IN THE HIGH COURT OF HIMACHAL PRADESH AT SHIMLA

ITA No.4 of 2024
Reserved on:27.05.2024
Pronounced on:31.05.2024

Pr. Commissioner of Income Tax-1, Chandigarh …Appellant

Versus

M/s I.A. Hydro Energy (P) Limited …Respondent

Coram:

Hon'ble Mr. Justice M.S. Ramachandra Rao, Chief Justice.
Hon'ble Mr. Justice Satyen Vaidya, Judge.

Whether approved for reporting?

For the appellant : Mr. Neeraj Shara & Mr. Ishan Kashyap, Advocates.

For the respondent : Nemo.

M.S. Ramachandra Rao, Chief Justice.

This appeal is preferred by the Revenue under Section 260-A of the Income Tax Act, 1961 (in short **"the Act"**), challenging the order dt. 11.10.2023, passed by the Income Tax Appellate Tribunal (in short **"the Tribunal"**), Bench 'A', Chandigarh, for the Assessment Year 2018-19.

2. The respondent-assessee is engaged in the business of Generation and Distribution of Hydro Electricity in the State of Himachal Pradesh.

3. It filed a Return for the Assessment Year 2018-19 on 15.10.2018, declaring loss of Rs.67,15,30,280/-.

4. The assessee had issued 2.25 crores equity shares with face value of Rs.10/- per share for a premium of Rs.90/- per share to *M/s Shri Bajrang Power & Ispat Ltd. and Shri Bajrang Energy Private Ltd*.

5. In its reply to the Notices issued u/s 143 of the Act, the assessee stated that prior to 23.02.2017, both the share subscribers were partners in the assessee-firm and the balances were showing as Partners Capital Account.

6. The assessee-company was having opening balance of unsecured loans as on 01.04.2017, which were converted into share capital as per agreement.

7. According to the assessee, the shares have been valued as per Discounted Cash Flow Method, prescribed in Rule 11UA of the Income Tax Rules and a Certificate was also obtained from the Chartered Accountant, as required under the Income Tax Rules.

8. The case of the assessee was selected for Limited Scrutiny under the e-Assessment Scheme.

9. Assessment was completed by the Assessing Office (Faceless), vide order dt. 12.04.2021 u/s 143(3) read with Section 143(3A) & 143(3B) of Act, at an income of Rs.135,36,85,457/- by making an addition of Rs.202.50 crores under the Head *'Income from Other Sources'* under Section 56(viib) of the Act, on account of excess amount per share paid as premium. The said order is Annexure P-2.

10. In the assessment order, the valuation report furnished by the assessee-company was rejected by the Assessing Officer (AO), holding that the

Discounted Cash Flow (DCF) valuation used by the assessee, is bogus and has no connection with the real figures. The said order stated that the valuation was done with fictitious figures having no correlation with actual affairs of the assessee-company. Thereafter, the Assessing Officer, National Faceless Assessment Centre, computed the fair market value of the unquoted shares on the basis of balance sheet figures as per NAV method and passed his order.

11. This was challenged by the assessee-company before the CIT(Appeals), National Faceless Assessment Centre.

12. The CIT(Appeals) deleted the additions made by the Assessing Officer, in its order dt. 13.05.2022.

The Appellate Authority held that since no money/consideration was received by the assessee on issue of shares and the shares are allotted merely on account of conversion of outstanding loans received in earlier years and source whereof was accepted to be satisfactorily explained into share capital, Section 56(2)(viib) of the Act in absence of receipt of consideration, is not applicable.

It also held that the valuation is done by the assessee as per DCF method, which is an internationally accepted method of valuation of shares, and is a permissible methodology as per Rule 11UA(2)(d) of the Rules.

It held that the right to select the method of valuation (NAV or DCF), is vested with the assessee, and the Assessing Officer erred in substituting the assessee's method of valuation, i.e. DCF, with his own method of valuation, i.e. NAV method, and had acted completely beyond his jurisdiction.

It also held that the report of the Technical Expert is binding on the Assessing Officer, which cannot be disregarded/rejected without any cogent reasons, and the impugned addition of Rs.202.50 crores, made under Section 56(2)(viib) of the Act, is required to be deleted.

The decision of the ITAT

13. The Revenue Department challenged this order before the Income Tax Appellate Tribunal, Bench *'A'*, Chandigarh, by filing ITA no.548/CHD/2022.

14. The Tribunal confirmed the finding of fact that the assessee did not receive any consideration for allotment of shares in the previous year relevant to the current assessment year, and upheld the view of the CIT (Appeal) if no consideration was received in the previous year under consideration, Section 56(2)(viib) of the Act has no application.

It held that the consideration in the form of unsecured loans were received from the partner of the erstwhile firm in the year 2010, as evidenced from loan agreement, and the Assessing Officer could not bring out any material facts to show that such conversion of loans to equity shares was a ploy to defraud revenue of the tax on such transaction.

The Tribunal went further and observed that the Assessing Officer is not authorized to pick and choose a particular method of valuation of shares, since the option in that regard is specifically given *only* to the assessee as per Rule 11UA(2) of Income Tax Rules,that the AO can only verify method of valuation adopted by the assessee, but the same cannot be substituted by the AO by a

different method i.e., NAV method, once the assessee has exercised option for the DCF valuation method.

It held that the Assessing Officer was not correct in rejecting the DCF method and proceeding to value the shares by NAV method merely on the ground that there was a huge difference in projected figures and actual results available for some years.

15. It relied on the judgment of Mumbai Income Tax Appellate Tribunal in ***Creditalpha Alternative Investment Advisors (Pvt.) Ltd.***[1].

The ITA

16. Challenging the said order, this appeal is filed.

17. The counsel for the Department-Revenue sought to contend that the orders passed by the Tribunal are not legal and proper and pressed the following contentions:-

> *"i) Whether the Hon'ble ITAT is right in law and on the facts and the circumstances of the case in holding that there is no case of application of Section 56(2) (viib) in the respondent's case where pre-existing unsecured loans of partners/shareholders were converted into equity shares at premium and the facts of the assessment order do not indicate any case of tax abuse involved in such share conversions?*
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> *ii) Whether the Hon'ble ITAT is right in law and on the facts and the circumstances of the case in holding that the unsecured loans received by the assessee in earlier years but converted to shares in the assessment year under appeal will not fall under the definition of "any consideration for issue of share received in the previous year" and therefore will not attract the provisions of section 56(2) (viib) of the Income tax Act, 1961?*

[1] (2022) 134 Taxmann.com 223 (Mumbai)

iii) Whether the Hon'ble ITAT has erred in not considering the fact that the unsecured loans received in earlier years were in the nature of liability of the assessee while upon being converted to shares, the nature of unsecured loans changed to consideration in lieu of shares during the assessment year and therefore will attract the provisions of Section 56(2) (viib) of the Income Tax Act, 1961?

iv) Whether the Hon'ble ITAT is right in law and on the facts and the circumstances of the case in holding that the unsecured loans were verified during the assessment in previous year and there is no abuse of tax laws although, the color of unsecured loans was changed from liability to ownership only upon allotment of shares in the year under appeal and therefore the provision of Section 56(2) (viib) will be applicable in the current assessment year?

v) Whether the Hon'ble Tribunal is right in law in holding that as the valuation of shares had been based upon the valuation report. The same could not be doubted by the Assessing Officer. The said finding smacks of perversity and whether it is legally sustainable or not in the eyes of law?

vi) Whether the Hon'ble ITAT erred in deleting the addition of Rs.202.50 crores under the Head "Income from Other Sources" u/s 56(2) (viib) of the Act on account of excess amount per share paid as premium and not allowing the Assessing Officer's decision to substitute DCF method of share valuation by NAV method in accordance with the Rule 11UA of the Income Tax Rules?"

18. We are of the opinion that the orders passed by the Income Tax Appellate Tribunal as well as the CIT(Appeals), are fairly comprehensive. Both of them have concurrently found that no consideration was received by the assessee-firm for allotment of the shares, therefore Section 56(2)(viib) of the Act would not apply, and that it would have applied only if consideration was received for such a transaction.

19. Also, both the Tribunal and the CIT(Appeals) have held that the Assessing Officer had no jurisdiction to substitute the NAV method of assessing the valuation of shares, once the assessee had exercised option of a DCF valuation method as per Rule 11UA(2) of the Income Tax Rules.

20. We agree with the reasoning adopted by the CIT(Appeals) confirmed by the ITAT on all aspects and find that no substantial questions of law arise in this appeal for consideration by this Court.

21. Accordingly, the appeal fails and is dismissed.

22. Pending miscellaneous application(s), if any, shall also stand disposed of.

(M.S. Ramachandra Rao)
Chief Justice

(Satyen Vaidya)
Judge

May 31, 2024
(Yashwant)