IN THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD BENCH 'A', HYDERABAD

BEFORE SMT. P. MADHAVI DEVI, JUDICIAL MEMBER
AND SHRI S. RIFAUR RAHMAN, ACCOUNTANT MEMBER

ITA No. 2045/Hyd/2018
Assessment Year: 2015-16

Apollo Sugar Clinics Ltd., Hyderabad.	vs.	Dy. Commissioner of Income-tax, Circle – 1(1), Hyderabad.
PAN – AAKCA6933D		
Appellant		Respondent

Assessee by: Shri Sriram Seshadri
Revenue by: Shri Y.V.S.T. Sai

Date of hearing: 04/02/2019
Date of pronouncement: 12/04/2019

O R D E R

PER S. RIFAUR RAHMAN, AM:

This appeal filed by the assessee is directed against the order of CIT(A) – 1, Hyderabad, dated, 21/08/2018 for AY 2015-16.

2. Brief facts of the case are, the assessee company, dealing in the business of diabetic clinics filed its return of income on 29/09/2015 for the AY 2015-16 declaring loss at Rs. (-) Rs. 7,49,45,944/- under normal provisions and book profit of Rs. (-)7,49,45,944/- u/s 115JB, which was processed u/s 143(1) of the Income-tax Act, 1961 (in short 'the Act'). Subsequently, the case was selected for scrutiny under CASS and notices u/s 143(2) and 142(1) were issued calling for information. In response to the said notice, the AR of the Assessee furnished the information as called for.

2.1 During the assessment proceedings, the Assessing Officer noticed that the assessee company collected an amount of Rs.70,54,53,000/- towards share premium. The assessee received share capital of Rs. 21.09 crores on 16/12/2014 with face value of Rs. 10/- each and with premium of Rs. 990/-. Similarly, on 29/01/2015 received Rs. 50.07 crores, which are issued to M/s Sanofi Synthelabo (India) Limited and M/s Apollo Health & Life Style Limited. The allotment of shares is as under:

Date of allotment	Name of the allottee	No of shares	Face value in Rs.	Premium in Rs.	Share capital in Rs.	Security in Rs.
29/01/2015	M/s Sanofi Synthelabo (India) Ltd.	406504	10	1220	4065040	495934880
29/01/2015	M/s Apollo Health & Lifestyle Ltd.	596	10	1220	5960	727120
16/12/2014	-do-	210900	10	990	2109000	208791000
29/11/2014	-do-	3000000	10	Nil	3000000	300
	Total	3618000			36180000	705453300

2.2 The Assessing Officer asked the assessee to justify and substantiate with evidences in arriving the share premium of Rs. 990/- and at Rs.1,220/- in the first year of its operations and the allotments made to M/s Sanofi Synthelabo (India) Limited and M/s Apollo Health & Life Style Limited. The assessee was asked to furnish the valuation report as per rule 11UA.

2.3 In response, the assessee company submitted the valuation report carried out by BSR and Associates and they stated that the "valuation carried out by us is solely for regulatory /nonfinancial reporting purposes and it is the prerogative of the parties to the transaction to decide the transaction price". According to assessee, the auditors expressed their opinion that the valuation applies only to comply with RBI regulations and not to the commercial transaction. It is therefore incorrect to read the valuation as applicable to all transactions, the share price evaluated is

wholly indicative and has no bearing whatsoever on the ultimate price at which these were issued. However, it is emphasized that there is no requirement under the income tax law to get the shares valued. Thus, the company is free to determine its own price with the intending purchaser after due negotiations and deliberations.

2.6 Further it was stated that the assessee is a public limited company and its shares are not listed on a recognized stock exchange and the value of its shares can be determined under Rule 11UA for the purposes of section 56(1) of the IT Act by applying fair market value.

2.7 The AO opined that the assessee has stated that the company was free to determine its own price with the intending purchaser after due negotiations and deliberations is not acceptable. The provisions of Rule 11UA for the purposes of section 56 of the IT Act, says that there is a prescribed method for value of shares at a share premium is under Rule 11UA(1)(b) for the purposes of section 56 of the IT Act, which is as follows:

> *"The fair market value of unquoted equity shares shall be the value on the valuation date of such unquoted equity shares as determined in the following manner:*
>
> *The fair market value of unquoted equity shares= (A-L2 x (PV) (PE)"*

2.8 Accordingly, the Assessing Officer concluded that from the Rule 11UA it is clear that the fair market value of the shares has to be determined in the prescribed manner and the assessee is not at liberty to determine its own price with the intending purchaser after due negotiations and deliberations, there should be some basis to evaluate the shares of the company at a premium, it cannot be evaluated by imaginary/surmises. On one side it has evaluated its shares by

following DCF method, while, on the other side it is stating that it need not follow the valuation report.

2.9 According to the AO, the assessee has neither adopted the value of Rs.741/- reported in the valuation report given by the chartered accountant under DCF method as it was evaluated by its own company nor adopted the method prescribed under the IT Act i.e., Rule 11UA. On the other hand, it has taken a stand that the company is free to determine its own price with the intending purchaser after due negotiations and deliberations. It shows that the assessee company has scant respect for the legislation passed by the Government of India. The intention of the legislation for determination of fair market value of the shares is to curb the misdeeds of the company who will involve in dubious methods for valuation of its shares and also to protect the monies of the investors who invest as a share premium.

2.9.1 In view of the above observations, the Assessing Officer concluded that the valuation report submitted by the assessee for determination of share premium is not from facts and it is imaginary with surmises and moreover there is very huge gap between the projections and actuals. Hence, the Assessing Officer did not accept the contention of the assessee that it is free to determine its own price and determined the share premium under Rule 11UA(1)(b) as follows:

The figures adopted as at 31.03.2015 as the figures as on allotment date of shares are not available.

The fair market value of unquoted equity shares = (A-L) X PV/PE

$$\frac{72,42,65,650 \times 10}{366,80,000} = 196.20$$

No of shares is 6,18,000 x 196.20 = 12,12,51,600

Share premium collected = 70,54,53,300

70,54,53,300-12,12,51,600= 58,42,01,700

In view of the above, the Assessing Officer disallowed the excess share premium collected amounting to Rs.58,42,01,700/- u/s 56 of the IT Act and added to the total income.

3. Aggrieved by the order of AO, the assessee preferred an appeal before the CIT(A).

4. Before the CIT(A), the assessee submitted that the name of the company was changed from M/s. Apollo Clinics (Gujarat) Limited to M/s. Apollo Sugar Clinics Limited. It had allotted equity shares to M/s. Apollo Health and Lifestyle Limited (AHLL) and M/s. Sanofi Synthelabo (India) Limited (SSIPL) at a premium and thereby received total amount of Rs.70,54,53,300/- towards share premium. The allotment of shares is as under:

Name of the party	No of shares	Share capital (Rs.)	Premium (Rs.)
SSIPL	4,06,504	40,65,040	49,59,34,880
AHILL	3,11,496	3,21,14,960	20,95,18,120
	Total	3,61,80,000	70,54,53,000

4.1 The assessee submitted that clause (b) item (B) to Section 2(18) is that where the shares of the company, carrying not less than 50% of the voting power have been held by and were throughout the relevant previous year beneficially held by (a) government, or(b) the statutory corporation, or (c) a widely held company or a wholly owned subsidiary of such widely held company. The assessee submitted that Apollo Hospitals Enterprise Limited (AHEL) is a parent company which is a public company listed on the Bombay Stock Exchange (Security Scrip : APOLLOHOSP) and the National

Stock Exchange (Security Scrip: APOLLOHOSP). Since Apollo Hospitals Enterprise Limited (AHEL) is a listed company, the same is a company in which public are substantially interest within the meaning of Section 2(18)(b)(A) of the Act. The assessee submitted that M/s. Apollo Health and Lifestyle Limited (AHLL) is a wholly owned subsidiary of AHEL, wherein 100% of the shares of AHLL were held by AHEL during the FY 2014-15. Since AHLL is a 100% subsidiary of AHEL (a listed company), AHLL is also a company in which public are substantially interested within the meaning of Section 2(18)(b)(B)(c) of the Act. The assessee is a subsidiary of M/s. Apollo Health and Lifestyle Limited (AHLL) wherein 80% of shares of the assessee were held by AHLL during the FY 2014-15. Since AHLL is a 100% subsidiary of AHEL (a listed company), and the assessee is 80% of subsidiary of AHLL, the assessee satisfies the condition laid down in Section 2(18)(b)(B)(c) of the Act. Hence, the assessee submitted that it is a company in which public are substantially interested within the meaning of Section 2(18) of the Act.

4.2 The assessee submitted that Section 56(2)(viib) of the Act are not applicable where premium on issues of shares is received by a company in which public are substantially interested. The assessee submitted that since specific provisions of Section 56(2)(viib) dealing with taxability of share premium are not applicable in the instant case, the general provisions of Section 56(1) of the Act also cannot be invoked. The assessee submitted Section 56(1) covers all those income which are otherwise not taxable under other heads of income. However, for section 56(1) to apply, the amount received by an assessee must be "income" under the Act. The assessee also submitted that Section 2(24) defines the term as "income", which does not include ‘receipts on

issue of shares'. The only exception to this is sub-clause (xvi) to Section 2(24) which covers share premium as in Section 56(2)(viib) of the Act. The assessee submitted that based on the above, the receipt of share premium is not taxable under the Act. Hence, the share premium may not be treated as taxable.

5. After considering the submissions of the assessee, the CIT(A) upheld the addition made by the AO by observing as under:

> *"6.9 The submissions of the appellant have been carefully considered. The issue before me is whether the share premium has been calculated as per the market valuation and based on due diligence report. It is seen the premium has varied from 12990 in different cases. On scrutiny, the Assessing Officer pointed out that from M/s.Sanofi Synthelabo (India) Limited, appellant charged share premium of Rs.1220/- while on majority share purchase in case of M/s. Apollo Health & Life Style Limited is Nil. The Assessing Officer has raised the calculation/valuation of share premium with actuals with regard to profit before taxes and found there is a huge gap between projections and actuals available of the company account. The valuation report submitted by BSR Associates also has lacunae and specifically based on*
>
> > *'…financial information and underlying management assumptions provided by the management for the valuation analysis of the company'.*
> >
> > *" …For the purpose of this engagement and report, we have made no investigation and assume no responsibility for the title to, or liabilities against ASCL. "*
> >
> > *" ….. valuation carried out by us is solely for regulatory /nonfinancial reporting purposes and it is the prerogative of the parties to the transaction to decide the transaction price".*
>
> *The above extracts from the findings of the Assessing Officer and the submissions made by the BSR Associates pin points the finding that*

a) The calculation / valuation is made on basis of management assumption

b) The calculation / valuation is made for statutory provision of RBI and SEBI.

During the appeal proceedings, the appellant was asked to submit the due diligence report on the issue raised by the Assessing Officer regarding the share premium. No such report was submitted before me, hence the finding of the Assessing officer, who is very specific to show that Section 56(2)(viib) is in applicable. On verification, it Is correct that provision of Rule 11UA for the purpose of Section 56 of IT Act, there is prescribed method for valuation of share premium under Rule 11UA(I)(b) for the purpose of Section 56 of Income Tax Act. The Appellant has not accepted the valuation of Rs.741/given by the Chartered Accountant under DCF Method nor under Rule 11UA of IT Act. It is to be noted that the Income Tax Act is very specific regarding the issue. The appellant may have used negotiations and deliberations during the transactions. But for Income Tax procedures the Rule 11UA will apply.

6.10 In the background of this, the appellant has not been able to support its stand. The addition made regarding the excess share premium collected is disallowed u/s.56 of IT Act. 1 have verified the issue and find that the Assessing officer is correct in disallowing Rs.58,42,01,700/- as excess share premium. The addition of Rs.58,42,01,700/- is upheld."

Disallowance of expenditure u/s.14A is Rs.6, 27,749/-

6. Further, during the assessment proceedings, the Assessing officer noticed that the assessee company earned exempt income of Rs.10,99,520/-. He observed that in terms of provisions of section 14A of the Act, any expenditure incurred directly or indirectly for earning income which does not form part of taxable income is not allowable. The assessee company has not disallowed any expenditure that might have or is incurred for earning the exempted income. Therefore, the Assessing Officer asked the assessee to file objections if any, as to why the provisions of Rule 8D could not be applied for

disallowance of expenditure u/s 14A of the Act though there are no borrowings and no direct interest expenditure during the year under consideration. In response, the assessee submitted as under:

> *"It is clarified that a sum of Rs.25 crores was invested in the mutual funds during the year. At the year end, the fair market value of the investment showed the value at Rs.25,10,99,520/-.Thus the investment yield unrecognized income of Rs. 10,99,520/- which was offered for taxation. No expenditure has been incurred to earn this income, hence no amount qualifies for any disallowance under this section. However the same was included under the head income from business and profession instead of being offered for taxation under the head income from other sources."*

The Assessing Officer relying upon the Honourable Bombay High Court's decision in the case of CIT Vs. Godrej Boyce Mfg. Co. Ltd. vis DCIT (2010) reported in 328 ITR 81 disallowed expenditure incurred in relation to earning the exempt income and by applying Rule 8D worked out the total disallowance at Rs. 6,27,749/-.

7. When the assessee preferred an appeal before the CIT(A), the CIT(A) upheld the disallowance made by the AO u/s 14A of the Act.

8. Aggrieved by the order of CIT(A), the assessee is in appeal before us raising the following grounds of appeal:

General grounds:

> *"1. The lower authorities erred, on facts and in law, in enhancing the returned income of the Appellant.*
>
> *2. The lower authorities erred in finalizing an order of assessment which suffers from legal defects, such as*

being passed in violation of principles of natural justice and the provisions of the Act and is devoid of merits and are contrary to facts on "cord and applicable law, and has been completed without adequate inquiries and as such is liable to be quashed.

Addition of receipt in the nature of share premium:

3. The law" authorities have erred in law and on facts, in treating the securities premium received by the Appellant ('share premium'), on allotment of its shares during the subject AY, as income taxable under section 56 of the Act.

4. The lower authorities have erred in law and on facts, in subjecting the alleged excess-receipt of share premium to tax, despite concluding that section 56(2)(viib) of the Act dealing with taxability of excess premium received by specified companies for allotment of shares is not applicable to the impugned transaction.

5. The lower authorities have erred in law and on facts, in holding that the Appellant is not free to determine the issue price of its shares, when the said transaction is outside the purview of any charging provisions under the Act and as such, the action of the lower authorities is beyond jurisdiction.

6. The lower authorities have erred in law and on facts, in holding that the value of 'he Appellant's shares can be determined under rule 11UA for the purpose of section 56(1) of the Act since the same are unquoted shares.

7. The lower authorities have erred in law and on facts, in making an addition towards the alleged excess receipt of share premium, by disregarding the Appellant's commercial contracts, negotiations and valuation reports, and also the applicable exchange control regulations.

8. The lower authorities have erred in law and on facts, in comparing the actual profits earned by the Appellant with the projected profits, based on which the valuation of shares of the Appellant was undertaken.

Disallowance under section 14A of the Act:

9. The lower authorities have erred in law and in facts, in disallowing expenses incurred and allowable by invoking section 14A of the Act.

The grounds of appeal raised by the Appellant herein are without prejudice to each other. The Appellant craves leave to add to and/or to alter, amend, rescind, modify the grounds herein above or produce further documents before or at the time of hearing of this Appeal.

8.1 Ground Nos. 1 & 2 are general in nature.

9. As regards ground Nos. 3 to 8 regarding addition of receipt in the nature of share premium, the ld. AR submitted that the year under consideration is the first year of operation and assessee-company is the second level subsidiary of M/s. Apollo Hospitals Enterprises Ltd., (AHEL). At the time of issue of shares, assessee-company was a 99.99% subsidiary of M/s. Apollo Health and Life Style Ltd., (AHLL) which is subsidiary of AHEL. Since AHEL is a public limited company and by virtue of Section 2(18)(vii) of the Act, the assessee-company also a company in which public are substantially interested. Hence, the provisions of Section 56(2)(viib) will not attract. This fact was also acknowledged by the Assessing Officer in his order. However, the Assessing Officer invoked provisions of Section 56(1) to bring this transaction as income from other sources. He has not considered the fact that this transaction is capital investment and not an income within the meaning of Section 14 of the Act. For this proposition, he relied on the following case law:

1. Vodafone India Services (P) Ltd., [2014] 368 ITR 1 (Bombay)
2. D.P. Sandu Bros. Chembur (P) Ltd., [2005] 273 ITR 1 (SC)
3. CIT Vs. Allahabad Bank Ltd., [1969] 73 ITR 745 (SC)
4. Nalinikant Ambalal Mody Vs. CIT, [1966] 61 ITR 428 (SC).

9.1 With regard to Section 14A disallowance, he submitted that assessee has not claimed any exempt income. Therefore, the provisions of Section 14A will not apply.

10. Ld. DR relied on the orders of Revenue authorities.

11. Considered the rival submissions and material on record. We noticed that assessee-company is step-down subsidiary of Apollo Hospitals Enterprises Ltd., The AHEL is a listed company in Stock Exchange in India with the Securities Contracts (Regulations) Act, 1956. Therefore, this company falls under the category of the company in which public are substantially interested. The subsidiary companies viz. AHLL and assessee-company come under the definition of Section 2(18)(b)(B) of the Act, as per which public are substantially interested. This fact was also acknowledged by the Assessing Officer in his order at Pg. 6, para 3.2 as it was agreed that the assessee's case does not fall u/s. 56(2)(viib). In order to invoke the provisions of Section 56(2)(viib), the assessee-company should be a company in which public are not substantially interested.

11.1 The Assessing Officer instead of invoking Section 56(2)(viib), he went ahead by disallowing the excess of the premium received by assessee by invoking the provisions of Section 56(1) of the Act. In order to invoke Section 56(1), the income earned by the assessee should be classified as revenue income as per Section 14 but should not fall within any of the head of income A,C,D or E. Since section 56(1) is residuary head of income, it falls in the head of income 'F' i.e. "income from other sources". This head of income consists of two parts i.e. section 56(1) and section 56(2). The first part i.e. sub-section (1) deals with income of every kind, which does not fall in any of the head of income A – E and also which is not to be excluded from the total income under this Act. The important thing is, it should fall within the definition of

income u/s 2(24) of the Act. At the same time, sub-section (2) of section 56, deals with specific income which is not income as per section 2(24) but specifically brought under the definition of income by the Legislature. Therefore, the income which cannot be brought to tax under section 56(2), under specific head, AO cannot bring to tax even u/s 56(1). As held in the case of Mercantile Corporation Vs. CIT, 83 ITR 700 (SC), "where there is a specific head for the income in question and specific section providing for the head, this residuary section cannot be called in aid". Similarly, when there is specific provision introduced by the Legislature to bring the specific transaction as income in section 56(2)(viib) because the transaction of issue of shares is capital in nature but under the circumstances as mentioned in above section, this transaction will be considered as income.

11.2 In the given case, the fact is clear that assessee has received share premium and Assessing Officer has mandate to invoke only Section 56(2)(viib) and no other section. This transaction will never fall in any of the heads of income as per Section 14 of the Act. Therefore, in our considered view, Assessing Officer is not correct in bringing this capital investment as income of the assessee after satisfying himself that assessee's case does not fall u/s. 56(2)(viib) of the Act. Therefore, the addition made by Assessing Officer is deleted.

11.3 With regard to 14A disallowance, we notice that assessee made investment in mutual funds and the value as on Balance Sheet date stood at Rs. 25,10,99,520/-. The difference between actual investment and value as on Balance Sheet was declared as dividend income. In our view, this is not actual receipt of dividend during this year, it is only difference in valuation of investment. The position will keep

changing every year. The same will be recognized in the Profit and Loss A/c. The investment value may increase compared to previous year status or decrease depending upon the performance of the fund. The actual increase in value will be determined only when it is transferred or matured.

11.4 In our view, this income recognised by assessee is not real dividend income and the real dividend income alone is exempt from tax net, not the notional recognition of the income at the Balance Sheet date. The value difference at the time of disposal will be chargeable to tax as Long Term Capital Gain not as dividend income. Therefore, in our view, this recognition of difference in value of investment is not the dividend income and hence, Assessing Officer cannot invoke Section 14A in this transaction.

11.5 Accordingly, grounds raised by assessee are allowed.

12. In the result, appeal of the assessee is allowed.

Pronounced in the open court on 12th April, 2019.

Sd/-	Sd/-
(P. MADHAVI DEVI)	(S. RIFAUR RAHMAN)
JUDICIAL MEMBER	ACCOUNTANT MEMBER

Hyderabad, dated 12th April, 2019.

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