

IN THE HIGH COURT OF BOMBAY AT GOA

WRIT PETITION NO. 510 OF 2010

1. The Commissioner of Income Tax,
Having office at Aayakar Bhavan,
Patto Plaza, Panaji
Goa

... Petitioner

V e r s u s

M/s Umicore Finance
Luxemborg,
C/o M/s Anandeya Zinc Oxides Pvt. Ltd.
Plot No. 23, GIDC,
Sancoale Industries Estate,
Zuarinagar,
Goa-403726

... Respondent

Ms. Asha Desai, Advocate for the Petitioner.

Mr. S. R. Wadhwa, Advocate with Mr. S. M. Singbal, Advocate for the Respondents.

Coram :- **F. M. REIS,**
NUTAN D. SARDESSAI, JJ.

Reserved for Judgment on : 11th August, 2016
Judgment to be pronounced on : 25th November, 2016

Heard Ms. Asha Desai, learned Counsel appearing for the
Petitioner and Mr. Wadhwa, learned Counsel appearing for the Respondent.

2. The above Petition filed by the Commissioner of Income Tax,
inter alia, takes exception to the Order dated 12.03.2010 and 15.06.2010
passed by the Addl. Commissioner of Income Tax (AAR).

3. Briefly, it is the contention of the Petitioners, that the Respondent is a non-resident Company incorporated under the laws of Luxembourg and it is the holding of its wholly owned subsidiary M/s. Anandeya Zinc Oxides Pvt. Ltd. (Anandeya in short), an Indian Company assessed with ACIT, Margao. It is further their case that the said Respondent purchased 15,49,500 shares of Rs.10/- each or 99.96% of the shares of Anandeya and the balance 500 shares of Rs.10/- each was purchased by the Respondent. It is further their case that on 13.09.2005, M/s. Anandeya was incorporated as a Private Limited Company succeeding erstwhile firm M/s. Anandeya Zinc Oxides whose conversion into a Private Limited Company was effected under part IX of the Indian Companies Act, 1956. It is further their case that on the date of the conversion, the partners of the erstwhile firm continued as shareholders having share holding identical with profit sharing ratio of the partners. It is further their contention that the firm set up a plant for manufacture of high purity white seal zinc oxide of annual capacity 5000 tones per annum and the plant commenced production in April 1995 and was converted into 100% export oriented unit in 1996. The Assets of the partnership was revalued for Rs. 5 crores as against the net worth of the business of Rs.3,05,896/- relevant to the assessment year 1998-1999. The excess of the revaluation of assets of Rs.4,96,94,104/- was credited to the respected partners account. The firm, however, continued to claim, the depreciation value of the asset prior to the revaluation for the purpose of computation of income under the Income Tax Act, 1961. It is further their

case that the Respondent-Company acquired the shareholding of Ms/. Anandeya and, therefore, has violated the provisions of Section 47(xiii)(d) read with Section 474A(3) of the Income Tax Act, 1961. Hence, the exemption from capital gains enjoyed by the assessee firm upon conversion into limited company ceased to be in force. It is further their case that the non resident Respondent M/s. Umicore Finance Luxembourg, acquired shares of M/s. Anandeya and was not connected in any way to the transaction which had taken place on 13.09.2005. Therefore, it is the case of the Petitioners that the transaction on 13.09.2005 was not within the purview of Section 245N(a)(i)(ii) or (iii) and the Order of the AAR is without jurisdiction. It is further their contention that the application for recall of admission order came to be rejected and by ruling the AAR was pleased to hold that there were no capital gains accrued or arose at the time of conversion of partnership firm into a private limited company under part IX of the Companies Act and, therefore, notwithstanding the non-compliance with clause (d) of the provision to Section 47(xii) of the Income Tax Act, by reason of premature transfer of shares the said company is not liable to pay capital gains tax. Being aggrieved by the said assessment, the Petitioners have filed the above Petition.

4. Upon hearing the learned Counsel appearing for the Petitioner and the Respondents who have reiterated the contentions raised in the Writ Petition and the findings of the AAR in the impugned Order, we shall proceed

to examine the contentions sought to be raised by the Petitioners herein.

5. The undisputed facts in the present Petition are that the Respondents entered into a share purchase Agreement on 01.07.2008 with Anandeya Zinc Oxides Private Limited for the purchase of 15,50,000 shares of Rs.10/- each representing 100% equity shares which was completed on 12.08.2008. The said M/s. Anandeya Zinc Oxides Private Limited was incorporated as Private Limited Company on 13.09.2005 succeeding erstwhile firm M/s. Anandeya Zinc Oxides and such conversion was effected on 13.09.2005 under part IX of the Indian Companies Act 1956. It is the contention of the Respondent-Company that when a firm is converted into a Company, there is no sale/extinguishment of any rights and no transfer of asset as envisaged in Section 45(1) of the Income Tax Act, can be stated to have taken place and, as such, even the provisions of Section 47(xiii)(d) are in violation, it does not attract capital gains to the Respondent's subsidiary because Section 47(xiii) applies only to firm that are succeeded by the company by sale. But, however, it is the contention of the Petitioner that Section 2(47) of the Income Tax Act, 1961, is an "inclusive provision" and transfer by modes other than those that are presently listed, can also be included in the definition of transfer. It is further pointed out that as in the present case where a distinct legal identity such as a private limited company has succeeded a collection of partners, namely the firm, which has no separate legal identity can be brought into the inclusive provision of

transfer under Section 2(47) of the Income Tax Act.

6. Dealing with this aspect, the AAR in the impugned Order has noted that on 09.10.2009, the Respondents have clarified that whilst converting the partnership firm into a Company, there was no revaluation of the assets and the assets and liabilities of the firm as also the partners, capital and current accounts were taken at their book value in the accounts of the Company. It is also pointed out that the first year audited accounts of the Company for the period 13.09.2005 to 31.03.2006, were also filed and found that the net worth of the Company as on the date of conversion was the same as it was in the hands of the erstwhile firm and there was no increase in such value.

7. Section 45(1), 47, 47A and 48 of the Income Tax Act, reads thus :

Section 45(1):

Capital gains.

45.(1) Any profits or gains arising from the transfer of a capital asset effected in the previous year shall, save as otherwise provided in sections 54, 54B, 54D, 54E, 54EA, 54EB, 54F, 54G and 54H, be chargeable to income-tax under the head “Capital gains”, and shall be deemed to be the income of the previous year in which the transfer took place.

Section 47 lays down that nothing contained in section 45 shall apply to the transfers specified therein. We are concerned with clause (xiii) in that section which reads thus:

Clause (xiii) of Section 47

Nothing contained in section 45 shall apply to the following:

(xiii) any transfer of a capital asset or intangible asset by a firm to a company as a result of succession of the firm by a company in the business carried on by the firm, or any transfer of a capital asset to a company in the course of demutualisation or corporatisation of a recognised stock exchange in India as a result of which an association of persons or body of individuals is succeeded by such company:

Provided that

(a) all the assets and liabilities of the firm [or of the association of persons or body of individuals] relating to the business immediately before the succession become the assets and liabilities of the company;

(b) all the partners of the firm immediately before the succession become the shareholders of the company in the same proportion in which their capital accounts stood in the books of the firm on the date of the succession;

(c) the partners of the firm do not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of allotment of shares in the company; and

(d) the aggregate of the shareholding in the company of the partners of the firm is not less than fifty per cent of the total voting power in the company and their shareholding continues to be as such for a period of five years from the date of the succession;

8. The learned AAR further noted that Section 47(xiii) specifically excludes different categories of transfers from the purview of capital gains taxation but it is subject to fulfilling the conditions laid down Clause (a) to (d). The fact that conditions (a) to (c) are satisfied, is not in dispute but, however, the question is whether clause (d) requires to be satisfied. The learned AAR has rightly pointed out that the first part of clause (d) has been satisfied but, however, it is noted by the learned AAR the requirements of second part of clause (d) i.e. the shareholding of 50% or more should continue to be as such for the period of five years from the date of succession, has not been fulfilled in the instant case by reason of the transfer of shares by the Indian Company to the Applicant before the expiry of five years. It is further noted that the effect of transgression of the conditions laid down in clause (xiii) is set out in Section 47A(3). Section 47A (3) reads thus :

47A Withdrawal of exemption in certain cases.

(1) & (2) xx xx xx xx xx
 xx xx xx

(3) Where any of the conditions laid down in the proviso to clause (xiii) or the proviso to clause

(xiv) of section 47 are not complied with, the amount of profits or gains arising from the transfer of such capital asset or intangible asset not charged under section 45 by virtue of conditions laid down in the provision to clause (xiii) or the proviso to clause (xiv) of section 47 shall be deemed to be the profits and gains chargeable to tax of the successor company for the previous year in which the requirements of the proviso to clause (xiii) or the proviso to clause (xiv), as the case may be, are not complied with.

9. Subsection(3) of Section 47A under which the transfer Company has forfeited its claim to seek exclusion uses the word “*the amount of profit or gains arising from the transfer of such capital asset or intangible assets*”. It is further noted that to attract such provision, it presupposes a transfer. The learned AAR has also noted at para 9.1 thus :

“9.1. In the case of *CIT v/s Texspin Engg. & Mfg. Works*, the learned Judges of the Bombay High Court while dealing with Section 45 have given the legislative background for introducing Section 46(xiii) and the basic postulates of this provision in the following words:-

“This clause was inserted with effect from April 1, 1999. Therefore, we are not concerned with the amendment. However, it provides a clue to the legislative intent. In our opinion, this clause has been introduced with effect

from April 1, 1999, in order to encourage more and more firms become limited companies. It also indicates the difference between transfer and transmission. Basically, when a firm is treated as a company under Part IX, it is a case similar to transmission. This is amply made clear by clause (xiii) of section 47, which states that where a firm is succeeded by a company in the business, the transactions shall not be treated as a transfer. Now, this amendment has been made in section 47 in view of the controversy arising on section 45(1) read with section 2(47)(ii)."

10. The learned AAR has also noted that the consequences of violation of those conditions have been specifically laid down in sub-section (3) of Section 47A which was also introduced by the same Finance Act. It is further pointed out that if no profit or gains arise earlier when the conversion of the firm into a Company took place or if there was no transfer at all of the capital assets of the firm at the point of time, the deeming provision under Section 47A(3) cannot be inducted to levy the capital gain stakes. The learned AAR further found that the shares allotted to the partners of the existing firm consequent upon the registration of the firm as a Company, did not give rise to any profit or gains. It is further noted that by such reconstitution of the Company under part IX of the Companies Act, the assets automatically get vested in the newly registered Company as per the statutory mandate contained under Section 575. It is further found that it cannot be said that the partners have made any gains or received any profits

assuming that there was a transfer of capital assets. It was also noted that worth of the shares of the partnership was not different from the interest of partners in the existing firm. The learned AAR also took support in the Judgment reported in **263 ITR 345** in the case of **Texspin Engg. Mfg. Works**, where the issue was viewed from another angle i.e. from the stand point of Section 48 of the Act in a case of similar conversion of a firm into a company. It is further noted that the full value of consideration cannot be attributed to the transaction. The learned AAR also noted that the Apex Court has held that the provisions of Section 48 has to be read as an integral part of the charging provision in Section 45. The learned AAR has further observed at para 12.1 and 13 thus :

“12.1 Though these observations were made in the context of Section 45(4), the ratio of the decision would equally apply to the present case. However, the question whether vesting by operation of law would be transfer has not been decided in that case. True, the decision in Texspin was rendered without taking resort to Section 47(xiii) and the Proviso thereto. But, the basic reasoning underlying the said judgment still holds good. Though we are not inclined to express a final opinion on the point of transfer, we would like to say this much: Section 47(xiii) read with Section 47A(3) cannot be construed to introduce a fiction to the effect that the income which is not liable to be taxed under the other

provisions of the Chapter on capital gains can be deemed to be capital gains, if the violation of conditions take place. May be, these provisions were introduced on a supposition that the conversion of the firm into company under Part IX of the Companies Act would lead to realization of profits or gains on account of transfer of capital assets. But, S.47A(3) does not achieve the desired objective, as the language of the said Provision now stands. Section 47A(3) only emphasizes the obvious, that is to say, the profits and gains resulting from the transfer of capital asset chargeable under the Provisions of the Act. To judge whether this prerequisite is fulfilled or not, we have to go back to the basic provisions, namely Section 45(1) and Section 48 and S.47-A(3) cannot be read as a 'stand alone' provision.

13. In the light of the above discussion, it is ruled that no capital gains accrued or arose at the time of conversion of partnership firm into a private limited company under Part IX of the Companies Act and therefore, notwithstanding the non-compliance with clause (d) of proviso to Section 47(xiii) of the Income Tax Act, by reason of premature transfer of shares, the said company is not liable to pay capital gains tax. No final opinion is expressed in regard to the question whether on the registration of company under Part IX of the Companies Act, there was 'transfer' of capital assets.”

11. On perusal of the said observations, we find that the learned AAR has in a very reasoned Order, has taken a view that no capital gains accrued or attracted at the time of conversion of the partnership firm into a Private Limited Company. In part IX of the Companies Act, therefore, notwithstanding the non-compliance with clause (d) of the proviso of Section 47(xiii) of the Income Tax Act by premature transfer of shares, the said Company is not liable to pay capital gains tax. These findings have been arrived at essentially looking into the fact that there was revaluation of assets at the time of conversion of the firm M/s. Anandeya Zinc Oxides Private Limited. The said finding of fact has not been disputed by the learned Counsel appearing for the Petitioners and, as such, the finding of the learned AAR that there was no capital gains in the transaction in question cannot be faulted. It is also to be noted that even immediately after such conversion in question from the partnership firm into a Private Limited Company, the assessment with regard to the income of the new Company as well as of the respective partners were filed and there was no objection or grievances raised by the Assessing Officer that any capital gains had to be paid on account of the incorporation of the Company in terms of the said provisions. The transfer of shares in favour of the Respondent by the erstwhile partners who were shareholders of M/s. Anandeya Zinc Oxides Private Limited and such partners/share holders are liable to pay capital gains even if acceptable, would not affect the decision passed by the learned AAR whilst coming to the

conclusion that there were no capital gains at the time of incorporation of the new Company by the said partnership firm.

12. The contention of the Petitioner that in view of the violation of clause (d) of Section 47(xiii), the exemption from capital gains enjoyed by the Assessing firm upon conversion into a Private Limited Company, ceases to be in force cannot be accepted. We have already examined that there are no capital gains which have accrued on account of such incorporation. In such circumstances, we find that the said contention of the learned Counsel appearing for the Petitioner that in view of the transfer of the capital assets or intangible assets, there are capital gain tax payable by the transferee Company, cannot be accepted. As pointed out herein above, there was no capital gains payable at the time of the incorporation of the Company from the erstwhile partnership firm.

13. The next contention of the learned Counsel appearing for the Petitioner is that the application under Section 245(N) of the Respondents itself was not maintainable. The main submission on that aspect is that the Respondents not being parties to the transaction, the question of seeking an advance ruling at the instance of the Respondents is not covered under clause (i) (ii) and (iii) of Section 245(N)(a) of the said Act. To examine such aspect, clause (i) of Section 245N(a) of the said Act defines advance ruling as thus :

(a) *“Advance ruling” means -*

(i) a determination by the Authority in relation to a transaction which has been undertaken or is proposed to be undertaken by a non-resident applicant.”

14. The learned AAR whilst dealing with such aspect has rightly observed in the Order dated 06.07.2009 at para 6 thus :

“6. It seems to us that the application is maintainable having regard to the wider language of sub-clause (i) of section 245N(a) in contrast with the language employed in sub-clause (ii). There is no specific requirement in sub-clause (i) that determination should relate to the tax liability of an on-resident. Going by the averments of the applicant, it is clear that the capital gain tax issue arising in the case of the acquired Indian company has a direct and substantial impact on the applicant's business in view of the stipulations in share purchase agreement. Sub-clause (i) has to be construed in a wider sense and moreover a remedial provision shall be liberally construed. We are, therefore, of the view that the question raised by the applicant falls within the definition of

'advance ruling' under section 245N9a) of the Act. Accordingly, the application is allowed under section 245R92) and posted for hearing on merits on 11th August, 2009.

15. Considering the said aspect and as looking into the question as reformulated, the question as to whether capital gains are liable to be paid or not in terms by the transferee Company being a non resident Company, the Respondent herein, would be a matter which would come within the scope of advanced ruling in terms of the said depreciation.

16. In this context, the High Court of Madras in the Judgment reported in **(2009) 222 CTR (Mad) 270** in the case of **Anurag Jain vs. Authority for Advance Rulings & anr..** has observed at paras 19, 20 and 24 thus :

“19. In that judgment, while dealing with the jurisdiction of the High Court under Article [226](#) of the Constitution of India apart from that of the Supreme Court under Article 136, the Supreme Court has confirmed with approval the earlier judgment in R.B. Shreeram Durga Prasad and Fatehchand Nursing Das v. [Settlement Commission MANU/SC/0429/1989](#)[1989]176ITR169(SC) that the court is concerned with the legality of the procedure followed and not the validity

of the order and the courts under judicial review are concerned not with the decision but with the decision-making. The relevant portion of the judgment of the Supreme Court in this regard is as follows (page 623 of 201 ITR):

The scope of enquiry, whether by the High Court under Article [226](#) or by this court under Article [136](#) is also the same whether the order of the Commission is contrary to any of the provisions of the Act and if so, apart from ground of bias, fraud and malice which, of course, constitute a separate and independent category, has it prejudiced the petitioner/appellant. Reference in this behalf may be had to the decision of this court in *R.B. Shreeram Durga Prasad and Fatehchand Nursing Das v. Settlement Commission* [MANU/SC/0429/1989](#) : [1989]176ITR169(SC) , which too was an appeal against the orders of the Settlement Commission. Sabyasachi Mukharji J., speaking for the Bench comprising himself and S.R. Pandian J., observed that, in such a case, this court is 'concerned with the legality of the procedure followed and not with the validity of the order'. The learned judge added 'judicial review is concerned not with the decision but with the decision-making process'. Reliance was placed upon the decision of the House of Lords in *Chief Constable of North Wales Police v. Evans* [1982] 1 WLR 1155 (HL). Thus, the appellate power under Article [136](#) was equated with the power of judicial review, where the appeal is directed against the

orders of the Settlement Commission. For all the above reasons, we are of the opinion that the only ground upon which this court can interfere in these appeals is that the order of the Commission is contrary to the provisions of the Act and that such contravention has prejudiced the appellant. The main controversy in these appeals relates to the interpretation of the settlement deeds though it is true, some contentions of law are also raised. The Commission has interpreted the trust deeds in a particular manner. Even if the interpretation placed by the Commission on the said deeds is not correct, it would not be a ground for interference in these appeals, since a wrong interpretation of a deed of trust cannot be said to be a violation of the provisions of the Income Tax Act. It is equally clear that the interpretation placed upon the said deeds by the Commission does not bind the authorities under the Act in proceedings relating to other assessment years.

20. Applying the said judicial dictum laid down by the Supreme Court to the facts of the present case even assuming that the first respondent authority has not interpreted the associated employment agreement which on fact forms part of the share purchase agreement in the proper manner, it is certainly not open to this court to go into the correctness or otherwise or validity or otherwise of the findings given by the first respondent.

...

24. Hence, it is not necessary for this court to give any finding as to the jurisdiction of this court under Article 226 of the Constitution of India.”

17. Considering the said observations and taking note of the findings of the learned AAR, we find that there is no case made out for interference by this Court under Article 226 of the Constitution of India. The Petitioners were given an opportunity by the learned AAR and the contentions raised were duly considered whilst passing the impugned Orders. We find no reason to interfere in the impugned Orders passed by the learned AAR. As such, the Petition stands rejected.

NUTAN D. SARDESSAI, J.

F. M. REIS, J.

arp/*