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Gift of shares by a foreign company prior to June 2010 treated as capital receipt, exempted under section 47(iii) of the Act

In brief

Recently, in the case of DP World Pvt. Ltd.¹ (the assessee), the Mumbai Income-tax Appellate Tribunal (the Tribunal) held that the gift of shares of an Indian company by a foreign company without consideration has to be treated as a gift within the meaning of section 47(iii) of the Income-tax Act, 1961 (the Act). Such gift of shares is a capital receipt and is neither taxable under section 56 of the Act nor under section 28(iv) of the Act in the hands of the assessee. The case pertained to assessment year (AY) 2008-2009 and thus, the amendments in section 56(2)(vii) of the Act were not applicable.

¹ DP World Pvt Ltd v. DCIT [TS-767-ITAT-2012(Mum)]

Facts

- The assessee, a company incorporated in India, is a wholly-owned subsidiary of Peninsular & Oriental Steam Navigation Co (POSN), a UK-based entity, which in turn is a 100% subsidiary of DP World Ltd, a Dubai-based entity.
- POSN owned 100% of another company viz British India Steam Navigation Co. (BISNCL), UK that held shares of Hill Park Ltd. (a company incorporated in India). By virtue of the said holding in Hill Park Ltd, BISNCL was entitled to use and occupy three residential flats that were owned by it. During the assessment year under consideration, BISNCL gifted the shares in Hill Park Ltd. under a gift deed dated 27 December 2007 to the assessee.

- The assessing officer (AO) held receipt of flats at Hill Park as income in the hands of the assessee under section 56(1) of the Act.
- The Commissioner of Income-tax (Appeals) (CIT(A)) confirmed the addition made by the AO but held that the income should be taxable as 'profit and gains from business and profession' under section 28(iv) of the Act.

Issue before the Tribunal

Among other issues, the key issue raised for consideration was whether the gift of shares of an Indian company by a foreign company without consideration will be treated as a gift within the meaning of section 47(iii) of the Act or whether the same shall be treated as income under the hands of the recipient or the donee and will be taxable under section 56 or section 28 of the Act.

Assessee's contentions

- The receipt of interest in residential apartments from BISNCL is on account of gift of shares which is a capital receipt and not chargeable to tax under the provisions of the Act.
- The receipt can neither be categorised as income from other sources under section 56 of the Act nor as business income under section 28(iv) of the Act.

Revenue's contentions

- A gift cannot be logically made by one artificial juridical entity to another because the basic condition of love and affection for making gifts does not exist between such artificial entities which are emotion neutral. The transfer has been given the color of a gift and is for business convenience.
- Any income can only be excluded from the total income of the assessee, if the Act specifically provides for such exemption. In this case, no exemption is

specifically provided for such income. Thus, the income arising in the hands of the assessee on receipt of properties is not to be excluded from its total income and should be taxable under the provisions of section 56 of the Act.

Tribunal ruling

The following was observed and held:

- Since the expression 'gift' is not defined under the Act, the **Tribunal** referred to the definition of gift under the Gift Tax Act, 1958 and the Transfer of Property Act, 1882.
- It held that the meaning of 'gift' as per Gift Tax Act, 1958 should not be imported for the purpose of section 47(iii) of the Act in accordance with the decision of the Calcutta High Court in the case of Shyam Narain Mehrotra².
- It was further held that under the Transfer of Property Act, 1882 there is no restriction that a 'gift' can be made only between natural persons out of love and affection. Therefore, a company can gift shares and such transaction may appear as 'strange' transaction but cannot be treated as a 'non-genuine' transaction.
- It observed that the company giving the gift or donor must be legally authorised to do so as per the laws of the country in which it is incorporated. The same may be permitted by the articles of association of such a donor company. In **this** case, it was factually established that BISNCL was authorised to make such a gift.
- The Tribunal ruled that the transaction is of a gift, which is a capital receipt in the hands of the assessee and therefore, it cannot be said to be a case of any benefit or perquisite arising from business. Thus, the provisions of section

² CIT v. **Shyam Narain Mehrotra** [1981] 122 ITR 313 (Cal)

28(iv) of the Act are not applicable. Simply because both the donor and the donee happened to belong to the same group cannot *ipso facto* establish that they have any business dealings.

- Section 56(2)(viiia) of the Act covers the issue involved in the present appeal and is made applicable for the transactions effected after 1 June 2010. Thus, the provisions of section 56(2) of the Act are not attracted in the present case.
- Accordingly, the gift of shares without consideration will be regarded as a capital receipt exempted under section 47(iii) of the Act and will not be taxable in India.

Conclusion

The gift of shares of an Indian company by a foreign company without consideration will be treated as a gift within the meaning of section 47(iii) of the Act and is a genuine transaction as it is not uncommon that transfer of shares between corporate groups takes place for internal reorganisation.

A similar view was taken by the Karnataka High Court in the case of Nadatur Holdings³ wherein it was held that a gift of shares by the shareholders to the company is a valid and a genuine transaction.

One also needs to consider the recent ruling by the Authority for Advance Rulings in the case of Orient Green Power Pte Ltd⁴ wherein it was held that inter-corporate gifts are 'strange' transactions and that such transactions may not be eligible for exemption under section 47(iii) of the Act, as it covers only gifts made by an individual, joint Hindu family or a human agency. The AO was directed to determine the validity and genuineness of the transaction in this case.

³ CIT v. Nadatur Holdings and Investment Pvt Ltd. [TS-656-HC-2012(Kar)]

⁴ Orient Green Power Pte Ltd . *In re*. [TS-608-AAR-2012]

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