

## In the absence of documentary evidence produced by the taxpayer, the tax officer has been directed to inquire into the genuineness and validity of the issue of shares to a sister concern under a family realignment without consideration

### Background

Recently, the Delhi Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Gagan Infraenergy Ltd.<sup>1</sup> (the taxpayer) dealt with an issue of taxability of gift of shares to a sister concern under a family realignment without consideration. The Tribunal observed that no agreement was executed between the group companies forming part of a family realignment and the taxpayer has not provided any documentary evidence to prove the genuineness and validity of transaction. The taxpayer has not shown the manner in which alleged transfer that has been effectuated, was authorised by its Articles of Association (AOA). When such transactions are entered into, involving assets substantially worth, the taxpayer has to establish the genuineness and validity of such transactions.

The Tribunal directed the AO to make proper enquiry on the question of reality, genuineness and validity of alleged transaction. If the taxpayer is able to prove the genuineness and validity of the transaction, no addition shall be called for.

### Facts of the case

- The taxpayer is a part of Jindal group. The taxpayer holds 11.16 million equity shares of Jindal Steel and Power Ltd (JSPL) as on 31 March 2008 valuing INR172.96 million. Subsequently, on 19 September 2009, the taxpayer received five bonus shares for one

share held in JSPL making total investment in equity shares 66.95 million equity shares valuing INR172.96 million. Further during the year, the taxpayer purchased 4,50,000 shares of JSPL making total holding of shares at 67.40 million.

- Pursuant to internal family realignment of Jindal group, the company transferred 17.69 million equity shares of JSPL without any consideration to its sister concern vide board resolution dated 18 March 2014 and passing a special resolution in the extra ordinary General meeting held on 20 March 2014.
- By way of transferring its investment of 17.69 million shares to its sister concern without any consideration, the company not only reduced its investments to nil and booked losses of INR172.96 million which were adjusted out of reserves of the taxpayer but also reduced its income to the extent that would have been accrued, if the company would have sold these shares in the open market at the market price.
- The Assessing Officer (AO) held that the transfer of shares to a sister concern was a transfer within the meaning of Section 2(47) of the Act, and is liable to be taxed under Section 45 of the Act. The AO computed the value of shares transferred to a sister concern by taking market value of each share transferred at INR280.70. Subsequently, the Commissioner of Income-tax Appeals [CIT(A)] upheld the order of the AO.
- Aggrieved, the taxpayer filed an appeal before the Tribunal.

<sup>1</sup> Gagan Infraenergy Ltd v. DCIT (ITA No. 1031/Del/2018) – <http://itatonline.org>

## Tribunal's decision

- Pursuant to internal family realignment of Jindal, it has been observed that huge volume of shares in a public limited company is transferred by the taxpayer without any consideration, without any proper documentation being executed as per law and giving it a nomenclature of 'gift'.
- In the case of DP World<sup>2</sup> there was a gift deed that was executed in respect of assets that was received by the taxpayer therein from its sister concern. However, in the present case, gift deed has not been executed by parties. Similarly, in the case of Redington India Ltd.<sup>3</sup> here was a voluntary transfer of shares without consideration to the stepdown subsidiary. The DRP reconfirmed regarding the transfer of shares as voluntary and without any consideration which is absent in the facts of the present case. In this case the AO himself has disputed the transaction to be a gift, and has instead computed consideration as fair market value of shares as on date of alleged transfer.
- On perusal of the decision of Redington India Ltd it has been observed that the genuineness of the transfer of shares without consideration was not questioned by the lower authorities and therefore the Delhi Tribunal decided that gift for the purposes of Gift Tax Act, 1958 qualifies as a property in money or monies worth to be transferred to a person which includes 'company' as well. It was observed therein that in Gift Tax Act, 1958, there's no attributes like love and affection. However, in the facts of the present case the issue is in respect of genuineness of transaction itself has been challenged by lower authorities in the absence of gift deed. Even that there is no proof of any family settlement being arrived when the transferee is a party.
- The Madras High Court in the case of KAY AAR Enterprises<sup>4</sup> had held that rearrangement of shareholding in the company amongst the family members under the family arrangement is not liable to capital gains tax. However, in the present case neither there is any family arrangement agreement that has been brought to the notice of lower authorities nor has the taxpayer declared what has been received by him in lieu of alleged transfer of shares.
- In the case of R. Jayanti (HUF)<sup>5</sup>, the Supreme Court held that transfer of shares by way of family arrangement would not attract capital gains tax as the arrangement was to avoid possible litigation amongst family members and was made voluntarily and was not induced by fraud or coercion. In the case of K. N. Madhusudan<sup>6</sup>, it was held that word 'transfer' in Section 45 of the Income-tax Act, 1961 (the Act) does not include partition or family settlement as defined in the Act and the facts recorded in the family settlement are akin to a partition and hence the transaction cannot be taxed. The Court observed that family members under the scheme of arrangement have an anterior title to the property which is a subject matter of partition or a family arrangement. However, in the present case the taxpayer has failed to establish its relation with sister concern as well as has admittedly not executed any documents/gift deed/family settlement, in order to establish the genuineness of the transfer. Merely by stating that the transfer was effectuated in lieu of a family realignment is not acceptable without supportive documents in the eyes of law.
- The AAR in the case of Goodyear Tire and Rubber Company<sup>7</sup> held that no consideration would accrue or arise to the applicant by transfer of shares and it cannot be presumed that by transfer of shares taxpayer would have derived any profit or gain. However, in the facts of the present case, the shares held by the taxpayer are by way of investments in a public limited company which has been transferred to a third company without establishing the commercial need to do so. There has been no agreement that has been executed for transfer of shares voluntarily and the taxpayer has failed to establish the genuineness of the transaction.
- Distinguishing the decision of Dana Corporation<sup>8</sup>, the Tribunal observed that there is no such urgency that has been brought to the notice by the taxpayer either of the lower authorities or before the Tribunal in order to accept the transaction to be genuine without there being any consideration.

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<sup>2</sup> DP World v. DCIT [2012] 26 taxmann.com 163 (Mum)

<sup>3</sup> Redington India Ltd v. DCIT [2014] 49 taxmann.com 146 (Chennai)

<sup>4</sup> CIT v. KAY AAR Enterprises [2008] 299 ITR 348 (Mad)

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<sup>5</sup> CIT v. R.Jayanti (HUF) (SLP (C) No. 9079/2008) (SC)

<sup>6</sup> K. N. Madhusudan [GTA No. 2/2008] (Kar)

<sup>7</sup> CIT v. Goodyear Tire and Rubber Company [2011] 334 ITR 69 (AAR)

<sup>8</sup> Dana Corporation [2010] 186 Taxman 187 (AAR)

- The Supreme Court in the case of PNB Finance Ltd<sup>9</sup> observed that PNB Bank was transferred as a going concern, which consists of not only tangible items but also intangible items like goodwill, manpower, tenancy rights and value of banking licence for which cost is not determinable. However, the ratio of the said decision is not applicable to the facts of the present case since in the present case only the shares held by the taxpayer as an investment has been transferred to a sister concern, cost of which is determined as on the date of transfer because the shares that were transferred is a listed company on NSE.
- Under Section 82 of Companies Act 1956, shares in a company are moveable property, transferrable in the manner provided by its Articles of Association (AoA). The taxpayer has not shown/established the manner in which alleged transfer that has been effectuated, was authorised by its Articles. It is difficult to imagine AoA of a company providing for gifting of assets in the company to another company by way of shares in a public limited company, unless it be one which has been set up for some purpose.
- The AO had rightly raised question regarding the reality and genuineness of transaction, in addition to its validity. In fact when such transactions are entered into, involving assets substantially worth, the taxpayer has to establish the factum, genuineness and validity of such transaction, the right to enter into such transaction and bonafides of such transaction, especially when tax department challenges the genuineness of such transaction itself.
- It has been observed that taxpayer has not demonstrated by way of documentary evidence or in any of the manner to prove the genuineness and validity of transaction. The taxpayer failed to establish the relation of the transferee company with that of any of the group/subsidiary companies. Further, there is no agreement/document that has been executed between group companies forming part of family realignment.
- A company can give away its assets free to another even orally, can only be aiding dubious attempts at avoidance of tax payable under the Act unless it is supported by documentary evidence. The Tribunal observed that the AO is in a better position to make proper enquiry into the question of reality, genuineness and validity of alleged transaction, entered into by taxpayer.
- Accordingly, the taxpayer is directed to provide all relevant information to assist the AO for his satisfaction, in determining correct

nature of the transaction. It is also directed that in the event the taxpayer fails to provide any document as called for, in order to establish the genuineness and validity of alleged transaction, the AO may compute the income in the hands of taxpayer as per law. On the contrary if the taxpayer is able to prove to the satisfaction of the AO regarding genuineness and validity of the transaction, no addition shall be called for.

## Our comments

The issue with respect to taxability of gift of shares to a sister concern under a family realignment has been a matter of debate before the Courts.

The Delhi High Court in the case of Ms Mayawati<sup>10</sup> held that a gift is to be treated as genuine when the taxpayer discharges onus cast on it for proving identity, creditworthiness and relationship.

The AAR in the case of Orient Green Power Pte Ltd<sup>11</sup> while declining to give ruling, observed that it was necessary for the applicant to demonstrate the genuineness and the validity of the transaction, of the right to enter into the transaction and the bonafides of the transaction.

The Delhi Tribunal in the present case held that in the absence of any proof of family settlement while gifting of shares to sister concern without consideration, the AO should make proper enquiry on the question of reality, genuineness and validity of alleged transaction. If the taxpayer is able to prove the genuineness and validity of the transaction, no addition shall be called for.

<sup>10</sup> CIT v. Ms Mayawati (ITA No. 438/2008, dated 3 August 2011) (Delhi High Court)

<sup>11</sup> Orient Green Power Pte Limited (AAR No. 973 of 2010) (AAR)

<sup>9</sup> PNB Finance Ltd v. CIT [2008] 307 ITR 75 (SC)

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