

Status of the company at the time of change in shareholding is relevant to determine applicability of section 79 of the Income-tax Act, 1961

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In brief

The Mumbai bench of the Income-tax Appellate Tribunal (Tribunal) ruled¹ that, for the purpose of applicability of section 79 of the Income-tax Act, 1961 (the Act) the status of the company at the time of change in shareholding is relevant. Section 79 will apply to a company becoming widely held company pursuant to the change in shareholding.

In detail

Facts

The taxpayer was a closely held company with shareholders as on 1 April, 2010.

- During assessment year (AY) 2011-12, the entire shares of the taxpayer was acquired by a 100% subsidiary of a listed company.
- The taxpayer in its return of income for AY 2011-12 sought set off of brought forward losses of AY 2010-11.
- In view of the change in the shareholding exceeding 51%, the tax officer disallowed the claim of set off of brought forward losses as per section 79 of the Act.
- The Commissioner of Income-tax (Appeals)

allowed set off of brought forward losses.

- Aggrieved, the tax authorities filed an appeal with the Tribunal.

Issue before the Tribunal

Based on the facts of the case, whether section 79 of the Act is applicable to the taxpayer?

Revenue's contentions

- The taxpayer was not a company in which public was substantially interested at the time when it was acquired by 100% subsidiary of the listed company.
- The taxpayer had become a company in which public was substantially interested post the acquisition.
- Therefore, the provisions of section 79 of the Act would be applicable to the

taxpayer.

Taxpayer's contentions

- Since 100% of its shares were held by a 100% subsidiary of a listed company, it was a "company in which public was substantially interested".

Therefore, the provisions of section 79 of the Act, would not be applicable.

Tribunal's ruling

- A company in which public are not substantially interested is referred to as a "closely held company", otherwise, it's referred to as "widely held company".
- The provisions of section 79 of the Act would apply if the following two conditions are satisfied:
 - (a) a change in the

¹ I.T.A No. 1501/Mum/2016

shareholding has taken place (exceeding 49%); and

- (b) the company was a closely held company at the time when the change has taken place.
- Section 79 of the Act, was introduced as an anti-abuse provision intended to curb taxpayers attempting at transferring losses incurred by a corporate entity by means of transfer of shareholding.
- Viewed from the object of

introducing the provisions of section 79 of the Act, it was held that the status of the company at the time when change in shareholding took place was relevant to determine the applicability of provisions of section 79 of the Act. If it was a closely held company at that point of time then the provisions of section 79 of the Act would apply and *vice-versa*.

- In the instant case, the taxpayer was a closely held company at the time when

change in shareholding took place. It had become widely held company after the change in shareholding. Therefore, the Tribunal held that the provisions of section 79 would apply to the taxpayer, and was not entitled to set off brought forward losses relating to AY 2010-11 and earlier years.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact your local PwC advisor

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