity shares of another company wherein the paid-up capital was reduced to Rs. 5/- from Rs. 10/- per share and subsequently, two equity shares of Rs 5/- each were

consolidated into one equity share of Rs. 10/- each. The holders of the original shares received new shares. Thus, it was a case of substitution of shares which is not the facts in the present case. This distinction on the facts as a Special Bench have been dealt by the ITAT Mumbai Bench in the case of Carestream Health INC vs. DCIT (2020) (ITA No. 826/Mum/2016). The majority judgement held that though the loss arising to the shareholder on account of reduction in share capital cannot be subject to the provision of Section 45 r.w.s. 48 and accordingly, the said loss is not allowable as a capital loss at best such loss can be described as notional loss, after relying to the decision of the Hon'ble Supreme Court in the case of B.C. Srinivasa Shetty (supra). However, they noted that in that case assessee had not suffered any loss of reduction of share capital because share had not been canceled but only number of shares had been reduced which was replaced by another set of shares and assessee's percentage of shareholding of 74.9% immediately before reduction of share capital and after such reduction remain same. Such capital has been reduced not only in the case of the assessee but also for all the shareholders of TGM. As per the minority judgment, the Hon'ble Accountant Member held that reduction of capital of a company by any more has the effect of reducing the liability of the company but its shareholder to the extent of the capital reduced and shareholders whose capital has been reduced is deprived of its right to receive that part of the share capital which has been so reduced and therefore, the consequence which follow of such reduction is loss.

40. One very important proposition which was highlighted in the dissenting judgment that, line of distinction needs to be drawn between cases in which the cost of acquisition or for that matter any other component of section 48 is incapable of ascertainment and cases in which it is ascertained as zero. If the cost of a capital asset cannot be identified or conceived due to the nature of such capital asset, its transfer does not lead to any profits or gain arising under section 45(1) except where such capital asset is covered under section 55(2). Where the cost of acquisition is nil the transfer of the capital asset would attract the applicability of section 45. The ratio of B. C. Srinivasa Setty would have no role to play, in other words, the charge under section 45 shall be attracted in all in which the cost of acquisition or full value of consideration is conceivable or ascertainable but is nil. On the reduction of capital, TGL did not pay anything to the assessee. Thus, the assessee received nil consideration it was not a case in which the full value of consideration is incapable of ascertainment. The full value of consideration was fully ascertained and identified as nil and was liable to be taken into consideration for the purposes of computing loss under section 45 at Rs. 22.21 crores. However, the ratio of the majority judgement can be interpreted against the assessee as it clearly held that reduction of shares where no consideration is received computation of capital gain and loss cannot be made, even though facts were different in that case.

41. However, we are not relying upon the minority judgment but we have to bear in mind that this is a case under revisionary jurisdiction u/s.263 wherein the ld. PCIT has cancelled the order of the ld. AO who has accepted the long term capital loss. The dissenting judgment goes to show that it is possible view and therefore, if a view has been taken by the AO in favour of the assessee, then it could not be held that order of AO is erroneous and therefore, can be set aside or cancelled. In any case we have already noted the judgment and the ratio of Hon'ble Gujarat High Court in the case of **CIT vs. Jaykrishna Harivallabhdas(supra)** wherein, similar proposition has been upheld that even if the sale consideration is 'Nil' then also computation of capital gain can be made and accordingly, we are following the judgment of Hon'ble Gujarat High Court upon the majority judgment given by ITAT Special Bench in the case of Bennett Coleman & Co. Ltd. Accordingly, we hold that AO has rightly allowed the computation of long term capital loss to be set off against the capital gain shown by the assessee, consequently order of Ld. PCIT u/s 263 is set aside. Accordingly, on merits, appeal of the assessee is allowed.

42. In the result, appeal of the assessee is allowed.

Order pronounced on 23rd January, 2024.

Sd/-	**Sd/-**
(GAGAN GOYAL)	**(AMIT SHUKLA)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Mumbai; Dated 23/01/2024

KARUNA, *sr.ps*

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent.
3. CIT
4. DR, ITAT, Mumbai
5. Guard file.

//True Copy//

BY ORDER,

(Asstt. Registrar)
ITAT, Mumbai