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TRIBUNAL UPHOLDS THE SANCTITY OF CORPORATE GIFTS MADE PURSUANT TO AN INTERNAL RESTRUCTURING EXERCISE; QUASHES REVISIONARY PROCEEDINGS

16 December 2019

In a recent decision in the case of M/s Direct Media Distribution Ventures Private Limited v Principal Commissioner of Income Tax (ITA No: 2211/Mum/2019), the Mumbai bench of the Income Tax Appellate Tribunal (Tribunal) while deciding on the issue of invocation of revisionary proceedings by the Commissioner of Income Tax (CIT) dealt with the taxability of a gift of shares between corporates. The Tribunal held that there is nothing in law which estops corporates from making a gift of shares to each other, more so when the intention of the parties is supported by an internal restructuring exercise, which was driven by commercial reasons. Per Section 263 of the Income Tax Act, 1961 (IT Act), a CIT has the power to invoke revisionary proceedings by modifying/enhancing an order of the tax officer if the same is erroneous and prejudicial to the interests of the revenue.

Background

The facts relating to the case are as follows: Direct Media Distribution Ventures Private Limited (Taxpayer) was engaged in the business of media distribution, including the distribution of television channels via cable network. For the relevant Financial Year (FY) 2013-14, the Taxpayer filed its return of income and disclosed that it had transferred equity shares of Dish TV India Limited (Shares) to its related party, Direct Media Solution Private Limited, as a gift pursuant to a corporate restructuring exercise.

It is to be noted that the above Shares had been acquired by the Taxpayer earlier, at Nil consideration from its group companies, under another restructuring exercise.

The return of income of the Taxpayer was accepted and the Tax Officer passed an order, accordingly. However, the CIT invoked its revisionary powers under the IT Act and sought to revise the Tax Officer's order treating it to be erroneous. The CIT revised the order to hold that the Taxpayer would be required to pay capital gains tax on the transfer of Shares by deeming the fair market value of such Shares as the sale consideration.

The Taxpayer being aggrieved by the order of CIT, filed an appeal before Tribunal. The Tribunal observed that:

- Upon enquiry by the Tax Officer regarding the transfer of Shares, the Taxpayer had made detailed submissions and explained that:

    - it had made disclosures in its annual report that the Shares were transferred for Nil consideration to consolidate onshore media assets, including the shares of listed companies and made filings before the Securities and Exchange Board of India;

- its constitution documents permitted acquisition and transfer of assets by way of gift and it had also sought due approvals before undertaking the transaction;
- law does not prohibit corporate gifts; and
- there are rulings by various benches of the Tribunal which have categorically held there is no prohibition on transfer of shares by way of gift by a company to another company. Moreover, the IT Act specifically exempts 'gift' from capital gains tax implication;

- If the acquisition of the Shares was pursuant to an internal restructuring exercise which was accepted by the tax authorities, there was no reason to question the veracity of the transfer of Shares. In fact, once the Taxpayer received the Shares by way of a gift, it obtained absolute rights vested with it on the Shares and the liberty to deal with it as it desired. Hence, the argument of the CIT that the Taxpayer had received the Shares previously by way of gift and had transferred the said Shares again by way of gift during the relevant FY, which is a colorable device, was devoid of merit; and
- the Hon'ble Supreme Court in the case of CIT v George Henderson and Company Limited *(66 ITR 622)* has categorically held that for the purpose of capital gains computation, the actual consideration cannot be substituted with the market value of the asset. Hence, the action of the CIT substituting the fair market value of the Shares for the purpose of capital gains computation in the hands of the Taxpayer was incorrect.

Taking the above into consideration, the Tribunal held that given that the Tax Officer had made due enquires and had taken a possible view on the transaction – which cannot be construed as erroneous, it was not open to the CIT to initiate a revision proceeding against the Taxpayer. Accordingly, the Tribunal held in favour of the Taxpayer.

Comments

This is a welcome ruling of the Tribunal reiterating that there is no prohibition under Indian law on the corporate gifting of shares or otherwise; and hence the donor company will be eligible to claim exemption from capital gains tax accorded under the IT Act. However, it is interesting to note that the Tribunal has also given due credence to the fact that the gift of shares by the Taxpayer was in furtherance of an internal restructuring exercise and hence, the transaction was driven by commercial expediency. In an era where general anti avoidance rules and fair value rules have been incorporated into the IT Act, it is of paramount importance to ensure that there is a sound commercial rationale and substance for undertaking corporate actions involving the transfer of any right and/or interest.

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