

IN THE HIGH COURT OF JUDICATURE AT CALCUTTA

SPECIAL JURISDICTION (INCOME TAX)

ORIGINAL SIDE

RESERVED ON: 28.07.2022

DELIVERED ON: 25.08.2022

CORAM:

THE HON'BLE MR. JUSTICE T.S. SIVAGNANAM

AND

THE HON'BLE MR. JUSTICE BIVAS PATTANAYAK

ITAT/56/2021

(IA NO: GA/02/2021)

PRINCIPAL COMMISSIONER OF INCOME TAX – 5, KOLKATA

VERSUS

M/S. TRIMEX FISCAL SERVICES PRIVATE LIMITED

Appearance:-

Mr. Om Narayan Rai, Adv.

.....For the Appellant.

Mr. Avra Mazumder, Adv.

Sk. Md. Bilwal Hossain, Adv.

Mr. Binayak Gupta, Adv.

.....For the Respondent.

JUDGMENT***(Judgment of the Court was delivered by T.S.SIVAGNANAM, J.)***

1. This appeal filed by the revenue under Section 260A of the Income Tax Act, 1961, (the Act for brevity) is directed against the order dated 20.11.2019 passed by the Income Tax Appellate Tribunal "C" Bench, Kolkata, (Tribunal) in ITA No. 892/Kol/2019 for the assessment year 2013-2014. The revenue has raised the following substantial question of law for consideration:-

- (i) *The Income Tax Appellate Tribunal at the time of dismissing the appeal of the Revenue, failed to consider the fact that the assessment order is erroneous is so far as it is prejudicial to the interest of revenue. Since as per section 56(viib) of the Act, the value of the shares has to be calculated based on the formula stipulated under Rule 11U and 11UA of the Income Tax Rule 1962 which has not been carried out by the Assessing Officer while passing order u/s 143(3). The Assessing Officer simply accepted the valuation furnished by the Assessee and thereby made the Assessment order erroneous. Upon applying the formula under Rule 11U and 11UA of the Rules, the valuation of the shares come to only Rs. 23/- approx. Therefore, if the section 56(2)(viib) is applied and amount of Rs. 127/- (Rs. 150-Rs.23) per share escaped assessment thereby in respect of 8,00,000 shares amount to Rs. 10,16,00,000/- is aggregate escaped assessment.*
- (ii) *According to the Income Tax Appellate Tribunal, the Assessee had furnished the details to Assessing Officer in order to substantiate the fair market value of shares by filing several documents. However, the Appellate Tribunal failed to consider that the Assessing Officer did not consider the fair market value of the shares by applying rule 11U & 11UA and passed the order of Assessment and thereby caused was loss of Revenue to the tune of Rs. 123/- per share amounting to Rs. 10,16,00,000/- which make the Assessment order erroneous and prejudicial to the interest of revenue. As such the Income*

Tax Appellate Tribunal erred in allowing the appeal of the Assessee.

- (iii) *The Income Tax Appellate Tribunal failed to appreciate the fact that the assessment was erroneous and prejudicial to the interest of revenue as the Assessing Officer did not determine the fair market value of the share by applying Rule 11A and 11U and curative action of Principal Commissioner of Income Tax-2 in its revisional jurisdiction u/s. 263 of the Act is well within the four corner of the law and provision of the Act.*

2. The assessee, a private limited company filed its return of income for the assessment year under consideration, A.Y. 2013-2014, declaring a total income of Rs. 56,76,233/-. The case was selected for scrutiny and the assessment under Section 143(3) of the Act was completed on 28.03.2016 determining the total income of Rs. 63,93,230/-. The assessment records were called for and on the basis of the verification, the Commissioner of Income Tax was of the opinion that the order of assessment is erroneous in so far as it is prejudicial to the interest of revenue. Show cause notice dated 23.02.2018 was issued stating that on perusal the assessment records reveals that the assessee issued 8,00,000 shares during the previous year corresponding to the assessment year 2013-2014 with a share premium of Rs. 140/- and face value of Rs. 10/- totaling to Rs. 150/- per unit of share. It is stated that as per the provisions of the Act, face value of the shares issued by a private limited company should not exceed the fair market value of shares issued during the year. By applying the Rule 11U and Rule 11 UA of the Income Tax Rules, 1962, (Rules), it was proposed that the fair market value of the share issued by the assessee can be recalculated at Rs. 23/- (approximately) per share. Thus, it was proposed that the value of the

shares issued by the assessee at Rs. 150/- per share exceeds the fair market value of shares determined as per Section 56(2)(viib) read with Rule 11U and Rule 11UA by Rs. 127/-. Therefore, the assessee was directed to show cause why the share value being in excess of the fair market value of share premium along with the share capital received by the assessee i.e. Rs. 127/- on 8,00,000 shares amounting to Rs. 10,16,00,000/- should not be added back to the total income of the assessee company. This notice was issued under Section 263 of the Act. The assessee submitted their reply contending that the value of Rs. 150/- per share is the fair value of shares of the company which has been worked out by obtaining certificate from Chartered Accountant. The assessee referred to the Explanation 1 to Clause 7(b) of Section 56 of the Act and submitted that the fair market value of the shares has been arrived at by substituting the cost price of the assets of the company with the fair market value of those assets. The basis of the valuation was explained by the assessee by stating that the assessee holds 12,90,000 equity shares of *M/s. Shiv Edibles* which is equal to 36.35% equity capital of the said company and similarly the company holds 3,50,000 equity shares of *M/s. Shiv Agrevo Limited* which is equal to 19.96 % equity shares of that company. It was stated that both the companies are the group companies/associates in which the assessee holds significant control and while arriving at the fair market value of the shares, the cost of these investments has been substituted that fair value of the same and accordingly, the fair value of the shares has been arrived at Rs. 150/- per share. Further the assessee stated that during the course of the scrutiny assessment under Section 143(3) of the Act, certificate was furnished before

the assessing officer justifying the valuation of shares. Therefore, it was contended that revising the assessment order under Section 263 of the Act does not arise.

3. The Commissioner held that the assessing officer has not examined the applicability of Section 56(2)(viib) read with Rule 11(U) and Rule 11UA. After referring to the said provision, the Commissioner held that with respect to fair market value of unquoted equity shares, the valuation provided under Rule 11UA (c)(b) has to be adopted and the valuation to be accordingly worked out. The Commissioner also opined that the assessing officer has not verified the computation of fair market value of the shares since relevant and tangible material was not placed before the assessing officer by the assessee during the course of assessment proceedings under Section 143(3) of the Act. It was held that in the absence of relevant and vital information regarding computation of the fair market value of the shares, the assessing officer could not have made proper verification which ought to have been made for coming to the conclusion that the computation under Rule 11UA of the rules is correct and therefore, held the assessment order to be erroneous in so far as it is prejudicial to the interest of revenue. Further the Commissioner held that enquiry conducted by the assessing officer was clearly vitiated due to absence of crucial and vital information on record and the assessing officer could not have formed an opinion to come to the conclusion that the computation is correct. After taking note of the decision of the Hon'ble Supreme Court with regard to the power of the Commissioner under Section 263, the Commissioner held that the assessment order is erroneous and prejudicial to the interest of revenue in accordance with

Explanation 2 below Section 263(1) of the Act and accordingly set aside the computation of fair market value of share and remanded the matter back to the file of the assessing officer. The assessee was directed to produce the valuation before the assessing officer as per Rule 11UA and the assessing officer to examine and verify the computation determining the fair market value of the equity shares at Rs. 150/- per share. Thus, the assessing officer was directed to initiate fresh assessment proceedings and carry out necessary verification and take action accordingly after verification of the correctness of the claim of the assessee.

4. The assessee filed an appeal before the tribunal contending that the assessing officer had conducted detailed enquiry, several questions were asked to the assessee during the assessment proceedings and in this regard, filed a paper book containing all the documents which were placed before the assessing officer. The copy of the paper book has also been placed before us which includes the copy of the Chartered Accountant Certificate, the calculation of fair value, the relevant forms issued by the Registrar of Companies, the copies of the audited balance sheet for the year ended 31.03.2013 and the copies of the order sheet entries to show that detailed enquiry was conducted by the assessing officer. It was further contended that a specific query was raised by the assessing officer as regards the applicability of Section 56(2)(viib) of the Act for which the assessee has submitted reply stating that shares have been issued by the company at fair value and to substantiate the same, the valuation certificate obtained from the chartered accountant was enclosed. The assessee also referred to the manner in which the fair market value was calculated. Hence, it was

contended that the Commissioner was wrong in concluding that the assessing officer did not make any enquiries and such conclusion was unsustainable in law. Further it was contended that two methods are envisaged for calculating the fair value of the shares and as per Rule 11U and Rule 11UA once such exercise is done, out of the two values thus computed, the value whichever is higher should be adopted. It was contended that during the course of enquiry, the assessing officer was convinced with the valuation as arrived at by the assessee was correct. The tribunal was of the view that the Commissioner to hold the view of the assessing officer to be erroneous as well as prejudicial to revenue, he has to conduct enquiry and record a finding that the assessee's calculation of fair market value of Rs. 150/- per share is unsustainable in law and the Commissioner having not done so, the order of assessment cannot be held to be prejudicial to the interest of revenue and accordingly the appeal filed by the assessee was allowed.

5. Mr. Om Narayan Rai, learned standing counsel for the appellant submitted that there are two modes to arrive at fair market value and one is in accordance with the Income Tax Rules and the other may be substantiated by the assessee to the satisfaction of the assessing officer. It is submitted that in the assessee's case records reveal that information was sought for from the assessee and a questionnaire was issued, the assessee submitted their reply and documents. However, there is nothing on record to show that the assessing officer was satisfied with the same and no reasons have been recorded by the assessing officer. Further it is submitted in a note appended to the assessment order, the assessing officer appears to have

applied his mind as regards high share premium with a view to assess whether the same were accommodation entries or not and it was not done to reach the satisfaction required by explanation to Section 56B (2)(viib). Further it is submitted that whether the shares issued were as accommodation entries or not was not the issue involved in the assessment and therefore, it is clear that the assessing officer failed to apply his mind. Further, since the assessing officer did not conduct proper enquiry either to reach the satisfaction or to determine the fair market value in terms of the rules, the Commissioner was right in holding that proper enquiry was not held and therefore the assessment was erroneous and prejudicial to the interest of revenue. Further it is submitted that the satisfaction which is required was not reached by the assessing officer which he was duty bound in terms of the rules. In support of his contention, reliance was placed on the decision in the case of ***Principal Commissioner of Income Tax – II Versus Shri Brahma Deb Gupta*** ¹, ***Toyota Motor Corporation Versus Commissioner of Income Tax*** ² and ***Nagal Garment Industries Private Limited Versus Commissioner of Income Tax-I and Another*** ³.

6. Mr. Avra Majumdar, learned advocate appearing for the respondent assessee submitted that there is no provision in the Act which requires the assessing officer to record reasons while accepting the claims of the assessee and reasons are required only when an issue is decided against the assessee. To support such contention reliance was placed on the decision in

¹ 2018 SCC Online (Del) 9946

² (2008) 17 SCC 535

³ 2018 (2) MPLJ 494 (MP)

the case of ***Commissioner of Income Tax Versus Gabriel India Limited***⁴, ***Commissioner of Income Tax Central – 1 Kolkata Versus J.L. Morrison (India) Ltd.***⁵ and ***Commissioner of Income Tax, Mumbai Versus Chandan Magaraj***⁶. Further it is contended that neither before the tribunal nor before this Court, the revenue has suggested any question that the assessment order was bad because it did not disclose reasons. Further it is submitted that a conjoint reading of the assessment order along with the documents filed in the paper book will clearly show that the assessing officer has conducted enquiry as the circumstances warranted and permitted before accepting the claim of the assessee and passing the assessment order. Further it is contended that there are two methods envisaged in the rules for calculating fair value of shares and the assessee adopted one such method which was accepted by the assessing officer after enquiry and therefore the assessment order cannot be considered as erroneous or prejudicial to the interest of the revenue. To support such contention, reliance was placed in ***Principal Commissioner of Income Tax, Surat – 2 Versus Shreeji Prints (P.) Ltd.***⁷ and ***Principal Commissioner of Income Tax, Mumbai Versus Sumatichand Tolamal Gouti***⁸. Further it is contended that the Income Tax department cannot sit in the arm chair of a businessman to decide what is profitable and how the business should be carried out. The commercial expediency has to be seen from the view point of the businessmen. Even under Rule 11 UA(2), though power has been

⁴ (1993) 203 ITR 108 (Bom)

⁵ (2014) 366 ITR 593 (Cal)

⁶ (2022) 135 taxmann.com 55 (Bom)

⁷ (2021) 130 taxmann.com 294 (SC)

⁸ (2019) 111 taxmann.com 287 (SC)

given to the assessing officer to substitute his own value in the place of the value determined, it would require recording of by the assessing officer to tinker with such valuation adopted by the assessee. Further the valuation being a question of fact depends upon appreciation of materials or evidence and the methodology adopted was accepted by assessing officer and the tribunal based on materials and facts available on record, therefore the tests laid down by the courts for interfering with the findings of a valuer are not satisfied in the case on hand as the assessee adopted a recognized method for valuation and the revenue is unable to show that the assessee adopted a demonstratively wrong approach or that the method of valuation was made on a wholly erroneous basis or that it committed mistake which goes to the root of the valuation process. In support of such contention, reliance was placed on the decision in the case of ***Principal Commissioner of Income Tax – 2 Versus M/s. Cinestaan Entertainment Private Limited***⁹.

7. We have heard Mr. Om Narayan Rai, learned Advocate for the appellant and Mr. Avra Majumder, learned Advocate assisted by Sk. Md. Bilwal Hossain and Mr. Binayak Gupta, advocates for the respondent.
8. To answer the substantial question of law suggested by the revenue, we have to first take note of the statutory provisions. Section 56 deals with income from other sources. Sub-Section 1 of Section 56 states that income of every kind which is not to be excluded from total income under the Act shall be chargeable to income tax under the head “income from other sources” if it is not chargeable to income tax, under any of the heads specified in items A to E. Sub-Section 2 states that in particular and without

⁹ 2021 (3) TMI 239 (Del.)

prejudice to the generality of the provisions of Sub-Section 1, the income mentioned in clauses (i) to (ix) shall be chargeable to income tax under head “income from other sources”. Sub-Section 2 of Section 56 would be relevant for our case. Clause (viib) of Section 56(2) together with explanation are quoted hereunder:

Income of every kind which is not to be excluded from the total income under this Act shall be chargeable to income tax under the head “Income from other sources”, if it is not chargeable to income-tax under any of the heads specified in section 14, items A to E.

In particular, and without prejudice to the generality of the provisions of sub-section (1), the following incomes shall be chargeable to income-tax under the head “Income from other sources”, namely:-

(i).....

(viib) 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 for such shares as exceeds the fair market value of the shares:

Provided that this clause shall not apply where the consideration for issue of shares is received—

(i) by a venture capital undertaking from a venture capital company or a¹⁰ [venture capital fund or a specified fund]; or

(ii) by a company from a class or classes of persons as may be notified by the Central Government in this behalf.

¹¹ *[Provided further that where the provisions of this clause have not been applied to a company on account of fulfilment of conditions specified in the notification issued under clause (ii) of the first proviso and such company fails to comply with any of those conditions, then,*

¹⁰ Subs. By the Finance (No. 2) Act, 2019, sec 21(i) (a), for “venture capital fund” (w.e.f. 1-4-2020)

¹¹ Ins. By the Finance (No. 2) Act, 2019, sec 21(i) (b), (w.e.f. 1-4-2020)

any consideration received for issue of share that exceeds the fair market value of such share shall be deemed to be the income of that company chargeable to income-tax for the previous year in which such failure has taken place and, it shall also be deemed that the company has under-reported the ¹²[said income] in consequence of the misreporting referred to in sub-section (8) and sub-section (9) of section 270A for the said previous year.]

Explanation.—For the purposes 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; or

(ii) as may be substantiated by the company to the satisfaction of the Assessing Officer, based on the value, on the date of issue of shares, of its assets, including intangible assets being goodwill, know-how, patents, copyrights, trademarks, licenses, franchises or any other business or commercial rights of similar nature,

whichever is higher;

9. Determination of fair market value of the property other than immovable property is contained in Chapter H occurring in Part II of the Income Tax Rules. Rule 11U deals with the meaning of the expressions used in determination of fair market value for the purposes of Rule 11U and Rule 11UA. Clause (a) of Rule 11U defines “accountant” (i) for the purposes of Sub-rule (2) of Rule 11UA to mean a Indian Institute of Chartered Accountants of India within the meaning of the Chartered Accountants Act, 1949 which is not appointed by the company as an auditor under Section 44 AB of the Act or under Section 224 of the Companies Act, 1956. Clause (i) of Rule 11U defines unquoted shares and securities to mean in relation to shares and securities which are not quoted shares or securities. Rule 11UA

¹² Corrected by Corrigendum Notification, for “income”, published in the Gazette of India, Extra., Pt II, Sec. 1, No. 47, dated 8th August, 2019

deals with determination of fair market value. In terms of Sub-Rule (1) of Rule 11UA, for the purposes of Section 56 of the Act a fair market value of the property, other than immovable property, shall be determined in the manner stipulated therein. Clause (c) in Rule 11UA (1) would be relevant for our case which is quoted hereunder:

“R. 11UA. Determination of fair market value.- [(1)] For the purposes of section 56 of the Act, the fair market value of a property, other than immovable property, shall be determined in the following manner, namely,—

(a).....

(b).....

(c) valuation of shares and securities,—

(a) the fair market value of quoted shares and securities shall be determined in the following manner, namely,—

(i) if the quoted shares and securities are received by way of transaction carried out through any recognized stock exchange, the fair market value of such shares and securities shall be the transaction value as recorded in such stock exchange;

(ii) if such quoted shares and securities are received by way of transaction carried out other than through any recognized stock exchange, the fair market value of such shares and securities shall be,—

(a) the lowest price of such shares and securities quoted on any recognized stock exchange on the valuation date, and

(b) the lowest price of such shares and securities on any recognized stock exchange on a date immediately preceding the valuation date when such shares and securities were traded on such stock exchange, in cases where on the valuation date there is no trading in such shares and securities on any recognized stock exchange”

10. The assessment was completed by order dated 28.03.2016 under Section 143(3) of the Act. On reading of the assessment order we find that the Assessing Officer has discussed three issues namely, issue arising under Section 40(A)(IA) of the Act, 'Employees' benefit expenses and expenses incurred in relation to income not includable in total income. After discussing the case on the above three heads, the assessment was completed and the total income was arrived at Rs. 63,93,230/-. The Assessing Officer has signed the assessment order and affixed his seal. Below the seal and signature there was a note titled "*note not for the assessee*". It is not clear as to whether the said note has to be read as part and parcel of the assessment order as it has been mentioned that it is a note not for the assessee. Then the question would be as to for what purpose the note was appended by the Assessing Officer after completing the assessment and affixing his signature and seal. Be that as it may in the note the Assessing Officer states that during the year the assessee issued 8,00,000 equity shares of Rs. 10/- with a premium of Rs. 140/- per share amounting to Rs. 12,00,00,000/- to five companies. The Assessing Officer further states that the assessee company produced minutes book about fixation of share premium to justify the premium fixed and also produced minutes books and other books of accounts of investor companies along with their directors. After mentioning so, the Assessing Officer states that considering the facts, question of artificially rising of capital by circular transaction does not arise in the case and hence, question of any credit from so-called paper, shell companies does arise. After making such an observation, the characteristics

of the investor companies were given in a tabulated form. The assessment records were perused by the Commissioner who exercised his power under Section 263 of the Act. The reason being that the fair market value of the shares have not been arrived at in terms of Rule 11U and Rule 11UA of the Act, in the opinion of the Commissioner, the fair market value of the assessee is approximately Rs. 23/- and accordingly, it was held that excess of fair market value of the share premium along with the share capital is Rs. 127/- for 8,00,000 shares amounting to Rs. 10,16,00,000/- which was to be added back to the total income of the assessee company. In the opinion of the Commissioner, no documents or records were verified by the Assessing Officer who did not apply his mind, failed to make an enquiry and, therefore, he was justified in invoking his power under Section 263 of the Act. The Commissioner further held that incorrect assumption of facts or application of law satisfied the requirement that the assessment order is erroneous and prejudicial to the interest of revenue. The assessee being aggrieved had preferred appeal before the Tribunal.

11. The Tribunal was of the view that the Commissioner committed an error in assuming jurisdiction under Section 263 of the Act as the records show that the Assessing Officer has raised several queries and in particular with regard to the applicability of Section 56 (2) (viib) of the Act and after discussion of the case has accepted the value as computed by the assessee to be the fair value of the shares and when two views are possible, substituting one of the views to that of the views recorded by the Assessing Officer is not a ground to invoke the power under Section 263 of the Act. The Tribunal also referred to the certificate issued by the chartered

accountant who has worked out the fair market value of the shares. The method of valuation was also examined and the Tribunal held that during the assessment proceedings, the Assessing Officer enquired about the fair market value of shares issued by the assessee at Rs. 150/- per share and same has been substantiated by documents. With the above reasoning, the appeal filed by the assessee was allowed.

12. In terms of Clause (viib) of Section 56(2) where a company not being a company in which public are substantially interested, receives, in any previous year from any person being a resident, any consideration for issuance of shares that exceeds the face value of such shares, the aggregate consideration received for such shares as exceeds fair market value of shares shall be deemed to be the income of that company chargeable to income tax for the previous year in which such failure has taken place and it shall also be deemed that the company has under reported the said income in the consequence of misreporting, referred to in Sub-Section (8) and Sub-Section (9) of Section 270A for the said previous year. Explanation under Clause 7B states that for the purpose of the said clause, 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 or (ii) as may be substantiated by the company to the satisfaction of the Assessing Officer, based on the value, on the date of the issuance of shares, of its assets, including tangible assets, being goodwill, knowhow, patent, copy right, trade market, license, franchise or any other business or commercial rights of similar nature whichever is higher. Thus, the key word occurring in Explanation A (a)(ii) is the “satisfaction” of the Assessing Officer. The

satisfaction of the Assessing Officer becomes paramount because for the purposes of arriving at the fair market value of the shares one of the two options provided in sub-Clauses (i) and (ii) have to be taken into account and whichever is higher has to be adopted. In the instant case, the assessee is stated to have substantiated the value based upon the Chartered Accountant Certificate and other documents which according to the assessee was placed before the Assessing Officer and also before the Tribunal. As noted, the crucial word occurring in the said provision is the satisfaction of the Assessing Officer.

13. Rule 11UA deals with determination of fair market value, under Clause (c) of Sub-Rule (1) of Rule 11UA valuation of shares and securities have been set out. This procedure or methodology has to be followed for the purposes of valuation of shares. The assessee's consistent case is that they have followed the methodology, placed materials and documents before the Assessing Officer who conducted an enquiry and accepted the valuation as done by the assessee. The question should be as to whether such explanation was found acceptable by the Assessing Officer and was he satisfied with the explanation. Under normal circumstances, if an authority issues a show-cause notice and the noticee is called upon to answer an allegation and if he does so by way of a reply, the authority while adjudicating the show-cause notice has to record reasons as to why in his opinion the reply given by the noticee is acceptable or not acceptable. The argument of the learned Advocate for the assessee is that no reasons need to be recorded when the claim made by the assessee is accepted.

14. In this regard, the decision in **Gabriel India Ltd., J.L. Morrison (India) Ltd.** and **Chandan Magraj Parmar** had been referred to. Firstly, we need to point out that in none of the decisions, the question relating to the procedure to be adopted in Section 56 (2)(viib) read with Rule 11U and Rule 11UA was subject matter of consideration. The underlying legal principle in all the decisions is that no elaborate discussion and reasoning need to be recorded by the Assessing Officer as required by a Court or a Tribunal. In fact, in **Gabriel India Ltd.**, the Court came to the conclusion that assumption of the jurisdiction by the Commissioner under Section 263 of the Act merely because the Assessing Officer could have written a more elaborate order could not have been the reason to exercise such power. In **J.L. Morrison (India) Ltd.** this Court noted a decision of the Tribunal wherein it was observed that the Assessing Officer is expected to record his own reasons for the conclusion reached therein and unless such reasons are recorded, the purpose of providing revisional/ appellate jurisdiction in the Income Tax Act would be defeated. Reliance was placed on the decision in **CIT Versus M/s. Infosys Technologies Ltd.**¹³ wherein an argument was advanced as done before us that there is no need for the Assessing Officer to spell out reasons while accepting the claim of the assessee. Such argument was rejected by holding that it would give a free hand to the Assessing Officer just to pass an order without reasoning and to spell out reasons only in a situation where finding needs to be against the assessee or any claim to be verified by the assessee is denied. Reference was also made to the decision of the Hon'ble Supreme Court in **S.N. Mukherjee Versus Union of**

¹³ (2012) 341 ITR 293 (Karnataka)

India ¹⁴ wherein it was held that except in cases where the requirement has been dispensed with expressly or by necessary implication an administrative authority exercising judicial or quasi-judicial function is required to record the reasons for its position. The Court also noted the decision in **S.S. Gadgil Versus Lal and Co.**¹⁵ wherein it was held the Income Tax authorities who have power and assess and recovery tax are not acting as judges deciding a litigation between a citizen and the State, they are administrative authorities whose proceedings are regulated by statutes, whose function is to estimate the income of the tax payers and to assess the tax on the basis of that estimate. Ultimately, the Court in **JL Morrison (India) Ltd.** held that the view taken by the Tribunal was not perverse and accordingly, the appeal filed by the revenue was dismissed.

15. We have referred to the decisions which were noted by the Hon'ble Division Bench in **J.L. Morrison (India) Ltd.** to examine as to what is the statutory duty cast upon the Assessing Officer who dealt with the assessment of the respondent assessee. The decision in **Chandan Magraj Parmar** cannot be applied to the facts and circumstances of this case as the question of law involved in the said case pertains to valuation of a property. The decision in the case of **Shreeji Prints (p) Ltd.** also is distinguishable on facts as ultimately, the Court held that the revisional power exercised by the Principle Commissioner of Income Tax in the facts of the case cannot be said to be erroneous. The decision in **Sumatichand Tolamal Gouti** was a case where the revenue's appeal was dismissed by the Hon'ble Supreme Court

¹⁴ AIR 1990 SC 1984

¹⁵ (1964) 53 ITR 231 (SC)

affirming the view taken by the Tribunal that the Assessing Officer conducted detailed enquiry with regard to the explanation furnished by the assessee. This decision cannot help the assessee. Much emphasis was placed by the learned Advocate for the assessee on the decision in the case of **Cinestaan Entertainment Pvt. Ltd.** contending that it is also a similar case of addition under Section 56 (2)(viib) of the Act. Though the said decision arose under Section 56 (2)(viib) of the Act, the question of law which was framed for consideration was whether the Tribunal erred in deleting the addition made under Section 56 (2)(viib) of the Act, by ignoring the sound reasoning and detailed analysis of the Assessing Officer, the Cash Flow projections were taken into account in the Discounted Cash Flow Method etc.

16. Thus, we are required to see as to whether the Assessing Officer had complied with the statutory requirement and if he had done so whether the Commissioner was right in invoking his power under Section 263 of the Act. As noted above, there are two methods to arrive at a fair market value of the shares. One being determined in accordance with such method as may be prescribed and the other as may be substantiated by the assessee to the satisfaction of the Assessing Officer and the higher of those figures has to be adopted. As rightly pointed out by the learned Standing Counsel for the revenue in none of the cases referred to by the learned Advocate for the assessee such an issue arose for consideration. In fact, in **Gabriel India Ltd.** the Hon'ble Division Bench of this Court refers to the decision cited by the revenue in the case of **S.S. Gadgil** wherein the Hon'ble Supreme Court has pointed out that the Income Tax Authorities are administrative

authorities whose proceedings are regulated by statutes. If such is the position, the Assessing Officer is bound by the statutory mandate. The Assessing Officer cannot be heard to say that by inference it has to be taken that he has applied his mind to the valuation submitted by the assessee. He has to record his satisfaction or in other words he has to spell out as to how he was satisfied with the valuation as adopted by the assessee. If the statute has not used the words “to the satisfaction of the Assessing Officer” things could have been otherwise. Satisfaction of an administrative or a quasi-judicial authority should be manifest and vivid on the face of the order or proceedings. There can be no inference as regards satisfaction, nor can the provision of law be read to connote deemed satisfaction. If such interpretation is to be accepted then it would tantamount to rewriting Section 56 (2)(viib) Explanation (e). There is a slight distinction to the words “recording reasons” and “recording satisfaction”. In **Shri Braham Dev Gupta** it was pointed out that the Assessing Officer should at least as regards what appears from the record and what are issues enquired into during scrutiny assessment, indicate briefest of reasons accepting or rejecting any argument. This interpretation was given bearing in mind, the scope of Section 143(3) of the Act which mandates the Assessing Officer to take into account all relevant materials which he has gathered and by an order in writing make an assessment of the total income of the assessee. Before passing such an order under Section 143(3) the assessee is required to be heard and is entitled to produce evidence. In the background of the said statutory provision, the Hon’ble Court opined that in a scrutiny assessment an Assessing Officer is bound to indicate reasons or at least

briefest of reasons. In ***Toyota Motor Corporation*** it was held that the decision of the Assessing Officer must be supported with reasons which was also a case arising under Section 263 of the Act though not under Section 56 (2)(viib) of the Act. In ***Malabar Industries Co. Ltd. Versus CIT***¹⁶, the Hon'ble Supreme Court upheld the exercise of jurisdiction by the Commissioner of Income Tax under Section 263 when the Income Tax Officer committed an error on assessment without application of mind and blindly accepting the entry in the statement of accounts filed by the assessee without making any enquiry. Similar view was taken in the case of ***Commissioner of Income Tax, Mumbai Versus Amitabh Bachchan***¹⁷.

17. After having noted the legal position from the above decisions if we revert back to the facts of the case, it may be true that the Assessing Officer issued a questionnaire to the assessee, containing a question with regard to the applicability of Section 56 (2)(viib) of the Act. The assessee submitted an explanation stating that the shares have been issued by the assessee at fair value based on the valuation certificate obtained by the chartered accountant. The assessee also enclosed the methodology of calculation as adopted and certified by the chartered accountant. Thus, the question would be whether the Assessing Officer has nothing else to do in the matter. The said question has to be answered in the negative to hold that it is at that point of time, the duty of the Assessing Officer commences to conduct enquiry as he is required to be satisfied that the market value of the share stated to be a fair market value by the assessee is correct, has the

¹⁶ (2000) 243 ITR 83 (SC)

¹⁷ AIR 2016 SC 2257

computation been done in terms of Rule 11UA of the Rules and it is thereafter, he has to accept the value whichever is higher. Thus, merely by conducting enquiry, calling for documents and materials discussing the case with the assessee are not sufficient to comply with the mandate in Section 56 (2)(viib). As mentioned earlier, satisfaction cannot be inferred and the statute does not provide for any deemed satisfaction. On a reading of the assessment order dated 28.03.2016 it is evidently clear that no satisfaction was recorded by the Assessing Officer, in fact, three issues which were discussed by the Assessing Officer are under Section 40AI; Employees benefit expenses and expenditure incurred in relation to income not includable in total income. Curiously enough after the Assessing Officer has affixed his signature and seal, a note has been mentioned in the assessment order and the note is not for the assessee. If that is not for the assessee for what purpose the note was appended is not clear. If the note is not for the assessee and it is for the departmental purposes or otherwise, the assessee cannot hinge upon the said note to justify their stand that due enquiry was conducted by the Assessing Officer qua Section 56 (2)(viib). Even assuming the note can be referred to by the assessee, the said note does not record any satisfaction as required under Section 56 (2)(viib). What weighed in the mind of the Assessing Officer appears to be as to whether the case of the assessee was a case of artificially rising of the capital by circular transactional. There was no such allegation when the Assessing Officer issued the questionnaire. If such is the case, we find that the note is of no consequence with regard to the fact in issue and therefore, the note requires to be ignored. The note also cannot be construed to be a rectification of the

assessment order as the Assessing Officer does not state that he has invoked his power under Section 154 of the Act. Therefore, we are of the view that the learned Tribunal committed a serious error in reversing the order passed by the Principle Commissioner of Income Tax, II Kolkata in exercise of his powers under Section 263 of the Act. It was submitted on behalf of the respondent assessee that the Income Tax Department cannot sit in the arm chair of a businessman and commercial expediency has to be seen from the view point of the businessman. Such issue does not arise for consideration in this appeal nor it was the case of the assessee before the Commissioner that the Commissioner is purporting to take business decisions on behalf of the assessee.

18. It is no longer *res integra* that reasons provide a live link between conclusion and evidence. This vital link is the safeguard against arbitrariness and prejudice to the interests, is a manifestation of the mind of a quasi-judicial authorities, Tribunal or a Court and it is a tool for judging validity of an order and, therefore giving reasons is an essential element of administration of justice. Thus, in the absence of any reasons given by the Assessing Officer by recording satisfaction as mandated under Section 56 (2)(viib) of the Act, the order passed by the Tribunal calls for interference.

19. Accordingly, the appeal filed by the revenue is allowed and the order passed by the Tribunal dated 20.04.2019 is set aside and the order passed by the Principal Commissioner of Income Tax-II Kolkata dated 19.03.2020 is restored and the Assessing Officer is directed to comply with the directions contained in paragraph 6 of the said order by passing a reasoned and speaking order after offering an opportunity of hearing to the assessee or

their authorized representative either through virtual hearing or physical hearing as expeditiously as possible but not later than sixty days from the date of receipt of the server copy of this judgment. No costs.

(T.S. SIVAGNANAM, J.)

I agree.

(BIVAS PATTANAYAK, J.)



(P.A.-PRAMITA/SACHIN)