

आयकर अपीलिय अधिकरण, 'ए' न्यायपीठ, चेन्नई।
IN THE INCOME TAX APPELLATE TRIBUNAL
'A' BENCH: CHENNAI

श्री वी. दुर्गा राव, माननीय न्यायिक सदस्य एवं
श्री जी. मंजूनाथा, माननीय लेखा सदस्य के समक्ष
BEFORE SHRI V. DURGA RAO, HON'BLE JUDICIAL MEMBER AND
SHRI G. MANJUNATHA, HON'BLE ACCOUNTANT MEMBER

आयकर अपील सं./ITA No.582/Chny/2021
निर्धारण वर्ष /Assessment Year: 2009-10

The Dy. Commissioner-
of Income Tax,
Central Circle-1(1),
Chennai.

v. M/s.Univercell
Telecommunications India-
Pvt. Ltd.,
281, TTK Road, Chennai.

(अपीलार्थी/Appellant)

[PAN: AAACU 7742 G]
(प्रत्यर्थी/Respondent)

Department by : Mr. AR.V.Sreenivasan,
Addl.CIT

Assessee by : Mr.Shrenik Chordia, CA

सुनवाई की तारीख/Date of Hearing : 22.08.2022

घोषणा की तारीख /Date of Pronouncement : 07.09.2022

आदेश / ORDER

PER G. MANJUNATHA, ACCOUNTANT MEMBER:

This appeal filed by the Revenue is directed against the order of the Commissioner of Income Tax (Appeals)-16, Chennai, dated 30.09.2021 and pertains to assessment year 2009-10.

2. The Revenue has raised the following grounds of appeal:

1. The order of the Id. Commissioner of IT. (Appeals) is erroneous on facts of the case and in law.

2.1. The Id. CIT(A) erred in deleting the addition of Rs.3.47 crores, by holding that there was no capital gain on transfer of goodwill at book value, by wrongly placing reliance on the Id. CIT(A)'s order dated 24.02.2015 passed in the case of erstwhile proprietor (Shri.D. Sathish Babu) of the erstwhile proprietary concern for asst. year

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2006-07 which has no relevance at all to the impugned issue raised in the assessment order of the assessee company for asst. year 2009-10.

2.2. The Id. CIT(A) failed to appreciate that the A.O. in the impugned assessment order has subjected to assessment the gains arising from transfer of proprietary concern to assessee company on account of violation of the proviso to section 47(xiv) invoking section 47A(3) of the IT. Act, and has not sought to assess goodwill as misunderstood by the Id. CIT(A).

2.3. The Id. CIT(A) failed to appreciate that the erstwhile proprietor, Shri.D. Sathish Babu, transferred 16.67% of his shareholding in the assessee successor company to his brother-in-law, Shri.Shankar S. Nathan on 10.10.2008, i.e., within 5 years from the date of transfer of proprietary concern into assessee company which took place on 27.09.2005, and thus failed to retain the shareholding of not less than 50% in the assessee successor company for a period of 5 years from the date of transfer of proprietary concern, and thereby violated the proviso to section 47(xiv) triggering the application of section 47A(3) of the IT. Act, 1961, and assessability of the gains to tax.

2.4. The Id. CIT(A) ought to have noted that as per section 47A(3) of the IT. Act, 1961, when there is violation of the conditions of section 47(xiv), as in the instant case, the gains which were exempt should be brought to tax in the hands of the successor company which is the assessee company.

3. For these grounds and any other ground including amendment of grounds that may be raised during the course of the appeal proceedings, the order of Id. CIT(A) may be set aside and that of the Assessing Officer be restored.

3. The brief facts of the case are that M/s.Univercell Telecommunications, a proprietary concern of Mr.Sathish Babu, has been converted into a Pvt. Ltd. Co., under the name and style of M/s.Univercell Telecommunications India Pvt. Ltd., on 28.09.2005. Pursuant to conversion, the proprietary concern becomes a Pvt. Ltd. Co., and transfer of assets and liabilities of proprietary concern, has been treated as exempt as per provisions of Sec.47(xiv) of the Act. During the course of assessment proceedings, the AO noticed that although, the conversion of proprietary concern into a Pvt. Ltd. Co., is coming under the provisions of Sec.47(xiv) of the Act, but the assessee has violated the conditions prescribed therein by transferring shareholding of Mr.S.Satish Babu, within

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a period of five years from the date of transfer of proprietary concern and thus, invoked Sec.47A of the Act, and assessed difference between assets and liabilities of company as long term capital gains and added back to the total income of the assessee.

4. Being aggrieved by the assessment order, the assessee preferred an appeal before the Ld.CIT(A). Before the Ld.CIT(A), the assessee contended that assuming for a moment, provisions of Sec.47A will come into operation, because, of violation of certain conditions of Sec.47(xiv) of the Act, but there is no liability to capital gains tax, because, the difference between assets and liabilities determined by the AO by excluding cost incurred for brand value, has been ignored while computing long term capital gains and if you consider the cost incurred by the assessee at the books of accounts of proprietary concern, then, there will be no capital gains on transfer pursuant to conversion of proprietary concern into Pvt. Ltd. Co. The Ld.CIT(A) after considering the relevant submissions of the assessee and by taking note of the order of ITAT in the case of Mr.D.Satish Babu, Proprietor of erstwhile proprietorship concern observed that there was no capital gains on transfer of goodwill at book value, because, if you consider the cost incurred by the assessee for creation of goodwill, then, the capital gains on transfer of said goodwill become 'nil' and thus, deleted the additions made by the AO. The relevant findings of the AO are as under:

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4.3 I have considered the matter. The AO, in his order, stated that Department had not gone in further appeal against the order of Hon'ble ITAT in case of Shri D. Sathish Babu. In that case, the Ld.CIT(A) decided the matter as under:

"The next observation of the Assessing officer is that the goodwill shown in the books of the assessee was a self-generated asset where the cost of acquisition is Nil. This observation by the Assessing Officer is not correct. As explained by the assessee, the goodwill is not a self-generated goodwill. The assessee has been in the process of building the brand image by incurring substantial amounts of advertisements and capitalized the books in the form of goodwill in all the years up to the date of transfer of the business to the private limited company, (in fact it can be seen from the assessee's books of accounts, i.e. on 31/03/2005 the goodwill in the books was only Rs.2,06,50,000/- and as on 27/09/2005, the value of goodwill was Rs.3,47,95,733/-. This could be possible only on account of additions/further cost incurred during the period). Only those expenses (Advertisements etc) which have immediate benefit were taken to the P&L Account and claimed as revenue expenditure. Hence, the goodwill of Rs.3.47 crores appearing in the books as on 27/09/2005, was nothing but the expenses incurred in the form of advertisement and related expenses which have been capitalized by the assessee in his books. Therefore, since the goodwill of Rs.3.47 crores was the actual expenses incurred and capitalized in the books and since the sale value of the goodwill (by including the sale under the slump sale at book value) was also at Rs.3.47 crores, the capital gains will also be Nil. Hence the Assessing Officer's action of determining the long term capital gains of Rs.3.47 crores on transfer of goodwill is neither factually correct nor justified."

As stated earlier, the decision of CIT(A) had been confirmed by Hon'ble ITAT. Therefore, in case of this assessee also, it is held that there was no capital gain on transfer of goodwill at book value.

The grounds taken are allowed.

5. The Ld.DR submitted that the Ld.CIT(A) erred in deleting the addition of Rs.3.47 Crs. by holding that there was no capital gains on transfer of goodwill at book value by wrongly placing reliance on the order of the Ld.CIT(A) dated 22.04.2015 passed in the case of erstwhile Proprietor of the erstwhile proprietary concern for the AY 2006-07, which has no relevance at all to the impugned issue raised in the assessment order. The Ld.DR referring to provisions of Sec.47A(3) r.w.s.47(xiv)(b) of the Act, submitted that in order to be exempt from capital gains tax on conversion of proprietary concern into Pvt. Ltd. Co., the assessee should satisfy certain conditions, as per which, the shareholding of erstwhile Proprietor and now

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Director cannot be transferred or reduced below specified percentage within five years from the date of conversion. In this case, the assessee has transferred 16.67% of his shareholding to his brother-in-law Mr.Shankar S.Nathan on 10.10.2008 within five years from the date of transfer of proprietary concern and thus, violated the provisions of Sec. 47(xiv)(b) of the Act, and consequently, provisions of Sec.47A(3) of the Act, would come into operation and as per which, capital gains on conversion, needs to be taxed in the hands of the assessee company. The Ld.CIT(A) without appreciating above facts, simply allowed relief to the assessee.

6. The Ld.AR for the assessee supporting the order of the Ld.CIT(A), submitted that no doubt the assessee has violated certain conditions prescribed u/s. 47(xiv)(b) of the Act, and thus, capital gains, if any derived from transfer of proprietary concern into Pvt. Ltd. Co., is taxable by virtue of withdrawal of exemption as per the provisions of Sec.47A(3) of the Act. However, facts remain that in the given case, there is no question of any capital gains, because, on conversion of proprietary concern into Pvt. Ltd. Co., the assessee has transferred all assets and liabilities at book value without any revaluation and thus, question of determination of capital gains does not arise. The Ld.CIT(A) after considering the relevant facts has rightly deleted the additions made by the AO and their orders should be upheld.

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7. We have heard both the parties, perused the materials available on record and gone through orders of the authorities below. M/s.Univercell Telecommunications, proprietary concern of Mr.Sathish Babu.D, was taken over by the assessee company on 28.09.2005 in terms of Sec.47(xiv)(b) of the Act. It is an undisputed fact that when proprietary concern was converted into a Pvt. Ltd. Co., conditions of Sec.47(xiv)(b) of the Act, has been satisfied. However, at later date, Mr.Satish Babu.D has transferred 16.67% of his shareholding to Mr.Shankar S.Nathan on 10.10.2018 i.e. within five years from the date of transfer of proprietary concern into the assessee company and thus, breached the conditions prescribed u/s. 47(xiv)(b) of the Act, i.e. retaining not less than 50% of the shares of successor company for a period of five years from the date of transfer of proprietary concern. Therefore, we are of the considered view that the assessee is hit by provisions of Sec.47A(3) of the Act, and as per the said provision, if certain conditions are violated, then, exemption granted u/s. 47(xiv)(b) of the Act, needs to be withdrawn for the impugned assessment year. To this extent, we cannot find fault with the findings of the AO. But, fact of the matter is that even after invoking the provisions of Sec.47A(3) of the Act, there cannot be any liability of capital gains on conversion of proprietary business into Pvt. Ltd. Co., because, the assessee has transferred all assets and liabilities of erstwhile proprietary ship into Pvt. Ltd. Co., on book value including so called goodwill of Rs.3.47 Crs. considered by the AO for taxation. As per the details filed by the assessee,

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goodwill considered by the AO is not self-generated but created by the erstwhile proprietary concern before assets and liabilities have been transferred to Pvt. Ltd. Co., which is evident from the fact that the assessee has filed necessary details of expenditure incurred for generation/creation of goodwill in the books of accounts of proprietary concern. Further, this fact is strengthened by the findings of the order of the Ld.CIT(A) in the case of Mr.D.Sathish Babu for the AY 2006-07, where the Ld.CIT(A) had categorically find that the assessee has spent a sum of Rs.3.47 Crs. towards goodwill and on account of transfer of proprietary concern to a Pvt. Ltd. Co., there will not be any capital gains. The ITAT Chennai in ITA No.1807/Mds/2015 order dated 31.01.2016 had upheld the findings of the Ld.CIT(A) in the case of Mr.Satish Babu and held that since the assessee has generated goodwill by paying consideration, on transfer of said goodwill, capital gains become 'nil'. From the above, it is very clear that even if you invoke the provisions of Sec.47A(3) of the Act, to withdraw exemption granted u/s.47(xiv)(b) of the Act, but, in principle there cannot be any capital gains on transfer of goodwill, because, said goodwill is not self-generated or created on account of conversion of proprietary concern into a Pvt. Ltd. Co., but acquired by incurring cost. If you consider cost incurred by the assessee for acquiring goodwill, then, capital gains on transfer of said goodwill would come to 'nil' amount. The Ld.CIT(A) after considering the relevant facts has rightly deleted the additions made by the

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AO. Hence, we are inclined to uphold the findings of the Ld.CIT(A) and dismissed the appeal filed by the Revenue.

8. In the result, the appeal filed by the Revenue is dismissed.

Order pronounced on the 07th day of September, 2022, in Chennai.

Sd/-

(वी. दुर्गा राव)

(V. DURGA RAO)

न्यायिक सदस्य/**JUDICIAL MEMBER**

चेन्नई/Chennai,

दिनांक/Dated: 07th September, 2022.

TLN

आदेश की प्रतिलिपि अग्रेषित/**Copy to:**

1. अपीलार्थी/Appellant
2. प्रत्यर्थी/Respondent
3. आयकर आयुक्त (अपील)/CIT(A)

Sd/-

(जी. मंजूनाथा)

(G. MANJUNATHA)

लेखा सदस्य/**ACCOUNTANT MEMBER**

4. आयकर आयुक्त/CIT
5. विभागीय प्रतिनिधि/DR
6. गार्ड फाईल/GF