

आयकर अपीलीय अधिकरण, 'ए' न्यायपीठ, चेन्नई
IN THE INCOME TAX APPELLATE TRIBUNAL, 'A' BENCH, CHENNAI
श्री ए. मोहन अलंकामणी, लेखा सदस्य एवं श्री धुव्वुरु आर.एल रेड्डी, न्यायिक सदस्य के समक्ष
BEFORE SHRI A.MOHAN ALANKAMONY, ACCOUNTANT MEMBER
AND SHRI DUVVURU RL REDDY, JUDICIAL MEMBER

आयकर अपील सं./I.T.A.No.1352/Chny/2018
(निर्धारण वर्ष / Assessment Year: 2014-15)

M/s. Vaani Estates Pvt. Ltd., No.60, Old No.100, IV Street, Abhiramapuram, Chennai – 600 018.	Vs	The ITO, Corporate Ward – 3(4), Chennai
PAN: AAECV0933A		
(अपीलार्थी/Appellant)		(प्रत्यर्थी/Respondent)

अपीलार्थी की ओर से/ Appellant by	:	Shri R. Vijayaraghavan, Advocate
प्रत्यर्थी की ओर से/ Respondent by	:	Shri Prabhu Mukunth Arunkumar, Sr. Standing Counsel

सुनवाई की तारीख/Date of hearing	:	12.06.2018
घोषणा की तारीख /Date of Pronouncement	:	27.08.2018

आदेश / ORDER

Per A. Mohan Alankamony, AM:-

This appeal by the assessee is directed against the order passed by the learned Commissioner of Income Tax(Appeals)-1, Chennai, dated 19.03.2018 in ITA No.199/16-17 for the assessment year 2014-15 passed U/s. 250(6) r.w.s. 143(3) of the Act.

2. The assessee has raised several grounds in its appeal however the crux of the issue is that the Ld.CIT(A) has erred in confirming the addition made by the Ld.AO amounting to Rs.23,31,68,600/- towards 'income from other sources' invoking the provisions of Section 56(2)(viib) of the Act.

3. The brief facts of the case are that the assessee is a private limited company engaged in real estate business filed its return of income for the assessment year 2014-15 on 29.09.2014 declaring loss of Rs.4,40,920/-. Initially the return was processed U/s.143(1) of the Act and subsequently the case was selected for scrutiny under CASS and notice U/s.143(2) of the Act was served to the assessee on 23.09.2015. Finally assessment order was passed U/s.143(3) of the Act on 16.11.2016 wherein the Ld.AO had made addition of Rs.23,31,68,600/- towards 'Income from other sources' invoking the provisions of Section 56(2)(viib) of the Act.

4. During the course of scrutiny assessment proceedings, it was observed by the Ld.AO that in the relevant assessment year, the assessee company had issued 10,100 equity shares having face value of Rs.10/- each at a premium of Rs.23,086/- to one of the

existing share holder. On query to justify the allotment of equity share at premium it was explained that the assessee company had acquired land for a consideration of Rs.23,09,57,869/- during the relevant assessment year i.e., on 12.12.2013 and therefore the fair market value per equity share of the company as on 31.12.2013 was Rs.23,096/-. However since the assessee company has computed the net worth of the equity share, after taking into account of the value of the new asset acquired which was subsequent to the receipt of share application money from Mrs.Sasikala Raghupathy, the Ld.AO opined that the assessee company had received excess price / share premium for the shares allotted to Mrs.Sasikala Raghupathy over and above the face value of shares which works out to Rs.23,31,68,600/- (i.e., 23,086 * 10,100). Accordingly the Ld.AO invoking the provisions of Section 56(2)(viib) of the Act, added the amount of Rs.23,31,68,600/- to the income of the assessee.

5. Before the Ld.CIT(A), the Ld.AR made the following submissions:-

“The Appellant Company had only two shareholders viz Mrs. Sasikala Raghupathy and her husband Mr. B. G. Raghupathy (each holding 5000 shares). On passing away of E.G. Raghupathy, his 5000 shares devolved on

her daughter Mrs. Vani Raghupathy. Therefore Mrs. Sasikala Raghupathy and her daughter Mrs. Vani Raghupathy were holdings 5000 shares each.

The Company proposed to acquire immovable property viz the land. The value of the land was approximately Rs.23.09 crores. Accordingly, Mrs. Sasikala Raghupathy who had the funds, brought in money about Rs.23.32 crores. She was allotted 10100 shares with a share premium of Rs.23.31 crores. The Assessing Officer has brought to tax, in the hands of the Company, Rs.23.31 crores under Section 56(2)(viib).

Section 56(2)(viib) was introduced by the Finance Act, 2012. The purpose of introduction of Section 56(2)(viib), as explained by the Finance Minister while introducing the Finance Bill, was to cover investment of unaccounted money by investing in shares with huge share premium. Further 3rd parties such investment at exorbitant rate of share premium, will be conferring benefit to the existing shareholders by enhancing the value of their shareholding.

Thus sec 56(2)(viib) was introduced to curb unconnected parties conferring benefit to the existing shareholders with an ulterior motive. Further the purpose of introduction of Section, as per the speech of the Finance Minister introducing these provision was to deter generation and use of the unaccounted money.

Thus, for the application this Section is to be seen whether unconnected parties confer benefit of enhanced shareholding to existing shareholders by bringing funds and being allotted shares at a huge share premium. This is basically a provision to attack tax avoidance and would apply to what can be considered as 'impermissible Transactions'.

But in the instant case, the entire share holding of the Company was held by the mother and the daughter. The Company wanted fund for acquiring landed property. As only mother had the necessary funds, she had brought in requisite amount to acquire the property.

If the amount brought in as a loan, it would be difficult to service or repay apart from the loan being considered as deposit against acceptance of deposit rules. Similarly, allotment of huge amount of shares (to the extent Rs.23 crores) would make the company top heavy and the shareholders cannot be serviced and would be difficult to attract further investments. Therefore, the Company (Shareholders) had decided on allotment of 10100

shares at face value to the mother and had considered the balance amount as share premium account.

Introduction of additional equity capital was not merely to benefit the existing shareholder but was required for specific purpose of the Company viz for acquisition of the land. Therefore, it was not an exercise to merely grant benefit to the existing shareholders by increasing the value of their shares. Thus, the specific requirement of the company has only one of the shareholders, the said money was brought in her shares and allotment of number of shares was based on the agreement between two shareholders. The share application money brought in for specific use of the Company, by the existing closely related shareholders and without involvement of funds brought in by any third parties, cannot be brought in within the scope of Section 56(2)(viib).

The purpose of this Section is to tax unnecessary benefit given to the existing shareholders, when funds are brought in by unconnected 3rd party for which shares are allotted for a small face value. Here, when the mother has brought in money, it cannot be said that it was for the sole purpose to benefit the other shareholder who is her daughter.

Further, the money already holds 50% of the shares and after allotment she was holding 75% of the shares. Therefore, the benefit accruing to the daughter can at best be only 25% and only that amount if at all can be brought to tax under Sec. 56(2)(viib).

It should also be understood that the purpose of Section is to tax un due benefit given to the existing shareholders by way of introducing large amount of share premium and thus, avoiding taxation under Section 56(2)(x). However, in the present benefit goes to daughter of the shareholders, who falls within the exempted category of relatives under sec 56(2)(x). Any benefit granted by mother to daughter is not taxable under Section 56(2)(x).

Again, Mother could have gifted 50% of the amount to the daughter, which is not taxable u/ s 56(2)(x). Both could have invested equal amount in the Company, on the same terms and conditions. Even then the company would be assessed to tax u/ s 56(2)(viib). That is to say, even if all the existing shareholders contribute additional equity in proportion of their shareholding (Rights issue) for the business of the Company, and if the shares are allotted at a premium, the Company will be taxed u/s 56(2)(viib). This would be against the purpose of introduction of the section.

A penal section should be interpreted in a harmonious manner achieve the purpose for which it was introduced, it has to be read down. It cannot be applied to penalize a genuine transaction which was never intended to brought within the mischief which was sought to be covered.

Therefore considering the purpose in which Section was introduced, considering the fact that the money brought in by the existing shareholders, considering the fact that two shareholders who closely related and conferment of benefit by one on other cannot be taxed under Section 56, Provisions of Sec. 56(2)(viib) are not applicable to the facts of the instant case.

In any event, (i)without prejudice the value of shares are to be determined under Section 56(2)(viib) after allotment of the shares and the difference between the amount brought in and the value of the shares after allotment can be brought to tax under Section 56(2)(viib). (ii) The fact that after allotment the mother was holding 75% of equity shares and the daughter was holding only 25% of the shares. Only the benefit that is deemed to accrue to the daughter out of her holding 25% of shares (i.e only one fourth of the additional amount brought in by mother should be assessed u/s 56(2)(viib).

However the Ld.CIT(A) confirmed the order of Ld.AO by observing as under:-

“6. As above, the assessee has submitted that prior to allotment of new shares, Mrs Sasikala Raghupathy and her daughter Mrs. Vani Raghupathy, were holding 5,000 shares each of the assessee company. The assessee company wanted to purchase a land of the value of Rs.23.09 crores. To fulfil the requirement of funds, the assessee company had allotted 10,100 shares at a premium of Rs. 23,086/- thereby receiving an amount of Rs.23.32 crores sufficient enough to purchase and register the immovable property. However, it is noted in this regard that the purchase of property has happened subsequent to the allotment of shares at premium. To that extent, the entire activity of purchase of property is post the share allotment activity and hence, not relevant in deciding whether the share premium received is liable for taxation 56(2)(viib).

7. In this regard, the wordings of section 56(2)(viib) are reproduced as under:.

"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 from such shares as exceeds the fair market value of the shares. "

Explanation - For the purpose 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.

8. *As above, the section is absolute in its wording and does not provide for any exceptions other than the ones specifically given. The Section further refers to the valuation of unquoted shares under Rule 11 UA which in-turn has given certain methods for valuing the unquoted shares. The assessee has not claimed being specifically covered by any futuristic method of valuation like the discounted cash flow or any other method. Under the circumstances, it is presumed that the net asset value for arriving at the fair market value of shares is accepted by the assessee. The Assessing Officer has also taken the valuation at NAV and has considered the entire share premium as being excessive and liable for taxation u/s 56(2)(viib). In this regard, the written submission of the assessee is perused. The assessee has claimed that shares are allotted at a premium to one of the shareholders who is a blood relative of the other shareholder. The AR contends that 56(2)(viib) is not attracted on account of the beneficial share purchaser being a relative of the other existing shareholder. However, this explanation of the assessee cannot be accepted as the exclusion of 'relatives' from the liability for taxation on account of beneficial transfer is provided only under 56(2)(v), 56(2)(vi) and 56(2)(vii). It is specifically noted that the liability for taxation u/s 56(2)(viib) has not been made specifically exempt when the beneficial transfer is between 'relatives'. In view of the same, the submissions made by the assessee for being excluded from the liability for taxation u/s 56(2)(viib) is rejected.*

9. *The AR for the assessee has also made a plea that the beneficial transfer from one shareholder to the other shareholder is only 25% of the shareholding and as such the taxation of share premium should also be restricted to only 25% of the total premium received. In this regard, it is noted that the section 56(2)(viib) does not provide any limitation from*

taxation of share premium which is in excess of the fair market value of the shares. The Assessing Officer has correctly worked out the fair market value of the shares and has arrived at the excess share premium received. The argument of the assessee presumes the beneficial transfer from one person/ shareholder to the other person/ shareholder ignoring the existence of the third person. In the instant case, the company which has received the share premium is by itself a person and is liable and assessed for taxation. The receipt in excess of FMV is received by the company and not by the shareholders. The benefit also accrues to the company and not to the individual. Moreover, the section has not provided for limiting the amounts attracted u/s 56(2)(viib) for taxation by considering the benefit which accrues to the existing set of shareholders on account of share allotment to new set of shareholders. Considering the totality of reasons as above, the second request of the AR to limit the share premium brought to taxation at 25% of the gross amount cannot be accepted. The request made in this regard is also denied. All grounds taken are rejected.”

6. Before us the Ld.AR reiterated the submission made before the Ld.Revenue Authorities and further referred to the Finance Minister speech of Finance Bill 2012 and the Finance Bill 2012, Bill No.11 of 2012 [As introduced in Lok Sabha on 16th March 2012] and argued by stating that Mrs. Sasikala Raghupathy one among the two share holder of the assessee company had brought in cash into the assessee company for allotment of equity shares with premium to purchase land and the benefit of the share premium has only passed on to the only other shareholder who is here daughter. It was further argued that Section 56(2)(viib) of the Act was brought in to deter generation and use of black money and in the case of the assessee company there was no such generation

and use of black money and therefore the provisions of Section 56(2)(viib) of the Act need not be invoked. It was therefore pleaded that the addition made by the Ld.AO which was further confirmed by the Ld.CIT(A) may be deleted. The Ld.DR on the other hand relied on the orders of the Ld.Revenue Authorities and argued in support of the same.

7. We have heard the rival submissions and carefully perused the materials on record. We find merits in the submission of the Ld.AR. The Hon'ble Finance Minister in his speech of Finance Bill 2012 had stated at para 155 as follows **“I propose a series of measures to deter the generation and use of unaccounted money.** To this end, I propose-

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- * ***Increasing the onus of proof on closely held companies for funds received from shareholders as well as taxing share premium in excess of fair market value.***
- * ***Taxing of unexplained money, credits, investments, expenditures etc., at the highest rate of 30%., irrespective of the slab of income.”***

The relevant portion of the Finance Bill 2012, Bill No.11 of 2012 [As introduced in Lok Sabha on 16th March 2012] is reproduced herein below for reference.

“Share premium in excess of the fair market value to be treated as income Section 56(2) provides for the specific category of incomes that shall be chargeable to income-tax under the head "Income from other sources".

It is proposed to insert a new clause in section 56(2). The new clause will apply where a company, not being a company in which the public are sub-stantially interested, receives, in any previous year, from any person being a resident, any consideration for issue of shares. In such a case if the consideration received for issue of shares exceeds the face value of such shares, the aggregate consideration received for such shares as exceeds the fair market value of the shares shall be chargeable to income-tax under the head "Income from other sources". However, this provision shall not apply where the consideration for issue of shares is received by a venture capital undertaking from a venture capital company or a venture capital fund.

Further, it is also proposed to provide the company an opportunity to substantiate its claim regarding the fair market value. Accordingly, it is proposed that the fair market value of the shares shall be the higher of the value-

(i) as may be determined in accordance with the 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 ~f its assets, including intangible assets, being goodwill, know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature.

This amendment will take effect from 1st April, 2013 and wilt accordingly, apply in relation to the assessment year 2013-14 and subsequent assessment years. [Clause 21]”

7.1 Further in the case of the assessee the following facts emerge and the same is not in dispute:-

- (i) The appellant company had only two shareholders at the beginning of the relevant financial year viz., Mrs. Sasikala Raghupathy and her husband Mr. B.G. Raghupathy each holding 5000 shares.
- (ii) On the demise of Mr. B.G. Raghupathy the shares devolved on their daughter Mrs. Vani Raghupathy.
- (iii) Thereafter Mrs. Sasikala Raghupathy introduced cash into the company amounting to Rs.23.32 crores against which she was allotted 10,100 shares at a premium of Rs.23.31 crores.
- (iv) Thus the total number of shares held as on the end of the relevant assessment year by Mrs. Sasikala Raghupathy stood at 15100 shares and the total number of shares held by Mrs. Vani Raghupathy stood at 5000 shares aggregating to 20100 shares.
- (v) The Ld.AO invoked the provisions of Section 56(2)(viib) of the Act, because 10,100 shares was allotted at an unrealistic premium of Rs.23.31 crores to Mrs. Sasikala Raghupathy.

7.2 From the above facts it is apparent that though Mrs. Sasikala Raghupathy had introduced cash into the assessee company amounting to Rs.23.31 crores for allotment of shares at premium of Rs.23,096/- per share when the intrinsic value of the share was only Rs.10/- per share which is the face value of the shares, the benefit of such investment at an unrealistic share premium has only passed on to her daughter because there are only two shareholders in the assessee company i.e., Mrs. Sasikala Raghupathy and her daughter Mrs. Vani Raghupathy at that point of time. Had Mrs. Sasikala Raghupathy gifted the money to her daughter Mrs. Vani Raghupathy and thereafter if the daughter would have brought the same into the assessee company for allotment of equity shares at face value, invoking of the provisions of Section 56(2)(viib) of the Act would not have aroused. Further as pointed out by the Ld.AR, it is evident from the Finance Minister's speech that the provisions of Section 56(2)(viiia) of the Act was introduced by the Finance Act 2012, only to curb generation and use of unaccounted money. In the absence of the provisions of Section 56(2)(viiia) & Section 56(2)(viib) of the Act it was possible for any company either closely held or otherwise to introduce unaccounted money as investment in equity share of the company

with inflated share premium through a deploy as investor. However in the case of the assessee company, the investors source of investment is genuine and not in dispute. The only other lone shareholder of the assessee company is the daughter of late Mr.B.G. Raghupathy and Mrs. Sasikala Raghupathy who is the new entrant in the business of her parents with no scope of possessing undisclosed cash. From these facts, it is evident that in the case of the assessee company, there is no possibility of generation and use of unaccounted money resulting from the transaction of infusing cash by Mrs. Sasikala Raghupathy into the assessee company in the form of equity share premium. Moreover when the whole transaction is viewed by lifting the corporate veil of the assessee company, it is apparent that 24.88% [*Mrs. Sasikala Raghupathy's percentage of shareholding : 15100 (total number of shares held *100 / 20,100 (Total number of shares allotted) = 75.12% and Mrs. Vaani Raghupathy's percentage of shareholding : 5000 (total number of shares held) * 100 / 20,100 (Total number of shares allotted) = 24.88%*] of the benefit arising out of the introduction of cash in the form of equity share with premium is only benefited from Mrs. Sasikala Raghupathy to Mrs. Vani Raghupathy i.e., from mother to daughter. Further it is pertinent to mention that by virtue of the provisions of Section 56(2)(vi) & (x) of the Act when gift is bestowed by mother to

daughter, it is not taxable. Thus in the case of the assessee, when the provisions of Section 56(2)(vi), (viib) & (x) of the Act, are interpreted in a harmonious manner lifting the corporate wheel of the assessee company, it is abundantly clear that the provisions of Section 56(2)(viib) of the Act, has no implication in the case of the assessee company, more-so keeping in view of the speech delivered by the Hon'ble Finance Minister referred herein above. It is also pertinent to mention that in the instant case the benefit of infusing cash into the assessee company by way of equity share with premium by Mrs.Sasikala Raghupathy will not benefit any other shareholders inducted in the company in future because in such event the shares will have to be allotted on the basis of the intrinsic value of the shares of the assessee company otherwise at that point of time the provisions of Section 56(2)(viib) of the Act will be instantly attracted. In the present situation we are also reminded of the principles of harmonious construction explained by Crawford in Statutory Construction *"Hence the Court should, when it seeks the legislative intent, construe all the constituent parts of the statute together and seek to ascertain the legislative intention from the whole Act, considering every provision thereof in the light of the general purpose and object of the Act itself and endeavouring to*

make every part effective, harmonise and sensible". Further mischief rule of interpretation also propagate that where a statute has been passed to remedy a weakness in the law, the interpretation which will correct that weakness is the one to be adopted.

7.3 It should be also kept in mind that provisions of Section 56(2)(viib) of the Act creates a deeming fiction and while giving effect to such legal fictions all facts and circumstances incidental thereto and inevitable corollaries thereof have to be assumed. At this juncture we are reminded of the decision of the Hon'ble Kolkata High Court in the case M.D. Jindal vs. CIT reported in 164 ITR 29, wherein it was held that *"legal fictions are created only for a definite purpose and they are limited to the purpose for which they are created and should not be extended beyond the legitimate field. But the legal fiction has to be carried to its logical conclusion within the framework of the purpose for which it is created."* Further it is apparent from the Finance Minister's speech that the provisions of Section 56(2)(viib) has been enacted to deter the generation and use of unaccounted money. At this juncture we are also reminded of the decision of the Hon'ble Apex Court in the case Allied Motors

Pvt. Ltd., vs. CIT reported in 224 ITR 677, wherein it was held that the Finance Minister's Budget speech explaining the provisions are relevant in construing the provisions. Moreover in the decision rendered by the Hon'ble Jurisdictional Madras High Court in the case CIT vs. Kay Arr Enterprises and others reported in 299 ITR 348 and in the decision of the Hon'ble Karnataka High Court in the case CIT vs. R. Nagaraja Rao it has been categorically held that *"where there are transactions involving family arrangement with respect to transfer of shares, the corporate veil of the company has to be lifted and inferred that there is no transfer of shares and accordingly capital gain tax is not exigible."* From the above it is apparent that even when there are transfer of shares physically, in the event of family arrangements, the Hon'ble High Courts have held that the entire transactions has to be viewed lifting the corporate veil and treat the transaction as if there is no transfer of shares and hence capital gain tax is not attracted. Similarly we are of the view that in the case of the assessee company also the corporate veil is required to be lifted and thereafter the transaction has to be viewed in the light of the relevant provisions of the Act.

7.4 Bearing in mind, the facts of the case, the decision of the higher Judiciary Authorities cited supra and the legal principles discussed herein above, we are of the considered view that provisions of Section 56(2)(viib) of the Act, cannot be invoked in the case of the assessee company because by virtue of cash being brought into the assessee company by Mrs. Sasikala Raghupathy for allotment of equity shares with unrealistic premium the benefit has only passed on to her daughter Mrs. Vani Raghupathy and there is no scope in the Act to tax when cash or asset is transferred by a mother to her daughter. Hence we hereby direct the Ld.AO to delete the addition made by invoking the provisions of Section 56(2)(viib) of the Act in the case of the assessee company.

8. In the result appeal of the assessee is allowed.

Order pronounced on the 27th August, 2018 at Chennai.

Sd/-
(धुव्वुरु आर.एल रेड्डी)
(Duvvuru RL Reddy)
न्यायिक सदस्य /Judicial Member

Sd/-
(ए. मोहन अलंकामणी)
(A. Mohan Alankamony)
लेखा सदस्य / Accountant Member

चेन्नई/Chennai,
दिनांक/Dated 27th August, 2018

RSR

आदेश की प्रतिलिपि अग्रेषित/Copy to:

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