



**IN THE INCOME TAX APPELLATE TRIBUNAL,
CUTTACK 'SMC' BENCH, CUTTACK**

BEFORE SHRI CHANDRA MOHAN GARG, JUDICIAL MEMBER

ITA No. 114/CTK/2019

Assessment Year : 2015-16

Alishan Palace Resorts Pvt Ltd., 410, Forum Mart, 89, Kharvel Nagar, Bhubaneswar.	Vs.	ITO, Ward 1(3), Bhubaneswar.
PAN/GIR No.AAFCA 1639 P		
(Appellant)	..	(Respondent)

Assessee by : Shri P.R.Mohanty , AR
Revenue by : Shri Ashutosh Pradhan, DR

Date of Hearing : 16 /06/ 2020
Date of Pronouncement : 16/06/2020

ORDER

This is an appeal filed by the assessee against the order of the CIT(A),1, Bhubaneswar dated 26.2.2019 for the assessment year 2015-16.

2. The only effective ground raised by the assessee is that the Id CIT(A) was not justified in confirming the addition of Rs.14,43,200/- u/s. 56(2)(viib) of the Act, which is against the principle of natural justice.

3. Facts of the case are that the assessee during the course of assessment proceedings, the Assessing Officer noticed from the balance sheet that the assessee has issued 80,000 numbers of shares at a face value of Rs.10/- and at a premium of Rs.40/- per share. The AO asked the

assessee to furnish the detailed calculation of fair market value as per section 56(2)(viib) of the Act of the shares alongwith documentary evidences, balance sheet as on date of issue of shares. Before the AO, the assessee furnished the computation of fair market value of shares but as per the AO, same is not in accordance with Rule 11UA(a)(c)(b) of the I.T.Rules. Therefore, the AO calculated the fair market value of shares under Rule 11UA at Rs.31.96 per share and as the assessee has received Rs.14,43,200/- over & above the FMV which is treated as income of the assessee u/s.56(2)(viib) of the Act.

4. On appeal, the CIT(A) confirmed the action of the Assessing officer.

5. Ld counsel for the assessee submitted that in this case, the Assessing Officer made addition on the basis of conjectures and surmises. Ld counsel submitted that the assessee submitted a calculation before the AO properly establishing the share value including share premium more than Rs.50 per share but the same was not accepted and the same was rejected at the threshold without any proper consideration. Ld counsel submitted that in para 4.4 of the assessment order, the AO himself noted that calculation placed by the assessee is not as per Rule 11UA(1)(c)(b) of I.T.Rules, 1962 (hereinafter 'the rules') but what is the provision as per said rule is not clear. Ld counsel vehemently pointed out that the AO calculated the value per share at Rs.31.96 which is not correct and justified in accordance with the Rule 11UA(1)(c)(b) of I.T.Rules.

6. Placing reliance on the order of ITAT Jaipur Bench in the case of M/s. Rameshwaram Strong Glass (P) Ltd., vs ITO in ITA No.884/JP/2016 for A.Y. 2013-14 order dated 12.7.2018, Id counsel for the assessee submitted that as per Rule 11UA(1)(c)(b) of I.T.Rules, the assessee has two options to value the shares and premium at fair market value viz; (1) discounted cash flow method or (2) book value method and it is the prerogative of the assessee to opt or chose one out of these two methods for valuing its shares. Further, drawing my attention towards calculation of fair market value of shares under discounted cash flow method as per projected profit and loss account, Id counsel submitted that as per this calculation, the fair market value of per share comes to Rs.51.85 which is more than Rs.50 per share and this calculation of valuation of share is in accordance with Rule 11UA(1)(c)(b) of the Rules, which cannot be challenged or disturbed by the revenue authorities without any cogent or justified reasons. Ld counsel lastly submitted that as the method applied by the assessee is as per Rule 11UA(1)(c)(b) of the Rules, the value of share including premium is Rs.51.85, therefore, no addition is called for u/s.56(2)(viib) of the Act. Ld counsel also drew my attention towards paras 4.5.5 & 4.5.6 of the order of the Tribunal Jaipur Bench (supra) and submitted that section 56(2)(viib) of the Act can only be invoked where the fair market value of such shares shall be the value determined in accordance with the method as may be prescribed in Rule 11UA(1)(c)(b) of the Income tax Rules and if exceed the

fair market value of such share, then provisions of section 56(2)(viib) cannot be invoked for making addition.

7. Replying to above, Id Departmental Representative (DR) supported the assessment as well as the first appellate order and submitted that the contention of the assessee that section 56 (2)(viib) of the Act is not applicable in this case is wrong as it is not a public company and the existing shareholders of the appellant are included in the ambit of section 56(2)(viib) being any person being a resident. Ld DR further submitted that as the appellant has received impugned amount over and above the fair market value of the share on the date of allotment, the said amount is correctly treated as income of the assessee u/s.56(2)(viib) of the Act.

8. On careful consideration of rival submissions, first of all, I may point out that undisputedly present case is pertaining to a case in which the public are not substantial interested and the shares of the assessee company are not listed or traded on any of recognized exchange. It is also not in dispute that during the financial year i.e. 2014-15 relevant to assessment year 2015-16, the assessee company has received consideration of sale/allotment of 80,000 shares at a face value of Rs.10 and at a premium of Rs.40 per share. The limited issue for my consideration is that whether the consideration so received exceeds the fair market value of the shares?. From the assessment order, I observe that the Assessing Officer has made a calculation in para 4.4 of the assessment

order determining the fair market value at Rs.31.96 per share taking the book value of the assets in the balance sheet as on 1.4.2014 but as per Rule 11UA(1)(c)(b) of the Rules, it is the prerogative of the assessee to estimate the fair market value of the shares issued by it adopting one method out of two methods i.e. discounted cash flow method or book value method and after properly exercising his right, the assessee submitted a valuation before the AO showing the valuation of share at Rs.51.85 per share by valuing discounted cash flow method. The revenue authorities cannot force the assessee to adopt particular method for valuing the fair market value of the share especially when Rule 11UA(1)(c)(b) provides that it is the option of the assessee to chose any method either discounted or book value method for estimating the fair market value of the shares issued by it during the relevant financial period. Therefore, I am not inclined to agree with the action of the AO and the conclusions recorded by the Id CIT(A) in confirming the addition.

9. In view of foregoing discussion and considering the totality of the facts and circumstances of the case as well as the ratio of decision laid down by the ITAT Jaipur Bench in the case of Rameshwaram Strong Glass Pvt Ltd (supra), I am of the considered opinion that when the fair market value of the shares issued by the assessee company is more than the consideration received by it from the allotment of the shares particularly when there is no occasion to invoke the provisions of section 56(2)(viib) of

the Act for making the addition in the hands of the assessee company. The relevant paras 4.5.5 & 4.5.6 of the Tribunal order read as follows:

“4.5.5 We find that a similar controversy came up before a coordinate bench of ITAT in the case ITO vs. M/s Universal Polysack (India) Pvt. Ltd. ITA No. 609/JP/2017 dated 31.01.2018 (Assessee's PB Pages 38-55). The facts noted by the Hon'ble Coordinate Bench in that case are identical with the facts of the present case wherein the Hon'ble Bench held as under:

“14 We have heard the rival contentions and pursued the material available on record. In the instant case, it is not in dispute that the assessee company is a company in which the public are not substantially interested and the shares of the assessee company are not listed or traded on any recognized stock exchange. It is also not in dispute that during the previous year, the assessee company has issued 11,500 shares of face value of Rs 100 at a premium of Rs 900 per share to M/s Terry Towel Industries Ltd and has thus received total consideration of Rs 1,03,50,000. The limited issue under consideration is whether the consideration so received for such shares exceeds the fair market value of the shares. Where the answer to the same is in affirmative, the excess so determined over the fair market will be brought to tax as income from other sources as per the provisions of section 56(2)(viib) of the act which reads as under:

“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 segregate consideration received for such shares exceeds the fair market value of the shares.”

15. The explanation to section 56(2)(viib) provides that the fair market value of such shares means the value determined in accordance with the method as may be prescribed. The method of valuation has been prescribed in rule 11UA which reads as under:

xxx.....

16 As it is clear from the above, sub-rule 2 of rule 11UA talks about method of valuation of unquoted equity shares of the assessee company specifically for the purposes of section 56(2)(viib) of the act and the same overrides the general provisions of sub-rule 1 of rule 11UA. In the instant case, the context in which the valuation of the shares have to be determined is in the context of the section 56(2)(viib) of the Act as invoked by the AO and therefore, both the assessee and the revenue are equally guided by the said provisions

and there is no discretion with either of the parties in terms of non-applicability of Sub-rule 2 of Rule 11UA. Therefore, we are unable to accede to the contention so raised by the Id DR4 that sub-rule 1 of rule 11UA which provides for determination of fair market value⁴ of unquoted equity shares as per book value as per formula so specified is applicable in the instant case. Rather, Sub-Rule 2 of Rule 11UA is more specific for the purposes of determination of fair market value of unquoted equity shares under section 56(viib) and shall be applicable in the instant case. The latter provides an option to the assessee to determine the fair market value of the shares either as per the book Value or Discounted Free Cash Flow Method. The exercise of such an option by the assessee is not subject to fulfillment of any specified conditions and it is left to the sole discretion of the assessee as it deems fit to apply. In the instant case, the assessee company has exercised its option to value its shares as per DCF method and we find that the objection of the AO is primarily directed at not adopting the book value of determination of value of shares as against DCF adopted by the assessee company. The exercise of such an option cannot therefore be challenged by the revenue once the same has been exercised at first place by the assessee.

17. Further, where the assessing officer is of the opinion that the methodology so adopted by the assessee and/or the underlying assumption while determining the share valuation as per DCF is not acceptable to him, there is no discretion with the AO to discard the DCF method of valuation and adopt book value method. At the same time, in our view the AO is well within his rights to examine the methodology so adopted by the assessee and/or the underlying assumption and where he is not satisfied with the same, he can challenge the same and suggest necessary modification/alterations provided the same are based on sound reasoning and rational basis. In the instant case, we find that certain basis objections have been raised by the Assessing Officer in terms of applying the estimated turnover numbers instead of actual numbers and discounting factor, etc which, in our view, has been satisfactorily explained by the assessee company during the appellate proceedings and nothing has been brought on record which can substantially challenge the methodology or the underlying assumption while determining the value of the shares. Further, the fact that the said valuation and the projected financials have been found acceptable by the Bank while sanctioning the term loan and working capital limits, it cannot be said that the same are purely hypothetical and not based on sound financial understanding and market dynamics of the industry in which the assessee operates.

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19. In light of above discussions and in the entirety of facts and circumstances of the case, the order of the Id CIT(A) is confirmed and the ground taken by the Revenue is dismissed.”

4.5.6 We also find that in the case of Vodafone M-Pesa Ltd. vs. PCIT (2018) 92 Taxmann 73 (Bombay) (DPB 79-83), the Hon'ble Mumbai High Court in para 9 has observed that

“9.Therefore, the Assessing Officer is undoubtedly entitled to scrutinise the valuation report and determine a fresh valuation either by himself or by calling for a final determination from an independent valuer to confront the petitioner. However, the basis has to be the DCF Method and it is not open to him to change the method of valuation which has been opted for by the Assessee.----- ”

The AO though observed that the assessee raised loans from the above associate concerns and has converted them into shares application/premium money. However, it has not shown how it will affect the correctness of the valuation claimed. It is not the case of the AO that the shares were allotted to the outsiders non-related persons but the existing amount of the loans from the related persons were converted into shares. Hence there cannot be any scope of introduction of assessee's unaccounted income through allotment of shares at unreasonably high priced shares. Therefore, such observations is not relevant and a mere suspicion. It appears that the authorities below have ignored Explanation (a) below S. 56(2)(viib).The said Explanation provides that 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 i.e. u/r 11UA; 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, licences, franchises or any other business or commercial rights of similar nature, whichever is higher. Accordingly, the value computed under the Rule at Rs.95.90 per share is higher than Rs. 65.31 or Rs.32.76 per share and therefore, the higher valuation has to be adopted. Moreover, it is only the Explanation (a)(ii) speaks of the satisfaction of the AO but there appears no such condition in the Explanation (a)(i) which therefore AO is not permitted to interfere in the valuation, once done in accordance with the method prescribed in the Rule 11UA(2). For the reasons stated above, we find no justification behind rejecting the declared valuation of the shares and in the impugned addition made by the AO but partly sustained by the CIT(A), which is hereby deleted.”

10. In view of above observation of Co-ordinate Bench of ITAT Jaipur (supra) and from the facts and circumstances of the case, I observe that the Assessing Officer proceeded to value the share by adopting book value method whereas the assessee adopted the value of shares by following discounted cash flow method (DCF) and the objection of the AO primarily rest on the premise that the method adopted by the assessee company is not appropriate. As I have noted above that it is the prerogative and privilege of the assessee to adopt one method and once the assessee has chosen discounted cash flow method for valuing its shares then the AO or any other revenue authorities cannot compel the assessee to adopt another method i.e. book value method. However, I may also make it clear that the exercise of such option cannot be therefore challenged by the revenue authorities with the same has exercised at first place by the assessee but the AO is undisputedly entitled to scrutinise, verify and examine the valuation report and determine the fresh valuation either by himself or from an independent valuation after confronting the assessee. But at the same time, it is ample clear that the basis has to be the DCF method and it is not open to the revenue to change the method of valuation which has been opted by the assessee.

11. In view of above, in the instant case, the value adopted and computed by the assessee as per Rule 11UA(2)(c)(b) by following DCF

method at Rs.51/85 and the assessee company has received shares and issued/allotted @ Rs.50 per share including premium and this rate has not been contested or challenged by the AO and during hearing before him by Id D.R. From a careful reading of the assessment order, I clearly observe that the AO merely compelled the assessee to change the valuation method from DCF method to another book value method, which is not permissible as per Rule 11UA(2)(c)(b) and other provisions of the Act. As per the Explanation (a) (ii) to Section 56(2)(viib), speaks about the satisfaction of the AO but there is no condition in the explanation (a)(i) that the AO is not permitted to interfere with the valuation once done in accordance with the method prescribed in the Rule 11UA (2)(c)(b) of the Rules. Therefore, the AO as well as Id CIT(A) was not correct in rejecting the adoption of DCFM by the assessee and invoking the provisions of section 56(2)(viib) of the Act for making addition on differential value of shares and valuation done as per book value method.

12. Therefore, in view of above discussion and respectfully following the ratio laid down in the case of Rameshwaram Strong Glass Pvt Ltd., (supra) and keeping in view the facts of the case and provisions of section 56(2)(viib) r.w. Rule 11U(1)(c)(b), I am compelled to hold that the addition made by the AO is not sustainable and, therefore, I dismiss the same.

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

Order pronounced on 16 /06/2020.

Sd/-
(Chandra Mohan Garg)
JUDICIAL MEMBER

Cuttack; Dated 16/06/2020
B.K.Parida, SPS

Copy of the Order forwarded to :

1. The Appellant : Alishan Palace Resorts Pvt Ltd.,
410, Forum Mart, 89, Kharvel Nagar,
Bhubaneswar
2. The Respondent. ITO, Ward 1(3), Bhubaneswar
3. The CIT(A)-1, Bhubaneswar
4. Pr.CIT- 1, Bhubaneswar
5. DR, ITAT, Cuttack
6. Guard file.
//True Copy//

By order

Sr.Pvt.secretary
ITAT, Cuttack