



Gift of shares without consideration by a company is exempt from capital gains tax liability

Recently, the Bombay High Court in the case of Asian Satellite Broadcast Pvt. Ltd.¹ (the taxpayer) while quashing reassessment proceedings held that the transfer of shares without consideration was a gift transaction which was valid, permissible and genuine. The High Court held that such transfer of shares by a company by way of gift are exempt from the provisions of capital gains.

Facts of the case

The taxpayer is engaged in the business of trading in fabric yarn, investment and finance. During the Assessment Year 2012-13, the taxpayer had transferred equity shares of an Indian listed company to its unlisted associate entity as a gift i.e., without consideration. For this transaction, the taxpayer incurred loss on transfer of such shares. The taxpayer declared loss of INR 369,126 while filing its tax return. Subsequently, the loss was revised at INR 191,940.

The Assessing Officer (AO) passed the assessment order assessing the total income of the taxpayer at total loss of INR 191,940. The taxpayer correctly disclosed all material/explanation during the regular assessment proceedings. Subsequently, the reassessment notice² was issued by the AO beyond four years from the end of the assessment year in question stating that he had reasons to believe that taxpayer's income chargeable to tax for the Assessment Year (AY) 2012-13 had escaped assessment. The AO observed that transfer of shares of listed entities at nil consideration amongst unlisted group entities was made with the sole purpose of evading payment of capital gains tax and such transfer clearly fell within the scope of a colourable device. Aggrieved, the taxpayer filed writ petition before the High Court.

Taxpayer's contentions

Gift of shares was permissible under Section 47(iii) of the Income-tax Act, 1961 and therefore, no tax on capital gains can be levied on such transfer. There was no capital gain on account of the transfer being a gift. All the materials/explanation were produced before the AO wherein he had accepted the transfer of shares as a gift and completed the assessment after due scrutiny under Section 143(3). Based on two letters of two tax officers subsequently a different view was taken by the AO that the transfer of shares was a colourable device used by the taxpayer as a mean to evade payment of income tax. This was nothing but change of opinion.

The Bombay High Court had issued notice and granted ad-interim stay to the reassessment notice by taking the view that it was a clear case of change of opinion and thus, impugned notice is without jurisdiction. Therefore, the AO had no jurisdiction to issue the impugned notice under Section 148.

High Court's decision

Section 47(iii) provides that nothing contained in Section 45 shall apply to any transfer of a capital asset under a gift or will or an irrevocable trust. However, as per the proviso, this clause shall not apply to transfer under a gift or an irrevocable trust of a capital asset being shares, debentures, etc. allotted by a company, directly or indirectly to its employees under any employees' stock option plan or scheme of the company offered to such employees in accordance with the guidelines issued by the central government in this behalf.

On conjoint reading of the above provisions it indicates that while any profits or gains arising out of transfer of a capital asset shall be deemed to be the income of the previous year in which the transfer took place chargeable to tax under the head 'capital gains', any transfer of a capital asset under a gift or will or an irrevocable trust shall not be liable to tax under the head 'capital gains'. Evidently, the proviso is not applicable to the case of the taxpayer.

¹ Asian Satellite Broadcast Pvt. Ltd. v. ITO (Writ Petition No.2749 of 2019) – Taxsutra.com

² Under Section 148

The Gujarat High Court in the case of Prakriya Pharmachem³ examined a challenge to re-opening of assessment on the ground that transfer of shares by way of a transfer deed led to escapement of income from assessment. After referring to Sections 45 and 47(iii), the Gujarat High Court held that nothing would apply to any transfer of capital assets under a gift or will or an irrevocable trust. The Gujarat High Court also held that it was not the case of the AO that the said case was not one of transfer of asset under a gift. It was held that reasons recorded by the AO to form the belief that income chargeable to tax had escaped assessment lacked validity. Therefore, the reassessment notice was set aside.

In the present case, notice was issued beyond four years from the end of the assessment year in question. It was also not the case where the taxpayer failed to file its tax return under Section 139 or in response to a notice issued under Section 142(1) or Section 148. Therefore, the AO must have reason to believe that any income of the taxpayer chargeable to tax has escaped assessment by reason of the failure on the part of the taxpayer to disclose fully and truly all material facts necessary for such assessment. The expressions 'reason to believe' and 'failure on the part of the assessee to disclose fully and truly all material facts' have been subjected to numerous judicial precedents.. There must be a live link between the reasons recorded and formation of the belief that income chargeable to tax has escaped assessment because of failure on the part of the taxpayer to disclose fully and truly all material facts necessary for assessment which must not be fanciful or based on suspicion. Both the conditions must co-exist in order to confer jurisdiction on the AO. The taxpayer is required to make a true and full disclosure of the primary facts at the time of the original assessment.

Production before the AO of books of accounts or other materials from which the required evidence with due diligence could have been discovered by the AO would not necessarily amount to disclosure contemplated by law. However, the duty of the taxpayer in any case does not extend beyond making a true and full disclosure of primary facts. Once he has done that, his duty ends. It is for the AO to draw the correct inference from the primary facts. Once such an inference is drawn which may subsequently appear to be erroneous that cannot be a basis for initiation of action for re-opening assessment as it would amount to change of opinion and change of opinion cannot be a ground for re-opening concluded assessment.

In the initial assessment proceedings, the AO passed the regular assessment order under accepting the claim of the taxpayer that the transfer of shares without consideration should be considered as a gift which was not liable to tax under Section 45. Though the assessment order as such is silent on this aspect, the

preceding communications between taxpayer and the AO would clearly demonstrate that the taxpayer had disclosed all the primary facts regarding transfer of shares without any consideration and as a gift.

The High Court⁴ vide its interim order had correctly taken a stand that the view taken by the AO was nothing but a change of opinion. While initially contention of the taxpayer that such transfer of shares was a gift without consideration was accepted, subsequently the above view was revised to treat the transfer of shares not as a gift and to tax the said transaction on the market value of the shares; this is nothing but change of opinion. Further, the Tribunal in the case of Jayneer Infrapower and Multiventures Private Limited⁵ recorded a categorical finding of fact that such transfer of shares without consideration was a gift which is valid, permissible and genuine. Referring to Section 47(iii) Tribunal held that transfer of shares by way of gift is exempt from the provision of capital gains and concluded that transfer made as a gift without consideration is not taxable under the provisions of capital gains.

Accordingly, the High Court held that the notice and the order passed by the AO rejecting the objections of the taxpayer for re-opening of assessment were set aside and quashed.

Our comments

The issue of taxability of transfer of shares by way of gifts (without consideration) by a company has been a subject matter of debate before the Courts and Tribunal.

The Karnataka High Court in the case of Nadatur Holdings and Investment Pvt Ltd⁶ held that there was no bar for gifting of shares to a company. The definition of gift means transfers by one person to another of an existing property made voluntarily and without consideration and includes deemed transfer or conversion of any property. Similarly, the Chennai Tribunal in the case Redington (India) Limited⁷ it was held that the transfer of shares by a company without consideration is a valid gift since the living person' includes a company, and the Act does not prescribe existence of 'natural love and affection' as a precondition for making a gift. Therefore, such transfer of shares cannot be regarded as transfer of capital asset for the purpose of capital gains taxation and it was eligible for exemption under Section 47(iii).

However, the AAR in the case of Orient Green Power Pte Ltd⁸ has held that inter-corporate gift is 'strange transactions' and that such transactions may not be eligible for exemption under Section 47(iii), as it covers only gifts made by an individual, Hindu Undivided Family, etc.

⁴ Order dated 16 October 2019

⁵ Jayneer Infrapower and Multiventures Private Limited v. DCIT [2019] 176 ITD 15 (Mum)

⁶ CIT v. Nadatur Holdings and Investments (P.) Ltd. [2012] 210 Taxman 597 (Kar)

⁷ Redington (India) Limited v. JCIT (ITA No.513/Mds/2014) (Chen)

⁸ Orient Green Power Pte Ltd. [2012] 346 ITR 557 (AAR)

³ Prakriya Pharmachem v. ITO [2016] 238 Taxmann 185 (Gu)

In the present case, the High Court has held that transfer of shares without consideration was a gift which is valid, permissible and genuine. The transfer of shares by way of gift is exempt from the provision of capital gains and concluded that transfer made as a gift without consideration is not taxable under the provisions of capital gains.

With respect to reassessment proceedings, the Supreme Court in the case of TechSpan India Private Limited & Anr⁹ held that the initiation of reassessment proceedings under Section 147 by the AO is not permitted if it is based on 'change of opinion' and under the same facts and circumstances which were already in his knowledge during the original assessment proceedings. Accordingly, the reassessment proceedings were set aside. Similarly, the High Court in the present case while quashing the reassessment proceedings held that the view taken by the AO was nothing but a change of opinion.



⁹ ITO v. Techspan India Private Ltd. & Anr. (Civil Appeal 2732 of 2007) (SC)

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