IN THE INCOME TAX APPELLATE TRIBUNAL,
MUMBAI BENCH "K", MUMBAI

BEFORE SHRI RAJESH KUMAR, ACCOUNTANT MEMBER AND
SHRI RAM LAL NEGI, JUDICIAL MEMBER

ITA No.1942/M/2015
Assessment Year: 2010-11

M/s. Aaradhana Realities Ltd. (Formerly known as Essar Investments Ltd.) Manickam Complex, Ground Floor, 1/3, General Patters Road, Chennai, Tamilnadu- 600 002 **PAN: AABCE0686Q**	Vs.	ACIT 6(2)(2), Aayakar Bhavan, M.K. Road, Mumbai - 400020
(Appellant)		(Respondent)

Present for:

Assessee by : Shri Nishant Thakkar, A.R.
Shri Hiten Chande, A.R.
Ms. Jasmin Amalsadvala, A.R

Revenue by : Shri Sunil Deshpande, D.R.

Date of Hearing : 11.12.2020
Date of Pronouncement : 08.01.2021

O R D E R

Per Rajesh Kumar, Accountant Member:

The present appeal has been preferred by the assessee against the directions vide order dated 29.12.2014 of the Dispute Resolution Panel-I [hereinafter referred to as the DRP] relevant to assessment year 2010-11 in the matter of assessment order dated 30 January 2015 under section 143(3) r.w. section 144C(13) of the Act..

2. The grounds raised by the assessee are as under:

"1. The Assessing Officer ("AO") has erred in assessing the Appellant's total income at Rs.247,79,28,937/- as against the returned loss (as per the revised

return of income) of Rs.86,37,46,423/-.

2. The AO, under the directions of the Dispute Resolution Panel ("DRP"), has erred in making a Transfer Pricing ("TP") adjustment of Rs.321,30,00,000/- on account of the Arm's Length Price (ALP) of the shares subscribed and another TP adjustment of Rs.2,33,000/- on account of the ALP of the shares purchased.

3. The AO, under the directions of the DRP, has erred in not appreciating that the subscription / purchase of shares by an assessee results in capital investment with no income arising from such transaction and therefore Transfer Pricing provisions are not applicable.

4. The AO, under the directions of the DRP, has erred in considering the subscription to shares as an international transaction covered under Clauses (i)(b) and (i)(c) of the Explanation under section 92B of the Act.

5. The AO, under the directions of the DRP, has erred in making the adjustment with respect to the subscription to / purchase of equity shares by rejecting the certificates obtained from independent valuers and not accepting the economic analysis undertaken by the Appellant in accordance with the provisions of the Act read with the Income Tax Rules, 1962.

6. The AO, under the directions of the DRP, has erred in not accepting the value at which the shares were subscribed / purchased by the Appellant from the AE, which was valid as per the regulations of the Reserve Bank of India.

7. The DRP has erred in upholding the action of the Transfer Pricing Officer (TPO) in the following, whilst determining the value of the shares subscribed by the Appellant, as per the Discounted Cash Flow (DCF) method:

(a) considering the Beta value of equity at 1.27 and equity market risk premium at 10.5%, while working out the cost of equity;

(b) considering the Discount factor / WACC at 11.72% for the purpose of computing the present value of free cash flows during the explicit period and the terminal value;

(c) considering the terminal value at Rs.965,84,05,547/-;

8. The DRP has erred in confirming the transfer pricing adjustment of Rs.183,01,50,853/- as per the TPO, towards the difference between the value at which the shares were subscribed by the Appellant and the value at which they were transferred to a third party later, as an alternative benchmarking of the shares subscribed.

9. While arriving at the ALP of the shares subscribed by the Appellant, the AO under the directions of the DRP, has erred in not considering the arithmetic mean of (a) the price arrived at as per DCF method and (b) the actual sale price as per the later transaction with a third party, both of which are considered as Comparable Uncontrolled Prices ("CUP"), as per the Proviso to Section 92C(2) of the Act.

10. The DRP has erred in holding that the transaction of subscription of shares and their sale during the year is a sham transaction and thus directing that the entire short term capital loss of Rs. 183,06,38,227/- be disallowed, as a third alternative.

11. The AO has erred in adding the amount of the TP adjustment of Rs.2,33,000/- on the value of the purchase of shares to the taxable income, contrary to the

directions of the DRP.

12. The AO has erred in computing the long term capital gain at Rs. 162,56,53,076/- as against a sum of Rs. 162,06,09,906/- as per the return of income and as accepted in the draft assessment order.

13. The AO, under the directions of the DRP, has erred in making a disallowance of the expenditure on leave encashment of Rs.1,44,60,288/- u/s.43B of the Act.

14. The AO has erred in not giving set-off of the brought forward loss / unabsorbed depreciation of earlier years against the income computed for the year.

15. The AO has erred in adding a sum of Rs.321,32,33,000/- towards the TP adjustment and another sum of Rs.3,21,62,602/- towards the provision for leave encashment to the net profit the Appellant, for working out the book profit u/s.115JB of the Act.

16. The AO has erred in adding a sum of Rs.183,01,50,853/- towards the TP adjustment and another sum of Rs.3,21,62,602/- towards the provision for leave encashment to the net profit of the Appellant, for working out the book profit u/s.115JB of the Act, under the alternative computation of income on protective basis.

The above grounds are without prejudice to each other. The Appellant craves leave to add any other ground(s) and / or modify or delete any of the above grounds before or during the course of hearing before the Hon'ble ITAT."

3. The issue raised in ground No.1 to 10 is against the transfer pricing adjustment of Rs.321,30,00,000 in respect of subscription / purchase of shares of Hybrid Capital Pte. Ltd. which has been upheld by the DRP by affirming the order of TPO on this issue.

4. The facts in brief are that the appellant assessee is a public limited company carrying on the business of promotion of industrial and infrastructural projects and rendering consultancy and business support services. The Appellant filed its return of income for AY 2010-11 on 15.10.2010 declaring loss of Rs. 50,06,18,071/- which was later on revised ion 31.3.2012 declaring loss of Rs. 86,37,46,423/-.

The assessee, inter alia, claimed a loss of Rs. 20.49 crore on account of sale of shares of Hybrid Capital which was net result of sale of 6,00,000 shares comprising 1,00,000 shares yielded a long-term capital gain of Rs. 162,56,53,077 and 5,00,000 shares incurring short-term capital loss of Rs.183,06,38,227/-. Thereafter, the case of the assessee was selected for scrutiny and statutory notices were duly issued and served upon the assessee. The AO after noticing that the appellant assessee has entered into international transactions with associate enterprises exceeding Rs. 15,00,00,000/-, referred the transactions reported by the assessee in audit report in Form 3CEB to Transfer Pricing Officer u/s 92CA(1) of the Act to determine the arm 's length price after obtaining the approval of Commissioner of Income Tax-5 Mumbai. The appellant had invested USD 1,00,000 equivalent to Rs. 45,74,740 1 USD = Rs 45.74) in Hybrid Capital Pte Ltd (hereinafter referred to as "Hybrid Capital"), its wholly owned subsidiary in British Virgin Islands, on 18 November 2005. Hybrid Capital was incorporated to carry on the business of financing and lending outside India. From its inception, Hybrid Capital carried on the business of lending and financing which is evident from the fact that for F.Y. 2006-07, Hybrid capital earned interest income of Rs. 124.69 crore and in F.Y. 2007-08, earned interest income of Rs. 78.10 lakhs .During F.Y. 2009-10, the appellant assessee spotted an opportunity to lend money to an overseas borrower namely Arya Infrastructure Holdings Limited (hereinafter referred to as "Arya Infrastructure"). However, section 6(3)(d) of Foreign Exchange Management Act, 1999 ("FEMA") read with

Regulation — 5 of Borrowing or lending in Foreign Exchange Regulations, 2000 prohibits an Indian resident to lend directly in foreign exchange to a person outside India. Since that Hybrid Capital was in the business of lending, the appellant decided to encash and make good the above referred opportunity by infusing the funds available with it Rs. 998,79,87,374/- into Hybrid Capital by way of equity contribution in accordance with the provisions of FEMA. The above referred infusion was effected beginning with June 2009 and ending in January 2010, aggregating to USD 212,836,000 equivalent to Rs. 998,79,87,374 towards share capital. Since Hybrid Capital was the appellant's wholly owned subsidiary and would continue to remain so even after the infusion, the number of shares to be issued did not really matter. However, to comply with the requirement under FEMA, the shares were valued on the basis of the Discounted Cash Flow method ("DCF method") taking into consideration the future earnings after infusion of the fresh capital of USD 212,836,000. As per the Valuation Report dated 12 February 2010, the value per equity share of Hybrid Capital was arrived at Rs. 20,550/- and for the sake of convenience it was decided to issue 5,00,000 shares to the appellant assessee at a price of Rs. 19,975/- per share. Equity Shares against this investment of USD 212,836,000 equivalent to Rs. 998,79,87,374/- were allotted by Hybrid Capital to appellant on 17 Feb 2010 at Face Value of USD 1 at a premium of USD 424.67. Hybrid Capital would continue to remain a 100% subsidiary of the appellant. Thus number of shares issued against the infusion of fresh

capital was wholly irrelevant and did not matter. It is only for convenience purposes that 5,00,000 shares was issued to the assessee in the wholly owned subsidiary. What is relevant here is the enterprise value arrived and that would remain constant whether 5,00,000 shares were issued, or 10,00,000 shares were issued. Hybrid Capital, in turn, lent the money infused by way of capital in it by the assessee to Arya Infrastructure on interest at 12% p.a. which is evident from Hybrid's balance sheet as on 15 March 2010 which showed balance of loans and advances at USD 214,201,860. Hence, the whole of the equity infusion of USD 212,836,000 was lent out to Arya Infrastructure.

5. During the year, Hybrid Capital earned interest from Arya of USD 9,101,781 equivalent to Rs. 43,13,94,079/- which comes to 12% p.a. The above interest income is duly reflected in the profit & loss account for the year in the accounts of the Hybrid Capital. From the interest earned of USD 9,101,781, Hybrid Capital paid a dividend of USD 6,000,000 equivalent to Rs. 28,43,80,000 to the appellant. Such dividend was duly offered to tax by appellant in its return of income. On 17 March 2010, appellant sold its entire stake (i.e. 100% shares) in Hybrid Capital to Arya Infrastructure at a value of USD 215,000,000 taking into consideration the Net Asset Value of Hybrid Capital as on 15 March 2010.It is pertinent to note here that the appellant earned USD 2,064,000 as gains on sale of shares and USD 6,000,000 as dividend declared by the Hybrid Capital out of interest earned. The gain of USD 2,064,000 on the sale of shares became capital loss upon conversion and was reported

as capital loss in its Return of Income due to foreign exchange fluctuation. This is explained as below:

a. On sale of shares of Hybrid Capital, the Appellant made a gain of USD 2,064,000 (USD 215,000,000— USD 212,936,000) which is equivalent to Rs. 9.39 crores (1USD = Rs. 45.53 INR).

b. However, the Appellant reported a Rs.20.49 crores loss in its return of income.

c. The Appellant submits that a gain of Rs. 9.39 crores converted to a loss of Rs.20.49 crores only on account foreign exchange fluctuation, i.e. because Re. appreciated vis-à-vis. the Dollar by Rs. 1.40 between the date of investment and the date of sale. This can be seen from what follows:

Gain on sale of Shares USD 2,064,000 (1USD =45.53) Rs. 9.39 crores	
Exchange rate difference (Rs. 1.40/USD * 212,836,000 USD)	Rs. (29.77 crores)
Net Capital loss	Rs. 20.38 crores

Accordingly, while computing capital gains under section 48 of the Act, the Appellant claimed a loss of Rs. 20,49,85,151 (on account of exchange fluctuation and indexation of cost).

6. The TPO passed an order dated 13 January 2014 under section 92CA(3) of the Act holding as under:

- The provisions of Chapter- X are applicable as Explanation to section 92B specifically covers the transaction of purchase of shares by

Associated Enterprise. And. the Appellant itself has reported the transaction of subscription of shares as an international transaction and has benchmarked the same on the basis of a Valuation Report therefore, it is not open to the Appellant to contend that the provisions of Chapter - X do not apply (Para 6.1 (i),(ii),iii) Pg. 3 of TP0's order).

- The Valuation Report dated 12 February 2010 has been obtained after the infusion of money by the Appellant, the valuation of the shares should have been carried out before making the investment therefore, such a valuation report cannot be accepted. Further, the valuation report is not reliable as the Valuer has made valuation report on the basis of certain assumptions and has not carried out the audit of cash flow projections therefore, the Valuation Report was liable to be rejected (Para 6.2(i),(ii) Pg. 5 of TP0's order).

- The arm's length price of the shares of Hybrid was Rs. 13,549/ share as the discounting rate (cost of equity) used by the Valuer of 7.27% is lower than the correct discounting rate of 11.72% (Pg.12 of TP0's order). Accordingly, transfer pricing adjustment of Rs. 321,30,00,000 was required to be made. To arrive at the discounting rate of I I .72%:

  i. The TPO considered market risk premium as 10.5% instead of 6% considered by the Valuer in the Valuation Report while computing cost of equity (Para (ii) Pg. 9,10 of TP0's order)
  ii. The TPO considered beta as 1.27 instead of 1.00 in the Valuation Report while computing cost of equity (Para (i) Pg. 9 of TP0's order)

- Without prejudice to above, the TPO held that CUP method can be applied to benchmark the transaction and took the price of Rs. 16,314/share at which the shares were sold by the Appellant to Arya as the Arm's length price and proposed all alternate transfer pricing adjustment of Rs. 183,01,50,583 (Para 6.5 Pg.12 of TP0's order).

7. Aggrieved by the order of ld TOP, the appellant assessee preferred an appeal before the DRP and the DRP passed an order dated 29 December 2014 upholding the order of the TPO. The DRP in the alternative held that the entire transaction of investing USD 212,836,000 for 5,00,000 shares and subsequent sale of 6,00,00 shares for USD 215,000,000 was orchestrated to generate short term capital loss of Rs. 1 83,06,38,227 on 5,00,000 shares to set off against long term capital gain of Rs. 162,56,53,076 on 1,00,000 shares and

therefore, the entire arrangement was sham and engineered one and was carried out for avoiding tax. The relevant portion of the order of DRP is extracted below for the sake of convenience and ready reference:

> "4.27 Considering the facts on record as well as the submissions of the assessee, the Panel is also of the view that the transaction of subscription of 5,.00,000 shares during the year at an enhanced price of Rs. 19,975/- per share and its sale within one month at an reduced price of Rs. 16314.70 per share is nothing but a design of tax avoidance by booking a loss in the books of the assessee company artificially to set off the Long Term Capital Gain on sale of 1,00,000 shares originally held. The show cause notice for enhancement and the reply of the assessee have already been reproduced at Para 4.9 and 4.10 above. Our finding is based on the following reasoning:
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> a) It is seen that during the year the assessee has purchased 5,00,000 Hybrid shares at a price of Rs,19975.97 per share. Earlier, the assessee was already holding 1,00,000 shares, which were purchased at Rs.45.74 per share. Thus the assessee, as a result held 6,00,000 shares. The 5,00,000 shares subscribed in current year were sold to a third party at Rs.16,314.70 per share to book a net short term capital loss of Rs. 1,83,06,38,227/- in addition to Long Term Capital Gains of Rs. 162,56,53,076/- on sale of original 1,00,000 shares. Just by routing the funds through the bank accounts and passing the entries in its books of accounts, the assessee has created an artificial ST loss which has been adjusted against other income.
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> b) The assessee was requested to furnish the details, documents and discussion amongst the management and the board of EIL that led to the decision of making investment of about Rs.998 crore in Hybrid, and thereafter what went wrong with Hybrid that the decision was made to make investment, and that immediately within 1 month of such investment, as a result of which the management exited Hybrid fully. The assessee was also requested to produce all documents, and files related to above decision making demonstrating the decision making process and considered for decision making. Despite the opportunity being provided no such documents have been produced, and the assessee has only claimed that it was on the basis of commercial prudence. However, the commercial prudence has not been substantiated in any manner. Non production of these documents can only lead to the conclusion that the entire transaction was a sham and the assessee is unable to substantiate its claim regarding the genuineness of the transaction.

c) Memorandum of Understanding dated 26.02.2010, referred to in the agreement for sale dated 17.03.2010 entered between the assessee, Arya Infrastructure Holding Ltd. Mauritius and Hybrid Capital Pte Limited has not been produced before us, although it was called for. Here again, non production of this document can only lead to the conclusion that the entire transaction was a sham and the assessee is unable to substantiate its claim regarding the genuineness of the transaction.

d) During the hearing the assessee was asked to explain the relationship if any between the assessee and Arya Infrastructure Holding Ltd, whether by way of investment in shares, directorships or any other relations between the management of the two companies. Other than stating that there is no relationship between Arya Infrastructure Holding Ltd and the assessee, the assessee has not produced any evidence to justify its position.

e) The assessee was asked to provide documents regarding approval obtained and correspondences made with RBI and other Govt. authorities at the time of subscription and sale of shares of Hybrid. Other than stating that the remittances for investment in Hybrid shares and inward remittances for sale of shares of Hybrid were made under the Automatic Route and that no approval from RBI was required, no documents what so ever have been produced by the assessee. The assessee has not even produced Form ODI filed with RBI regarding these transactions. The documents submitted regarding filings with authorized dealer banks do not prove the genuineness of the transaction.

f) As regards the claim that the sale was a single negotiated transaction and It is not correct to consider part of transaction as valid and other part as invalid, the Panel is of the view that the entire dispute is regarding the tainted transaction of 500000 shares only, regarding which the assessee has not been able to produce the relevant evidences. Hence/the fact that on paper the sale of 600000 shares is shown as a single transaction, it automatically does not make the non genuine transaction in relation to 500000 shares as genuine.

g) The assessee argues that while investing it has relied on the valuer's certificate valuing the same at Rs. 20550 /- per share and, while disinvesting they have considered the NAV of Rs. 16514/- per share. When the assessee had the valuer's report dated 12.02.2010 (assuming for arguments sake to be correct) valuing at Rs. 20550/- per share, there was no reason for it to sell the same at Rs.16314/- per share and book a loss, more so when no prudence in incurring the loss has been demonstrated. On corollary, if the sale was made on the basis of NAV, then even the subscription should have been made on the basis of NAV only. This shows that the entire transaction was only a sham transaction to book the artificial loss to off set the long term capital gains generated on originally held 1,00,000 shares. Reliance is placed on the decision of Hon'ble Supreme Court in the case of Sumati dayal 214 ITR 801(SC), wherein it has been held that 'if *explanation of the assessee is not found satisfactory by the Assessing Officer, acting reasonably, there is a prima facie evidence against assessee and if assessee fails to rebut the same, such unrebutted evidence can be used against him'.* In the present case, the assessee has a valuer's report showing value per share of Rs. 20550/- per share, but sells it at Rs. 16514/-per share and provides no rationale or evidence to justify the same. This would only mean that it is a device to book artificial loss.

4.28 In this regard, attention is drawn to a recent decision of Hon'ble Delhi High Court in the case of **Shiv Raj Gupta in ITA No. 41/2002 dated 22.12.2014**, wherein the Hon'ble High Court has elaborately dealt with the ratios of the decisions in the case of *Vodafone International Holdings B.V. versus Union of India,[2012]* 341 ITR 1 (SC), *McDowell and Co. Ltd. versus Commercial Tax Officer* (1985) 154 ITR 148 (SC) and *Union of India versus Azadi Bachao Andolan* [2003] 263 ITR 706 (SC), and also

dealt with the principles laid down in the case of *IRC v. Duke of* Westminster,[1936 AC 1 (HL)], Ramsay [(1981) 1 All ER 865 (HL)] *Furniss v. Dawson* [(1984) 1 All ER 530 (HL)], *Craven v. White* (Stephen)[(1988) 3 All ER 495 (HL)], and other subsequent decisions in the case of *Ensign Tankers (Leasing) Ltd. versus Stokes* [1992] 1 AC 655. After elaborately considering the ratios of these decisions, the Hon'ble Court at Paras 39 to 54 held as under:

> *39. Expressions "tax avoidance, tax evasion and tax mitigation" are often spoken about, but differently understood. Rule of law mandates and requires a measure of certainty in understanding the said terms. Juristic explications on the subject are indicative of equivocating and divergent stand points. The distinction between the expressions; tax avoidance, tax evasion* and tax *mitigation has been a subject matter of several erudite articles with different perspectives like Morality on Tax Avoidance by Zoe Prebble and John Prebble; Interpretation of Tax Statutes: tax avoidance and the intention of the Parliament by Judith Freedman; Tax Avoidance, Tax Evasion and Tax Mitigation by Philip Baker; and, Corporate Social Responsibility and Tax Avoidance: A comment and reflection by John Hasseldine and Gregory Morris. We acknowledge benefit of exposition and analysis in these articles as we elaborate on the said distinction. Discussion even after Vodafone's case (supra) is reflective that penetrating and perfect clarity of the said terms is not easy to discern and determine. To us the determination and ratio in **Vodafone's** case is clear.*
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> *40. The aforesaid decision in Vodafone's case (supra) does not prescribe criterion simply predicated on preordained, circular or self cancelling transactions with a step or steps having no commercial or business purpose other than obtaining tax advantage. The decision does not exert the doctrine of economic substance. The ratio steers clear from using the said tests or principles. The said propositions and premise as specific tests stands disapproved and rejected.*
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> *41. The precise test enunciated and prescribed as a tenet, negates and disqualifies colourable device, deceiLand sham as a legitimate and acceptable tax event. These terms have some-what ethical and casuistical connotations and are the elective test for differentiating tax planning from abusive tax avoidance.*
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> *42. To appreciate the concept of abusive tax avoidance, it would be appropriate to first delineate with precision the expressions "tax mitigation" and "tax evasion" as their boundaries and confines would enable us to draw lines amongst the four concepts; tax mitigation, tax evasion, acceptable tax avoidance and abusive tax avoidance. Each of the said expressions involves an element of tax planning. It would be hard to conceive of a situation where the assessed does not indulge to some sort of tax planning, be it tax mitigation, acceptable tax avoidance, abusive tax avoidance or tax evasion, "Tax planning", being common to all situations, cannot be the distinguishing feature, but nature and character of the planning and its nexus with the transaction is decisive.*

43. Tax mitigation in simple words would refer to a taxpayer taking advantage or benefit of a beneficent provision under the tax code and complying with the requisites to his lower the tax liability. In the words of Lord Nolan in CIR versus Willoughby [1997] 4 All ER 65, it is:-

> *"The hallmark of tax mitigation, on the other hand, is that the taxpayer takes advantage of a fiscally attractive option afforded to him by the tax legislation and genuinely suffers the economic consequences that Parliament intended to be suffered by those taking advantage of the option".*

The aforesaid quote uses the expression "economic consequences that Parliament intended" which as per some, causes confusion and is self contradictory. However, the said criticism overlooks that if the intention of the Parliament is clear and unambiguous; taking advantage or benefit as envisaged by the provision is a case of tax mitigation. Even in case of debate, when the intention of the Parliament is favourable and adjudication decides the question in favour of the assessee, it would be a case of tax mitigation. Courts are trusted and given the power to determine as to what was the intent of the Parliament while enacting a particular provision.

When the court decision interpreting the legislative intent is in favour of the assessee, there is no avoidance of tax because the conduct is consistent with the taxing provision. If there is no tax avoidance, the question of abusive tax avoidance does not arise, for the latter refers to a particular category of transactions that are unacceptable being pejorative, i.e. sham, colourable device or deceitful and is distinct from tax mitigation. Albeit, where the Parliament's intention is to the contrary and the finding negates the assessee's submission, it would be a case of tax avoidance, whether acceptable or abusive is a different and another matter. Thus, the term "tax mitigation" is simple, intelligible and unequivocal. It is a positive term and refers to the assessed taking benefit or advantage of a provision which the tax code intends and wants to confer, Deductions under Chapter VIA, exemptions under Sections 10A, 10AA, 10B etc. of the Act are all provisions relating to tax mitigation. If an assessee takes benefit or advantage by complying with the stipulated conditions therein to reduce his tax liability, it would be a case of tax mitigation.

44. Tax evasion is illegal and consists of wilful violation or circumvention of applicable tax laws to minimise tax liability. The assessed breaches the relevant law and it involves contumacious behaviour or actual *knowledge of wrong doing. This can happen when an assessee deliberately fails to report an item in the income tax return, or knowingly claims a deduction which he is aware he is not entitled to, or consciously omits to supply information even when there is duty to furnish the said details. It can also apply to situations when the assessee fails to clarify a matter, which has been misunderstood by the income tax authorities, and keeps quiet. In these cases, there is element of wilfulness, dishonesty or contemptuous conduct or even absence of honest belief. If the taxpayer cannot show that*

he had an honest belief that he was not liable to tax or liable to a lower tax, then prima fade such conduct would fall within the ambit/scope of tax evasion.

45. Tax avoidance by elimination would mean the residual and surplus, after we exclude cases of tax mitigation and tax evasion. Tax mitigation and tax evasion are two end points. It is easier and more beneficial to follow this discernment to define tax avoidance, for the confines and bounds of tax mitigation and tax evasion are easier to decipher and define legally and also identify with some exactness in practice. (Refer Tax Avoidance, Tax Evasion & Tax Mitigation by Philip Baker.)

46. It is equally important to distinguish and differentiate acceptable tax avoidance and abusive tax avoidance. The Supreme Court in CIT versus Roman (A.) & Co. [1968] 67ITR 11, at p. 17 had observed:-

> *"Avoidance of tax liability by so arranging commercial affairs that charge of tax is distributed is not prohibited. A taxpayer may resort to a device to divert the income before it accrues or arises to him. Effectiveness of the device depends not upon considerations of morality, but on the operation of the Income-tax Act. Legislative injunction in taxing statutes may not, except on peril of penalty, be violated, but it may lawfully be circumvented."*

47. In clear and categorical terms the aforesaid ratio was resonated and approved by the Supreme Court in the Vodafone's case (supra). Thus, the test of 'devoid of business purpose' or 'lack of economic substance' is not accepted and applied in India as it is too broad and unsatisfactory. The said test, if ardently applied, would contradict and would be irreconcilable with taxpayers' right to arrange once affairs within the confines of law, which is not prohibited or barred.

48. Naturally, the dividing line between acceptable and abusive tax avoidance cannot be deduced or inferred from lowering or elimination of the tax liability. Latter is the consequence and the tax effect. It is the post facto consequence under the tax code of the event selected by the assessed. The test applied should not curtail the freedom of choice to adopt a particular transaction or combination of transactions to reduce or eliminate the tax liability.

*49. At the same time, the dividing line as per the ratio in **Vodafone's** case (supra) is ethically principled and moralistic as tax avoidance is disapproved when the assessee adopts a colourable device, dubiousness and otherwise indulges in a sham arrangement or transaction. This would mean that pre-ordained, circular or selfcancelling transaction with a step or steps having no commercial purpose or lack of economic or business purpose could in a given case be, though not necessarily, a relevant fact, vet they are not the touchstone, yardstick or the final test. These could be circumstances or facts to infer and discern whether the taxable event selected was a colourable device, sham or deceit and not the tax event*

intended by the parties. Right to choice to select the most beneficial legal way and manner to execute a transaction is unquestionable and perennial. A fact is not the test: rather the corrupt and mendacious conduct, i.e. colourable device, sham or deceit, is the specified bright line, dividing acceptable tax avoidance from abusive tax avoidance.

50. The assessed is well within his right to choose any one event between two or more events and select an event to minimize or reduce his tax liability. The Act, i.e. the Income Tax Act, 1961, imposes and saddles tax liability on the chosen tax event. The Act per se, unless a provision so stipulates, does not restrict or curtail the right of choice. Tax is determined and gets crystallized on the tax event adopted by the assessee. For example, in ***Vodafone's*** *case (supra), the assessed had several options and therefore, right to choose a particular tax event. As long as the choice is within the framework of law, the Assessing Officer cannot disturb the tax effect or liability, which is the consequence of the event. The choice of the assessee is not abrogated or invalidated. For example, a company has several legal options, and therefore, right to choose how to dispose of a capital asset, as in* ***Vodafone's*** *case (supra). Similarly, an assessee can opt for and has multiple options for raising debt to finance business expansion plans. The assessed may have several legally permissible alternatives to effect and divide the assets on partition. Such examples are numerous. The choice might result in mitigation of tax liability, but the tax effect would not classify or help us differentiate between tax avoidance and abusive tax avoidance. Any attempt to minimize or eliminate tax liability would not make the choice of the tax payer abusive tax avoidance. The foundation of the said principle is that the tax code by its nature differentiates between different types of actions, transactions, arrangements and activities and then identifies and stipulates the consequences. The tax code, i.e. the Income Tax Act, 1961 is rule based and complex. The Act is not entirely principle based. The provisions are read and applied. Principle of purposive interpretation both in favour of Revenue or assessed can be applied but within four corners of law. In fact, in some cases, the assessed may find themselves taxed at a higher liability for failure to choose a more tax friendly event. But the right of choice is hedged with one significant condition. The event selected, as noticed above and subsequently, should be real and not a colourable device, sham and deceit.*

51. Tax reduction is not on evil if you do not do it evilly [Murphy Logging Co. *vs. US. 378 F.2d 222 (1967)]. The assessee acts evilly when there is camouflage or dubiousity to mask and masquerade the real intent of the transaction which the parties intended and the document(s)/transaction(s), is at variance with the actual intent The assessed in such cases does not choose the real event as one from the multiple choices, but adopts a sham or colourable event. The* assessed *then acts fraudulently, deceitfully or in a corrupt manner. He does not choose an event which is useful, viable and tenable, but employs deception and visors to pretense a state of affair which is different from the actual or real state of affairs. The event propounded is contrary to his intention. When the event selected is*

artificial it can be treated as colourable, deceitful or sham. The artificial event is one which purports to be one thing but in fact is another. Thus, abusive tax avoidance is a matter of evil intention and a result of dishonest behavior of the assessed.

52. In such cases, question of ignorance as to tax or *administrative incompetence would arise for consideration, for abusive tax avoidance scheme requires a mind set and propensity to act evilly. It requires a degree of knowledge and absence of honest belief.*

53. The aforesaid doctrine of abusive tax avoidance is a Judge made law or a *judicial doctrine. The Parliament can legislate and has enacted provisions to negate and nullify specific anti-tax avoidance rules/provisions. Section 2(22)(e), i.e. the principle of deemed dividend, Section 94 relating to dividend stripping, clubbing of income of minors, are few such provisions where the legislature has enacted specific anti-tax avoidance rules. It is the obligation and duty of the court/tribunal to apply the said provisions in terms of the legislative mandate. When a specific anti-tax avoidance section/rule is invoked, the court and the tribunal must look at and interpret the relevant provision to decipher whether the chosen tax event falls within the said provision and accordingly the tax consequences will apply.*

54. A caveat, the aforesaid discussion does not examine and elucidate scope and ambit of Section 271(l)(c) of the Act.

4.29 Coming to the facts of our case , as discussed above, the assessee has subscribed 5,00,000 Hybrid shares at a price of Rs.19975.97 per share which were sold to a third party at Rs.16,314.70 per share within one month of allotment. Although the subscription and sale of 500000 shares has been shown as two transaction, in effect it is a preordained transaction to book a net short term capital loss of Rs.1,83,06,38,227/- in addition to Long Term Capital Gains of Rs. 162,56,53,0767- on sale of original 1,00,000 shares with the sole purpose of offsetting the long term capital gains on original 1,00,000 shares. Just by routing the funds through the bank accounts and passing the entries in its books of accounts, the assessee has created an artificial ST loss which has been adjusted against other income.

4.30 The real intention was to create artificial loss, to set off against taxable income. If the transaction of subscription of shares was real, then there was no need to dispose off the entire shareholding within one month. At least, the assessee has not demonstrated any commercial prudence, or reason, or any evidence to substantiate the real intention as claimed by it. We hold so because, despite the directions of the Panel, the assessee has not produced the details, documents and discussion amongst the management and the board of EIL that led to the decision of making investment of about Rs.998 crore in Hybrid, and thereafter what went wrong with Hybrid and with the decision earlier made to make investment, that immediately within 1 month of such investment, the management exited Hybrid fully. The assessee has also not produced documents, and files related to above decision making demonstrating the decision making

process and considered for decision making. Even the claim of commercial prudence has also not been substantiated in any manner. The Memorandum of Understanding dated 26.02.2010, has also not been produced. Moreover, other than stating that there is no relationship between Arya Infrastructure Holding Ltd and the assessee, the assessee has not produced any evidence to justify its position. The assessee knowingly transacted in 500000 shares through automatic route, so as to avoid scrutiny of RBI and FEMA.

4.31 The subscription of 500000 shares in February 2010 and its sale in March 2010 without demonstrating any commercial reasons shows that it is a pre-ordained, circular or self cancelling transaction having no commercial purpose or lack of economic or business purpose except for the sole purpose of tax avoidance by offsetting the LTCG by booking artificial short term capital loss. This unsubstantiated action of the assessee and the circumstantial evidence of setting off, of the artificial loss against taxable gain, demonstrates the corrupt and malicious conduct of the assessee and proves that the entire transaction is nothing but a colourable device, sham or deceit. Hence, we hold this transaction as one of abusive tax avoidance.

4.32 The fact that the assessee has acted fraudulently, deceitfully or in a corrupt manner is further proved because it argues that while investing it has relied on the valuer's certificate valuing the same at Rs. 20550/- per share but, while disinvesting it has considered the NAV of Rs. 16514/- per share. When the assessee had the valuer's report dated 12.02.2010 valuing at Rs. 20550/- per share, there was no reason for it to sell the same at Rs. 16314/- per share and book a loss. The assessee before entering into the transaction of sale knew before hand that it would have STCL which it would be eligible to set off against other taxable income. The assessee in this case has not chosen the real event as one from the multiple choices (there were no multiple choices). The real intention was always to dispose off the originally held 100000 shares. But, to set off the huge Capital gains on which it would be liable to pay tax, it entered into this sham transaction of subscription and sale of additional 500000 shares. Thus, the event propounded is contrary to its claim. It has not chosen an event which is commercially useful, viable and tenable, but has employed deception and visors to pretense a state of affair which is different from the actual or real state of affairs. Since, the entire transaction of subscription of 5,00,000 shares and immediate sale thereof is artificial, it is treated as colourable, deceitful or sham as it purports to be transaction of subscription and sale but in fact is a device for abusive tax avoidance. This, abusive tax avoidance, is not allowed.

4.33 We may also mention that the fact that "the Income Tax Authorities are entitled to lift the corporate veil and expose the tax avoidance device/scheme" has been recognised in a number of other decisions also, some of which are being cited here under:

(i) Juggi Lal Kamlapat v CIT, 73 ITR 702 (SC)
(ii) D. H. N, Food distributors Ltd v Tower Hamlets London Borough Council (1976) (3 Ali ER 462)
(iii) Scottish Co-operative Wholesale Society Ltd V Meyer (1959) Comp Cas 1 (HL) AC 324
(iv) State of UP v Renusagar Power Co, AIR 1988 SC 1737

(v) Hackbridge Hewittic & Easun Ltd v GEC Distribution Transformers Ltd, (1992) 74
Comp Cas 543 (Mad)
(vi) U.K. Mehra v Union of India, (1997) 88 Comp Cas 213
(vii) CITv Dalmia L N. 207 ITR 89 (Cal)
(viii) Nayantara G Agarwal v CIT, 207 ITR 639 (Bom)
(ix) Hela Holdings Private Limited v CIT, 263 ITR 129 (Cal) etc.

4.34 Accordingly in view of the above discussion, we hold that the transaction of subscription of 500000 shares in February 2010 and its sale in March 2010 is a sham transaction. Hence, the entire Short term capital Loss of Rs. Rs.1,83,06,38,227/- is directed to be disallowed.

Conclusion:

4.35 In view of the discussions above, benchmarking of the transaction of subscription of 500000 shares of Hybrid by the TPO proposing an adjustment of Rs. 321,30,00,000/- is upheld. The AO is directed to consider this amount in determination of COA of 5 lakh shares of Hybrid in computation of STCG arising on transfer of these shares during the year. However, in the event of this determination being reversed in appeal proceedings, the **alternate determination** proposing an adjustment of Rs.1,83,06,38,227/- will still hold good and AO would then consider this amount in determination of COA of 5 lakh shares of Hybrid in computation of STCG arising in transfer of these shares during the year.

4.36 We also hold that the transaction of subscription of 5 lakh shares of Hybrid is a design of tax avoidance by booking a loss in the books of the assessee company artificially to set off the Long Term Capital Gain on sale of 1,00,000 shares originally held. Accordingly, the ST Capital Loss on sale of 5 Lakh shares of Rs.1,83,06,38,227/- is disallowed. However, this finding will arise only if the TP adjustments of the **Rs. 321.30.00,000/- and** Rs.1,83,06,38,227/- are both rejected by appellate authorities.

4.37 We also uphold the, **benchmarking of the transaction of purchase of 50000 shares of ESKL by the TPO proposing an adjustment of Rs. 2.33.000/**-. The AO is however directed to consider this amount in determination of COA of these shares in computation of Capital Gains whenever these shares are transferred."

8. The ld AR Shri Nishant Thakkar vehemently assailed the order of DRP upholding the order TPO which entirely wrong and against the facts on records and also contrary to the ratio laid in the various judicial pronouncements. The ld AR challenged the order of DRP on various counts putting across various propositions each of which are without prejudice to the other for the consideration of the Hon'ble Bench.

8.1. Arguing on the first proposition, the ld AR submits that a transaction of subscription of shares by Holding Company in its wholly owned subsidiary cannot be benchmarked under Chapter X of the Act. The ld AR submits that the transaction of appellant infusing USD 212,836,000 in its wholly owned subsidiary Hybrid Capital does not attract the provisions of Chapter X of the Act since, a determination of arm's length price for such a transaction would only result in change in number of shares to be issued by wholly owned subsidiary to the Holding company which is completely irrelevant as the holding of the company continued to be at 100% before and after infusion of money. It is important to note that the infusion of USD 212,836,000 was made so that wholly owned subsidiary could lend money to Arya Infrastructure. Therefore, the value of share and number of shares to be issued by the wholly owned subsidiary was completely irrelevant to the entire transaction. Therefore, the ld AR submits that the provisions of Chapter X relating to determination of arm's length price do not apply to infusion money in the wholly owned subsidiary. The ld AR argues that if the shares were to be issued at the value of Rs. 13,549/- per share as determined by the TPO then it would have only resulted into 7,37,175 shares being issued to the Appellant and consequently the Appellant would have sold higher number of shares to Arya Infrastructure at USD 215,000,000 and suffered the same amount of capital loss of Rs. 20.49 crore on the said transaction. Similarly, had the shares been issued at the alternate value of Rs. 16,314/- per share determined by the TPO, the wholly owned subsidiary would have issued

6,12,208 shares and would have resulted into same amount of capital loss on sale of shares to Arya Infrastructure. As can be seen from the above, the determination of arms' length price is wholly irrelevant to the transaction and therefore, it is submitted that the provisions of Chapter X do not apply to the aforesaid transaction between the Appellant and its wholly owned foreign subsidiary. In defense of his arguments ld AR places reliance on the following decisions:

i) ITO vs. Sterling Oil Resources (P.) Ltd. (67 taxmann.com 2)(Mum Tri).
ii) Ucal Fuel Systems Ltd. vs. ACIT (ITA No.725/Mds/2015) (Chennai Tribunal)

The ld AR submitted that the aforesaid first decision of the Tribunal in the case of ITO Vs Sterling Oil Resources (P) Ltd.(Supra) has been affirmed by the Hon"ble Bombay High Court in PCIT vs. Sterling Oil Resources (P.) Ltd. (1TA No. 341 of 2017) and hence, the Judgment of the High Court is the only operative decision on this point and is binding on the Tribunal. In this regard, the Appellant relies on the Judgment of Gujrat High Court in case of Nirma Industries Ltd. vs. DCIT (283 ITR 402) (Guj.) wherein High Court has held that dismissal of appeal results into merger of the order of the Tribunal with the order of High Court and is binding on the Tribunal. In view of the above, it is clear that it is not necessary that in all cases provisions of bench marking contained in Chapter X of the Act must be made applicable simply because there is an international transaction. It is therefore submits that the provisions of Chapter X do not apply to the transaction of appellant infusing USD 212,836,000 in its wholly owned subsidiary Hybrid Capital and consequently, transfer pricing adjustment of Rs. 321,30,00,000 made by

the TPO deserves to be deleted.

8.2. On the second proposition, the ld AR submits that given the peculiar nature of the transaction, it cannot be benchmarked under Chapter X of the Act. The TPO assumes jurisdiction to benchmark the transaction of subscription of share capital and makes an adjustment by observing that in page 10 of TP0's order that *"...Consequently this office is of the opinion that even the figures adopted by the assessee for cash flows and expenses were to be relied upon and by reasonably correcting the above glaring defects the valuation of shares would come to Rs. 13,549/- which is much lesser than the value of Rs. 20,550 that was given in the DCF study. The correctness of the computation done by this office is also supported by the fact that as per valuation done by this office equity infusion should have been done at Rs. 812.95 crore..." The ld AR submits that a*fter taking the equity value at Rs. 812.95 crore, the TPO computes value per share at Rs. 13,549 (812.95 crore / 6,00,000 shares) and makes the adjustment of Rs, 677,45,00,000 (Rs. 13549 * 5,00,000 shares) holding as under (Pg. 12 of TP0's order) "*thus the valuation of equity share of Hybrid Capital Pte. Ltd. is worked out at Rs. 13,549 per share. The assessee has subscribed to 5 lakh equity shares. Hence the arm's length price for the investment is worked out at Rs. 677,45,00,000/-. The assessee has made the investment Rs. 998,75,00,000. Thus, the resultant adjustment to the international transaction of subscription in the shares of the subsidiary company, is worked out at Rs. 321,30,00,000"* The ld AR therefore submitted that the adjustment made by the TPO is absurd, bereft of any rationale and is without jurisdiction, as can be seen from following:

i) It is not within the jurisdiction of the TPO to dictate to the Appellant what amount it should have invested. Once that be so, the no. of shares to be issued by a wholly owned subsidiary its parent is wholly irrelevant and cannot be benchmarked. The Appellant submits that it is not within the jurisdiction of the TPO to hold that how the business of the assessee is to be carried on. The TPO cannot restructure and recharacterize the transaction and dictate terms to the assessee as to how a particular transaction should have been carried out by the assessee. Therefore, the finding of the TPO that the Appellant should have invested only Rs. 677,45,00,000 is manifestly absurd and beyond jurisdiction. On this count alone the TP addition deserves to be deleted,

ii) The TPO has failed to appreciate that the infusion of USD 212,836,000 (Rs.998,79,87,374) was based on an opportunity whereby the entire infusion of capital was to be lent to Arya infrastructure by Hybrid Capital. Therefore, it is absurd to suggest that the Appellant should have infused only Rs. 677,45,00,000 even after knowing that the entire amount of USD 212,836,000 was to be lent to the prospective borrower,

iii) Secondly, had the Appellant invested only Rs. 677,45,00,000 then the wholly owned subsidiary would not have been able to carry out the lending transaction with Arya Infrastructure and earn the interest income of USD 9,101,781 (i.e. Rs. 43,13,94,079).

iii)Thirdly, had the Appellant invested only Rs.

677,45,00,000 then it would not have received USD 215,000,000 which is evident from the fact that before infusion of money as on 31 March 2009, the net asset value of Hybrid capital was Rs. 6.98 crores however, after infusion of money the net asset value of Hybrid Capital was INR 990 crores (USD 215,000,000) which was derived basis infusion of money of USD 218,360,000 by the Appellant (Pg. 268 of Paper book).

8.3. Arguing on the third proposition the ld AR submits that Chapter X has no application as no income arises from the international transaction of subscription to shares by a holding company in its wholly owned subsidiary. It is submitted that Section 92 of the Act states that "(1) *Any income arising from an international transaction shall be computed having regard to the arm's length price."* In the present case, the transaction under dispute is subscription to shares of Hybrid Capital by the appellant and on subscribing to shares of Hybrid capital, no income arises in the hands of Appellant under the provision of the Income-tax Act, 1961. Hence, in the absence of "any income", provisions of Chapter — X of the Act (i.e. transfer pricing provisions) do not apply to this transaction. It is important to note that provision of section 56(2)(viib) r.w. section 2(24)(xvi) are effective w.e.f. 1st April 2013 to tax the income in the form of excess premium received by a company on issue of shares. However, before introduction of this section, there was no provision under the Income- tax Act which provide for taxing the excess premium received by a company. Therefore, for the year under

consideration A.Y. 2010-11, no income arises in the hands of the Appellant as there is no provisions which bring to tax income on purchase / subscription of shares in the hands of the Appellant. Hence, in the absence of income, the provisions of Chapter — X are not applicable in the instant case. The ld Counsel of the assessee relies on following decisions in support of his arguments:

i) Vodafone India Services P. Ltd. vs. U01(368 ITR1)(Bom)
ii) **Shell** India Markets (P.) Ltd. *vs.* ACIT (369 ITR 516) (Bom).
iii) Tops Group Electronic Systems Ltd. vs. ITO (67 taxmann.com 310)(Mum Tri)

The ld AR submits that the Tribunal in the case of Tops Group Electronic Systems Ltd. vs. ITO (Supra) has held that the ratio laid down by the Hon'ble Bombay High Court in the case of Vodafone India (supra) and Shell India (supra) is equally applicable to a situation where an assessee makes outbound investment in a subsidiary outside India. The decision of Tribunal in case of Tops Group (supra) has been affirmed by the Bombay High Court in PCIT vs. Tops Group Electronics Systems Ltd. (ITA No. 1721 of 2016). In view of the above, it is submitted that the provisions of Chapter do not apply as there is no "income" which arises on subscription of shares of Hybrid Capital. Further, it is submitted that even before the Judgment of Bombay High Court in case of Vodafone India (supra) and Shell India (supra), the Tribunal in the following decisions had taken a view that the provisions of section 92B do not cover the transaction of subscription of shares of an Associate Enterprise:

a)Vi jai Electricals vs. Addl. CIT (36 taxrnann.com 386)
b)Hill Country Properties Ltd. vs. Addl. CIT (48 taxmann.com 94)

It may be noted that Finance Act, 2012 also amended

provisions of Section 92B of the Act and broadened the scope of meaning of "international transaction" by insertion of an explanation and has included even the transaction of purchase of shares as an international transaction. However, it is submitted that the amendment to Section 92B is applicable prospectively from AY 2013-14 onwards and the Appellant will still be governed by the erstwhile provisions as interpreted by Vijai Electricals (Supra) and Hill Country (supra). The following Tribunal decisions have held the amendment to section 92B is not applicable to years prior to A.Y. 2013- 14:

a) Siro Clinpharm (P.) Ltd. vs. DCIT (177 TTJ 609) (Para 17 & 18 Pg. 489-490 of Paper book);
b) Jindal Steel & Power Ltd vs. ACIT (106 taxmann.com 179) (Para 213-217 Pg. 545- 547 of Paper book)

In view of the above, it is submitted that since the amendment to section 92B is not applicable to the year under consideration, the transaction of subscription of shares is not an international transaction and consequently, the provisions of Chapter X are not applicable. The TPO and DRP have held that the provisions of Chapter - X are applicable as the Appellant itself has reported transaction of subscription of shares of Hybrid Capital as an international transaction in Form 3CEB. It is submitted that the transaction was reported by way abundant caution and in any case, mere reporting of a transaction in Form 3CEB will not make the provision of Chapter - X applicable. This contention of the Department has been rejected by Hon'ble Bombay High Court in the case of Vodafone India Services P. Ltd. vs. UOJ (supra) (Refer Para 27 on Pg. 384 of Paper book).

8.4. On fourth Proposition, the ld AR submits that the provisions of Chapter – X are not applicable as there is no shifting of profits outside India. The ld AR referred to para 55.5A of Circular No. 14/2001 issued by Central Board of Direct Taxes (`CBDT') wherein it has been explained that the basic intention of introducing transfer pricing provisions in India was to ensure that profits taxable in India are not understated and there is no shifting of profits outside India. In the present case, it is submitted that the Appellant has not shifted any profits outside India. On the contrary, pursuant to infusion of funds by Appellant into its wholly owned subsidiary, these funds were lent to the third party and the subsidiary earned interest of USD 9,101,781, i.e. 12% p.a. Out of the money earned by Hybrid, the appellant received a dividend of USD 6,000,000 i.e. Rs. 28,43,80,000 from Hybrid Capital **(**Pg. 264 of paper book) which was offered to tax by Appellant in its return of income a copy of which is filed at Pg. 269 of Paper book. Such dividend works out to an effective return of 7.91% on the monies infused by appellant into Hybrid Capital (Pg. 848 of Paper book) which is more than the arm's length interest rate of 4-5% determined by the Tribunal based on LIBOR rates in the following cases:

a) CIT vs. Adani Ports (104 taxmann.com 368)
b) Videocon Industries Ltd. vs. Addl. CIT (55 taxmann.com 263)

In addition, the Appellant has also made a profit in foreign currency amounting to USD 2,064,000 on sale of 100% shares of Hybrid Capital. Therefore, it is submitted that there is no shifting of profits outside India and consequently, the provisions of Chapter — X do not apply.

The Appellant also submits that the profit of USD 2,064,000

(Rs. 9.39 crore) got converted into a net short-term capital loss of Rs. 20.49 crore primarily on account of fluctuation of foreign exchange rate between the time of infusion of funds into Hybrid Capital and receipt of funds from Arya Infrastructure upon sale of shares by Appellant. The same is evident from the bank statements of Appellant evidencing payments on account of infusion into Hybrid (Pg.179 to Pg.204 of Paper book) and receipt of funds on sale of Hybrid's shares (Pg.205 of Paper book). Such foreign exchange fluctuations are beyond the control of Appellant.

In view of the above, it is submitted that the provisions of Chapter X do not apply as the basic requirement of shifting of profits outside is not satisfied.

8.5. Submitting on the fifth proposition, the ld AR contended that rejection of Valuation Report by TPO and DRP is wrong and without any basis. The TPO has rejected valuation report dated 12 February 2010 and has determined the value of shares at Rs. 13,549/- per share after making changes to the market risk premium and Beta used to arrive at the cost of equity. It is submitted that the TPO is not an expert in determining the value of shares, therefore, he cannot reject Valuation Report prepared by a Chartered Accountant who is an expert in the field of valuation of shares. The TPO has not brought any material to show as to why the value of shares determined in the Valuation Report is not appropriate. On the contrary, he has used the same cash flow projections and valuation method which was used by the Chartered Accountant in the report dated 12 February 2010. It is

submitted that the TPO was duty bound to make a reference to Department Valuation Officer and determine the value of shares before rejecting the Valuation Report prepared by a Chartered Accountant. In this regard, reliance is placed on the following orders of the Tribunal, wherein it has been held that the TPO cannot reject Valuation Report prepared by an expert without making a reference to Department Valuation Officer ("DVO").

a) ACIT vs. Koch Chemical Technology Group (I) Ltd. (64 taxmann.com 464) (Para 7 Pg. 773 of Paper book)
b) GKN Sinter Metals (P.) Ltd. vs. ACIT (71 taxmann.com 297) (Para 11 Pg. 789 of Paper book)

In view of the above, it is submitted that the rejection of valuation report without making a reference to DVO for determination of value of shares is bad and unsustainable in law.

8.6. Without prejudice to above, it is submitted that the Valuation Report has been incorrectly rejected by the TPO and DRP on the basis of reasons which are unlawful and deserve to be rejected. The reasons given by the lower authorities for rejecting report are dealt as under:

a) The TPO has held that the valuation report is incorrect as the shares have been valued after the amount of Rs.998,79,87,374 invested by the assessee. It is submitted that for arriving at the correct market value of shares it was necessary to factor in the income that would be earned by Hybrid Capital after infusion of money by the Appellant. In fact, valuation of shares without considering the income to be earned on account of infusion of money would have led to incorrect valuation of shares of Hybrid Capital. In fact, the TPO himself has valued the shares after considering the infusion of money and resultant income from such infusion (Pg. II of TPO's order). In this regard reliance is also placed on the Judgment of Supreme Court in the case of Reva Investment (P.) Ltd. vs. (249 1TR 337) (SC) (Para 12 Pg. 405 of Paper book) wherein Supreme Court has held that for determining the correct value of shares, it must be valued after considering the infusion of capital. Therefore,

the reasons given by TPO for rejecting the valuation report are bad and unsustainable in law.

b) The DRP in its order has held that the cash flow projections are unrealistic as a company with weak financials in the past could not make such huge profits. It is submitted that the cash flow projections were entirely based on the opportunity spotted by the Appellant regarding lending of money to a borrower (Last extract under Para viii on Pg.9 of DRP directions). Therefore, estimation of cash flow was not at all unrealistic. On the contrary, the cash flow projections were reasonably accurate as the Appellant for the year ending 31 March 2010 had estimated interest income of Rs. 43.15 crore (approx.) (Pg. 35 of Paper book) which matches with the actual interest income of Rs. 43.13 crore earned by Hybrid Capital (Pg. 264 of Paper book) and the TPO himself has used the same cash flow projections for valuation of shares (Pg. 11 of TP0's order). Therefore, the suggestion of the DRP that cash flow projections were unrealistic is incorrect and contrary to facts on record.

c) The DRP and TPO have observed that the financial statements of Hybrid Capital are not reliable however, apart from making bald statement, both the authorities have not brought any material or evidence on record to substantiate as to how the financial statements prepared by the Appellant are not reliable. It is also submitted that section 98 and 99 of BVI Companies Act, 2004 do not specify any particular format for maintenance of books of accounts or preparation of financial statement (Pg. 926 of Paper book). Therefore, the allegations of TPO and DRP are incorrect and bad in law.

Therefore, it is submitted that the TPO and DRP have erred in holding that the financial statements of Hybrid Capital are not reliable.

8.7. On sixth proposition, the ld AR submits that the alterations made by the TPO to “market risk premium” and “beta” to arrive at the discounting rate of 11.72% (instead of the 7.27% arrive at by the Appellant’s Valuer) used for the purposes of arriving at the enterprise value under the Discounted Cash Flow (DCF) Method, is ex-facie erroneous and contrary to facts on record. In arriving at the discounting factor to ascertain the present value of future cash flow under the DCF Method, it is required to compute the Weighted Average Cost of Capital. Weighted Average Cost of Capital comprises of two components

namely cost of Debt and Cost of Equity. The TPO does not alter the Cost of Debt. However, in arriving at the Cost of Equity to compute Weighted Average Cost of Capital and in turn the discounting rate to be applied, the TPO has altered the "Market Risk Premium" and "Beta" i.e. the industry risk number. These factors have led to an increase in Weighted Average Cost of Capital (`WACC') from 7.27% (as considered in the independent valuation report — Pg.35-36 of Paper book) to 11.72% (Pg.11-12 of TP0's order) and thus, the value per share has decreased from Rs 19,975 per share to Rs 13,549 per share. It is submitted that the TPO has used incorrect data for beta and market risk premium and if correct data from the TP0's own sources of information (Pg.9 of TPO order) is used, the figures for beta and market risk premium would stand corrected and would match with the respective figures considered in valuation report obtained by Appellant. Insofar as the "Market Risk Premium" is concerned :

a) The Appellant's Valuer has taken the "Market Risk Premium" at '6' whereas the TPO has taken "Market Risk Premium" at '10.5' (See para (ii) on Page 9 of the TP0's order)

b) TPO relies on study on Market Risk Premium published by Dr. Pablo Fernandez for the year 2008 (Pg. 850 of Paper book) in order to consider market risk premium for India as 10.5% (Pg. 858 of Paper book). However, TPO failed to appreciate that a similar study was published by Dr. Pablo Fernandez for the year 2010 (Pg.884 of Paper book) and as per

that study, market risk premium for India stood at 6.1% (Pg. 891 of Paper book) which is in line with the market risk premium of 6% considered by the Valuer. It is submitted that TP0's erred in considering data for year 2008 as the shares were allotted on 17 February 2010 and hence the market risk premium data published for the year 2010 will be correct data to be used, rather than market risk premium data which is 2 years old and does not pertain to the year under consideration. Therefore, the TPO erred in taking the market risk premium of 10.5% relying on an incorrect document.

Insofar as the "Beta" (viz. the Industry Risk Premium) is concerned —

a) The Appellant's Valuer has taken the "Industry Risk Premium" at '1' whereas the TPO has taken Industry Risk Premium" at '1.27'. (See para (ii) on Page 9 of the TP0's order)

b) TPO relies on beta information published by Prof. A. Damodaran on his website and has considered the unlevered beta of "Investment Co. (Foreign)" which stood at 1.27 (Pg. 911 of Paper book). It is submitted that the TPO failed to appreciate that Hybrid Capital carried on the business of lending and financing as also held by DRP at Para (xi) Pg. 10 of DRP order). Therefore, beta of Investment Companies could not be taken for the purpose of valuation. Given the business of Hybrid Capital, beta of Banks and

Financial Services industry is appropriate and ought to be considered for the purpose of valuation. The Beta of Banks and Financial Services industry works out to average beta of 0.99 (rounded off to 1.00 in Valuation report). In fact the unlevered beta of Banks and Financial Services industry of 0.49 (Pg.913 of Paper book) and if that is considered the value of the shares would increase even further. However, on a conservative basis the levered Beta of Banks and Financial Services industry may be considered which is '1.00'. It is in these circumstances submitted that Beta of 1.27' adopted by the TPO is incorrect. Without prejudice to foregoing, it is submitted that even if Beta of "Investment Companies (Foreign)" is included along with the Beta of Banks and Financial Services industry, the average beta for all the 3 industries works out to 1.02 and unlevered beta works out to 0.62 (Pg.9 13 of Paper book). It is therefore submitted that the alteration by the TPO of the Beta is wholly incorrect and irrational and should not be accepted.

8.8 Submitting on the seventh proposition, the ld AR argued that CUP method cannot be considered for the purpose of benchmarking the international transaction between the assessee and its foreign subsidiary. It is submitted that in the Valuation Report the valuer has valued the shares of Hybrid Capital using DCF method as is clear from Pg.35 of Paper book. The TPO has also computed the value of Hybrid

Capital's shares using DCF method at Pg. 11 of TPO's order and therefore, once it is accepted that the correct method to determine value of Hybrid's shares is DCF method and there is no dispute on the same, it is incorrect to determine value of Hybrid's shares using another method (i.e. CUP method). The TPO has not given any reasons for using CUP method when he himself has accepted DCF method as the most appropriate method for valuation of shares. Therefore, in the absence any reasons given, the CUP method cannot be used for the purpose of valuation of shares. Without prejudice to above, it is submitted that the TPO and DRP applying CUP method, have taken the value at Rs. I 6,594/share i.e. the rate at which the shares were sold to Arya Infrastructure. Both the authorities have failed to appreciate that since the transaction of purchase / subscription and sale of Hybrid capital was carried out in foreign currency i.e. USD therefore, for the purpose of CUP method the rate should be considered in USD terms without converting into Indian rupees. As, the conversion of USD into INR would automatically factor in the foreign exchange fluctuation therefore, to nullify the impact foreign exchange fluctuation the price per share should be considered in USD terms. In this regard, reliance is placed on the decision of High Courts and Tribunal wherein it has been held that for benchmarking interest rate on loan given in foreign currency, interest rate linked with such foreign currency should be considered:

a) CIT vs. Tata Autocomp Systems Ltd. (374 ITR 516) (Bom.)

b) CIT vs. Cotton Natural (I)(P.) Ltd. (23 1 Taxman 401)

(Del.)

Accordingly, if price per share is considered in USD terms, the sale price per share received is USD 358.33 (i.e. USD 215,000,000 / 600,000) whereas the average cost price per share is USD 354.89 [i.e. (USD 100,000 + USD 212,836,000) / 600,000]. Therefore, no transfer pricing adjustment can be made as the sale price of shares is higher than the average cost per share. Without prejudice to the foregoing it is submitted that the value of shares sold to Arya Infrastructure cannot be compared to the value of the shares when monies were infused as the biggest income generating asset viz. the loan to Arya Infrastructure generating approximately 12% income will no longer be available, inasmuch as the loan by Hybrid Capital was to Arya Infrastructure itself and the purchaser is also Arya Infrastructure, hence it would be absurd to expect the Arya Infrastructure will pay to its wholly owned subsidiary interest @ 12%. It is consequently absurd to suggest that the value of shares in the absence of such a source of income continuing, can be compared to the value of shares which have been arrived at taking into consideration the source of income by applying the DCF method.

8.9. Eighth proposition of the ld AR is that the allegation of DRP that the transaction is “sham” is perverse and unsustainable in law. The DRP has held that the transactions of subscription to 5,00,000 shares of Hybrid and sale of all 6,00,000 shares were undertaken during AY 2010-11 in order to create an artificial loss, which could be set off against the long term capital gains of Rs 162,56,53,077 earned on original 1,00,000

shares held by Appellant in Hybrid Capital. While drawing such a baseless conclusion, the DRP has completely disregarded the fact that the long term capital gain of Rs 162,56,53,077 on 1,00,000 shares has arisen only on account of money infused by Appellant into Hybrid capital during A.Y. 2010-11 itself, which has resulted in an increase in the net worth of Hybrid. Therefore, without the infusion of money during the year, the gain of Rs. 162,56,53,077 on sale of 1,00,000 shares would have never arisen. Therefore, the finding of the DRP that transaction of sale and purchase / subscription were carried out to create an artificial loss is unsustainable and bad in law. If infusion of Rs. 998,79,87,374 was not made the sale value of 1,00,000 shares of Hybrid Capital would be Rs 6,98,56,577 and the gain on sale of 1,00,000 shares would have been Rs 6,40,39,824 after considering indexed cost of acquisition. Separately for the year under consideration (i.e. during AY 2010-11), the Appellant had incurred a business loss of Rs 196,63,08,552 and these losses were sufficient in order to absorb the gain of Rs. 6,40,39,824 that could have arisen to Appellant on sale of 1,00,000 shares of Hybrid Capital without the infusion. Moreover, the Appellant had brought forward losses of Rs 1,56,11,02,680 (comprising of Business losses of Rs. 1,522,063,935 and Unabsorbed depreciation of Rs. 3,90,38,745) from earlier AYs (Pg. 269-270 of Paper book). Therefore, the finding of the DRP is ex facie absurd. It is also submitted that DRP cannot, on one hand, hold that the entire transaction as sham, but on the other hand, consider the same transaction for the purpose of benchmarking under CUP method

failing to appreciate that 1,00,000 shares could have never fetched a price resulting in a long term capital gain of Rs 162,56,53,077 if the infusion of funds of USD 212,836,000 was not made during the year by Appellant. As already submitted above, Appellant has finally made a profit of USD 2,064,000 on sale of all 6,00,000 shares in Hybrid to Arya in USD terms. The net short term capital loss of Rs 20,49,85,151 on sale of 6,00,000 shares of Hybrid has arisen primarily on account of fluctuation of foreign exchange rate between the time of infusion of funds into Hybrid and receipt of funds from Arya upon sale of shares by Appellant during A.Y. 2010-11. The same is evident from the bank statements of Appellant evidencing payments on account of infusion into Hybrid (Pg.179 to Pg.204 of Paper book) and receipt of funds on sale of Hybrid's shares (Pg.205 of Paper book). Such foreign exchange fluctuation is beyond the control of Appellant and therefore, the finding of the DRP is perverse and unsustainable in law. Further, the DRP has also observed that Appellant has not produced any evidence to justify that Arya is not an AE of the Appellant. It is submitted that the Appellant has time and again submitted that the Hybrid Capital and Arya Infrastructure are not AEs within the meaning of section 92A of the Act (Para 6.5 Pg. 12 of TPO's order and Para 4.27 (d) Pg. 26 of DRP's order). The Appellant cannot be asked to prove the negative and the burden is on the revenue to prove otherwise by adducing material to show that the provisions of section 92A are applicable. However, the TPO and DRP have not brought any material on record to show that the Appellant and Arya infrastructure are related entities. On the contrary, the TPO and

DRP both have considered the sale of shares to Arya Infrastructure as comparable transaction under CUP method (Para 6.5 Pg. 12 of TP0's order), this could have been done only on the footing that Arya Infrastructure is not an AE of the Appellant as Rule 10(A)(ab) does not allow transaction between AEs to be taken for the purpose of benchmarking. Therefore, even the DRP and TPO have accepted that Arya Infrastructure was not the AE of the Appellant. It is submitted that the burden to prove that the transaction is "sham" is on the Revenue as held by Supreme Court in the following Judgments:

a) Vodafone International Holdings B.V. vs. U01 (341 ITR 1) (Para 46 & 48 Pg.652-653 of Paper book);
b) Jaydayal Poddar vs. Bibi Hazra (AIR 1974 SC 171) (Para 6 Pg.690 of Paper book).

It is submitted that as demonstrated above, the DRP, far from having discharged its burden, has not been able to put forth even a comprehensible story.

The DRP further observed that when the price as per the independent valuer's report was Rs 20,550 per share, there was no reason to sell the shares to Arya Infrastructure at Rs 16,514 per share. As explained earlier, Hybrid Capitals' shares were being bought by Arya Infrastructure (from whom Hybrid generated interest income). Thus, such shares could never have been sold based on a DCF valuation since the basis of the DCF projections itself was the potential interest income that Hybrid Capital was expected to earn from Arya Infrastructure and which would not be earned by Hybrid Capital after transfer of shares. Further, Arya Infrastructure would not agree to purchase Hybrid Capital on a DCF value which is based on the potential income that Hybrid Capital

earns from Arya Infrastructure itself. Therefore, net asset value was the most appropriate method to be adopted at the time of sale of shares to Arya Infrastructure.

8.10. Only to allay the baseless allegation put forth by the DRP, the Appellant had filed an Affidavit of Mr. Suresh Sundaram, the Director of the Appellant at the relevant point in time. This was filed vide application for admission of additional evidence dated 13.08.2019. The DR has on 22 August 2019 taken time to seek comments of the revenue on the said affidavit. Not during the course of the hearing on 11 December 2020 (i.e. after having sufficient time to peruse and consider the affidavit) the DR has not raised any objections on the admissibility as also the correctness of the averments made therein. The Appellant therefore submits that that the facts and circumstances averred in the said Affidavit as supported by the documents annexed is a complete and full answer to the wild allegations made by the DRP. In summary, vide the affidavit, Appellant has submitted the following:

a) Copy of board minutes wherein decision to infuse funds into Hybrid was undertaken:
b) Intention of infusing approx. Rs 1,000 crore into Hyrbid during AY 2010-11 — Appellant spotted an opportunity of lending money to Arya;
c) Reason as to why the money could not be lent directly by Appellant to Arya;
d) Working for amount and rate of interest earned by Hybrid from funds lent to Arya;
e) Reasons as to why funds were needed by Appellant and the urgent requirement to sell stake in Hybrid for which negotiations were undertaken with Arya;
f) f) Copy of board minutes wherein decision to sell Hybrid's 100% shares was taken and how those funds were applied by Appellant in view of the urgent requirement.

9. Per contra, the ld DR submitted that the whole arrangement was orchestrated and engineered to infuse the

funds into foreign subsidiary and selling the same at loss is nothing but sham transactions.

10. In the rejoinder, the ld AR submitted that the DR has not disputed the Propositions 1,2,4,5,6 and 7 made by the appellant. With respect to third proposition ,the DR has submitted that since the gains computed on sale of shares involve taking into consideration the cost of acquisition, hence the bench marking of cost of acquisition is necessary. In reply, the Appellant has explained as under:

- Income arises from sale and not from subscription.
- The two transactions are different.
- The 'international transaction' to which Chapter X is sought to be applied is the transaction of subscription / purchase of shares and not sale. It is clarified that the transaction of sale of shares is not an international transaction since the sale is to a person who is not an "associated enterprise".
- Explanation to section 92B of the Act does not apply inasmuch as it covers allowances or costs that are implicit in the international transaction — for e.g. Reliance is placed on the Judgment of Bombay High Court in case of Vodafone India (supra) wherein the High Court has held as under:

  "31. Similarly, the reliance by the revenue upon the definition of International Taxation in the sub clause (c) and (e) of Explanation (I) to Section 92B of the Act to conclude that Income has to be given a broader meaning to include notional income, as otherwise Chapter X of the Act would be rendered otiose is far fetched. The issue of shares at a premium does not exhaust the universe of applicability of Chapter X of the Act. There are transactions which would otherwise qualify to be covered by the definition of International Transaction. The transaction on capital account or on account of restructuring would become taxable to the extent it impacts income i.e. under reporting of interest or over reporting of interest paid or claiming of depreciation etc. It is that income which is to be adjusted to the ALP price. It is not a tax on the capital receipts. This aspect appears to have been completely lost sight of in the impugned order."

The DR spent considerable time in reading the allegation of sham by the DRP, however did not counter any of the explanation put forth by the Appellant during the course of the hearing. Since the findings of the DRP on sham have already

been explained above, the Appellant does not submit anything further, save and expect to repeat and Ld. DR on the observations/findings of the DRP.

11. We have heard the rival contentions and perused the materials on records. The undisputed facts are that the assessee has a wholly owned foreign subsidiary Hybrid Capital in British Virgin Islands. The appellant had invested USD 1,00,000 equivalent to Rs. 45,74,740/- (1 USD = Rs 45.74) in Hybrid Capital, on 18 November 2005. Hybrid Capital was incorporated to carry on the business of financing and lending outside India. Right from inception, Hybrid Capital carried on the business of lending and financing. The said subsidiary has earned interest income during F.Y. 2006-07 of Rs. 124.69 crore and during F.Y. 2007-08, of Rs. 78.10 lakhs. During F.Y. 2009-10, the appellant assessee in order to lend money to an overseas borrower, Arya Infrastructure, infused and invested a sum of USD 212,836,000 equivalent to Rs. 998,79,87,374 in the share capital. The investment in the subsidiary was made solely with the objective that the funds could be lent further to overseas borrower, Arya Infrastructure as the assessee could not have lent money directly to overseas borrower due to imbargo placed by section 6(3)(d) of Foreign Exchange Management Act, 1999 ("FEMA") read with Regulation — 5 of Borrowing or lending in Foreign Exchange Regulations, 2000 which prohibits an Indian resident to lend directly in foreign exchange to a person outside India. Pertinent to note that Hybrid Capital was in the business of money lending. The said investment was made by the assessee between June 2009 to January 2010

by way of equity contribution in accordance with the provisions of FEMA. In order to comply with the requirement under FEMA, the shares were valued on the basis of the Discounted Cash Flow method ("DCF method") taking into consideration the future earnings after infusion of the fresh capital of USD 212,836,000. As per the Valuation Report dated 12 February 2010, the value per equity share of Hybrid Capital was Rs. 20,550. Consequently 5,00,000 Equity Shares against this infusions and investment of USD 212,836,000 equivalent to Rs. 998,79,87,374/- were allotted by Hybrid Capital to appellant on 17 Feb 2010 at Face Value of USD 1 at a premium of USD 424.67 and in terms of Indian rupees at Rs. 19,975 per shares. Hybrid Capital continued to be a 100% subsidiary of the appellant even post infusion. Hybrid Capital, in turn, lent monies to Arya Infrastructure. During the year, Hybrid Capital earned an interest from Arya Infrastructure of USD 9,101,781 equivalent to Rs. 43,13,94,079/- which comes to 12% p.a. The above interest income is duly reflected in the profit & loss account for the year in the financial statements of Hybrid Capital. We also note that out of the interest earned of USD 9,101,781, Hybrid Capital paid a dividend of USD 6,000,000 equivalent to Rs. 28,43,80,000 to the appellant and the dividend was offered to tax by appellant in its return of income. On 17 March 2010, appellant sold its entire stake (i.e. 100% shares) in Hybrid Capital to Arya Infrastructure at a value of USD 215,000,000 taking into consideration the Net Asset Value of Hybrid Capital as on 15 March 2010. The Appellant had made a gain of USD 2,064,000 on the sale of

shares but upon conversion reported a capital loss in its Return of Income due to foreign exchange fluctuation. In other words on conversion of the investment and sale into INR, there was short term capital loss which has resulted due to exchange rate fluctuation. On sale of shares of Hybrid Capital, the Appellant made a gain of USD 2,064,000 (USD 215,000,000— USD 212,936,000) which is equivalent to Rs. 9.39 crores (1USD = Rs. 45.53 INR).However, the Appellant reported a Rs.20.49 crores loss in its return of income. The Appellant submits that a gain of Rs. 9.39 crores converted to a loss of Rs.20.49 crores only on account foreign exchange fluctuation, i.e. because Re. appreciated vis-à-vis. the Dollar by Rs. 1.40 between the date of investment and the date of sale.

11.1. On the first proposition, the main argument of the learned AR for the assessee was that infusion of USD 212,836,000 in the wholly owned subsidiary – Hybrid Capital are not covered by the provisions of Chapter-X of the Act. Since the determination of arm's length price for such a transaction would only result in change in number of shares to be issued by the wholly owned subsidiary to the holding company which appears to be otiose, as the holding company would continue to be holding 100% share in the subsidiary company before and after infusion of money. We note that if the shares were to be issued at a price of Rs. 13,549/- as determined by the TPO, then it would have resulted into 7,37,175 shares being issued to the assessee and as a result , the assessee would have sold higher number of shares to Arya Infrastructure at USD 215,00,000 and incurred the same

amount capital loss of Rs. 20.49 Cr. Likewise , had the assessee been issued shares by the Hybrid Capital at alternate value of Rs. 16,314/- as determined by the TPO, the foreign subsidiary would have issued 6,12,208 shares and the sale of these shares to Arya Infrastructure would have resulted into the same amount of capital loss. Thus the determination of arm's length price is wholly irrelevant to the transaction and the provisions of Chapter X do not apply to the aforesaid transaction between the assessee and Hybrid Capital. In this case we note that the assessee has infused USD 212,836,000 in Hybrid Capital solely and primarily for the propose of lending out to Arya Infrastructure and, therefore, value of shares and number of shares to be issued by Hybrid Capital is completely irrelevant. Thus, we find merit in the contentions of the learned AR that the provisions of Chapter X relating to determination of arm's length price do not apply to infusion of money in the wholly owned subsidiary company. The case of the assessee finds support from the decision of co-ordinate Bench in the case of Income Tax Officer vs. Sterling Oil Resources (P.) Ltd. (supra), wherein it has been held that no transfer pricing adjustment can be made when holding company gives money to the wholly owned subsidiary as the issue of shares is entirely irrelevant to the transaction, the operation part of the order is as under:

> "9... *What the TPO and DRP have overlooked is that since the assessee was only shareholder of the subsidiary company, the fruits of this investment belong to the assesse only and in entirety. On giving thus money to the subsidiary and on use of this money by the subsidiary, the assessee, in its capacity as sole owner of the subsidiary, is beneficiary of all the gains of the subsidiary company. Whether the assessee was allotted these shares or not, the assessee was the only shareholder of the subsidiary company and beneficial owner of all the earnings and all the assets of the company. Non allotment of these shares, during the period of payment of*

share application money till the actual date of allotment, did not, therefore, prejudice assessee's position anyway. All the earnings of the subsidiary company belonged to the assessee in any situation. For example, if the fluids available pr *dividend distribution for this year were say Rs 1,00,000 and the assessee had 100 shares before new allotment of shares and 1000 shares after the allotment, the assessee would be entitled to* Rs *1,00,000 only the either way- whether as Rs 1,000 per share fin- 100 in pre new allotment situation or whether as Rs 100 per share fir 1,000 shares in post new allotment situation. In absolute terms, the dividends remain the same. Whether the assessee is allotted more shares or not is wholly academic as the assessee is a single shareholder of the subsidiary conwany and the face value of shares does not affect the actual benefits of the assessee, the percentage of ownership is the only material factor- which remains at 100% pre new allotment as also post new allotment..."*

We also note that the aforesaid decision of the Tribunal has been affirmed by the Hon'ble Bombay High Court in PCIT vs. Sterling Oil Resources (P.) Ltd. (supra). Thus, the decision of Hon'ble High Court on this point is binding on us as has been laid down by Hon'ble Gujarat High Court in the case of Nirma Industries Ltd vs. DCIT (supra), wherein it has been held that dismissal of appeal results into merger of the order of the Tribunal with the order of the High Court. The case of the assessee is also supported by the decision of Chennai Benches of the Tribunal in the case of Ucal Fuel Systems Ltd. vs. ACIT (supra), wherein the Tribunal has held that the transaction between assessee and its wholly owned subsidiary could not be subjected to the process of benchmarking under Chapter X of the Act wherein again the Tribunal has held that the transaction between assessee and its wholly owned subsidiary could not be subjected to the process of benchmarking under Chapter — X of the Act. The relevant portion of the order is extracted as under:

"46... However, the party to which loan was advanced by the assessee here was not only a subsidiary but also one whose capital stood completely eroded, and which was suffering continuous losses. No banker would have advanced any sums to such a company since the risk would have been too much. Thus the only

source for such a subsidiary to raise any funds was its principal alone. It is an accepted position that the subsidiary company of the assessee to which the advances were made was sick. Thus, finding a comparable uncontrolled transaction, where a loan was given to an entity which was subsidiary to the tested party, and whose capital stood completely eroded due to loss was not practical or feasible. The simple reason is that no other person would have given any loan to such an entity, whatever might he the interest rate since the chances of recovery was negligible. In such a situation, when there could have been no reasonably identifiable comparable uncontrolled transaction, computation of comparable uncontrolled price by applying of Rule 10B(I), fell at the threshold. Section 92C(1) prescribes computation of ALP by comparable uncontrolled price method, resale price method, cost plus method, profit split method, transactional net margin method and any other method prescribed by the Board could have been applied. In our opinion, the question of benchmarking the transaction of the nature mentioned, applying any of the methodology prescribed in sec .92C(1) did not arise at all due to the particular facts and circumstances. According to us, fastening of an interest rate on the assessee when there was no comparable uncontrolled rate that could have been identifiable was incorrect. We, therefore, have no hesitation in deleting the addition made by the Assessing Officer/TPO in this regard. Ground Nos. 2 to 4 are allowed."

In view of the above facts of the assessee's case viz-a-viz the ratio laid down by the various judicial forums as discussed above, we are inclined to accept the contentions of the learned AR for the assessee that Chapter X does not apply to the transaction of infusion of funds by the assessee into its wholly owned subsidiary company- Hybrid Capital and, consequently, the transfer pricing adjustment of Rs 321,30,00,000 made by the TPO cannot be sustained. So on this proposition the order of the DRP has to be set aside and the addition has to deleted.

11.2. On the second proposition, we find that the TPO has assumed the jurisdiction of benchmarking the transaction of investment in the wholly owned subsidiary company on the basis of defects in the valuation of shares, which according to the TPO comes to Rs 13,549/-, which is much lower to the value of Rs 20,550 as per the valuation report given by the valuation expert under DCF method. According to the TPO if the valuation

report is corrected then the equity infusion into the subsidiary company should have been done at Rs 812.95 crore as against the actual investment of Rs 998.75 crores. We note that the TPO calculated the transfer pricing adjustment by applying the rate of Rs 13,549 per share to 5 lac equity shares and, thus the arm's length price for investment was worked out at Rs 677,45,00,000/-. By doing so the TPO has exceeded his jurisdiction in coming to the conclusion that a particular sum should have been invested by the assessee in the wholly owned subsidiary company by issuing the shares at Rs. 13,549/-. In our considered opinion, the TPO cannot dictate the assessee what amount it should have invested in its foreign subsidiary and, therefore, we are not in agreement with the findings and conclusion of the TPO that the assessee should have invested Rs 677,45,00,000/- which is not the jurisdiction of the TPO. In this case, we note that the assessee has found an opportunity to invest in the foreign country to lend money to Arya Infrastructure through its wholly owned foreign subsidiary Hybrid Capital and only with that purpose the assessee infused a sum of ISD 212,836,000 which is equivalent to 998,75,00,000. We also note that the subsidiary Hybrid Capital has advanced money to Arya Infrastructure immediately after the assessee infused the money in the foreign subsidiary. The assessee resorted to the route of investment in the subsidiary and got money lent to Arya Infrastructure in view of the restriction imposed by Section 6 (3)(d) of Foreign Exchange Management Act, 1999 read with Regulation 5 of borrowing or lending in Foreign Exchange Regulation, which prohibits Indian residents to lend directly in foreign exchange to a person outside India.

Had the assessee invested Rs 677,45,00,000 as per TPO's version, then the subsidiary could have only lend to Arya Infrastructure money to that extent only. We also note that the net assets of the subsidiary Hybrid Capital were 6.98 crores, which became 990 crores after infusion of money. So on this proposition also we find merit in the contention of the learned AR for the assessee and consequently, the transfer pricing adjustment made by the TPO cannot be sustained.

11.3. On the third proposition, assessee's contention is that under the provisions of section 92 any income arising from an international transaction shall be computed having regard to the arm's length price. We note that the assessee had subscribed to the shares of Hybrid Capital and out of this transaction no income has or arisen or accrued to the assessee. Therefore, we find merit in the contentions of the learned AR that provisions of Chapter X of the Act qua transfer pricing cannot be applied to this transaction. We further note that provisions of section 56(2)(viib) read with section 2(24)(xvi) were brought on the statute book to bring to tax the excess premium received by a company on issue of shares. However, such provision is not applicable to year under consideration as the same is effective prospectively and were applicable from A.Y. 2013-14. Therefore on this count also provisions of Chapter X cannot be invoked to determine the arm's length price of transaction which involved investment into a foreign subsidiary. The case of the assessee finds support from the decision of jurisdictional High Court in the case of Vodafone India Services P. Ltd. vs. UOI (supra), wherein it has been held that unless any income chargeable to

tax arises on account of international transactions, the provisions of Chapter — X being machinery provisions do not apply in the absence of income. (Para 24 & 25 Pg. 383-384. Similar view has been taken by Hon'ble Bombay High Court in the case of Shell India Markets (P.) Ltd. vs. ACIT (supra). This issue has further been decided by co-ordinate Bench in the case of Tops Group Electronic Systems Ltd. vs. ITO (supra), wherein the Bench following the decisions of the Hon'ble Bombay High Court in the case of Vodafone India Services P. Ltd. vs. UOI and Shell India Markets (P.) Ltd. vs. ACIT has held that provisions as contained in Chapter X cannot be applied to outbound investment in a subsidiary company outside India. This decision of the Tribunal has been affirmed by Hon'ble Bombay High Court in the case of PCIT vs. Tops Group Electronics Systems (supra). We further note that co-ordinate Benches in the case of Vijai Electricals vs. Addl. CIT (Supra) and Hill Country Properties Ltd. vs. Addl CIT (supra) have taken a view that provisions of section 92B of the Act do not cover the transaction of subscription of shares in the Associate Enterprise even prior to the decision of Bombay High Court in the case of Vodafone India Services P. Ltd. vs. UOI (supra) and Shell India Markets (P.) Ltd. vs. ACIT (supra). We further, note that the provision of section 92B of the Act were amended by the Finance Act, 2012 broadening the scope of meaning of "international transaction" by inserting an explanation, which has included the transaction of purchase of shares as an international transaction. However, the said amendment to section 92B is applicable prospectively from A.Y. 2013-14 onwards and thus the assessee will be governed by the erstwhile provisions as

interpreted by Vijai Electricals vs. Addl. CIT (Supra) and Hill Country Properties Ltd. vs. Addl CIT (supra). We note that the co-ordinate Benches have also taken a view that the amendment to section 92B is not applicable to the years prior to A.Y. 2013-14 in the cases of Siro Clinpharm (P) Ltd. vs. DCIT (supra) and Jindal Steel & Power Ltd. vs. ACIT (Supra).In view of the above facts and circumstances and the ratio laid down by various co-ordinate Benches, we are inclined to set aside the directions of the DRP by holding that the provisions of section 92B as amended by the Finance Act, 2012 are not applicable and, consequently, the transfer pricing provision cannot be applied to the transaction of subscription of shares by the assessee in its wholly owned foreign subsidiary company Hybrid Capital even if assessee has reported the transaction as international transaction in Form 3CEB. The mere reporting of transaction as international transaction in Form 3CEB will not ipso facto make the provisions of Chapter- X applicable. We note that this contention of the Revenue has been rejected by Hon'ble Bombay High Court in the case of Vodafone India Services P. Ltd. vs. UOI (supra).

11.4. The fourth proposition the learned counsel for the assessee was that there is no shifting of profits outside India as the assessee has only made investment in the foreign subsidiary. We have perused para 55.5A of Circular No.14/2001 issued by Central Board of Direct Taxes, which clarifies that the basic intention of introducing transfer pricing provisions in India was to ensure that profits taxable in India are not understated and there is no shifting of profits outside

the country. In the present case, there is no shifting of profits outside India but a transaction of infusion of funds was made by the assessee into its wholly owned subsidiary company so that the same could be lent to a third entity. We also note that the foreign subsidiary earned interest on the said money advanced to Arya Infrastructure and out of this earning the assessee received dividend of USD 60 lacs i.e. Rs 28,43,80,000/- from the foreign subsidiary, which was offered to taxation by the assessee in its return of income. Such dividend worked out an effective return of 7.91% on the monies infused by the assessee in the foreign subsidiary which is more than the arm's length interest rate of 4% to 5% determined by the Tribunal based on LIBOR rates in the case of CIT vs. Adani Ports (104 taxmann.com 368) and Videocon Industries Ltd. vs. Addl. CIT (55 taxmann.com 263). Further the assessee has also made profit of USD 20,64,000 on sale of 100% shares of Hybrid Capital to Arya Infrastructure which has resulted into net short term capital loss of Rs 20.49 crore when converted into Indian currency due to Foreign Exchange fluctuations. So on this ground also the adjustment made by the TPO and confirmed by the DRP is held to be erroneous and against the provisions of the Act.

11.5. On the fifth proposition, the learned AR has objected to the action of the TPO in rejecting the valuation report submitted by the assessee. We note that the assessee got the shares valued by the report dated 12.02.2010, whereby the value of shares were determined at Rs 20,550 and the shares were issued at Rs 19,975 whereas the TPO determined the value of share at Rs 13,539 after making changes to the Market Risk

Premium and Beta used to arrive at the cost of equity. The TPO has taken the Market Risk Premium at 10.5 as against 6 taken by the assessee's Valuer. We note that the TPO has taken the market Risk Premium 10.5 on the basis of Study on the subject published by Dr Pablo Fernandez for the year 2008 whereas the assessee's valuer relies on the similar study on Market Risk Premium by Dr Pablo Fernandez for 2010 where the Market Risk Premium was 6. Since the assessee was allotted shares on 17.02.2010, the Valuer took the Market Risk Premium at 6 which is correct for the simple reason that when the shares were allotted in 2010 , the Market Risk Premium has to be taken for 2010.Thus adoption of Market Risk Premium at 10.5 is wrong. So far as the Beta i.e. Industry Risk Premium is concerned, the assessee's valuer took it at 1 whereas the TPO adopted 1.27. We note that the TPO adopted the unlevered beta at 1.27 as per the paper published by Dr Damodaran on his website in respect of Investment Co(foreign) by ignoring the fact that assessee's foreign subsidiary is engaged in the business of lending and financing. Thus considering the line of business of the Hybrid Capital the beta of Banks and financial services which 0.99 is appropriate and should have been considered by the TPO. The assessee's valuer considered beta at 1 based on all these relevant information available which appears to be correct and germane. We find merit in the submissions of the AR that TPO is not an expert to value the shares whereas the valuation report by the assessee was prepared by a Chartered Accountant, who is an expert in the field of valuation of shares. Moreover, we find the TPO has not brought any material on record to prove the valuation report submitted by the assessee was wrong. We also

note that the TPO has used the same cash flow projections and valuation method as relied upon by the Chartered Accountant in the report dated 12.02.2010. It is also seen that the TPO has not made any reference to the valuation officer of the department before rejecting the valuation report submitted by the assessee which in our opinion is wrong and against the provisions of the Act. The case of the assessee finds support by the decision of the co-ordinate Benches in the case of ACIT vs. Koch Chemical Technology Group (i) Ltd. (supra) and GKN Sinter Metals P. Ltd. vs. ACIT (supra), wherein it has been held that TPO cannot reject the Valuation Report prepared by an expert without making a reference to the Department Valuation officer. On this count also the transfer pricing adjustment made by the TPO cannot be sustained. Besides we note that the assumption made by the TPO while rejecting the report were also wrong. While rejecting the report, he held it to be incorrect on the ground that to arrive at the correct value of shares, the amount invested in the foreign subsidy amounting to Rs 998,78,87,374 should not have been considered. But in view the valuation could only be determined after taking into account the income which could be earned by the foreign subsidiary after infusing of funds. In our opinion, the valuation without considering such investments would give a misleading and fallacious valuation of shares. The TPO has himself valued the shares after considering the infused money and resultant income from such infusion. This contention of the assessee finds support from the decision of Hon'ble Supreme Court in the case of Reva Investment P. Ltd. **(**249 ITR 337), wherein it has been held that for determining the correct value of shares, it

must be valued after considering the infusion of capital. On this score the reasoning of the TPO in rejecting the valuation report cannot be sustained.

11.6. We also note that in the valuation report, the shares were valued by following DCF Method. The TPO also followed the same method of DCF in valuing the shares. In other words both the Valuer and TPO used the DCF Method for valuing the shares and thus agreed that DCF Method is the correct method to value the shares. Then certainly it is not correct to use CUP Method to value the shares of Hybrid Capital for which the TPO has not given any reasons or justification. We also find merit in the without prejudice contentions of the assessee that both TPO and DRP have taken the value of shares at Rs. 16,594/- at which the shares were sold to Arya Infrastructure thereby not appreciating the fact that when the transaction of purchase and sales are made in foreign currency i.e. USD, then for applying the CUP method , the rate has to be considered in foreign currency i.e. USD and not after converting into Indian currency. The plea of the assessee finds support from the decision of the jurisdictional High court in the case of CIT Vs Tata Autocomp System Ltd(supra) wherein it has been held that in order to benchmark the interest rate on loan in foreign currency, interest rate linked with foreign currency should be considered. Similar ratio has been laid down by the Hon'ble Delhi High Court in the case of CIT Vs Cotton Natural (I) (P) Ltd.(supra).

11.7. We further note that both the authorities below namely the TPO and DRP have held the transaction of subscription of 5,00,000 shares of Hybrid Capital and sale of 6,00,000 shares

to Arya Infrastructure in AY 2010-11 as sham transactions for the reasons that the allotment of shares was made to foreign subsidiary primarily to set off the long term capital on sale of 1,00,000 shares Rs. 162,56,53,077/- against the short term capital gain resulting from sale of 5,00,000 shares. But the conclusion drawn by the both the authorities is devoid of any merit as both of them have overlooked the fact that long term capital gain on 1,00,000 shares have arisen only because of infusion of funds by the assessee in its subsidiary Hybrid Capital in consideration of which it got the allotment of 5,00,000 shares in the assessment year 2010-11. Had this infusion of funds not made by the assessee, this long term capital gain would have never arisen. Therefore on this proposition, we find merit that the conclusion of both the authorities to the effect that both subscription and sale of shares were undertaken to create artificial short term capital loss can not be sustained.

11.8. Accordingly, ground nos. 1 to 10 are allowed.

12. Ground no.11 reads as under:

> "The AO has erred in adding the amount of TP adjustmentof Rs. 2,33,000/-on the value of purchase of sharesto the taxable income contrary to the directions of DRP."

12.1.The issue raised in this ground is qua the transfer pricing adjustment of Rs 2,33,000 in respect of purchase of shares of Essar Steel Karnataka Ltd. The facts in brief are that the TPO made an adjustment of Rs 2,33,000 with respect to 100% shares of Essar Steel Karnataka Ltd. purchased by the assessee from its AE. The DRP directed the TPO to delete the adjustment of Rs 2,33,000 however, even after the direction by the DRP to delete

adjustment , the AO in the final assessment order sustained the adjustment of Rs 2,33,000/-

12.2. The ld AR submits that all the arguments as made in support of ground No. 1-10 are applicable to this ground also. Therefore, ld AR submits that the adjustment made by the TPO is liable to be deleted. The ld AR submits that in any case, the DRP has directed the AO to delete the adjustment however, the AO has incorrectly sustained it therefore, the TP adjustment of Rs.2,33,000 deserves to be deleted and a direction may kindly be issued. The ld Dr on the other hand fairly conceded that DRP has already directed to delete the TP addition of Rs. 2,33,000/-.

12.3. After hearing both the parties and perusing the directions of the DRP, we find that the addition of Rs 2,33,000 has been deleted by the DRP, however, the AO has not deleted the same in the final assessment order. We direct the AO to delete the said transfer pricing adjustment of Rs 2,33,000/-. We have also dealt with identical issue while disposing of ground nos. 1 to 10 above where we have directed the deletion of TP adjustment. Therefore we direct the AO to delete the addition of Rs. 2,33,000/-. Consequently ground no. 11 is allowed.

13. Ground no.12 reads as under:

> "The AO has erred in computing the long term capital gainat Rs. 1,62,56,53,076/- as against a sum of Rs. 1,62,06,09,906/-as per the return of income and as accepted in the draft assessment order".

13.1. The issue relates to erroneous computation of long term capital gains. The facts in brief are that the assessee filed its return of income showing total long term capital gain of Rs 162,05,20,414/- and after setting off other short term capital

loss of Rs 792,174,181, the net total long term capital gain was shown at Rs 82,84,35,725/- However, the AO in the final assessment order passed u/s. 143(3) has incorrectly computed the total long term capital gains at Rs 162,56,53,076 at page 14 of the final assessment order.

13.2. After hearing the rival submissions and perusing the material on record, we observed that in the draft assessment order dated 27th March, 2014, the AO had correctly calculated the net long term capital gain at Rs 82,84,35,725/-. However, while framing the final assessment order, the AO has wrongly calculated the long term capital gain at Rs. 162,56,53,076/-and not considered the capital losses incurred from other transactions. Therefore, considering the facts and circumstances of the case, we find that this is a mistake on the part of the AO while passing the final assessment order. Accordingly, we direct the AO to compute the capital gain in consonance with the draft assessment order dated 27th March 2014. The ground no. 12 is allowed.

14. Ground no.13 reads as under:

> "The AO, under the direction of DRP,has erred in making a disallowance of the expenditure on leave encashment of Rs. 1,44,60,288/- u/s 43B of the Act."

14.1. The grievance of the assessee in this ground relates to the disallowance u/s. 43B of the Act. The facts in brief are that during the year under consideration, the assessee had claimed a deduction pertaining to provisions created for leave encashment amounting to Rs. 3,21,62,602/- as per the ratio laid down by the Hon'ble Calcutta High Court in the case of Exide Industries Limited vs. Union of India (292 ITR 470) wherein it has been

held the provisions of section 43B(f) to be unconstitutional. During the assessment proceedings, the Assessing Officer was not convinced with the contention of the assessee and, accordingly, added the provision for leave encashment to the income of the assessee by disallowing the same u/s. 43B on the ground that the same was not actually paid.

14.2. We have heard both the parties and perused the material available on record including the judgment of Apex Court in the case of UOI vs. Exide Industries Limited (425 ITR 1) (SC), which has reversed the judgment of Calcutta High Court and has held that liability towards leave encashment would be allowed under Section 43 B of the Act only in the year in which the payment has been made. Thus, we find merit in the contention of the learned AR of the assessee that direction may be issued to the Assessing Officer to allow deduction on account of leave encashment in the year of payment. Accordingly, we direct the Assessing Officer to allow deduction in respect of leave encashment paid in respect of prior years as to be allowed in the year of payment. The ground no. 13 is allowed.

15. The ground no.14 is reproduced as under:

"The AO has erred in not giving set off of brought forward losses/unabsorbed depreciation of earlier years against the income computed for the year."

15.1. This ground relates to non-grant of set-off of brought forward losses/ unabsorbed depreciation. Briefly, the facts of the case are that during the year under consideration, the Appellant had carried forward unabsorbed depreciation and losses from the earlier years. However, the Assessing Officer while passing

the final assessment order has not granted the set off of the brought forward losses/ unabsorbed depreciation claimed by the assessee.

15.2. After hearing the contentions of both the sides and perusing the provisions of Section 72 of the Act, we find that the assessee is entitled to claim the set off the brought forwarded losses and unabsorbed depreciation against the income of the current year. Thus, the Assessing Officer's action in not allowing set off of brought forwarded losses and unabsorbed depreciation is wrong and against the provisions of the Act. We, accordingly, direct the AO to allow set-off of losses and unabsorbed depreciation in accordance with provisions of the I T Act. The ground no. 14 is allowed.

16. The ground no. 15 and 16 are reproduced as under:

> "15.The AO has erred in adding a sum of Rs. 321,32,33,000/-towards TP adjustments and another sum of Rs. 3,21,62,602/- towards provisions leave encashment to the net profit of the appellant for working out the book profit u/s 115JB of the Act."
>
> "16.The AO has erred in adding a sum of Rs.183,01,50,853/-towards TP adjustments and another sum of Rs. Rs. 3,21,62,602/- towards provisions leave encashment to the net profit of the appellant for working out the book profit u/s 115JB of the Act under the alternative computation of income on protective basis."

16.1. The issue in these grounds relate to adjustments in the computation of book profits under Section 115JB of the Act. Briefly, the facts of the case are that during the year under consideration, the assessee had declared a loss under the normal provisions of the Act as well as a book loss under Section 115JB of the Act. The Assessing Officer while computing the income chargeable to tax under the normal provisions of the Act

computed assessed income after taking into consideration the aforementioned TP adjustment, disallowance under Section 43B of the Act and disallowance under section 14A of the Act read with Rule 8D. While computing book profit under section 115JB of the Act, the Assessing Officer added disallowance under section 14A r.w. Rule 8D. However, while passing the final assessment order, the Assessing Officer added transfer pricing adjustment of Rs. 321,32,33,000 and provision for leave encashment Rs. 3,21,62,602 to the book profit.

16.2. The learned AR submitted that addition made by the Assessing Officer directly in the final assessment order under section 115JB with respect to transfer pricing adjustment of Rs. 321,32,33,000 and provision for leave encashment of Rs. 3,21,62,602 is contrary to the provisions of section 144C of the Act. He further submitted that the Assessing Officer cannot make a disallowance which was not made in the draft order passed under section 144C(1) of the Act. In this regard, the learned AR relied on the following decisions of Tata Motors Ltd. vs. DCIT (105 taxmann.com 7) and PCIT vs. Woco Motherson (406 ITR 375).The learned AR, without prejudice to the above, also submitted that transfer pricing adjustment made under section 92CA of the Act cannot be added while computing book profits under section 115JB of the Act as the Explanation - 1 to section 115JB does not provide for it. In support of his arguments, the learned AR relied on the orders of the Tribunal in the case of Owens Corning (India) P. Ltd. vs. DCIT (70 taxmann.com 395), wherein a similar view has been taken. The learned AR further submitted that the provision for leave

encashment cannot be disallowed under section 115JB of the Act as it is not in the nature of unascertained liability. In support of this he placed reliance on the decision of the Tribunal in the case of CIT vs. Kirloskar Systems Ltd. (220 Taxman 1) (Kar.); Caprihans India Ltd. vs. DCIT (114 taxmann.com 538) and Torm Shipping India Pvt Ltd. vs. ITO (88 taxmann.com 859). The ld AR therefore prayed that the grounds raised by the assessee may kindly be allowed.

16.3. The learned DR relied on the orders of the authorities below.

16.4. We have heard both the parties and perused the facts on record. We find that in this case the TPO has made adjustment with respect to transfer pricing and provision for leave encashment directly in the final assessment order. We note that the Assessing Officer has not made any disallowance in the draft assessment order passed u/s. 144C(1) of the Act. We, therefore, find merit in the contentions of the learned AR that the additions/adjustments which are not made in the draft assessment order cannot be made in the final assessment order. The case of the assessee finds support from the decisions in the case of Tata Motors Ltd. vs. DCIT (supra) and PCIT vs. Woco Motherson (supra). In view of the above facts and the ratio laid down by the co-ordinate Bench, we direct the Assessing Officer to delete the adjustments made in respect of transfer pricing adjustment of Rs. 321,32,33,000 and provision for leave encashment Rs. 3,21,62,602. Even such additions can not be made u/s 115 JB ofv the Act as the same do not fall under the Explanation 1 to that section. We are therefore inclined to allow

the grounds raised by the assessee. Ground no. 15 and 16 are allowed.

17. The assessee has also raised additional ground under rule 29 of Income Tax Appellate Tribunal rules, 1963 which as under:

> "1. The Learned Assessing Officer (AO) erred in making disallowance under section 14A of the Act amounting to Rs.10,89,38,861/- under the normal provisions as well as under section 115JB of the Act.
>
> 2. Without prejudice to the above, the Ld. AO erred in making disallowance under section 14A of the Act in excess of exempt income i.e. dividend received during the year under appeal. "

17.1 Briefly, the facts of the case are that the assessee had earned dividend income of Rs 29,84,73,040, out of which amount of Rs 2,53,70,047 has been claimed as exempt under Section 10 of the Act and rest was offered to tax as dividend received from foreign subsidiary. The Assessing Officer during the course of the assessment proceedings invoked provision of section 14A r.w. Rule 8D and made a disallowance of Rs.10,89,38,861 under normal computation as well as under section 115JB of the Act. Thus, the disallowance made by the Assessing Officer has exceeded the exempt income of Rs. 2,53,70,407.

17.2 The learned AR submitted before us that the issue raised in the additional ground is arising out of the assessment record and does not require any further verification of facts and, accordingly may be admitted. In defence, he relied on the decision of Hon'ble Apex Court in the case of National Thermal Power Co. vs CIT (2291TR 383) wherein it has been held that

ground not raised before the lower authorities can be raised for the first time before the Tribunal.

17.3 The learned DR, on the other hand, strongly objected to the admission of additional ground.

17.4 After hearing both the parties we find that the issue is emanating out of the assessment record and, therefore, we are inclined to admit the same for adjudication I view of the ratio laid down by the Hon'ble Apex Court in the case of National Thermal Power Co. vs CIT (supra).

17.5 We have heard the parties and have perused the material on record. We observe that in this case the exempt income is Rs 2,53,70,407 whereas the disallowance made by the Assessing Officer is Rs. 10,89,38,861 under the normal provisions of the Act as well as u/s. 115JB. In our opinion, the amount of disallowance cannot exceed the exempt income as has been held by Hon'ble Supreme Court in the case of Maxopp Investment Pvt. Ltd. Vs. CIT (2018) 91 taxman.com 154 SC. Besides, the disallowance made u/s. 14A cannot be added to the book profit as computed u/s. 115JB of the Act as has been held in the case of Tata Motors Ltd. vs. DCIT (105 taxmann.com 7) and DCIT vs. Edelweiss Commodities (121 taxmann.com 223). Accordingly, we direct the Assessing Officer to restrict the disallowance u/s. 14A to Rs 2,53,70,407 under the normal provisions of the Act and further directed the Assessing Officer not to make any addition u/s. 115JB of the Act while computing book profit. In the result, additional ground No.1 is allowed. Since we have allowed the additional

ground No.1 in favour of the assessee, the additional ground No.2 does not require any adjudication.

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

Order pronounced in the open court on 08.01.2021.

Sd/-	**Sd/-**
(Ram Lal Negi)	**(Rajesh Kumar)**
JUDICIAL MEMBER	**ACCOUNTANT MEMBER**

Mumbai, Dated: 08.01.2021.

* Kishore, Sr. P.S.

Copy to: The Appellant
The Respondent
The CIT, Concerned, Mumbai
The CIT (A) Concerned, Mumbai
The DR Concerned Bench

//True Copy//

By Order

Dy/Asstt. Registrar, ITAT, Mumbai.