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Transfer of shares through a share transfer agreement including indirect transfer of immovable property does not invoke deeming fiction of section 50C

In brief

In the case of Irfan Abdul Kader Fazlani¹ (the assessee), the Mumbai Income-tax Appellate Tribunal (Tribunal) held that provisions of section 50C of the Income-tax Act, 1961 (the Act) have to be interpreted strictly and should not be invoked for the computation of capital gains on transfer of shares of the company. The case pertains to assessment year (AY) 2007-08.

Facts

- The assessee, a shareholder in Kamala Mansion Pvt. Ltd. (KMPL), transferred his portion of shares to third parties for a consideration and offered the gain arising on sale of shares as long-term capital gains in the relevant AY.
- KMPL owns two flats in Mumbai, which are regularly given on rent. The rent is declared by the assessee as 'income from the house property'.
- The assessing officer (AO) concluded that sale of shares is an indirect way of transferring the immovable properties. Hence, provisions of section 50C of the

¹ Irfan Abdul Kader Fazlani v ACIT [TS-21-ITAT-2013 (Mum)]

Act are applicable to the transfer of shares. The AO treated this as an eligible case for piercing the corporate veil.

- Further, the amount paid by the transferee to KMPL to clear its liabilities towards the assessee has been treated as a sale consideration in the hands of the assessee, as the latter being a director received his dues from the company.
- The Commissioner of Income-tax (Appeals) (CIT(A)) confirmed the view of the AO.

Issues

- Whether the provisions of section 50C can be invoked even though the documents for sale of shares were not required to be registered with the stamp authorities.
- Whether the additional money received by the assessee through KMPL is sales consideration for the sale of shares.

Revenue's contentions

- The orders of AO and CIT(A) were relied upon and it was contended that there is a need to pierce the corporate veil.

Assessee's contentions

- Provisions of section 50C are deeming provisions and the meaning of the same cannot be extended as the provisions have to be strictly interpreted as held in the decision in the case of Shrishakti Trading Co ².

² CIT v. Shrishakti Trading Co [1994] 207 ITR 442 (Bom)

- Section 50C is not applicable as the agreement is for sale of shares. The assessee placed reliance on various judicial precedents³.
- The Finance Act (No. 2), 2009 substituted the expression 'assessable' in section 50C of the Act prospectively to enable the AO to adopt the same valuation even though agreement for the sale of immovable property is not registered and no stamp duty is adjudicated. In the given case, the relevant assessment year is AY 2007-08.
- For lifting of the corporate veil, the assessee relied on the following arguments among others:
 - KMPL is a separate legal entity distinct from its shareholders.
 - As per the Supreme Court's decision in Vodafone International Holding BV⁴, to lift the corporate veil, the revenue has to look at the transaction as a whole and not adopt a dissecting approach.
 - The corporate veil has been wrongly lifted based on facts that KMPL was incorporated 38 years back and the property was purchased 20 years back.

Tribunal ruling

- The expression 'assessable' was inserted into the statute for prospective application effective 1 October, 2009 which is not applicable to the relevant AY.
- Section 50C of the Act is a deeming provision and has to be interpreted strictly in accordance with the spirit of the provisions. The expression 'transfer' shall

³ Carlton Hotels Pvt Ltd v ACIT [2009] 122 TTJ 475 (Luck), Ran Mal Bhansali v ACIT [2012] 143 TTJ 65 (Jd) (UO), Navneet Kumar Thakkar v ITO [2008] 298 ITR 42 (AT) (JP) and Vijay Laxmi Bhadhha v ITO [2009] 20 DTR 365 (JP)

⁴ Vodafone International Holding BV v. UOI [2012] 341 ITR 1 (SC)

mean direct transfer as defined under section 2(47) of the Act. The AO's decision to invoke provisions of section 50C of the Act to the tax planning adopted by the assessee does not have the sanction of the provisions of the Act.

- The shares in the company have been transferred by the assessee and not the land or building or both as envisaged in section 50C of the Act. The assessee also does not have full ownership on the flats owned by KMPL.
- The transfer of shares was never a part of the assessment of the stamp duty authorities of the state government.
- In regards to the additional consideration, the transaction actually took place between the transferee and KPML and the assessee only received his dues. The dues received by the assessee cannot be equated with the additional sales consideration.

Conclusion

Though this appeal dealt with an AY prior to insertion of the term 'assessable' in section 50C of the Act, the ruling would be useful defense for transfer of shares or an indirect transfer of immovable property based on facts. The length of holding of shares and property could be used to defend against lifting the 'corporate veil'.

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