IN THE HIGH COURT OF PUNJAB AND HARYANA AT CHANDIGARH

Date of decision: 27.09.2023

1. **ITA No.72 of 2018 (O&M)**

Principal Commissioner of Income Tax (Central), Gurgaon …Appellant

Vs.

Smt. Meenu Satija …Respondent

2. **ITA No.75 of 2018 (O&M)**

Principal Commissioner of Income Tax (Central), Gurgaon …Appellant

Vs.

Sh. Sunil Satija …Respondent

3. **ITA No.76 of 2018 (O&M)**

Principal Commissioner of Income Tax (Central), Gurgaon …Appellant

Vs.

Sh. Dharmendra Bhandari …Respondent

4. **ITA No.79 of 2018 (O&M)**

Principal Commissioner of Income Tax (Central), Gurgaon …Appellant

Vs.

Sh. Dharmendra Bhandari …Respondent

5. **ITA No.129 of 2018 (O&M)**

Principal Commissioner of Income Tax (Central), Gurgaon …Appellant

Vs.

Sh. Sunil Satija …Respondent

CORAM: HON'BLE MS. JUSTICE RITU BAHRI
HON'BLE MRS. JUSTICE MANISHA BATRA

Present: Mr. Varun Issar, Junior Standing Counsel,
for the appellant(s).

Mr. Akshay Bhan, Senior Advocate,
with Mr. Shantanu Bansal, Advocate,
and Mr. Yugank Goyal, Advocate,
for the respondent(s).
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Ritu Bahri, J. (oral)

1. This judgment shall dispose of ITA Nos.72, 75, 76, 79, 129 of 2018 together as common questions of law and facts are involved in all the appeals. For reference, facts are being taken from ITA No.72 of 2018.

2. The instant appeal (ITA No.72 of 2018), under Section 260A of the Income Tax Act, 1961, has been filed against the order dated 27.07.2017 passed by the Income Tax Appellate Tribunal, Delhi Bench "B", New Delhi, whereby appeal (ITA No.2490/Del/2017) filed by the assessee-Smt. Meenu Satija against the order dated 16.03.2017, has been accepted by observing as under:-

> "6. The circumstances and facts in the present case are identical to the facts in assessee's own case for the Assessment Year 2010-2011, reproduced hereinabove and accordingly, in the present case, provision would not be applicable to bonus/right shares as there is no increase or decrease in the wealth of the share holders on account of bonus/right shares and there is no element of gift in issuing of bonus/right shares to the assessee by the company. Reliance is placed upon the decision of Hon'ble Supreme Court in the case of Khoday Distrilleries Ltd. vs. CIT, reported in (2008) 307 ITR 312. The issue is also covered by the decision of Mumbai Tribunal in the case of Sudhir Menor HUF (2014) 148

ITD 206 (mum) and as per the decision of Hon'ble Supreme Court in the case of Khoday Distilleries Ltd. (supra), no property is being conveyed to the share holder by issue of bonus/right share in as much as the property therein is comprised in the existing share holder of the allottee. Similarly, no property, however, is being passed on to the assessee in the instant case before us on allotment of bunus/right shares and no addition could be made by applying the provisions of Section 56 (2) (vii) as the case may be. Accordingly, the order of the learned PCIT is bad in law and is directed to be quashed and all grounds of the assessee are allowed."

3. In the facts of the present case, on 04.07.2012 a search was carried out in the business premises of M/s Bestech Group of companies and residential premises of their directors. During the search, documents were seized and thereafter, notice under Section 153A (1) (a) of the Income Tax Act was issued to the assessee on 18.03.2013 requiring her to file her return of income with respect to the preceding assessment year relevant to the previous year, in which the search was conducted. In response to the said notice, the assessee filed her return of income for the assessment year 2012-2013 on 22.08.2013 declaring an income of Rs.18,12,410/-. Thereafter, notices under Section 143 (2) and 142 (1) of the Income Tax Act along with a questionnaire were issued to the assessee on 05.02.2014. After service of the notices, Sh. Rajesh Sood, C.A., and Sh. Deepak Gupta, C.A., the authorized representatives on behalf of the assessee, attended the assessment proceedings from time to time. The return of income of Rs.18,12,410/- was accepted.

4. On examination of the assessment records, it was noted by the Principal Commissioner of Income Tax (Central), Gurgaon that the assessee

was a shareholder of M/s Bestech India Pvt. Ltd. During the year under consideration, the company had allotted 11,01,499 number of bonus shares to the assessee on 27.03.2012 without consideration by way of capitalization of share premium account and reserve account. It is also noticed that shares were allotted to outsiders i.e. parties not related to promoters of the company on 29.03.2012 @ 1240 per share on face value of Rs.10/- per share. By applying Rule 11UA of Income Tax Rules, 1962, there was an increase in assessee's net wealth on account of allotment of bonus shares and the provision of Section 56 (2) (vii) (c) of the I.T. Act were clearly attracted.

5. As per Rule 11UA, the fair market value of shares of M/s Bestech India Pvt. Ltd. was calculated, which comes to Rs.39.17/- per equity share. The total value of shares held by the assessee before receipt of bonus shares was Rs.5.19 Cr. and the value of shares received by the assessee for the Assessment Year 2012-2013 comes Rs.7.39 Cr. i.e. total holding of shares. Thus, net accretion of wealth was Rs.2.2 Crore. The fair market value of shares as computed under Rule 11U & 11UA of the Income Tax Rules comes to Rs.4,31,45,715/- (Rs.39.17*11,01,499), which was received during the Assessment Year 2012-2013 by Mrs. Meenu Satija. Accordingly, the provisions of Section 56 (2) (vii) (c) are applicable on fair market value of bonus shares received by the assessee. After considering the reply and arguments raised by the assessee, order under Section 263 of the Income Tax Act, 1961 directing the A.O. to re-compute the income by making addition of Rs.4,31,45,715/- under Section 56 (2) (vii) (c) of the Act was passed on 16.03.2017 (Annexure A-2). Against this order, the assessee filed an appeal (for the assessment year 2012-2013) before the Tribunal, which was allowed vide order dated 27.07.2017 (Annexure A-3) by holding that the provisions

of Section 56 (2) (vii) (c) of the Income Tax Act, 1961 would not be applicable to bonus shares as there was no increase or decrease in the wealth of shareholders on account of allotment of bonus shares and there was no element of gift involved. It was further held that no property was conveyed to the assessee on allotment of bonus shares in as much as the property therein was comprised in the existing shareholding of the allottee and no addition could be made by applying the provisions of Section 56 (2) (vii) of the Act.

6. The Revenue has challenged the order dated 27.07.2017 (Annexure A-3) on the following substantial questions of law:-

> (i) Whether the facts and in the circumstances of the case and in law, the Hon'ble ITAT was justified in deleting the addition of Rs.4,31,45,715/- made under Section 56 (2) (vii) (c) of the Income Tax Act, 1961 for receiving 11,01,499 bonus shares of Bestech India Pvt. Ltd. for nil consideration against the Fair Market Value of Rs.39.17 calculated under Rule 11U & 11UA of the Income Tax Rules, 1962.
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> (ii) Whether on the facts and in the circumstances of the case and in law, the Hon'ble ITAT was right in law in deleting the addition ignoring the fact that issuance of bonus shares by diverting share premium amount to promoters led to increase the net wealth of the promoters.
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> (iii) Whether on the facts and in the circumstances of the case and in law, the Hon'ble ITAT was right in deleting the addition ignoring the fact that the allotment of bonus shares was disproportionate and not based on any rational formula or computation and it has been done simply to transfer disproportionate value of assets to the assessee in garb of bonus shares.
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> (iv) Whether on the facts and in the circumstances of the case and in law can such disproportionate allotment be strictly

regarded as allotment of bonus shares not inviting the rigors of the provisions of the Section 56 (2) (vii) (c) of the Act.

Learned counsel for the respondent has referred to the judgment passed by the High Court of Karnataka in ***Pr. Commissioner of Income Tax and another vs. Dr. Ranjan Pal,*** 2020 SCC OnLine Kar 4981, where the assessee was an individual engaged in the business of medical profession. He filed the return of income for the assessment year 2012-2013 on 28.09.2012 declaring total income of Rs.3,22,43,330/-. A search and seizure operation under Section 132 of the Act was conducted in the premises of the assessee on 12.04.2011 and during search, some books of accounts, notes and materials were seized. The assessee had admitted an amount of Rs.12.03 crores as an undisclosed income for the relevant years. However, the assessee incorporated the additional income disclosed in the return of income for assessment year 2011-2012. Thereafter, scrutiny proceedings under Section 143 (2) of the Act were initiated. The Assessing Officer, vide order dated 06.03.2014, held that the assessee had received 1,00,00,000 bonus shares issued by M/s Manipal Education and Medical Group (India) Pvt. Ltd. The Assessing Officer invoked the provisions of Section 56 (2) (vii) of the Act and treated the receipt of bonus shares as income from other sources and assessed the fair market value of the bonus shares at Rs.12,49,00,000/-. The assessee filed an appeal before the Commissioner of Income Tax (Appeals), which was allowed vide order dated 04.08.2015 on the ground that conversion of reserve into capital did not involve release of profit and therefore, provisions of Section 56 (2) (vii) of the Act were not applicable to the assessee and a direction was given for deletion of a sum of Rs.12,49,00,000/-. The Revenue went in appeal before the Income Tax

Appellate Tribunal. The Tribunal, vide order dated 22.10.2016, by referring to the decision given by Hon'ble the Supreme Court in ***CIT vs. Dalmia Investment Co. ltd.,*** 252 ITR 567, held that provisions of Section 56 (2) (vii) of the Act were not attracted to the fact situation of the case and dismissed the appeal preferred by the Revenue. The Revenue, thereafter, approached the High Court. The High Court of Karnataka, after going through the record, observed that the issue arose for consideration in the appeal was, whether the fair market value of bonus shares computed as per Rule 11U and Rule 11UA of the Income Tax Act could be considered as income from other sources as per Section 56 (2) (vii) of the Act. It was held that the above said section contemplates two contingencies, firstly, where the property was received without consideration and secondly, where it was received for consideration less than the fair market value. The issue of bonus shares by capitalization of reserves was merely a reallocation of the companies funds. There was no inflow of fresh funds or increase in the capital employed, which remained the same. The total funds available with the company remained the same and issue of bonus shares did not result in any change in respect of capital structure of the company. Hence, there was no addition or alteration to the profit making apparatus and the total funds available with the company remained the same. There was no material on record to infer that bonus shares had been transferred with an intention to evade tax, which was the object of the provision in question. The view expressed by the Commissioner of Income Tax (Appeals) as well as the Tribunal was upheld that **when there was an issue of bonus shares, the money remained with the company and nothing came to the shareholders as there was no transfer of the property** and provisions of Section 56 (2) (vii) (c) of the Act were not attracted. Finally, the appeal filed by the Revenue was dismissed. Learned counsel for the respondent further referred to the judgment passed by Hon'ble the Supreme Court in ***Khoday Distilleries Ltd. vs. Commissioner of Income Tax,*** 2009 (1) SCC 256, wherein the question for consideration was with respect to allotment of shares. In that case, the appellant-company allotted right share to seven shareholders as remaining shareholders did not subscribe for such shares. It was held that allotment of right shares was not a deemed gift under Section 4 (1) of the Gift Tax Act, 1958 as there is no transfer and the company was not held liable to gift tax.

7. Learned counsel for the respondent referred to another judgment passed by Hon'ble the Supreme Court in ***M/s Hunsur Plywood Works Ltd. vs. The Commissioner of Income Tax,*** 1998 AIR (SC) 340. In that case, the appellant was a public limited company. The appellant-assessee had filed return of income for the assessment years 1972-1973, 1973-1974 and 1974-1975 and claim towards allowance of development rebate under Section 33 of the Income Tax Act, 1961 was made. The assessing authority allowed the claim as made by the company. Subsequently, the assessing authority noticed from the balance sheet of the company that the company had made a transfer of sums from the development rebate reserve to share capitalization account by issue of bonus shares. The assessing authority concluded that the issuance of bonus shares amounted to distribution of profits by capitalization and thus, the assessing authority was of the view that the provisions of Section 155 (1) (ii) (a) of the Act applied to the instant case, as the development rebate reserve had been utilised for distribution by way of dividend or profits. The assessing authority passed an order under Section 154 of the Act withdrawing the

development rebate claim allowed earlier. Against the said order, the company filed an appeal, which was allowed by the appellate authority and claim of the appellant for development rebate was sustained. The Revenue went in appeal before the Tribunal, which concurred with the view taken by the first appellate authority. Thereafter, the Revenue filed an appeal before the High Court. The High Court, after examining the provisions of Section 34 (3) (a) (i) and Section 155 (5) (ii) (a) of the Income Tax Act, held that the issue of bonus shares resulted in distribution of profits and therefore, the statutory requirement of Section 34 (3) (a) (i) of the Act had been violated. The High Court answered both the questions in the negative and in favour of the Revenue. Feeling aggrieved, the assessee preferred an appeal before Hon'ble the Supreme Court. Hon'ble the Supreme Court examined the case of the assessee in view of the judgment passed in ***Inland Revenue Commissioners vs. Blott,*** (1921) AC 171. In this judgment, the mechanism and effect of issue of bonus shares have been explained by the English Courts. It has been held that an amount equal to the face value of the shares could not be regarded as received by the shareholders. A contrary view was taken by Lord Dunedin and Lord Sumner, who held that the word "capitalisation" was somewhat hazy and the amount that was capitalised had to be treated as to have been paid to the shareholders. Thereafter, Hon'ble the Supreme Court referred to another decision given in ***Commissioners of Inland Revenue vs. Fisher's Executors,*** (1926) AC 395, wherein the Court dealt with a case of a company, which had large undistributed profits. It decided to capitalise a part of these profits and distribute it *pro rata* among the ordinary shareholders as a bonus in the form of 5% debenture stock. The stock was duly issued, conditions providing that the Company might redeemed the stock after a certain time and in certain events. The question that came up for decision was, whether the bonus paid in the form of debenture stock was income in the hands of the shareholders and was, therefore, liable to super tax. It was held that the whole transaction was "bare machinery" for capitalization profits and involved no release of assets either as income or as capital. It was further observed as under:-

> "17. In our view, the principle stated by Lord Finlay really resolves the controversy raised in this case. The profits made by the Company may be distributed as dividends or retained by the Company as its reserve which may be used for improvement of the company's works, buildings and machinery. That will enable the company to make larger profits. There cannot be any dispute that the shareholders will benefit from the improvements brought about in the profit making apparatus of the Company. Likewise, if the accumulated profits are capitalised and capital base of the Company is enlarged, this may enable the Company to do its business more profitably. The shareholders will also benefit if the share capital is increased. They may benefit immediately by issue of bonus shares. But neither in the case of improvement in the profit making apparatus nor in the case of expansion of the share capital of the Company, can it be said that the shareholders have received any money from the Company. They may have benefited in both the cases. But, this benefit cannot be treated as distribution of the amount standing to the credit of any reserve fund of the Company to its shareholders."

8. Thereafter, Hon'ble the Supreme Court referred to the judgment passed in ***Commissioner of Income-Tax, Bihar vs. Dalmia Investment Co. Ltd.,*** (1964) 52 ITR 567, wherein Justice Hidayatullah, had preferred the view expressed by Viscounts Haldane, Finlay and Cave to the dissenting

view taken by Lord Dunedin and Lord Sumner. Hon'ble the Supreme Court held that "the floating capital used in the company which formerly consisted of subscribed capital and the reserves now becomes the subscribed capital of the Company." The certificates in the hands of the shareholders were property from which, income will be derived in future. Finally, the appeal of the assessee was allowed by observing that the view of the High Court that bonus shares amounted to distribution of accumulated profits of the company shown as Development Rebate Reserve Fund, was not correct.

9. In the facts of the present appeal(s), the ratio of the above said judgments, referred to by learned counsel for the respondent(s), applies in favour of the respondents-assessee.

10. Learned counsel for the appellant has not been able to cite any judgment passed by Hon'ble the Supreme Court, where the transfer of bonus shares has been held to be an income in the hands of the assessee, as in the case of transfer of shares, there was no distribution of profits to the share holders.

11. In view of the above discussion, no ground is made out to interfere in the impugned order(s). Resultantly, the present appeals i.e. ITA Nos.72, 75, 76, 79, 129 of 2018, filed by the Revenue, are dismissed.

(RITU BAHRI)
JUDGE

(MANISHA BATRA)
JUDGE

27.09.2023
ajp

Whether speaking/reasoned : Yes/No
Whether reportable : Yes/No