आयकर अपीलीय अधिकरण," ए" खंडपीठ मुंबई
INCOME TAX APPELLATE TRIBUNAL,MUMBAI-"A",BENCH
सर्वश्री जोगिन्दर सिंह, न्यायिक सदस्य एवं राजेन्द्र, लेखा सदस्य
Before S/Shri Joginder Singh,Judicial Member & Rajendra,Accountant Member
आयकर अपील सं./ITA No./6468/Mum/2013 ,**निर्धारण वर्ष /**Assessment Years: 2010-11

Korn Ferry International Pvt. Ltd. Piramal Tower, Penninsula Coporate Park, Lower Parel,Mumbai-400 013. **PAN:AAACW 0577 B**	Vs.	DCIT-3(2) Mumbai-400 020.

आयकर अपील सं./ITA No./6269/Mum/2013 ,**निर्धारण वर्ष /**Assessment Years: 2010-11

DCIT-3(2) Mumbai-400 020	Vs.	Korn Ferry International Pvt. Ltd. Mumbai-400 013.

(अपीलार्थी **/Appellant**) (प्रत्यर्थी **/ Respondent**)

Revenue by: Ms. Radha K. Narang
Assessee by: Shri Madhur Agarwal & Ms. Priyanka –(AR)

सुनवाई की तारीख **/ Date of Hearing: 07.04.2016**
घोषणा की तारीख **/ Date of Pronouncement: 22.04.2016**

आयकर अधिनियम,1961 की धारा 254(1)के अन्तर्गत आदेश
Order u/s.254(1)of the Income-tax Act,1961(Act)

<u>लेखा सदस्य राजेन्द्र के अनुसार Per Rajendra A.M.-</u>

Challenging the order dt.06.08.2013 of the CIT(A)-4 Mumbai the assessee and the Assessing Officer(AO) have filed cross-appeals for the year under consideration.The assessee has raised following Grounds of appeal:

1.The Hon. Commissioner of Income Tax (Appeals) -4,grossly erred in confirming the disallowance made U/s. 14A of the Income Tax Act, 1961, amounting to Rs 3,45,910/- .

1.1 The Hon. Commissioner of Income Tax (Appeals) erred in ignoring the fact the disallowance U/s 14A can be made only if there is actual nexus between tax free income and expenditure and no such nexus has been established in the appellants case.

1.2 The Hon. Commissioner of Income Tax(Appeals) erred in ignoring the fact, without rendering any opinion on the correctness of Appellant's claim of not spending any amount for earning exempt income, the learned AO could not have made a disallowance by applying the provisions of section 14A r.w.r. 8D.

1.3The Hon. Commissioner of Income Tax (Appeals) grossly erred in overlooking the fact that the principle of apportionment embedded in section 14A had no application where no direct expenditure was incurred to earn exempt income and entire expenditure was incurred for business purposes only.

2 The Hon Commissioner of Income Tax (Appeals),grossly erred in confirming the disallowance of ESOP expenses, amounting to Rs 52,08,592/-.

2.1 The Hon. Commissioner of Income Tax (Appeals) grossly erred in ignoring the fact that the amount of Rs. 52,08,592/- represents the cost of stocks granted to the employees of the Appellants, under an ESOP scheme to compensate them for services rendered by them and is therefore similar to salary cost which is allowable business expenditure.

2 The appellants crave leave to add, alter, amend or delete any of the above grounds of appeal.

Grounds of appeal filed by the AO read as under:

1. "Whether on the facts and circumstances of the case and in law, the Ld. CIT(A) was justified in allowing the appeal of the assessee without appreciating the fact that the assessee has indulged in the activity of buyback of shares as a colorable device only for the purpose to avoid dividend distribution tax.

2.Whether on the facts and circumstances of the case and in law, the Ld. CIT(A) was justified in allowing the appeal of the assessee without appreciating the fact that the assessee has not declared any dividend inspite of making regular profit.

3. Whether on the facts and circumstances of the case and in law, the Ld. CIT(A) was justified in allowing the appeal of the assessee without appreciating the decision of Authority of Advance Rulings (Income Tax) in the case of M/s. A Ltd. wherein it is held that where a Mauritan shareholder of an Indian Company, accepted offer of buyback of shares given by Indian company,the amount receivable would be taxable in India as dividend.

4. Whether on the facts and circumstances of the case and in law,the Ld. CIT(A) was justified in allowing the appeal of the assessee without appreciating the decision of Hon'ble Apex Court in the case of M/ s.McDowell wherein it is held that the assessee can't use colourable device to mitigate its tax liability which was used by the assessee in the instant case by way of buyback of shares.

5. The appellant prays that the order of CIT(A) on the above ground be set aside and that of the Assessing Officer be restored.

6. The appellant craves leave to amend or alter any ground or add a new ground which may be necessary."

Assessee-company,engaged in the business of executive search,consulting and related search, filed its return of income on 12.10.2010 declaring total income of Rs.9.13 crores.The AO completed the assessment u/s.143 of the IT Act on 24.01.2013,determining the income of the assessee at Rs.9.69 crores.

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2.First effective ground of appeal is about disallowance made u/s.14 A of the Act,r.w.Rule 8 of the Income tax Rules,1962(Rules),amounting to Rs. 3,45,910/-.

During the course of hearing before us the Authorised Representative (AR) and the Departmental Representative (DR) agreed that identical issue had arisen in the earlier year and the Tribunal had decided the issue in favour of the assessee in ITA No.5152/Mum/2012 (AY-08-09; dt.31/3/2016).We find that,while deciding the appeal for 2008-09 the identical issue -except for the amount involved-was dealt by the Tribunal as under :

"2.*The first Ground of appeal is about disallowance of Rs.2.74 laks, made u/s.14A of the Act. During the assessment proceedings the AO found that the assessee had claimed dividend income of Rs.18.33 lakhs,that it had offered no disallowance u/s. 14A on account of expenses relating to dividend income.The AO applied Rule 8D of the Income tax Rules, 1962(Rules) and made a disallowance of Rs.2,74,489/-(0.5% of average value of investment).*

3.*Aggrieved by the order of the AO,the assessee preferred an appeal before the First Appellate Authority(FAA).Before him, it was argued that the assessee had made investment in Mutual Funds only, that investment was made out of assessee's own funds, that no other expenditure was incurred regarding dividend income.*

After considering the submission of the assessee and the assessment order the FAA held that no disallowance had been made under the head interest expenditure, that making of investment out of own funds had no relevance,that only other administrative expenses had been disallowed as per Rule 8D of the Rules. Referring to the judgment of Godrej & Boyce Ltd.(328ITR81) the FAA upheld the order of the AO.

4*.Before us,the Authorised Representative (AR) stated that it had claimed an expenditure for earning the dividend income,that the AO had mechanically applied the provisions of section 14A r.w.Rule 8D of the Rules.He relied upon the case of Om Prakash Khaitan (376ITR390) of Hon'ble Delhi High Court.Departmental representative (DR) left the issue to the discretion of the Bench.*

5.*We have heard the rival submissions and perused the material before us.We find that the AO had not mentioned as to how much expenditure was incurred by the assessee for earning tax free income. We are of the opinion that, if the assessee had not incurred any expenditure to earn tax free income, then, the AO cannot invoke the provisions of section 14A r.w. Rule 8D of*

the Rules.First of all, the AO has to record his satisfaction about invoking the provisions and has to decide the issue after obtaining the explanation of the assessee .We also do not endorse the view of the FAA that investment out of the own funds has no relevance for making the disallowance.We find that in the case of Om Prakash Khaitan(supra), the Hon'ble Delhi High Court has held that in order to disallow the expenditure there must be a nexus between the expenditure incurred and the income not forming the part of the total income.Considering the above, we reverse the order of the FAA.Ground No.1 is decided in favour of the assessee."

Respectfully following the above order,first effective ground is decided in favour of the assessee.

3.Next ground of appeal deals with confirming the disallowance of ESOP expenses, amounting to Rs 52,08,592/-.During the course of hearing before us,the representatives of both the sides agreed that the issue stands covered by the order of the Tribunal for the earlier year (ITA/5152/Mum/2012,dtd.31.03.2016).We find that the Tribunal has deliberated upon the issue and has decided it as under:

"6.*Next Ground of appeal is about addition of Rs.56.40 lakhs out of the expenditure incurred under ESOP(Employee Stock Option Scheme).During the assessment proceedings,the AO found that the assessee had debited an amount of Rs.1.07 crores under the head cost of stock awarded to KF India Employees.Before the AO, the assessee stated that the expenditure was on account of ESOP.On perusal of the tax audit report, the AO found that the assessee had paid Fringe Benefit Tax(FBT)only on amount of Rs.50.65 lakhs.The AO directed the assessee to explain as to why FBT had not been paid to whole amount.The assessee vide its letter,dt.29.12.12,stated that the value of FBT taken for ESOP(Rs.50.65lakhs) as against cost of stock awarded to KF Employees(Rs.1.07crores),that the amount of Rs.50.65 represented the value of ESOP, that had been vested with the employees during FY 2007-08 and consequently considered for FBT, that the amount of Rs.1.07crores represented the amount charged by Korn Ferry International USA to Korn Ferry International Pvt. Ltd. India, towards stock awarded to the employees of the assessee .*

After considering the same the AO held that during the year under consideration only a part (Rs. 50. 65 lakhs)out of the total amount (Rs.1.07crores) was debited to P&L A/c. was vested in employees,that the balance amount would be vested in employees over a period of time, that the assessee had not paid FBT on Rs.56.40 lakhs,that liability could eventually increase or decrease in future,that it had not produced any evidence as to the fact that amount in question was actually paid.Finally,the AO made an addition of Rs.56,40,195/- to the total income of the assessee.

7.*Aggrieved by the order of the AO, the assessee preferred an appeal before the FAA. Before him,it was argued that allowability of ESOP expenses and payment of FBT for ESOP were two different concepts,that the FBT would become payable upon vesting of the ESOP in the hands of the employees accordingly the assessee had paid FBT during the year, that assessee had made full payment of Rs.1.07 crores to its parent company ,that it had claimed the cost of stock awarded to its employees entirely based on ESOP Scheme governed by the SEBI Guidelines,that the ESOP expenditure was a measure in the nature of compensation cost and was fully deductible in computing the taxable income.The FAA ,in his order, held that the assessee itself had not treated the entire amount as liability, that ESOP would be effective only on the discretion of the employees to opt for stocks, that payment for shares was either a provision or an investment,that no liability in that regard had crystallised.*

8.*Before us,the AR reiterated the arguments that were advanced before the FAA.He relied upon the case of Biocon Ltd.(144ITD21)(SB)(Bang.); Novo Nordisk India Pvt. Ltd.(42 taxmann.com168).DR supported the order of the FAA.*

9.*We have heard the rival submissions and perused the material before us.We find that stock options of the parent company were offered to the employees of the assessee company,that the assessee had made payment of Rs.1.07 crores to the parent company,that during the year FBT was paid for sum of Rs.50.65 lakhs.In our opinion,once a stock option is granted to and exercised by the employee of an assessee the liability in that behalf is ascertained and cost is*

allowable in the year in which stock options are granted.We find that in the case of Novo Nordisk India Pvt. Ltd.(supra),it has been held that in terms of ESOP if an assessee offers shares of its parent company to its employees,the difference between the FMV of the shares of the parent company on date of issue of shares and the price at which those shares were issued by the assessee to its employees had to be regarded as expenditure incurred for business purposes allowable u/s. 37(1) of the Act.Respectfully following the above decision, we decide Ground No.2 in favour of the assessee ."

Respectfully following the above order,we allow the appeal of the assessee with regard to second ground.

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4.The effective Ground of appeal filed by the AO is about buyback of shares. During the assessment proceedings the AO had held that assessee had indulged in activity of buy back of shares,that the same was a colourable device for the purpose of avoiding dividend distribution tax, that the assessee had not declared dividend inspite of making regular profit. In the appellate proceedings, the FAA had upheld the disallowance of Rs.52.08 lakhs.But he did not agree with the AO that buyback of shares was an instrument to avoid dividend distribution tax.

5.During the course of hearing before us,the DR and the AR stated that identical issue had arisen in the matter of Goldman Sachs(India) Securities Pvt. Ltd (ITA/3726/Mum/2015,AY. 2011- 12, dtd.12. 02. 2016), that the Tribunal had decided the issue in favour of the assessee . We find that the Tribunal had deliberated upon the issue and had decided as under :

"The assessee is a wholly owned subsidiary of Goldman Sachs (Mauritius) LLC(GS-M).It was set up to undertake merchant banking and security business in India.Registered under the STPI scheme,the it had set up a 100% export oriented unit in Bangalore to serve as a global support centre for the Goldman Sachs Group entities.On 24.11.2010, the assessee had remitted an amount Rs.1,88,99,97,781/- to GS-M under a buyback of shares scheme,whereby 4,03,93,199/- equity shares having face value of Rs.10 each were bought back from GS-M by the assessee @Rs.46.79/-per share.Taking into account the face value of Rs.10 per share, the AO in his order, passed u/s.201(1) and 201(1A) r.w.s. 195 of the Act,on 27.01.2014 held that the excess payment of Rs.36.79/-per equity share for 4,03,93,199 shares bought back amounting to Rs.1,48,60, 65,791/-was nothing but its distribution of its accumulated profits to its ultimate beneficiary and the only shareholder i.e.GS-M,that the buyback of equity shares by the assessee from its holding company was a colourable transaction to avoid the payment of dividend distribution tax (DDT). The excess payment of Rs.1,48,60,65,791/-was held by the AO to be in the nature of dividend as per provisions of section 2(22)(d) of the Act.As the assessee had not deducted any DDT u/s.115 of the Act,such dividend income was found by the AO not to qualify for exemption u/s.10(34) of the Act and therefore,was taxable in the hands of the recipient GS-M,namely.He further held that on remittance of such amount to a non-resident representing its income by way of dividend, tax deduction was required to be made u/s.195 of the Act. As the assessee company had not deducted any tax while making such remittance, it was held to be an 'assessee in default' in terms of the provisions of section 201 of the Act.Further, the assessee was also found to be liable to pay simple interest u/s.201(1A) of the Act. Tax at the rate of 5% of the gross amount of such dividend was determined by the AO as payable by the assessee in terms of para 2(a) of Article 10 of the India Mauritius Tax-Treaty.

3.*Aggrieved by the order of the AO,the assessee preferred an appeal before the First Appellate Authority (FAA).Before him,it was argued that a transaction of buy back of shares referred to section2(22) (iv) of the Act was different from a transaction of capital reduction dealt by section 2(22)(d) of the Act, that the transaction in question was one of buy back of shares and not a case of capital reduction.After considering the submissions of the assessee and the order of the AO,the FAA held the AO had obtained the annual report of the assessee company for the five preceding years and from such annual reports he noticed that it had been earning profits*

after tax for each of those years, that the reserves and surplus increased from Rs.81,01,34,000/- for the year ending 31.03.2008 to Rs.3,46,03,20,000/-for the year ending 31.03.2010,that inspite of regular profits being earned by it Directors of the assessee-company did not recommend any dividend payment on its equity shares,that money had a time value and postponement of grant of a share in the profits to a shareholder would be for purposes of re-investment in the business for the purposes of enhancing future profits,that the assessee had not shown any such requirement or compulsion as a justification for the non-grant of dividend in the regular course, inspite of the continuous accumulation of profits in its books,that the AO had specifically required the assessee to explain the commercial reason, if any, for the non issue of dividend although the profits were being accumulated year after year,that it chose to remain silent on this show cause notice issued by the AO,that by permitting the profits to accumulate in its books it had avoided the payment of DDT that would have been payable if such accumulated profits had been distributed to its share-holders,that a portion of such accumulated profit was finally passed on to the sole shareholder on 24.11.2010 by way of payment on account of buy back of shares,that it had claimed the exemption available u/s.2(22)(iv) of the Act that excluded any payment made by a company on the purchase of its own shares from a shareholder in accordance with the provisions of section 77-A of the Companies Act,1956.The FAA further observed that the definition of dividend given in section 10(22) of the Act was an inclusive definition that sought to extend the scope of amounts chargeable to tax as deemed dividend but payments in the nature of dividend would always be coming within the ambit of the term dividend,that the commercial significance of a transaction of a buyback of equity shares was normally for the purposes of consolidating the share-holding of the remaining share holders and to enhance the value of the shares remaining in the hands of the continuing share holders,that GS-M was the sole equity share holder of the assessee-company both prior to and after the buyback of shares by the it,that the arrangement of buy-back of shares would not lead to any consolidation or a change in the value of its holdings in the assessee-company,that there was no commercial purpose was served through the buyback arrangement, that the assessee was a wholly owned subsidiary of GS-M,that the latter was in a position to ensure that the returns out of the profits of the assessee-company would be given to it not through dividend,that payment of dividend would have been liable to DDT,that the transaction of the receipt of its share of profits in the assessee company was given an artificial colour of capital gains,that capital gain on such transaction was exempt from tax in the hands of the recipient,that the non-distribution by way of dividend of the accumulated profits,the transaction of buy back of shares offered by it and the exercise of such option by its sole share-holder was carried out not for any commercial reasons,that whole transaction was arranged for the purposes of enabling an evasion of taxes due on such distribution of Profits,that the receipt by GS-M would come within the ambit of income from a share-holding or a participation in the profits of a subsidiary,that the assessee through the recourse to the arrangement of the buyback of shares sought to give the colour to this transaction as not being in the nature of a receipt of dividend but a capital gain of the concerned share holder,that the arrangement was made to use of the provisions of section 46A of the Act and to claim exemption from tax in India on the basis of Article 13(4) of the India Mauritius Tax Treaty.The FAA referred to the case of a Indian Company that was decided by the AAR in Case No. P of 2010 vide its order dated 22.03.2012 and held that it had persuasive value.He further held that section 100 to 105 of the Companies Act dealt with reduction of capital,that the annual accounts of the assessee showed that its share-capital actually got reduced and was so reflected in the books after the buy-back of the shares,that buy-back of shares was one of the ways of capital reduction,that reliance by the AO on the provisions of section 2(22)(d) of the Act dealing with capital reduction, as including a transaction of buy-back of shares was justified,that the provisions of section 10(34) would apply only if DDT had been paid u/s.115-0 of the Act,that no DDT was paid by the assessee,that the recipient would not be entitled to any exemption u/s. 10(34) of the Act,that the receipt in its hands would be chargeable to income tax,that the treatment by the AO of the assessee as an A-I-D and the raising of demand u/s.201(1) and 201(1A) r.w.s. 195 of the Act was justified.Finally, he decided the issue against the assessee.

4.*Before us,the Authorised Representative(AR)argued that the assessee had bought back the shares as per the resolution passed in the general meeting in the Board of Directors on 4.11.2010 (Pg 14 of PB), that the offer for buy back opened on 5.11.2010 and closed on 20.11.2010, that the shareholder tendered the shares on 23/.11.2010, that after the amendment to section 77A of the Company's Act there was no need to approach the courts to buy back the shares if the percentage of buy bought shares were less that a certain limit, that correspondingly provisions of sec.2(22)(d) of the Act were amended w.e.f 1.6.2001, that sub clause of (iv) of Section 2(22)(d) of the Act dealt with the dividends, that the amount in question was to be assessed under the head capital gains, that even after amendment to section 115QA of the Act burden of payment of tax has not been shifted to shareholders , that the AAR had not considered the provisions of sub clause (iv) of section 2(22) of the Act while deciding the application filed before it, that the payment made by the assessee was for the purchase of shares, that there was no reduction in capital.The Departmental Representative(DR)contended that the facts of the case decided by the AAR were applicable to the case under appeal, that the buy-back was not genuine, that it was a case of colourable device, that the scheme had resulted in reduction in capital, that the FAA had rightly held that provisions of section 2(22)(d) of the Act were applicable.*

5.*We have heard the rival submissions and perused the material before us.We are of the opinion that for deciding the issue before us,it would be useful to consider the provisions of section 77A and100-105 of the Companies Act(CA) and section 2(22) and 46A of the Act.Section 77A of the CA deals with buying back of shares in following manner:*

(1) Notwithstanding anything contained in this Act, but subject to the provisions of sub-section (2) of this section and section 77B, a company may purchase its own shares or other specified securities (hereinafter referred to as "buy-back") out of-

(i) its free reserves ; or

(ii) the securities premium account ; or

(iii) the proceeds of any shares or other specified securities :

Provided that no buy-back of any kind of shares or other specified securities shall be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities.

(2) No company shall purchase its own shares or other specified securities under sub-section (1) unless-

(a) the buy-back is authorised by its articles ;

(b)a special resolution has been passed in general meeting of the company authorising the buy-back

Provided that nothing contained in this clause shall apply in any case where-(A) the buy-back is or less than ten per cent. of the total paid-up equity capital and free reserves of the company ; and (B) such buy-back has been authorised by the board by means of a resolution passed at its meeting :

Provided further that Provided further that no offer of buy-back shall be made within a period of three hundred and sixty-five days reckoned from the date of the preceding offer of buy-back, if any.

Explanation — For the purposes of this clause, the expression "offer of buy-back" means the offer of such buy-back made in pursuance of the resolution of the board referred to in the first proviso ;

(c) the buy-back is of less than twenty-five per cent. of the total paid-up capital and free reserves of the company :

Provided that the buy-back of equity shares in any financial year shall not exceed twenty-five per cent. of its total paid-up equity capital in that financial year ;

(d) the ratio of the debt owed by the company is not more than twice the capital and its free reserves after such buy-back :

Provided that the Central Government may prescribe a higher ratio of the debt than that specified under this clause for a class or classes of companies.

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(5) The buy-back under sub-section (1) may be-

(a) from the existing security holders on a proportionate basis ; or

(b) from the open market ; or

(c) from odd lots, that is to say, where the lot of securities of a pub-lic company whose shares are listed on a recognised stock exchange, is smaller than such marketable lot, as may be specified by the stock exchange ; or

(d) by purchasing the securities issued to employees of the company pursuant to a scheme of stock option or sweat equity."

Section 100-105r.w.s.391of the CA deal with reduction of capital and obtaining permission of the Court.Clearly,both deal with different situations.The Hon'ble Jurisdictional High Court has dealt with the schemes of buyback of shares and reduction of capital in the case of Capgemini India Private Limited (Company Scheme Petition No.434 of 2014 dated 28.04.2015) as under:

4.The entire case of the Regional Director revolves around his contention that the buyback of shares must be effected only under Section 77 A of the Companies Act, 1956/Section 68 of the Companies Act,2013. According to the Regional Director if a buyback of shares is effected under Section 77A/Section 68, then the distributed income of the company as defined in Section 115QA of the Income Tax Act, would be charged to tax and it is for this reason that the company is not following the procedure prescribed under Section 77A/Section 68 and has opted for the procedure under Section 391 which would not attract such a tax under Section 115QA of the Income tax Act. According to the Regional Director by this colourable device the company is evading its liability to pay tax.

5. One of the contentions raised by the petitioner is that a view of the Circular dated 15th January 2014, the Regional Director has no locus in respect of tax matters, particularly when the Income tax Authorities have not raised any objection. This aspect has been considered in detail by this Court in the case of Casby CFS Pvt. Ltd. and it has-been held that the Regional Director has the requisite locus standi to raise all objections in respect of a scheme including objections pertaining to taxation laws. He can do so even if the Income Tax Authorities do not raise any objection. It has been held that this is the duty and obligation of the Regional Director. In view of the aforesaid decision of this Court the objection of the Petitioner with regard to the locus of the Regional Director is untenable and deserves to be rejected.

6. The Petitioner has submitted that it is open to the Petitioner to follow either the procedure under section 77A/section 68 or the procedure under section 391 read with Sections 100 to 104 to effectuate the buyback of shares and there is no compulsion for the Petitioner to follow only the procedure prescribed by Section 77 A/Section 68. In any event, under Section 77 /Section 68 a company can buyback only 25% of the total paid up capital and free reserves of the company whereas under the Scheme the company proposes buyback of 30% of its paid up capital and free reserves, which is not possible under Section 77 /Section 68. Consequently the only manner in which the company can buyback the said shares is by following the procedure under Section 391 read with Sections 100 - 104 of the 1956 Act. In support of its contentions the Petitioner has relied upon the decision of the Division Bench of this Court in the case of SEBI V/s. Sterilite Industries (India) Limited.

7. The Division Bench of this Court in the case of Sterilite Industries (supra) has held that a Company may either follow the procedure under Section 391 read with Sections 100 to 104 of the 1956 Act or the procedure under Section 77A (now Section 68). It is not mandatory for a company to buy back its shares only by following the procedure prescribed by Section 77 A. In this regard paragraphs 22 and 23 of the Sterilite decision are relevant and the same are reproduced below for convenience:

> "22. The opening words of Section 77A, viz. "notwithstanding anything contained in this Act,but subject to the provisions of sub-section(2) of this section and section 77B, a company may purchase its own shares or other specified securities…" shows that section 77A is a facilitating provision which enables companies to buy-back their shares without having to approach the court under section 391 and section 100 to 104 subject to compliance with the provisions of sub-sections (2), (3) and (4). Prior to the introduction of section 77 A, the only manner in which a company could buy-back its shares was by

following the procedure set out under sections 100 to 104 and section 391 which required the calling of separate meetings of each class of shareholders and creditors as well as (if required by the court) the drawing up of a list of creditors of the company and obtaining of their consent to the scheme for reduction. The legislative intention behind the introduction of section 77 A is to provide an alternative method by which a company may buy-back upto 25 per cent of its total paid- up equity capital in any financial year subject to compliance with sub-sections (2), (3) and (4). It does not supplant or take away any part of the pre-existing jurisdiction of the company court to sanction a scheme for such reduction under sections 100 to 104 and section 391.

23. The submission of the appellants that the non obstante clause in section 77A gives precedence to that section over provisions of sections 100 to 104, section 391 is misconceived. The non obstante clause in section 77 A namely "notwithstanding anything contained in this Act .... " Only means that notwithstanding the provisions of section 77 and sections with the conditions mentioned in that section without approaching the court under sections 100 to 104 or section 77A to indicate that the jurisdiction of the court under section 391 or 394 has taken away or substituted. It is well settled that the exclusion of the jurisdiction of the court should not readily be inferred, such exclusion should be explicitly or clearly implied. There is nothing in the language of section 77 that gives rise to such an inference. We are, therefore, inclined to hold that section 77 A is merely an enabling provision and the courts powers under sections 100 to 104 and section 391 are not in any way affected. The conditions provided in section 77A are applicable only to buy-back of shares under section 77A. the conditions applicable to sections 100 to 104 and section 391 cannot be imported into or made applicable to a buy-back under section 77A. Similarly the conditions for a buy-back under section 77A cannot be applied to a scheme under sections 100 to 104 and section 391. The two operate in independent fields".

4.However,it is necessary to note that the above was the position in law under the1956 Act in view of the language of the provisions of Section 391 and Section 77 A of that Act. In the 2013 Act Sub-section 10 of Section 230 provides as follows :-

"10. No compromise or arrangement in respect of any buy-back of securities under this section shall be sanctioned by the Tribunal unless such buy-back is in accordance with the provisions of section 68."

This provision may have an impact on the law as laid down by this Court in the Sterilite case. However, at present Section 230 has not come into force and hence this question does not arise for consideration in this question does not arise for consideration in this case and hence the same need not to be considered. At present the law as laid down in Sterilite Industries prevails and will be applicable to the present case.

5.In the circumstances it is open to a company to buy back its own shares by following the procedure prescribed under section 77A/Section 68 or by following the procedure prescribed under section 391 read with Sections 100 to 104 of the 1956,Act.The contentions of the Regional Director are therefore clearly contrary to the prevailing lega1 position."

The above observations of the Hon'ble Court does not leave any doubt that buyback of shares cannot be equated with reduction of capital.

5.1.*We find that while amending the CA,by introduction of section 77A of the Act,Legislature had made amendments to the Income tax Act too.We would like to reproduce Section 2(22)(d) and section 46A of the Act and same read as under:*

(22) "dividend" includes-

(a) …….

(b) …….

(c) ……..

(d) any distribution to its shareholders by a company on the reduction of its capital, to the extent to which the company possesses accumulated profits which arose after the end of the previous year ending next before the 1st day of April, 1933, whether such accumulated profits have been capitalised or not ;"

"46A. Where a shareholder or a holder of other specified securities receives any consideration from any company for purchase of its own shares or other specified securities held by such shareholder or holder of other specified securities, then, subject to the provisions of section 48, the difference between the cost of acquisition and the value of

consideration received by the shareholder or the holder of other specified securities, as the case may be, shall be deemed to be the capital gains arising to such shareholder or the holder of other specified securities, as the case may be, in the year in which such shares or other specified securities were purchased by the company.

Explanation.—For the purposes of this section, "specified securities" shall have the meaning assigned to it in Explanation to section 77A of the Companies Act, 1956 (1 of 1956)."

The reasonable conclusions that can be drawn from the scrutiny of the above sections are that buy back of shares and reduction of share-capital are different concepts,that buyback of shares of a corporate entity cannot to be characterised as deemed dividend,that profit arising out of the buyback schemes had to taxed under the head capital gains.

Here,it would be useful to take notice of the Speech of the Finance Minister while introducing the amendment to the Act with regard to the buyback of shares.Relevant part of the speech of the FM reads as follow:

"95.Very recently, the Companies Act, 1956 has been amended to permit transactions relating to buy-back of shares. There is some ambiguity in the interpretation of the law as to whether such transactions would be treated as subject to dividend tax in addition to capital gains. In view of this, I propose to amend the law to put it beyond doubt that on buy-back of shares, the shareholders will not be subject to dividend tax, and would only be liable to capital gains tax."

Central Board of Direct Taxes had issued a circular(Circular no.779,dated 14.09.2099) with regard to taxability arising out of the buyback of shares and circular reads as under:

"28 Clarification of tax issues arising out of the provision to allow buy-back of shares by the companies

28.1 The Companies (Amendment) Ordinance, 1998 [subsequently enacted as the Companies (Amendment) Act, 1999] inserted section 77A in the Companies Act, 1956 which allows a company to purchase its own shares subject to certain conditions. The shares bought back have to be extinguished and physically destroyed and the company is precluded from making any further issue of securities within a period of 24 months from such buy-back.

28.2 The above newly introduced provisions of buy-back of shares threw up certain issues in relation to the existing provisions of the Income-tax Act. The two principal issues are whether it would give rise to deemed dividend under section 2(22) of the Income-tax Act and whether any capital gains would arise in the hands of the shareholder. The legal position on both the issues were far from clear and settled and there was apprehension that there will be unnecessary litigation unless the issues are clarified with finality.

28.3 The Act, therefore, has amended clause (22) of section 2 of the Income-tax Act by inserting a new clause to provide that dividend does not include any payment made by a company on purchase of its own shares in accordance with the provisions contained in section 77A of the Companies Act, 1956. It has also inserted a new section, namely, section 46A in the Income-tax Act, to provide that any consideration received by a shareholder or a holder of other specified securities from any company on purchase of its own shares or other specified securities shall be, subject to provisions contained in section 48, deemed to be the capital gains.

28.4 This amendment will take effect from 1st day of April, 2000 and will, accordingly, apply in relation to the assessment year 2000-2001 and subsequent years."

It is worth mentioning that provisions of section 115Q have been amended w.e.f. 01.04.2013 and profit arising out of buyback of shares is to taxed at a particular tax rate.But,the AY.,before us, is prior to the April,1st,2013.Therefore,we have to decide the issue as per the prevailing law applicable on the date of the transaction in question.There is no ambiguity about the provisions that would govern the buyback of shares.Section 2(22)(d)(iv)r.w.s.46A of the Act would be applicable to the buyback scheme.Accordingly, the transaction cannot be treated deemed dividend.

5.2.*Now,we would deal with the issue of treating the assessee as A-I-D for not deducting tax at source.Once it has been decided that the profit arising out of buyback would be taxed as capital*

gains the next step is to determine as to whether the capital gains are taxable in the hands of parent company of the assessee in light the Indo-Mauritius Tax Treaty.Article 13 of the said DTAA provides that capital gains would not be taxable in the hands of GS-M.If the assessee was not liable to deduct taxes as per the provisions of section 195 of the Act, it cannot be held A-I-D.For invoking the provisions of section 201 of the Act,non deduction of taxes at source is a pre-condition.We also find force in the alternate argument raised by the assessee.Even if the payment to GSM is considered as dividend u/s.2(22)(d) of the Act,then the taxes on the same have to be charged by way of DDT as per section 115-O of the Act.As per section 10(34) of the Act, any income by way of dividend referred to in section 115-O of the Act does not form part of total income in the hands of the recipient and company declaring dividend will be in default as per section 115Q.So,the provisions of TDs would not be applicable for dividend covered under section 2(22)(d) of the Act.

5.3.*We would also like to discuss the issue of the alleged colourability of the transaction. We find that in the matter of Capgemini India Private Limited(supra),the Hon'ble Bombay High Court has deliberated upon the almost identical facts and circumstances and has held as under:*

> 6. According to the Regional Director if the Scheme is sanctioned it will amount to evasion of income tax and outflow of foreign exchange to the tune of Rs.248 crores and therefore on this ground the Scheme should be rejected. The Regional Director has not furnished any particulars in support of the aforesaid contention. Be that as it may, if the law permits a company to buy back back its shares in more than one way; the company cannot be compelled to follow only the method that results in payment of income tax. It is well settled that an assessee can always manage his affairs in a manner so as to avoid payment of tax. In the present case since it is legally permissible for the company to buy back its shares by following the procedure under Section 391 read with Sections 100 to 104 of the 1956 Act, the fact that the same may not attract income tax will not amount to it being a device to evade tax.
>
> 7. Even the argument of the Regional Director that foreign exchange amounting to Rs.248 crores will be drained away if the Scheme is sanctioned, is of no avail once it is held that the procedure adopted by the company is permissible in law. Moreover, the Regional Director has not shown that the law prohibits the transfer of shares by a non-resident to resident. In fact, he does not dispute that the same is permissible. The Petitioner has placed on record RBI's Circular No.49 dated 4th May 2010 which provides that shares of an unlisted Indian company can be transferred by a non-resident to a resident under the general permission of the RBI if the transfer price does not exceed the fair market value as determined by a Chartered Accountant or a SEBl registered Merchant Banker as per the DCF method. In the present case the transfer price has been arrived at in accordance with the aforesaid circular of the RBI. The Regional Director has not disputed the fair market value of the shares so determined. In these circumstances it is clear that the buyback of shares under the Scheme is in accordance with the RBI Guidelines and that being so, there is no question of there being any draining away of foreign exchange.
>
> 8. in view of the above and particularly the fact that in law the Petitioner is entitled to buy back its own shares by means of a scheme under Section 391 read with sections 100-104of the 1956 Act, the scheme cannot be said to be a colorable device to evade income tax. It is a legally permissible procedure which the Petitioner is entitled to follow to buy back its shares."

Following the above order,we hold that transaction in question would not fall under the category of colourable device.If an assessee enters into a deal which does not violate any provision of the Act of applicable to a particular AY.the deal cannot be termed a colourable device,if it result in non-payment or lesser payment of taxes in that year.The whole exercise should not lead to tax evasion.Non-payment of taxes by an assessee in given circumstances could be a moral or ethical issue.But,for that the assessee cannot be penalised.In light of the above discussion,we are reversing the decision of the FAA and deciding the effective ground of appeal in favour of the assessee."

Following the above order effective ground of appeal is decided against the AO.

As a result, appeal filed by the assessee stands allowed and appeal of the AO is dismissed.
फलतः निर्धारिती द्वारा दाखिल की गई अपील मंजूर की जाती है और निर्धारिती अधिकारी द्वारा दाखिल की गई अपील नामंजूर की जाती है.

Order pronounced in the open court on 22nd April, 2016.
आदेश की घोषणा खुले न्यायालय में दिनांक 22 अप्रैल, 2016 को की गई।

Sd/-	Sd/-
जोगिन्दर सिंह /Joginder Singh)	**(राजेन्द्र / RAJENDRA)**
न्यायिक सदस्य **/ JUDICIAL MEMBER**	**लेखा सदस्य / ACCOUNTANT MEMBER**

मुंबई Mumbai; दिनांकDated : 22 .04.2016.
Jv.Sr.PS.

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :

1.Appellant /अपीलार्थी **2.** Respondent /प्रत्यर्थी
3.The concerned CIT(A)/संबद्ध अपीलीय आयकर आयुक्त, **4.**The concerned CIT /संबद्ध आयकर आयुक्त
5.DR "A " Bench, ITAT, Mumbai /विभागीय प्रतिनिधि, खंडपीठ,आ.अ.न्याया.मुंबई
6.Guard File/गार्ड फाईल

सत्यापित प्रति //True Copy//

आदेशानुसार/ **BY ORDER,**
उप/सहायक पंजीकार **Dy./Asst. Registrar**
आयकर अपीलीय अधिकरण, मुंबई **/ITAT, Mumbai.**