

INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH "A": NEW DELHI

BEFORE SHRI R.K. PANDA, ACCOUNTANT MEMBER
AND
SHRI N. K. CHOUDHRY, JUDICIAL MEMBER

ITA No.167/Del/2019
(Assessment Year: 2015-16)

Jt. Commissioner of Income Tax, Special Range-10, New Delhi (Appellant)	Vs. Sh. Bhanu Chopra, M-140, Greater Kailash-II, Delhi PAN: AGWPC5625R (Respondent)
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Revenue by :	Shri R. K. Sharma, Ld. Adv
Assessee by:	Shri Ishtiyaque Adhmed, Ld. CIT DR

Date of Hearing	11/04/2022
Date of pronouncement	29/04/2022

ORDER

PER N.K. CHOUDHRY, J. M.:

1. The revenue has preferred the instant appeal against the order dated 05.10.2018, impugned herein, passed by the Ld. Commissioner of Income-tax (Appeals)-10, New Delhi (in short 'Ld. Commissioner) u/s 250(6) of the Income-tax Act, 1961 (in short "the Act"), for the assessment year 2015-16, whereby the assessment order passed by the AO u/s 143(3) of the Act was upheld.

2. In this case the Assessee had declared income of Rs. 31,99,25,740/- by filing its return of income on dated 25.08.2015 which resulted into an addition of Rs. 47,21,93,975/- u/s 56(2)(vii)(c) read with section 2(24)(xv) of the Act.

3. The Assessee challenged the making of the addition in his hand before the Id. Commissioner who deleted the same, against which the Revenue Department is in appeal before us.

4. Heard the parties and perused the material available on record. The Id. DR relied upon the order passed by the AO, whereas the Id. AR supported the impugned order while relying upon CBDT Circulars and various decisions of the Hon'ble Apex Court, High Courts and Tribunal to the effect that provisions of section u/s 56(2)(vii)(c) of the Act would not apply to bonus shares.

4.1 The only issue involved in the instant case relates to acquiring of bonus shares and applicability of the provisions of section 56(2)(vii)(c) of the Act to the same.

4.2 The AO computed the FMV of bonus share by HCL Technologies Ltd in terms of Rule 11UA of the Rules to the tune of Rs. 47,21,93,975/- and consequently, added the said amount in the total income of the Assessee by applying the provisions of section 56(2)(vii)(c) of the Act. The AO further observed that section u/s 56(2)(vii)(c) read with section 2(24)(xv) is charging section which created entirely new charge of tax on the case of the individuals and HUF on receipt of property without consideration or at a consideration which is less than fair market value. The provision applies only when the recipient of the property is an individual or HUF. Further, the taxable event is receipt of property without consideration or for a consideration which is less than the fair

market value. The AO also observed that from the plain reading of the provision of the Act it is clear that section 55 seeks to define 'cost of acquisition' for the purpose of computation of capital gains. Section 55 does not apply for the purpose of the computation of income under head "income from other sources".

4.3 It was also observed by the AO that the taxable event is receipt of property without consideration or for a consideration which is less than FMV. It was further observed by the AO that the Assessee had received property in the form of Bonus Share without consideration and therefore mischief of section 56(2)(vii)(c) is applicable in the case of the Assessee. The AO also observed that from the harmonious reading of the provision of section 56(2), 55(2)(a)(a) and section 49(4) it becomes clear that there is no conflict between section 55(2)(a)(a) and section 56(2)(vii)(c) of the Act. The Assessee also has tried to take benefit of loss on sale of original unit twice. The first benefit or first set off was claimed in Assessment Year 2015-16 as the Assessee had actually set off the actual loss arising on sale of original units against the LTCG earned on sale of shares of Ridaan/Rate Gain. The second benefit is also claimed in the same Assessment Year i.e. 2015-16 as the Assessee has not offered income on receipt of bonus units u/s 56(2)(vii)(c) of the Act. It was further observed that once the loss of original shares has been offset against the gain made on sale of shares of Ridaan, there is no loss left which can be brought to offset the gain on bonus units.

4.4 The Ld. Commissioner in the impugned order, while deleting the said addition made by AO U/s 56(2)(vii)(c) of the Act, observed as under:

5.3 In this regard, the appellant has submitted that issue of bonus shares is capitalization of its profits by

the issuing company. There is neither any increase nor decrease in the wealth of the shareholder (or of the issuing company) on account of a bonus share issue. What in effect transpires is that the value of existing share gets split in existing and new bonus shares. It is further submitted that there is no receipt of any property by the shareholder, and what stands received by him is the split shares out of his holding. Accordingly, there is no gift or accretion to property. The shareholder is getting only the value of his/her existing shares, which stands reduced to the same extent. The same has the effect of reducing the value per share. Further, it is submitted that there is a specific Section 55(2)(aa)(iiia) of the IT Act which provides that for the purposes of section 48 and 49, the cost of acquisition in relation to the financial asset allotted to the assessee without any payment and on the basis of holding of any other financial asset (i.e. Bonus' shares etc), shall be taken to be Nil. Hence, specific provision would prevail over the general provisions. Cost of bonus shares shall be considered as Nil and subsequent sale of such bonus shares shall be liable for capital gain tax as per then provision of the IT Act. Further, since the cost of bonus shares is Nil in the hands of recipient, there is no benefit / income being availed by recipient on receipt of bonus shares. The appellant has submitted that bonus shares are not something which has been received free or for a lesser FMV. Consideration has flown out from the holder of the shares, which is reflected in the depression in the intrinsic value of the original shares held by him. It is submitted that there must be a real 'gain' in the hands of the assessee - so as to hold that 'income' has resulted to him and thereby, tax is attracted as a statutory consequence. A 'gain is conceivable when some enrichment results to the assessee from a transaction. In short, there must be a betterment in the wealth position of the assessee by the transaction. Whereas in the case of appellant, the Bonus shares were allotted at NIL cost. Factually, Bonus shares does not result in getting a property without consideration or for inadequate consideration, reason being the shareholders are entitled to the bonus shares because of his existing shareholding in the company and that the value of existing shares gets split into original shares and Bonus shares. In other words, it results in a pro-

rata decrease in the value of original equity shares upon issuance of Bonus shares. The issue of Bonus shares is nothing other than capitalization of shares. In other words, there is no receipt of any property by shareholder and what stands received by him is the split shares out of his own holding. The said principle is clearly manifest from reading of section 56 of the IT Act. Further, it is contended that taxing of the difference between the consideration paid by the assessee and the market value of the property is only a computation provision and not a charging one. It is only provides a means to measure the gain. In short, the charge of income tax u/s 56(2) of the IT Act is only on a 'gain' and it is only if there is a gain in the real sense that the same gets measured in terms of the quantifier i.e. the difference between the market value of the property and the consideration paid. On the other hand, if there is no gain, then there is no need to resort to the computational provision at all. The appellant has also referred to section 2(24)(xv) in respect of definition of 'income'. Issue of bonus shares to shareholders is mere capitalization of the existing profits and reserves of the issuer company and what the shareholders receive by way of bonus shares are their pre-existing entitlements only and therefore, there is no new gain created to the allottees on allotment of bonus shares. On allotment of bonus shares, there is neither 'gain' nor betterment in his wealth position to the allottee in absence of income in qualitative sense. It is also submitted that there is no 'transfer' involved in allotment of shares by a company to the share applicants as has been observed by the Hon'ble Supreme Court in the case of Khoday Distilleries Ltd. vs. CIT (civil appeal no. 6654 of 2008 dated 14-11-2008). The Supreme Court in this case observed that the bonus shares are nothing but mere capitalisation of the profits of the Company in respect of which certificates are issued to the shareholders entitling them to participate in the amount of the reserve. It doesn't involve release of assets either as income or as capital.

5.4 The assessment order and the submission of the appellant have duly been considered. It is noted that the AO has not given any adverse finding in respect of transactions of purchase and sale of shares / bonus shares. The crux of the matter is that since bonus shares were received without any consideration, the

provisions of Section 56(2)(vii)(c) are applicable. The „ AO has also given the finding that the appellant has tried to take benefit of the loss on sale of original shares twice. The first benefit or first set off was claimed in A.Y. 2015-16 as the appellant has actually set off the actual loss arising on sale of original shares of HCL Technologies Ltd against the LTCG earned on sale of shares of Ridaan. The second benefit is claimed in the same A.Y. 2015-16 as the appellant has not offered income on receipt of s shares u/s 56(2)(vii)(c) of the Act. In this context, it is noted that under section 70 of the / the assessee is eligible for set off of the loss arising under the same head of capital gains, is noted that issue of bonus shares is by definition capitalization of its profits by the issuing company. There is neither any increase nor decrease in the wealth of the shareholder or of the issuing company on account of issue of bonus shares and as a result the value of existing share gets split in existing and new bonus shares. There is no receipt of any property by the shareholder, and what stands received by him is the split shares out of his existing holding of shares. As a result, there is no gift or accretion to property. Bonus shares are not something which has been received free or for a lesser FMV. Consideration has flown out from the holder of the shares, which is reflected in the decrease in the intrinsic value of the original shares held by him. In this regard, reliance is placed on the decision of the Hon'ble Supreme Court in the case of CIT v. Dalmia Investment Co. Ltd. (1964) 52 ITR 567 (SC). In the said case, the issue was valuation of bonus shares and it was observed by the Hon'ble Court that -

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Further, in the case of Dr. RajanPai, Bangalore Vs Department of Income Tax by ITAT Bangalore vide ITA No. 1290/Bang/2015, it was held that the allotment of bonus shares cannot be considered as received for an inadequate consideration and therefore, it is not taxable

as income from other sources u/s 56(2)(vii)(c) of the IT Act. The Hon'ble ITAT observed that the issue of bonus shares is by definition capitalization of its profits by the issuing company. It is held that when bonus shares are received, it is not something, which has been received free or for a lesser FMV. Consideration has flown out from the holder of the shares, may be unknown to him/her, which is reflected in the depression in the intrinsic value of the original shares held by him/her. The relevant observations of the Hon'ble ITAT in the case of Dr. RajanPai are reproduced as under:-

“There is neither any increase nor decrease in the wealth of the shareholder (or of the issuing company) on account of a bonus issue, and his percentage holding therein remains constant. What in effect transpires is that a share get split (in the same proportion of all the shareholder), as for example by a factor of two in case of a 1:1 bonus issue. Reference in this regard may be made to the decision in CIT vs. Dalmia Investment Co. Ltd [1964] 52 ITR 567 (SC) as well as in Khoday Distilleries Ltd (supra), wherein reference stands made to the former, also quoting therefrom, besides inter alia to Hunsur Plywood Works Ltd. vs. CIT [1998] 229 ITR 112 (SC), where the same were referred to as 'capitalization shares'. In other words, there is no receipt of any property by the shareholder, and what stands received by CIT (A) - 10, New Delh Sh. Bhanu Chopra (AY2015-16) him is the split shares out of his own holding. It would be akin to somebody exchanging a one thousand rupee note for two five hundred or ten hundred rupee notes. There is, accordingly, no question of any gift of or accretion to property; the share-holder getting only the value of his existing shares, which stands reduced to the same extent. The same has the effect of reducing the value per share, increasing its mobility and, thus, liquidity, in the sense that the shares become more accessible for transactions and, thus, liquidity, i.e., considered from the holders' point of view.”

Further, it has been observed by the Hon'ble ITAT as under:-

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Further, in the case of Sudhir Menon HUF (ITA No. 4887/Mum/2013), order was passed by the ITAT Mumbai Bench on the similar grounds.

5.5 It is also noted that if the cost of the bonus shares is governed by section 55(2)(aa)(iiia) of the Act, then by applying the provisions of section 56(2), its FMV would be charged to tax twice, once at the time of receipt u/s 56(2) and secondly at the time of its sale as the cost of Bonus Shares is required to be taken at Nil as per the provisions of the Act. It is further noted that there is a specific provision under section 55(2)(aa)(iiia) of the Act which provides that for the purposes of section 48 and 49, the cost of acquisition in relation to the financial asset allotted to the assessee without any payment and on the basis of holding of any other financial asset in the form of Bonus shares etc. shall be taken to be Nil. Since there are specific provisions in respect of cost of Bonus Shares, the same would prevail over the general provisions.

5.6 Considering the above factual matrix of the case and the judicial pronouncements in this regard, I find that provisions of section 56(2)(vii)(c) are not applicable in the case of the appellant and therefore, addition of Rs.46,21,93,975/- is deleted. Accordingly, the above ground of appeal is allowed.

4.5 We observe that the Id. CIT(A) while controverting the findings of the AO and coming to the conclusion that provisions of section u/s 56(2)(vii)(c) are not applicable to the case of the Assessee, also followed the judgment of the Hon'ble Apex Court in the case of CIT Vs. Dalmia Investment Co. Ltd (1964) 52 ITR 567 (SC) wherein, it was held as under:-

"A stock dividend really takes nothing from the property of the corporation, and adds nothing to the interests of the shareholders. Its property is not diminished, and their interests are not increased. ... The proportional interest of each shareholder remains the same. The only change is in the evidence which represents that interest, the new shares and the original shares together representing the same proportional interest that the original shares represented before the issue of the new ones. ...In short, the corporation is no poorer and the stockholder is no richer than they were before. ...If the plaintiff gained any small advantage by the change, it certainly was not an advantage of Rs 417,450 the sum upon which he was taxed.

... What has happened is that the plaintiff's old certificates have been split up in effect and have diminished in value to the extent of the value of the new."

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"In other words, by the issue of bonus shares pro rata, which ranked paripassu with the existing shares, the market price was exactly halved, and divided between the old and the bonus shares. This will ordinarily be the case but not when the share do not rank paripassu and we shall deal with that case separately. When the shares rank paripassu the result may be stated by saying that what the shareholder held as a whole rupee coin is held by him, after the issue of bonus share, in two 50 NP Coins. The total value

remains the same but the evidence of that value is not in one certificate but in two."

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"It follow that though profits are profits in the hands of the company, when they are disposed of by converting them into capital instead of paying them over to the shareholders, no income can be said accrue to the shareholder because the new shares confer a title to a larger proportion of the surplus assets at a general distribution.

The floating capital used in the company which formerly consisted of subscribed capital and the reserves now becomes the subscribed capital."

4.6 The Id. Commissioner while deciding the issue, also relied upon the orders passed by the Hon'ble Tribunal in the case of Dr. Rajan Vs. Department of Income Tax { ITA No. 1290/Bang/2015} wherein, the judgment referred above of the Hon'ble Apex Court in the case of the CIT Vs. Dalmia Investment Co Ltd (Supra) was also relied upon by the Hon'ble Tribunal and in the case of Sudhir Menon HUF Versus The ACIT (ITA No. 4887/Mum/2013) wherein, it was clearly held by the Hon'ble Tribunal that allotment of bonus shares cannot be considered as received for an inadequate consideration and therefore, it is not taxable as income from other sources u/s 56(2)(vii)(c) of the Act. Further, the issue of bonus share is by capitalization of its profit by the issuing company and when the bonus shares are received it is not something which has been received free or for a lesser FMV. Consideration has flown out from the holder of the shares may be unknown to him/her, which is

reflected in the depression in the intrinsic value of the original shares held by him/ her.

For ready reference the observations of the Hon'ble Tribunal in the case of Rajan Pai Bangalore Vs. Department of Income Tax (Supra) are reproduced herein below:-

"It is easy to see that the new share partakes a part of the value of the existing share, which is only on the basis of the underlying assets on the company's books. The excess (over face value), or Rs. 1,400/-, gets apportioned over two shares as against one earlier, which is already the shareholders' property. This is also the basis and the premise of the decisions in the case of Dhundabhoj Kapadia vs. CIT [1967] 63 ITR 651 (SC) and H. Hoick Larsen vs. IT [1972] 85 ITR 285 (Bom), relied upon and referred to by the parties before us. As long as, therefore, there is no disproportionate allotment, i.e. shares are allotted pro-rata to the shareholders, based on their existing holdings, there is no scope for any property being received by them on the said allotment of shares: there being only an apportionment of the value of their existing holding over a larger number of shares. There is, accordingly, no question of section 56(2)(vii)(c), though per se applicable to the transaction, i.e., of this genre, getting attracted in such a case."

4.7 We find that even the CBDT Vide Circular No. 06/2014 issued on dated 11.02.2014 clarified that bonus units at the time of issue

would not be subjected to additional income tax u/s 115R of the Act, since issue of bonus units is not akin to distribution of income by way of dividend. This may be inferred from provisions of section 55 of the Act which prescribed that "cost of acquisition" of bonus units shall be treated as Nil for purposes of computation of capital gains tax.

4.8 Further, the CBDT vide circular 717 dated 14.08.1995 clarified that "in order to overcome the problem of complexity, a simple method has been laid down for computing of cost of acquisition of bonus shares. For the sake of clarity and simplicity, the cost of bonus shares is to be taken as 'Nil' while the cost of original shares is to be taken as the amount paid to acquire them. This procedure will also be applicable to any other security where a bonus issue has been made."

4.9 The issue under consideration has been elaborately considered by the Hon'ble Tribunal in various cases such as Rajan Pai Bangalore Vs. Department of Income Tax and Sudhir Menon HUF (supra) and even by the Hon'ble Apex Court in the case of CIT v. Dalmia Investment Co. Ltd. (Supra) as relied upon by the Ld. Commissioner while holding that the provisions of section 56(2)(vii)(c) of the Act are not applicable to the bonus shares.

4.10 Even otherwise we do not find any material and reason to controvert the findings of the Ld. Commissioner on the issue under consideration, therefore in view of aforesaid analysis and respectfully following the Judgments referred above of the Hon'ble Apex Court and the Hon'ble tribunal and the Circulars issued by the CBDT, the appeal of the revenue is liable to be dismissed. Hence, ordered accordingly.

5. In the result, appeal filed by the Revenue Department stands dismissed.

Order pronounced in the open court on 29/04/2022.

-Sd/-
(R.K. PANDA)
ACCOUNTANT MEMBER

-Sd/-
(N.K. CHOUDHRY)
JUDICIAL MEMBER

Dated: 29/04/2022
A K Keot

Copy forwarded to

1. Applicant
2. Respondent
3. CIT
4. CIT (A)
5. DR:ITAT

ASSISTANT REGISTRAR
ITAT, New Delhi