

आयकर अपीलीय अधिकरण, 'सी' न्यायपीठ, चेन्नई
IN THE INCOME TAX APPELLATE TRIBUNAL, 'C' BENCH, CHENNAI
श्री न्यायाधीश पी.पी. भट्ट, अध्यक्ष एवं श्री जी.मंजुनाथ, लेखा सदस्य के समक्ष
BEFORE SHRI JUSTICE P.P.BHATT, PRESIDENT
AND SHRI G. MANJUNATHA, ACCOUNTANT MEMBER

I.T.A.No.1816/Chny/2019
(निर्धारणवर्ष / Assessment Year: 2016-17)

M/s. Sindya Securities and Investments Pvt.Ltd., 609, Lakshmi Bhavan, 5 th floor Sundaram Avenue, Mount Road, Nungambakkam, Chennai-600 034.	Vs	The Assistant Commissioner of Income Tax, Corporate Circle-6(2), Chennai.
PAN: AALCS 3297B		
(अपीलार्थी/Appellant)		(प्रत्यर्थी/Respondent)

अपीलार्थीकीओरसे/ Appellant by	:	Mr. T.Banusekar, C.A
प्रत्यर्थीकीओरसे/Respondent by	:	Mr. Abani Kanta Nayak, CIT

सुनवाईकीतारीख/Date of Virtual hearing	:	09.12.2020
घोषणाकीतारीख /Date of Pronouncement	:	04. 03.2021

आदेश / ORDER

PER G.MANJUNATHA, AM:

This appeal filed by the assessee is directed against the order of the learned Commissioner of Income Tax (Appeals)-15, Chennai dated 29.04.2019 and pertains to assessment year 2016-17.

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

“1. For that the order of learned CIT(A) is contrary to law, facts and circumstances of the case to the extent prejudicial to the interest of the assessee and at any rate is opposed to the principles of equity, natural justice and fair play.

2. For that the Commissioner of Income Tax (Appeals) failed to appreciate that the order of the Assessing Officer is without jurisdiction.

3 For that the Commissioner of Income Tax (Appeals) failed to appreciate that order of assessment is bad in law.

4. For that the Commissioner of Income Tax (Appeals) failed to appreciate that no opportunity of being personally heard was provided to the appellant during the course of assessment proceedings.

5. For that the Commissioner of Income tax (Appeals) erred in upholding the addition of ₹17,46,25,000/- u/s.56(2)(viib).

6. For that the Commissioner of Income Tax (Appeals) failed to appreciate that the provisions of section 56(2)(viib) are not invocable in the facts and circumstances of the appellant's case.

7. For that the Commissioner of Income tax (Appeals) failed to appreciate that the provisions of section 56(2)(viib) are invocable only when the consideration for issue of shares exceeds the face value of shares and not when they are issued at face value.

8. For that the Commissioner of Income tax (Appeals) failed to appreciate that the appellant did not receive any consideration excess of the face value of shares issued.

9. For that the Commissioner of Income Tax (Appeals) having accepted that the shares have been allotted at face value, failed to appreciate that the provisions of section 56(2)(viib) are thus not invocable.

10 For that the Commissioner of Income Tax (Appeals) failed to appreciate that the Assessing Officer cannot determine the face value of a share under any provisions of the Income Tax Act.

11. For that the Commissioner of income Tax

(Appeals) failed to appreciate that the Assessing Officer erred in concluding that the face value of the preference shares was fixed at an exorbitant price, without any basis in order to circumvent the provisions of section 56(2)(viib).

12. For that the Commissioner of Income Tax (Appeals) erred in not considering the explanations and submissions provided by the appellant.

13. For that the appellant objects to the levy of interest u/s.234B and 234C.”

3. Brief facts of the case are that the assessee company is engaged in the business of investment activities filed its return of income for the assessment year 2016-17 on 17.10.2016 declaring Nil total income. During the year under consideration, the assessee had issued 17,500 preference shares at face value of ₹ 10,000/- each to M/s. Kalpatharu Infrastructure Development Company Pvt. Ltd. The case was taken up for scrutiny and during the course of assessment proceedings since there is increase in share capital, the Assessing Officer called upon the assessee to file necessary details including allotment of preference shares etc. In response, the assessee vide letter dated 06.12.2018 submitted that it has issued 17,500 preference shares with face value of each ₹ 10,000/- to M/s. Kalpatharu Infrastructure Development Company Pvt. Ltd. for

a total consideration of ₹ 17.50 crores and such share capital has been raised to repay the existing loan liability of the company. The assessee further submitted that provisions of section 56(2)(viib) of the Act, has no application, because the assessee has not issued shares at premium over and above face value of such shares. Therefore, there is no question of application of provisions of section 56(2)(viib) of the Act, to consider excess consideration as income of the assessee. The Assessing Officer, however, was not convinced with the explanation of the assessee and according to him, transactions between the assessee and M/s. Kalpatharu Infrastructure Development Company Pvt. Ltd. is not a simple commercial transaction of raising share capital, because the assessee has issued preference shares at face value of ₹ 10,000/- per share, whereas face value of equity shares was fixed at ₹ 10/- per share. Further, fair market value of share as on date of issue was at Rs. 4.73, which is far lower than the face value fixed by the assessee. The Assessing Officer further noted that although the provisions of Companies Act, 2013 requires to specify the purpose of issue of preference shares and also requires basis for fixation price, but the assessee has not substantiated face value of

preference shares at ₹ 10,000/- per share, when the asset base of the company is not supporting such valuation. The Assessing Officer further was of the opinion that the assessee has also failed to furnish confirmation letter from person who has invested in share capital. The Assessing Officer has discussed the issue at length in light of shareholding pattern of the assessee company and investor company and their business relationship to come to the conclusion that the assessee has not established that transaction is commercial transaction which passed the test of genuineness in order to simply consider under the provisions of section 56(2)(viib) of the Act. Therefore, he opined that excess consideration received on allotment of preference shares over and above fair market value of shares as on date of allotment is unexplained income of the assessee and accordingly, brought to tax u/s.56(2)(viib) of the Act.

4. Being aggrieved by the assessment order, the assessee preferred an appeal before the learned CIT(A) . Before the learned CIT(A), the assessee reiterated its submissions made before the Assessing Officer and argued that the provisions of section 56(2)(viib) of the Act has no application when shares are issued at

face value, therefore, merely for the reason that face value of preference shares is higher than fair market value of shares as per book value, the Assessing Officer cannot consider it as sham transaction and further, cannot hold that assessee has structured transaction to circumvent the provisions of section 56(2)(viib) of the Act. The learned CIT(A), after considering relevant submissions of the assessee and also by analysis of the financials of assessee company came to the conclusion that receipt of share capital by allotment of preference shares with face value of ₹ 10,000/- per share is not based on realistic valuation and therefore, genuineness of the same is doubtful and unacceptable. The learned CIT(A) further noted that from the financials submitted by the assessee shares were overvalued at the time of allotment of share capital without considering the actual potential of the company. The learned CIT(A) has discussed the issue at length in light of various facts including financials of the company and held that assessee has artificially enhanced face value of preference shares to circumvent the provisions of section 56(2)(viib) of the Act and hence, it can be fairly held that transactions between the assessee and the investor for raising share capital is not a commercial transaction but a sham

transaction to overcome the tax liability on account of excess amount received for allotment of shares. Therefore, he opined that excess consideration received in the form of share capital over and above fair market value has to be assessed u/s. 56(2)(viib) of the Act. Aggrieved by the learned CIT(A) order, the assessee is in appeal before us.

5. The learned AR for the assessee submitted that learned CIT(A) has erred in law, facts and circumstances of the case while confirming additions made by the Assessing Officer towards consideration received for allotment of preference shares over and above fair market value of shares as on date of value without appreciating the fact that the provisions of section 56(2)(viib) of the Act will come into operation only in a case where shares has been issued at a premium over and above face value of such shares. The AR further submitted that in this case assessee has issued non-convertible cumulative preference shares with face value of ₹ 10,000/- each without any premium, therefore, question of application of the provisions of section 56(2)(viib) of the Act is misplaced. He further submitted that although the Assessing Officer has given various reasons to consider transactions of issue of

shares is not a commercial transaction, but if you consider the manner in which share capital has been raised by assessee and purpose of raising share capital there should not be any doubt of whatsoever as considered by the Assessing Officer, because assessee has fulfilled all conditions prescribed under the Companies Act, 2013 and rules made thereunder for issue of preference shares. The assessee has also furnished necessary evidences including financials of subscriber to share capital and explained that transaction between the parties is a genuine commercial transaction and purpose of issue of shares is to clear existing debt of the company. Further, the assessee has redeemed preference shares in subsequent financial year out of call option money received, therefore, reasons given by the Assessing Officer to arrive at a conclusion that transaction is not a simple commercial transaction is purely on suspicious and surmises manner without any evidences.

6. The learned DR, on the other hand, supporting the order of learned CIT(A) submitted that the Assessing Officer as well as learned CIT(A) has brought out various facts to come to the conclusion that transaction of issue of preference shares is not a

commercial transaction between the parties, but an arranged transaction to circumvent the provisions of section 56(2)(viib) of the Act. Therefore, arguments of the assessee that it is a genuine transaction for raising share capital for the purpose of business of the company are incorrect. The learned DR drew our attention to page 22 of the paper book 1, in which under Note 13, the assessee has made disclosure about regulatory investigation in 2G scam and PMLA and argued that the assessee is part of 2G scam and the assessee had investment in M/s.Deccan Digital Networks Pvt.Ltd. to the extent of 74% of equity share capital, which in turn held 35% share capital of Aircel Ltd. From the above, it is clear that entire preference shares transaction is sham transaction. The DR further submitted that it is surprising how a company having negative results received funds from M/s. Kalpatharu Infrastructure Development Company Pvt. Ltd. by paying such a huge value for preference shares without any support of asset or business. The DR further submitted that manner in which preference shares are issued and conditions of issue of shares give rise to various doubts and hence, reasoning given by authorities below including learned CIT(A) are on sound footing, which clearly shows that transaction of

issue of preference shares is sham transaction and accordingly, invoked the provisions of section 56(2)(viib) of the Act.

7. Per contra, the learned A.R for the assessee submitted that although the learned DR referred to regulatory investigation under 2G scam and PMLA, but it is neither the contention of the Assessing Officer nor learned CIT(A) that transaction is sham. Further, the Hon'ble Supreme Court decision in the case of McDowell's is on impermissible tax avoidance arrangements and the same is not applicable to the case of the assessee, because the assessee has merely issued preference shares at par and redeemed the same at cost in the next year. The AR further submitted that the allegation of the learned DR that share price fixed for issue of preference shares is not backed by any asset / business of the assessee is incorrect, because the assessee has issued preference shares to M/s. Kalpatharu Infrastructure Development Company Pvt. Ltd. in order to raise funds to repay loan from Directors, who had settled dues to bank which originally funded the investment made by the assessee in equity shares of M/s.Deccan Digital Networks Pvt. Ltd. Therefore, it is incorrect to say that assessee has structured transaction to circumvent the provisions of section 56(2)(viib) of the Act.

8. We have heard both the parties, perused the material available on record and gone through orders of the authorities below. The Assessing Officer has made additions towards excess consideration received for allotment of preference shares over and above fair market value of such shares as on the date of issue on the ground that assessee has not explained and filed necessary evidence to justify face value of preference shares at ₹ 10,000/- per share. Therefore, in order to verify the issue, it is necessary to consider the provisions of section 56(2)(viib) of the Act and its application to the relevant transactions. The provisions of section 56(2)(viib) of the Act was introduced by Finance Act, 2012 w.e.f. 01.04.2013 to bring into tax consideration for issue of shares that exceeds face value of such shares as income of the assessee. A plain reading of section 56(2)(viib) makes it very clear that if a company in which public are not substantially interested issued share capital and received consideration in excess of face value of such shares, then aggregate consideration received over and above fair market value of such shares is assessable as income of the assessee. In other words, in order to invoke section 56(2)(viib) of the Act, shares should be issued over and above face value of such shares. In this

case, the assessee has issued shares at face value of ₹ 10,000/- per share. Therefore, in a simple term the provisions of section 56(2)(viib) has no application, if shares are not issued with premium. But, the case of the Assessing Officer was that it is not a case of simple commercial transaction between the parties, but a transaction arranged to circumvent the provisions of section 56(2)(viib) of the Act. The Assessing Officer, to arrive at such conclusion has given various reasons including the manner in which such shares were issued and terms & conditions of issue of such shares. Therefore, it is essential to see whether transaction of issue of preference shares is commercial transaction between two prudent persons or a sham transaction arranged by parties to overcome the provisions of section 56(2)(viib) of the Act.

9. The assessee has issued 17,500 preference shares at face value of ₹ 10,000/- each in financial year 2015-16 to M/s. Kalpatharu Infrastructure Development Company Pvt. Ltd. Admittedly, the assessee and M/s. KIDCO are related parties, because both the companies are having common directors and functioning in same premises. Further, assessee share capital was

originally consisting of equity shares alone, however, assessee has amended its share capital clause in Memorandum of Association vide AGM held on 2.1.2014, where share capital has been divided into equity shares and preference shares. Further, the assessee has retained face value of equity shares at ₹ 10/- per share, but face value of preference shares has been fixed at ₹ 10,000/- per share. Admittedly, at the time amendment to share capital and also at the time of issue of preference shares, net worth of assessee company was negative, which is evident from the fact that the Assessing Officer has computed negative face value of ₹ -4.73 per share. Therefore, in this factual background, if you examine the amendment carried out to share capital clause and fixation of face value of 10,000 equity shares, certainly doubt arises about the manner in which such share capital was amended and face value of preference shares was fixed. Admittedly, except certain privileges including first preference over dividend and repayment of capital, there are no special privileges to preference shareholders. Therefore, while examining allotment of preference shares, this factor needs to be considered. Moreover, provisions of section 55 of the Companies Act, 2013 and Rule 9 of Companies (Share capital

and Debentures) Rules, 2014 deals with issue and redemption of preference shares, as per which before issue of preference shares assessee should specify purpose of issue of preference shares and also justify the value of such shares. In this case, the assessee has justified purpose of issue of preference shares as per which preference share capital was raised to repay the existing debt of the company, but the assessee has not explained the basis for fixing face value of preference shares at ₹ 10,000/- per share, although Rule 9 of Companies (Share capital and Debentures) Rules, 2014 says so. Therefore, it is very essential to decide whether assessee has justified basis of fixing share price of preference shares at ₹ 10,000/- or not, more particularly, when the financials of the company was not supporting such valuation. Admittedly, the assessee was having negative net worth and there is no significant business activity except investments in equity shares of M/s.Deccan Digital Networks Pvt. Ltd. In fact, a major share capital of the company has been invested in M/s.Deccan Digital Networks Pvt.Ltd. Further, M/s.Deccan Digital Networks Pvt. Ltd had invested in equity shares of M/s. Aircel Ltd. It is an admitted fact that that Aircel Ltd. is almost a defunct company. Further, it is well known fact that

investment of Assessee Company in the shares of M/s.Deccan Digital Networks Pvt. Ltd is not having any value or valuation. Therefore, under these circumstances, fixing share price at ₹ 10,000/-per preference share is not based on any scientific method or method prescribed under Rule 11UA of Income Tax Rules, 1962. Further, the assessee has not filed any valuation report or evidence to justify value of shares. The assessee has also not explained basis for fixing different share price for equity shares and preference shares. The assessee has also not filed any evidence to explain how a prudent businessman would invest in a company, where its net worth is negative and book value of shares is far less than the face value of preference shares. Therefore, under these circumstances, it is very difficult to accept the arguments of the assessee that transaction of issue of preference shares is a normal commercial transaction and purpose of raising capital is for genuine business purpose of the company. We, further, are of the considered view that from sequent of events and manner in which preference share capital was raised, including terms of repayment, rate of return and period of shares, it can be easily concluded that transaction of issue of preference share capital is arranged

transaction in the nature of sham transaction to overcome the amended provisions of section 56(2)(viib) of the Income Tax Act, 1961. In this regard it is very essential to recollect the land mark decision of Hon'ble Supreme Court in the case of *Mc Dowell & Co Ltd. Vs Commercial tax Officer*(1985) 154 ITR 148, where it was held that *the tax planning may be legitimate provided it is within the framework of law. Colourable devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honourable to avoid the payment of tax by resorting to dubious methods. It is the obligation of every citizen to pay the taxes honestly without resorting to subterfuges. Courts are now concerning themselves not merely with the genuineness of a transaction, but with the intended effect of it for fiscal purposes. No one can now get away with a tax avoidance project with the mere statement that there is nothing illegal about it. The Hon'ble Court further observed that it is neither fair nor desirable to expect the Legislature to intervene and take care of every device and scheme to avoid taxation. It is up to the Court to take stock to determine the nature of the new and sophisticated legal devices to avoid tax and consider whether the situation created by the devices could be related to the existing legislation with the aid of 'emerging' techniques of interpretation was done in *Ramsay, Burma Oil and Dawson*, to expose the devices for what they really are and to refuse to give judicial benediction.*

10. In this view of the matter and considering facts and circumstances of the case, we are of the considered view that assessee has failed to explain and justify issue of preference shares with a face value of ₹ 10,000/- per share when the fair market value of the shares of the company is ₹ -4.73 per share. Therefore, we are of the considered opinion that the reasons given by the Assessing Officer to treat the transaction as a colourable device to circumvent the provisions of section 56(2)(viib) of the Act, appears to be on sound footing. Hence, we are inclined to uphold the order of the learned CIT(A) in upholding additions made towards excess consideration received towards allotment of preference shares over and above the fair market value of shares under section 56(2)(viib) of the Act and dismiss appeal filed by the assessee.

11. In the result, appeal filed by the assessee is dismissed.

Order pronounced in the open court on 4th March, 2021

Sd/-
(न्यायाधीश पी.पी. भट्ट)
(Justice P.P.Bhatt)
अध्यक्ष/ President

चेन्नई/Chennai,
दिनांक/Dated 4th March, 2021
DS

Sd/-
(जी.मंजुनाथ)
(G. Manjunatha)
लेखा सदस्य / Accountant Member

आदेश की प्रतिलिपि अग्रेषित/Copy to:

1. Appellant
2. Respondent
3. आयकर आयुक्त (अपील)/CIT(A)
4. आयकर आयुक्त/CIT
5. विभागीय प्रतिनिधि/DR
6. गार्ड फाईल/GF.