

**THE INCOME TAX APPELLATE TRIBUNAL
DELHIBENCH 'C', NEW DELHI**

Before Sh. C. M. Garg, Judicial Member

Dr. B. R. R. Kumar, Accountant Member

ITA No. 1309/Del/2020 : Asstt. Year: 2016-17

ACIT, Circle-10(1), New Delhi-110001	Vs.	M/s Gamma Pizzakraft (Overseas) Pvt. Ltd., 802, Ansal Bhawan, 16, KG Marg, New Delhi-110001
(APPELLANT)		(RESPONDENT)
PAN No. AACCG8016D		

**Assessee by : Sh. T. M. Shiva Kumar, Adv. &
Ms. S. V. Rateria, Adv.**

Revenue by : Mohd. Gayasuddin Ansari, CIT DR

Date of Hearing: 16.02.2023

Date of Pronouncement: 12.05.2023

ORDER

Per Dr. B. R. R. Kumar, Accountant Member:

The present appeal has been filed by Revenue against the order of Id. CIT(A)-4, New Delhi dated 20.01.2020.

2. Following grounds have been raised by the Revenue:

"1. Whether on the facts and circumstances of the case and in law, the Id. CIT(A) has erred in deleting the addition of Rs.24,80,39,169/- made by the AO on account of valuation of shares at a premium of Rs.55.65 per share u/s 56(2)(viib) of the Income Tax Act, 1961."

Facts of the Case:

3. The assessee is a Private Limited Company and holding company of wholly owned subsidiaries namely, M/s Gamma Pizzakraft Private Limited, M/s Gamma Pizzakraft Lanka Private Limited and M/s French Restaurants Private Limited. The assessee company is doing its operational and business activities of operating a bakery restaurant and operating quick service restaurants (QSR) in India and Sri Lanka through its wholly owned subsidiaries (WOS).

4. The assessee had filed its return of income for AY 2016-17 on 08.10.2016 declaring a loss of Rs. 10,24,33,542/-. The AO passed order u/s 143(3) of the Act assessing the income at Rs. 14,56,05,630/- after making an addition of Rs.24,80,39,169/- under section 56(2)(viib) of the Act.

5. During the year, the assessee company had issued 54,33,548 equity shares to Sapphire Foods India Pvt. Ltd. at a premium of Rs.55.65 for the share of Face Value of Rs.10/- and received a total of Rs.30,23,74,146/-. Sapphire Foods Pvt. Ltd. is an entity of large venture capitalists [Goldman Sachs Investments Holding (Asia) Limited] and the investment in the assessee company was part of overall transaction of acquisition of Pizza Hut and KFC outlets in India and Sri Lanka. The overall transaction has been cleared by the Competition Commission of India (CCI) vide its order dated 13.08.2015 under section 31(1) of Competition Act, 2002.

Invocation of Section 56(2)(viib):

6. The assessee company has obtained a valuation report from the Chartered Accountant as required under Rule 11UA(2)(b) of IT Rules, 1963 who had certified the fair market value ('FMV') of unquoted equity share of the company to be Rs.65.65 per share by adopting Discounted Free Cash Flow Method ("DCF") for valuing the shares.

7. In the course of assessment proceedings, the AO examined the valuation report prepared by the Valuer Sh. Ashok Kumar Verma, CA and noted that the valuer has determined the FMV of the shares at Rs.65.65/- per share while the same worked out to Rs.10/- per share under Net Asset Value Method. Further, the AO compared the projections of Profit After Tax (PAT) made in the valuation report with the actuals achieved in the intervening period and observed that there was a difference between the actual profit/loss as per financial statements for the next two years i.e. F.Y.2016-17 and F.Y.2017-18 and the figures as projected in the valuation report.

8. Thereafter, the AO summoned the valuer and recorded his statement. Based on this statement, the A.O. made observation that the valuer has not verified the data and the valuation has been made on the basis of projections and other details provided by the management. The AO further noted that the valuer has also failed to produce all the documents relied upon while preparing the valuation report. The AO held that according to the Valuer, if the projections are not achieved, the basis of valuation shall lose its sanctity as DCF method.

9. The A.O. show-caused the assessee on 22.11.2018 which reads as under:

"CA Neeraj Wadhawan, VP Finance in the group companies and Authorized Representative of assessee attended today. Assessee has issued shares to M/s Sapphire Foods India Pvt. Ltd. @ 65.65 per share of Rs.10/- face value and received Rs.55.65 as premium. Assessee has followed and relied on DCF method and valuation was done by CA Sh. Ashok Kumar Verma. In this regard Valuer CA Sh. Ashok Kumar Verma was summoned and his statement was recorded with regard to valuation report as prepared by him. During recoding of statement, Mr. Ashok Kumar Verma accepted that DCF is based on projections and if projections have failed valuation of shares will lose their its sanctity. Further, if assessee was aware that in upcoming years, it will perform as per projections made in DCF report, why did it not pay advance tax as per projections. To sum up since valuation report as per DCF prepared by Mr.Ashok Kumar Verma has lost its sanctity & company has not performed accordingly. Therefore assessee through its authorized representative is hereby show caused as to why valuation report submitted by assessee should not be rejected & value per share should be taken as per method provided in rule as per I.T. Rules, 1962. After taking value of shares as per Rule 11UA, necessary addition to be made in assessee's income as per S.56(2)(viib) of the I.T. Act."

10. In response to the said show cause, the assessee filed its reply on 03.12.2018 highlighting the following points:

- a) As per the requirement under the Act, the company had obtained a report from the accountant who has determined FMV of the share under DCF method and that DCF method

was the most appropriate method for valuation of share of a going concern.

- b) For larger businesses entities, DCF value is commonly a sum-of-the-parts analysis, where different business units are modeled individually and added together.
- c) Even though DCF is based essentially on projections, it is not correct to expect the same figure in actual performance. The projections are always estimates and the same may or may not match with the actual performance figures as the business environment is very dynamic and keeps on changing every moment.
- d) The statement of the CA that the DCF method loses its sanctity if the actual figures did not match with projections cannot be a ground for rejection of valuation done under DCF method.
- e) The assessee was a holding company and its valuation is dependent on the business of its subsidiaries. Even if the subsidiaries outperform the projections, there would be no income tax liability in the hands of the holding company and that is why the assessee need not have paid higher advance tax on the basis of the projections made in the DCF method.
- f) The Book Value method which is based on historical cost method is not appropriate method for valuing the shares of a going concern like the assessee. In support of the same, copy of technical guide issued by ICAI was submitted to the AO.
- g) The investors are well known business owners having vast business experience and obtained the best price for the shares.

h) The assessee submitted that certain general statement of the valuer could not be a basis for making additions.

11. It is a fact on record that the assessee made further submissions on 07.12.2018 vide letter dated 06.12.2018. The AO refused to accept the said letter on 07.12.2018. The assessee attempted to submit the letter through Speed Post also met with "unclaimed" remark by the Postal Authorities and in that background the Assessee uploaded the reply on the portal on 10.12.2018. [Relevant facts are summarized at para 12 of Order of CIT(A)].

12. The AO passed the Assessment Order rejecting the valuation of shares under DCF method and determined the value of shares at Rs.10/- per share by adopting "Net Asset Value/ Book Value method" and made an addition of Rs.24,80,39,169/- being difference between the "Consideration received" and the "Book Value of the shares".

13. Aggrieved by the Assessment Order, the assessee filed first appeal under section 246A of the Act before CIT(A)-4, New Delhi on 24.01.2020.

14. Before the Id. CIT(A), the assessee filed the following documents to support their case:

- Evidence of speed post of reply dated 06.12.2018 on 7.12.2018 on 19.56 hrs which is not acknowledged by AO
- Confirmation as available on e-filing portal of appellant w.r.t. to fact that reply dated 06.12.2018 was uploaded on 10.12.2018 as e-proceedings were not closed though Order is of date as 09.12.2018.

- Sworn Affidavits of Ashok Kumar Verma, Chartered Accountant Valuer of FMV of Equity Shares issued during the financial year ending 31.03.2016 relevant for assessment year 2016-17.
- Document and Papers relied by the Valuer for preparing the Valuation report.
- Audited financial statements of the company as provided by the management for the year ended March 31, 2014.
- Provisional financial statements of the company as provided by the management for the year ended March 31, 2015.
- Financial projections of the company for years ended on March 31, 2016 (part period); March 31,2017; March 31,2018; March 31,2019 and March 31,2020.
- Management certificate of fair value of share of its subsidiaries In Sri Lanka viz. French Restaurants (Private) Limited and Gamma Pizzakraft Lanka (Private) Limited from respective management of its subsidiaries.
- Information on the business and profile of the Company.
- Information and explanations provided to the valuer for the valuation of shares - Shareholder's agreement dated 28.04.2015 entered by and among following parties.
- Existing shareholders listed in Schedule I of the said agreement AND Gamma Pizzakraft (overseas) Private Limited (appellant); AND Sapphire Foods India Private Limited (Investor).
- Order under section 31(1) of the Competition Act, 2002 by the Competition Commission of India.

15. At this juncture, it is relevant to reproduce the order of the Id. CIT(A) with regard to the sequence of events pertaining to explanation of the assessee to the show cause issued by the AO and the subsequent events that took place.

"12. From the assessment order, it is clear that the AO had duly show-caused the Appellant on 22.11.2018 to submit its rebuttals against his proposal to reject the valuation of shares under DCF method based on the statement of the Valuer Ashok Verma, CA. The appellant seems to have furnished certain reply on 03.12.2018 which did not satisfy the AO. Thereafter according to the appellant, it tried to submit further letter and details on 07.12.2018 vide letter dated 06.12.2018 which were not entertained by the AO. On AO's refusal to entertain their submissions, the appellant has sent the same letter and details by Speed Post on 07.12.2018 at 19:56 hrs. (proof has been submitted as part of additional evidence). The AO, however has 'refused' to accept the Speed Post which is evident from the postal remark 'Refused' on the envelope submitted as part of the additional evidence. Left with no other alternative, the appellant had uploaded the letter on the e-filing portal on 10.12.2018. 8th and 9th Dec 2018 happen to be non-working days being weekend. The appellant has submitted that the successful uploading of the response on the e-filing portal indicated that the e-proceedings had not been closed by then, though Assessment Order is dated 09.12.2018. According to the Appellant, the order was passed on 11.12.2018 though it is dated 09.12.2018. The Appellant has submitted the affidavits of Mr. Neeraj Wadhawan, the AR in explaining the details of how all this took place. In the Remand report the AO has stated that the assessment order has been passed on 09.12.2018 itself as is evident from the system date on the order and that system does not allow backdating of the order.

13. *The Appellant has also submitted the documents, which were required to be filed by the Valuer to the AO, as additional evidence. They have also filed an affidavit from the Valuer who has claimed that he had visited the office of the AO on the appointed date i.e. 26.11.2018 but had to return without filing the details as the AO was busy with some other matter and he could not wait longer as he had some other appointment. In the Remand Report, the AO has stated that this fact is not emerging from the Assessment Order and that the AO has clearly stated that the Valuer did not submit the details till the date of order.*

14 *Finally the AO, in her Remand Report, requested this office not to entertain the Additional Evidences as the conditions specified under Rule 46A are not satisfied.*

Decision on admission of additional evidence

15. *Examination of facts shows that the appellant had made an attempt to submit certain reply and details vide letter dated 06.12.2018. This fact is established by the Speed Post details, affidavit of the AR and also the uploading of the letter on 10.12.2018. All these events could not have been an afterthought as the same are supported by hard evidences. As regards, date of order, I agree with the AO that the system does not allow backdating of the order and thus the appellant's submission that the order was passed on 7.12.2018 cannot be accepted. However, it cannot be denied that the appellant did try to submit the reply by at least before the date on which the order seems to have been passed. It is noted here that the Speed Post is dated 07.12.2018 and the order is dated 09.12.2018. The refusal by the AO of the Speed Post on 10.12.2018 (supported by postal remark 'Refused') indirectly supports the claim of the appellant that they tried to file the details before the AO on 07.12.2018 and only after their failure they had sent the letter by Speed Post. Further, the Valuer is a third party*

who may not be much bothered about the Appellant's fate due to his wrong conduct. If he had not furnished the documents required by the AO, it was for the AO to have enforced his attendance and ensured compliance.

16. From the above facts, it is clear that the AO had refused to admit the evidences which he should have admitted, as the same were relevant to the matter under consideration by him. The assessment was getting barred by limitation only on 31.12.2018 and he had sufficient time to entertain the appellant's submissions. This also amounts to not giving sufficient opportunity to the appellant before making such huge addition to the total income."

16. Having considered the submissions of the assessee, the Id. CIT(A) diligently raised the following issues:

- i. Whether AO was correct in rejecting the DCF method and the fair market value (FMV) determined under DCF method by comparing the actual performance figures with the projections used under the DCF method.
- ii. Whether the AO can change the method of valuation of unquoted shares under Rule 11UA of I.T. Rules 1962.
- iii. Whether the AO erred in rejecting the DCF method because the Valuer failed to furnish the documents called for by him.
- iv. Whether DCF is the most appropriate method in the instant case as espoused by the appellant.
- v. Whether AO can reject the DCF method when this method has been duly prescribed under the law itself.
- vi. Whether there is any requirement to show the existence of intention to evade tax in order to invoke provisions of section 56(2)(viib) of the Act.

- vii. Whether the AO erred in observing that the appellant should have deposited advance tax as per the projection figures.

17. The decision of Ld. CIT(A) on each of these issues is at para 20-26 of the order which has been duly perused.

Issue no. 1:

18. Whether AO is correct in rejecting the DCF method and the FMV determined under DCF method by comparing the actual performance figures with the projections used under the DCF method?

The appellant had issued shares to M/s Sapphire Foods India Pvt. Ltd. at Rs.65.56 per share of face value Rs.10/- per share. The valuation has been carried out by Shri Ashok Verma, CA who determined the value based on DCF method. He has relied upon the projections as estimated by the Management. The question here is whether he is required to independently verify the correctness of the projections given by the Management. It is a fact that a chartered accountant / valuer is an expert in valuing the shares as per certain set rules and guidelines issued by Accounting bodies such as the Institute of Chartered Accountant of India (ICAI). He is not expected to have an expertise on the potential of any business operation. Hence, his reliance on the estimated projection of financials given by the Management cannot be faulted in

entirety. However, it is noted here that if the projections are very unrealistic and any unusual fact is apparent on the very face of it, then a valuer is required to verify if there are any factors which he should consider while determining the value of the share. In the instant case, the AO has compared the actual performance of the company post valuation date with the projections. The AO thus has the benefit of hindsight. But the valuers do not have it. The AO has not pointed out any relevant facts which should have been considered by the Valuer at the time of valuation which he had missed out. Basing his decision on the basis of hindsight is not only unfair but also goes against the very principles of valuation of shares today on the basis of projecting their future performance. The performance should always match with the projections made at the time of valuation, unless it is shown that the Valuer missed considering a vital fact which was available at that point of time and that the same affected the final value arrived at.

Even otherwise, it is noted that the AO has overlooked that the appellant is a holding company and its share value would depend on the performance of business of its subsidiaries. The appellant has produced the performance figures as per its consolidated audited financial statements. A perusal of the same shows that the performance, in fact, was much better than the projections adopted

in the DCF method for F.Y. 2016-17 and 2017-18. The comparison between profit figures considered in the Valuation Report and Profit as per Consolidated Audited Balance sheet as laid down in appellant's letter dated 06.12.2018 are noted below:

PARTICULARS	FY- 2016-17	FY- 2017-
EBITDA		
<i>As per Projections</i>	27,851/-	42,436/-
<i>As Per Actual</i>	1,40,179/-	1,35,845/-
PAT		
<i>As per Projections</i>	15,766/-	24,452/-
<i>As Per Actual</i>	34,349/-	32,246/-

19. Hence, the Id. CIT(A) concluded that in the instant case there is no merit in rejecting the DCF method on the ground of mismatch between the projections adopted in DCF method and those achieved during the first two years post-valuation date.

Issue no. 2:

20. Whether the AO can change the method of valuation of unquoted shares under Rule 11UA of I.T. Rules 1962?

21. The provisions of Section 56 and Rule 11UA as under:

"Income from other sources.

56. (1) Income of every kind which is not to be excluded from the total income under this Act shall be chargeable to income-tax under the head "Income from other sources", if it is not chargeable to income-tax under any of the heads specified in section 14, items A to E.

(2) In particular, and without prejudice to the generality of the provisions of sub-section (1), the following incomes, shall be chargeable to income-tax under the head "Income from other sources", namely :—

(i) dividends;

(ia) income referred to in sub-clause (viii) of clause (24) of section 2;

ib).....

(viib) where a company, not being a company in which the public are substantially interested, receives, in any previous year, from any person being a resident, any consideration for issue of shares that exceeds the face value of such shares, the aggregate consideration received for such shares as exceeds the fair market value of the shares:

Provided that this clause shall not apply where the consideration for issue of shares is received—

(i) by a venture capital undertaking from a venture capital company or a venture capital fund; or

(ii) by a company from a class or classes of persons as may be notified by the Central Government in this behalf.

Explanation.—For the purposes of this clause,—

(a) the fair market value of the shares shall be the value—

(i) as may be determined in accordance with such method as may be prescribed; or

(ii) as may be substantiated by the company to the satisfaction of the Assessing Officer, based on the value, on the date of issue of shares, of its assets, including intangible assets being goodwill, know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature, whichever is higher;

(b) "venture capital company", "venture capital fund" and "venture capital undertaking" shall have the meanings respectively assigned to them in clause (a), clause (b) and clause (c) of Explanation to clause (23FB) of section 10;"

22. From the above, it is evident that the FMV of the unquoted share be the value as determined by the prescribed method or as substantiated by the assessee whichever is higher. The appellant has chosen to the first option i.e. value as per the prescribed method. The method of determining the FMV is given in Rule 11UA(2) of IT Rules 1962 which are reproduced below:

"Notwithstanding anything contained in sub-clause (b) of clause (c) of sub-rule (1), the fair market value of unquoted equity shares for the purposes of sub-clause (i) of clause (a) of Explanation to clause (viib) of sub-section (2) of section 56 shall be the value, on the valuation date, of such unquoted equity shares as determined in the following manner under clause (a) or clause (b), at the option of the assessee, namely:—

(a) the fair market value of unquoted equity shares $= (A-L) \times (PV)/(PE)$ where, A = book value of the assets in the balance-sheet as reduced by any amount of tax paid as deduction or collection at source or as advance tax payment as reduced by the amount of tax claimed as refund under the Income-tax Act and any amount shown in the balance-sheet as asset including the unamortised amount of deferred expenditure which does not represent the value of any asset;

L = book value of liabilities shown in the balance-sheet, but not including the following amounts, namely:—

(i) the paid-up capital in respect of equity shares;

(ii) the amount set apart for payment of dividends on preference shares and equity shares where such dividends have not been declared before the date of transfer at a general body meeting of the company;

(iii) reserves and surplus, by whatever name called, even if the resulting figure is negative, other than those set apart towards depreciation;

(iv) any amount representing provision for taxation, other than amount of tax paid as deduction or collection at source or as advance tax payment as reduced by the amount of tax claimed as refund under the Income-tax

Act, to the extent of the excess over the tax payable with reference to the book profits in accordance with the law applicable thereto;

(v) any amount representing provisions made for meeting liabilities, other than ascertained liabilities;

(vi) any amount representing contingent liabilities other than arrears of dividends payable in respect of cumulative preference shares;

PE ~ total amount of paid up equity share capital as

shown in the balance-sheet;

PV = the paid up value of such equity shares; or

(b) the fair market value of the unquoted equity shares determined by a merchant banker or an accountant as per the Discounted Free Cash Flow method. "

23. From the above, it is evident that Rule 11UA(2) prescribes two methods - Book Value method and DCF method. However, the said rule also provides that the method to be adopted is left to the choice of the assessee.

24. Thus, the option to choose the method to be adopted to determine the FMV of unquoted shares is not with the AO but with the assessee. In the instant case the assessee opted for the DCF method and the AO could not have switched the method from DCF to Book Value method for determining the FMV of the unquoted shares.

Issue no. 3:

25. Whether the AO erred in rejecting the DCF method because the Valuer failed to furnish the documents called for by him?

26. The AO has rejected the DCF method by observing that the Valuer did not have proper understanding of the methodology and intricacies of the DCF method and that the Valuation report is just of 4 pages. The AO required the Valuer to appear before him along with his working papers which he failed to carry on the date when his statement was recorded. The AO asked him to produce the same on 26.11.2018 which he failed to do. On the other hand the Valuer has submitted in the Affidavit that he had visited the AO's office on the appointed date but could not meet the AO as he was busy with some other matter and that the he (valuer) could not wait longer as he had other appointments. Further, the appellant has provided answers to the queries raised by the AO to the Valuer and also supplied the documents /projection estimates given to the Valuer. The AO has not accepted this. It is noted here that there is merit in the AO's observation that the valuation report is very brief. However, in the absence of any prescribed format or size, one cannot reject the valuation merely on that ground. Further, the AO has not pointed out any specific deficiency in the Valuation Report itself Hence, it would be incorrect to reject the DCF method solely on that ground.

Issue no. 4:

27. Whether DCF is the most appropriate method in the instant case as espoused by the appellant?

28. The appellant besides explaining DCF in detail has also submitted that DCF method is a scientific method of valuation of share duly recognized by professional and accounting bodies worldwide and also the ICAI. DCF method is often used for valuation of unquoted equity shares of a going concern as it is

based on present value of projected future cash flow of the business, which are dependent on various variable factors.

29. The provisions of Rule 11UA shows that the legislature has not made any distinction as going concern or otherwise in valuation of unquoted equity shares. The Rules give option to choose between the two methods and the only criteria to choose is the option to be exercised by the assessee. In the absence of any such prescription under the law, one cannot read into the statute anything without showing that the Legislature intended it. Hence, the AO has erred in not accepting DCF as the most appropriate and scientific method for valuing shares of the appellant.

Issue no. 5:

30. Whether AO can reject the DCF method when this method has been duly prescribed under the Law itself?

31. The DCF method is one of the duly prescribed methods for valuing unquoted shares of a company. Rule 11UA gives option to the assessee to choose between the two methods. The said rule nowhere fixes any hierarchy between the two methods. Once the option has been exercised by the assessee, AO has no right to reject the method. However, the rejection of method is not appropriate not because it is a prescribed method but because the AO has no role in selection or rejection of the method under Rule 11UA. Hence, the AO has erred in rejecting the DCF method especially when it is one of the duly prescribed methods under the IT Rules.

Issue no.6:**32. Whether there is any requirement to show the existence of intention to evade tax in order to invoke provisions of section 56(2)(viib) of IT Act?**

33. The appellant has stated that there was neither the intention nor actual evasion of the taxes while issuing shares and that the subscriber of the shares was an entity of well known "Venture Capitalists" and that the prices were duly accepted after the due diligence by reputed experts. This throws up the issue as to whether there is any requirement to show the existence of intention to evade tax in order to invoke provisions of section 56(2)(viib) of IT Act.

34. The appellant has submitted that section 56(2)(viib) has been introduced in the Act by the Finance Act, 2012 as one of the measures to prevent generation and circulation of unaccounted money. The Hon'ble Finance Minister has also clarified the main purpose of introducing as series of measures to deter the generation and use of unaccounted money. The appellant has also quoted the Speech of Hon'ble Finance Minister in its submissions. Further it has been submitted that from basic contents of Hon'ble Finance Minister's Speech, Finance Bill, 2012 and the Act, it was quite evident that the provisions of section 56(2)(viib) have been introduced to as an anti-abuse measure to prevent receiving unreasonable share premium to account for unaccounted money of the company and its existing shareholders. In that background it is the contention of the appellant that the AO has erred in invoking the provisions of 56(2)(viib) even when there was no case of

accommodation entries or intension of introducing unaccounted money of the company or its shareholders.

35. The AO cannot be burdened with proving the intension to avoid tax by introducing unaccounted money in the garb of share premium. The law is very clear that the moment there is a difference in the FMV of the shares and the consideration received therein, the provisions of section 56(2)(viib) would trigger. There is no requirement to prove or show that the company or its shareholders are trying to introduce their unaccounted money. This is very clear by the language used in the charging provision of section 56(2)(viib). Therefore, the ground raised by the assessee to this effect cannot be accepted.

Issue no. 7:

36. Whether the AO erred in observing that the appellant should have deposited advance tax as per the projection figures?

37. The AO has observed in the assessment order that non-payment of advance tax as per the projection of financial figures in the DCF method would show that the projections were meant only to arrive at the desired value of shares under DCF method.

38. Thus, after detailed analysis of the issue, the Id. CIT(A) deleted the addition.

39. Aggrieved by the order of CIT(A), the revenue has filed appeal before us.

40. The Id. DR argued that the Id. CIT(A) has erred in deleting the addition when the AO examined the valuer and disputed that the valuer is not competent enough to do the valuation. The Id. DR argued that the entire valuation has been made at the behest of the assessee company and the inputs given by them and there was no independent analysis or application of mind by the valuer. He referred to the statement of Sh. Ashok Kumar Verma, Chartered Accountant recorded by the AO with specific reference to Question No. 3, 13, 16 and 17. The Id. DR has also argued that the book value of the shares has to be considered and any payment beyond the value of the company received by the assessee be treated as infusion of an unaccounted money and hence the provisions of Section 56(2)(viib). It was argued that the very failure of the assessee to pay the advance tax in the instant year itself proves that the assessee is clear about the lack of profits but still got valued the shares at higher rate only to get higher share premium. Further, it was argued that the non-achievement of projections clearly proves that the DCF method embarked upon by the assessee was defective. The Id. DR relied on the order of the ITAT Delhi in the case of M/s Agro Portfolio Pvt. Ltd. Vs. ITO.

41. On the other hand, the Id. AR prayed invoking Rule 27 of the ITAT Rules, 1963. He argued that the subsequent results cannot be considered which were not available to the valuer at the time of valuation and it was only in the hind sight that the AO tried to collate the value at the time of valuation and at a later time. He reiterated that DCF method is the right method for ongoing concern and the assessee had choice to resort to

any of the methods prescribed under Rule 11UA and the AO is not empowered to change the method of valuation.

42. Heard the arguments of both the parties and perused the material available on record.

43. We have gone through the facts of the case, reasons of the AO for making addition u/s 56(2)(viib) and the ratio of the Id. CIT(A). The AO has recorded the statement of the valuer during the assessment proceedings.

44. The relevant part of the statement is as under:

"Q.6. Kindly explain DCF method formula in detail?"

Ans: Under this DCF method one needs to value the share on the basis of the prescribed procedure taking into account weighted average cost of capital (WACC), Beta Factor and Equity Risk Premium.

Q.7. What do you mean by Weighted average cost of capital and hoe have you calculated it in respect of M/s Gamma PizzaKraft (Overseas) Pvt. Ltd. (PAN: AACCG8016D)?

Ans: WACC is a weighted average of companies equity and debt the said has been worked out using the following prescribed formula:

Risk Free Return + (Beta x Equity Risk Premium)

Q.8. What was the risk premium return and equity risk premium for the M/s Gamma PizzaKraft (Overseas) Pvt. Ltd. (PAN: AACCG8016D) and how have you calculated this?

Ans: Risk free return I have taken at 7.85 based on return of government securities. Further, I consider equity risk premium equal

to 7%. This is based on the expected market return over and above risk free rate considering the risk of investment in the security.

Q.9. Can you provide the details of Government securities where risk free return is 7.8% and equity risk premium which is 7% in this case as taken by you? Further, these figures has been taken by you or given by the assessee company i.e. equity risk premium which is 7% in this case i.e. M/s Gamma PizzaKraft (Overseas) Pvt. Ltd. (PAN: AACCG8016D)

Ans: The company did not provide me these information. These rates keep on fluctuating with the passage of time I took these rates at the time of preparing report from the information available on authenticated internet sites containing these information.

Q.10. Can you name few sites where you got these information?

Ans: These information can be procured by making a search on google.

Q.11. Please provide formula for equity risk premium?

Ans: There is no formula for equity risk premium it is one of the factor to calculate valuation of shares under DCF Method.

Q.12. Are you aware with any method which is being used for calculating equity risk premium?

Ans: As conveyed earlier equity risk premium which is considered at 7% is applied as this was the rate which are prevalent during the period of valuation of shares.

Q.13. Have you ever heard about CAPM Method for calculating equity risk premium?

Ans: I am not aware with CAPM Method, however, I thought it prudent to apply 7% rate which are prevalent at that time.

Q.14. What are the constituent of CAPM Method?

Ans: Right now I cannot recollect the details of CAPM Method.

Q.15. Please tell full form of CAPM.

Ans: Right now I am not aware.

Q.16. Please communicate in details the components used in DCF Method.

Ans: Valuation in DCF Method is based on projections and the use of the prescribed formula.

Q.17. Do you know anything else about the formula and method used by you as you are still not telling or mentioning the components of technical formula which are used while applying DCF Method?

Ans: I have already explained the components of the formula for valuation of shares.

Q.18. Do you know any other method/Formula for valuation of shares?

Ans: There are few more methods like underlying asset approach which is primarily used for concerns doing the business not as a going concern. This is also known as historic method. There is also another method which is known as market price method, this method is primarily in relation to share of those companies whose shares are listed in stock exchange.

Q.19. According to you which method is the most scientific method for valuation of share and on what basis?

Ans: The selection of the method of valuation of shares depends upon several factors in the present case as the company was not listed and further as the company was running as a going concern I

consider this DCF method which is appropriate for the valuation of shares.

Q.20. You have prepared share valuation report in respect of M/s Gamma PizzaKraft (Overseas) Pvt. Ltd. (PAN: AACCG8016D) without mentioning the basis of valuation, valuation process in detail, market situation, growth phase. Why?

Ans: There are different templates of share valuation reports. Although my report might not have contained mention of these attributes, I considered all these attributes to the extent possible for compiling valuation report.

Q.21. What do you understand by discount factor? And how have you calculated discount factor of 0.51 in the present case and what material documents/papers did you use for calculating this discount factor?

Ans: As the name DCF stands for discounted cash flow it is based on future projections, the future incomes and other financial information needs to be discounted to ascertain the present value. The discount factor as shall be evident from the report varies from year to year. It was .89 in relation to F. Y. 2015-16 and it kept on reducing from year to year.

Q.22. How you have reached to these values of discount factor of 0.89, 0.77, 0.67, 0.58, 0.51 for F.Y. 2015-16 to F.Y.2019-20. Please produce calculation? I am again asking that what material documents/papers did you use for calculating this discount factor?

Ans: The base discounting factor for F.Y. 2015-16 was determined on the basis information available on different internet sites and the same rate was applied for the subsequent years.

Q.23. This means that you not done any calculation and just relied only on internet for calculation discount factor and equity risk premium etc. Please explain?

Ans: Our calculations are based on rate picked from reliable authenticated web contents are available.

Q.24. Please tell the name of few sites where authenticated web contents are available.

Ans: These websites can be sourced by making search in the google.

Q.25. Please tell that except the internet material what papers/documents did you use for calculating of cash flow and other components of DCF Method?

Ans: I relied on sources of information as para 4 of our report.

Q.26. As para 4 you have mentioned that you have relied on the information made available by the management of the company. Please tell that except audited financial statements for year ending 31.03.2014 and projections for 31.03.2016, 31.03.2017, 31.03.2018, 31.03.2019 and 31.03.2020 what else document were provided by the management of the assessee company. Please be specific in your answer and mention names and title of documents.

Ans: Apart from above, I were provided projections for the future period till 31.03.2020. Also I ask for valuation of shares of its two subsidiaries.

Q.27. Who certified these audited financial statements and projections as mentioned in preceding questions.

Ans: Audited accounts downloaded from ROC records. And the projections were sent to me through mail.

Q.28. Who mailed you these projections and did you rely on mailed projections only? Did you also make some enquiries on your own with regard to these projections?

Ans: The projections were mailed by the company and sent to me by the finance official of the company. As discussed in the para 4.6 I also discussed with the concern staff about the projections.

Q.29. You have not mentioned any formula in your report with regard to DCF, why?

Ans: The whole process has been explained very clearly in terms of para 6 of the report.

Q.30. What do you understand by WACC? On what basis/calculation WACC has been taken as 14.85%?

Ans: As has been explained earlier WACC stands for weighted average cost of capital. Please see page 6 of our report last two tables, the set two tables contains complete details about the calculation of WACC

Q.31. In the valuation report prepared by you, you have not mentioned any formula/calculation, you have just arrived at the different values such as cash flow of explicit period as 34641, present value for the terminal value as 270696. Kindly explain.

Ans: Terminal value was calculated on the basis of the specific formula, this has been calculated in excel sheet.

Q.32. And what about cash flow for explicit period?

Ans: The figure of cash flow has been ascertained and taken from annexure 1 above.

Q.33. You have not annexed any separate sheets for calculation with valuation report as you are mentioning. Please explain.

Ans: All the calculation in relation to valuation of shares as per annexure attached with the report.

Q.34. However, in annexure 1 there are only figures based on audited financial statements or projections in upcoming years there is no any calculation in annexure 1.

Ans: In case you see the annexure 1 in totality there are calculation also.

Q.35. You were requested to bring all the documents and papers which you relied on for preparing report. Are you carrying these documents please show me.

Ans: I am carrying some of the documents, rest are there in our computer. In case you need any specific documents in relation to the same I can file the same as when required,

Q. 36. Please produce all the documents and papers which you relied on for preparing of report.

Ans: I will provide all the documents before 26.11.2018.

Q. 37. Have you ever done audit for any financial year of M/s Gamma PizzaKraft (Overseas) Pvt. Ltd.?

Ans: No.

Q. 38. Are you aware that projections as provided by company for preparing valuation report has been proved wrong?

Ans: As conveyed earlier I compiled share valuation report based on the projections provided by the management. Thereafter, I never had any interaction with the said company. As such I am not aware whether projections eventually proved correct or not.

Q. 39. If projections have proved wrong, what is you say about the validity of valuation report prepared by you following DCF Method.

Ans: The projections are projections only these may be achieved or may not achieved. I agree in case projections are not achieved the basis of valuation shall lose its sanctity as DCF Method is only based on projections.

Q. 40. I am showing you the audited financial statements of the M/s Gamma Pizza Kraft (Overseas) Pvt. Ltd. where you can see that projections which you relied on for preparing the valuation report have completely failed. In these circumstances what is the sanctity of valuation report prepared by you.

Ans: I can't comment on this point as I am not aware what went wrong in the functioning of the company as I was never associated with the company in any capacity after issuing the certificate.

Q. 41. Do you want to say any this else?

Ans: No

*Oath taken
Ashok Kumar Verma
Chartered Accountant*

*Oath Administered,
Prashant Shukla (DCIT)*

45. We have re-examined the pertinent questions raised by the Id. DR. The AO asked about CAPM method for calculating equity risk premium which the valuer is not aware. The valuer could not answer the details of CAPM method or its full form. This led to a passive allegation that the valuation made by the valuer is not correct and the valuer is not competent enough We find that the Capital Asset Pricing Model (CAPM) is a model that describes the relationship between the expected return and risk of investing in a security. It shows that the expected return on a security is equal to the risk-free return plus a risk premium, which is based on the beta of that security. CAPM formula is as under:

Expected Return (Ra) = Risk-Free Rate (Rrf) + [Beta (Ba) × Expected Return of the Market (Rm) – Risk-Free Rate (Rrf)] i.e.
 $Ra = Rrf + [Ba \times (Rm - Rrf)]$

46. Thus, we find that the query of the AO with regard to CAPM to the valuer is irrelevant and does not castigate the DCF method resorted by the valuer.

47. The provisions of Rule 11UA are as under:

*(2) Notwithstanding anything contained in sub-clause (b) of clause (c) of sub-rule (1), the fair market value of unquoted equity shares for the purposes of sub-clause (i) of clause (a) of Explanation to clause (viib) of sub-section (2) of section 56 shall be the value, on the valuation date, of such unquoted equity shares as determined in the following manner under clause (a) or clause (b), **at the option of the assessee, namely:—***

48. The Rule 11UA prescribes FMV of the unquoted equity shares as determined as per DCF method determined by a Chartered Accountant (subsequently by a merchant banker)

or by the formula of

$$\frac{(A-L)}{(PE)} \times (PV)$$

49. Thus, we find that the assessee has option of DCF method and the formula given under Rule 11UA. The option given to the assessee cannot be read as the option given to the Assessing Officer. Hence, the Assessing Officer has no right to change the

method of valuation. The AO can refuse the method of valuation after proving that the methodology resorted by the assessee is incorrect or not as per the standards laid down. The courts have held this view as is evident from the following observations of Hon'ble High Court of Delhi in Pr. Commissioner of Income Tax Vs. M/s Cinestaan Entertainment Pvt. Ltd. in ITA 1007/2019 dated 01.03.2021.

".....There is no dispute that methodology adopted by the Respondent-Assessee has been done applying a recognized and accepted method. Since the performance did not match the projections, Revenue sought to challenge the valuation, on that footing. This approach lack material foundation and is irrational since the valuation is intrinsically based on projections which can be affected by various factors. We cannot lose sight of the fact that the valuer makes forecast or approximation, based on potential value of business. However, the underline facts and assumptions can undergo change over a period of time. The Courts have repeatedly held that valuation is not an exact science, and therefore cannot be done with arithmetic precision. It is a technical and complex problem which can be appropriately left to the consideration and wisdom of experts in the field of accountancy, having regard to the imponderables which enter the process of valuation of shares."

50. The above decision of the Hon'ble jurisdictional High Court has also been followed in Abhirvey Projects Pvt. Ltd. Vs. ACIT, Circle-1 (2) in I.T.A. No. 9400/DEL/2019.

51. With regard to the actual performance, we also find that the actual performance did not fall short of the projections as duly submitted before the AO vide letter dated 06.12.2018 which was reproduced in his order by the Id. CIT(A).

52. With regard to the contents of the Valuation Report, we find that the same is prepared by covering all the required

points as per the valuation methodology prescribed under DCF method. The Valuer has approached the valuation in a systematic manner. He has included at Para-4 of his report a detailed list of source of information relied upon by him that includes Five years' financial projections, provisional Financial Statements etc. as well the different topics which he discussed with the Management. Thereafter he has discussed the methodology of valuation approached by him describing therein the different methods of valuation available and why he has adopted the DCF method. Further he has given very detailed step-wise process of Valuation done as per DCF method. From the same it would be seen that the Valuer has not only given details of the Formulae in the DCF method but also explained and the figures adopted by him, hence, it cannot be said that there is lack of application of mind by the valuer.

53. He was examined by the AO u/s 131 of the Act wherein he had given clear cut answers to all the questions relating to the DCF method and justified his stand on each and every aspect of the Valuation Report prepared by him. He had submitted that there were different templates of the valuation report and various attributes like market situation etc have been duly considered by him for compilation of the said report. He had explained in detail the meaning of and the methodology of DCF method of valuation of shares how the same was carried out by him including the meaning of different terms used in the DCF method. Hence, it can be said that the valuer being a Chartered Accountant is authorized to do the valuation as per the provisions of the Act.

54. The transaction has been cleared by the Competition Commission of India (CCI) and the investor in the company namely Sapphire Foods Pvt. Ltd. is a venture capitalist and the investment in the assessee company was part of overall acquisition of Pizza Hut and KFC outlets in India and Sri Lanka. The buyer is an entity promoted by venture capitalist, namely, Goldman Sachs Investments Holding (Asia) Limited and it holds 34.36% of the equity capital in the subscriber company.

55. Further, reliance is being placed on the order of the Coordinate Bench of ITAT in the case of Intelligrape Software Pvt. Ltd. Vs. ITO in ITA No.3925/Del/2018 wherein the assessee had issued equity shares of face value Rs.10/- at a premium of Rs.6,165/- per share to its own group company. It had also got the valuation certificate from the Chartered Accountant who had valued the shares under DCF Method as provided under Rule 1 IUA(2)(b). The AO as well as the CIT(A) had rejected the valuation on the ground that year wise results projected were far from the actual results declared in the final accounts. The AO therefore adopted Networth Method and arrived at a value of Rs.23.21/- per share and made an addition of about Rs.1.59 Crore under section 56(2)(viib) of the Act towards excess premium charged being more than the FMV. The Tribunal disagreed with the authorities below by holding that the AO/CIT(A) had no power/authority to change the valuation methodology from DCF to Book Value Method and hence such action was arbitrary. It was also held that the valuation based on future projections at the time of issue of shares cannot be inferred as the actual figures may vary depending on the market conditions and host of other factors.

56. Hence, keeping in view that DCF is correct method of determining the FMV of the unquoted shares, the assessee has option to determine the method of valuation and the AO has no power to reject the method resorted by the assessee, the results in the instant case of the holding company have exceed the projections, as no infraction of methodology has been brought out by the AO and non-payment of advance tax cannot be a collateral reason to reject the DCF method, we decline to interfere with the well reasoned order of the Id. CIT(A).

57. In the result, the appeal of the Revenue is dismissed.
Order Pronounced in the Open Court on 12/05/2023.

Sd/-

(C. M. Garg)
Judicial Member

Sd/-

(Dr. B. R. R. Kumar)
Accountant Member

Dated: 12/05/2023

Subodh Kumar, Sr. PS

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(Appeals)
5. DR: ITAT

ASSISTANT REGISTRAR