आयकर अपीलीय अधिकरण "C" न्यायपीठ मुंबई में।

IN THE INCOME TAX APPELLATE TRIBUNAL "C" BENCH, MUMBAI

श्री महावीर सिंह, न्यायिक सदस्य एवं श्री एन. के. प्रधान लेखा सदस्य के समक्ष ।

BEFORE SRI MAHAVIR SINGH, JM AND SRI N.K. PRADHAN, AM

आयकर अपील सं./ ITA No. 1944/Mum/2018

(निर्धारण वर्ष / Assessment Year 2012-13)

Periar Trading Company Private Limited
147-Jussawalla Wali, Juhu Tara Road,
Juhu, Mumbai-400 049
Maharashtra ...... **(अपीलार्थी / Appellant)**

Vs.

Income Tax Officer 10(3)(3)
Aayakar Bhavan, M.K. Road
Mumbai-400 020 ...... **(प्रत्यर्थी / Respondent)**

स्थायी लेखा सं./**PAN No. AACCP0593L**

अपीलार्थी की ओर से / **Appellant by**	:	Shri Percy Pardiwala, Shri Jeet Kandar, ARs'
प्रत्यर्थी की ओर से / **Respondent by**	:	Shri Somnath M. Wagale, DR

सुनवाई की तारीख / **Date of hearing:**	13-08-2018
घोषणा की तारीख / **Date of pronouncement :**	09-11-2018

आदेश / O R D E R

PER MAHAVIR SINGH, JM:

This appeal of assessee is arising out of the order of Commissioner of Income Tax (Appeals)-17, Mumbai [in short CIT(A)], in appeal No. CIT(A)-17/IT-251/15-16 dated 16.02.2018. The Assessment was framed

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by the Income Tax Officer, Ward 10(3)(3), Mumbai (in short 'ITO'/ AO) for the A.Y. 2012-13 vide order dated 25.03.2015 under section 143(3) of the Income Tax Act, 1961 (hereinafter 'the Act').

2. The first issue in this appeal of assessee is against the order of CIT(A) confirming the action of the AO in making the addition on account of conversion of cumulative and compulsory convertible preference shares (CCPS) into equity shares treating the same as transfer within the meaning of section 2(47) of the Act and accordingly, computing the long term capital gain as per section 45 of the Act. For this assessee has raised the following ground No. 1: -

> *"1. The Hon'ble Commissioner of Income-tax (Appeals)-17, Mumbai [CIT(A)] has erred in law and on facts and in circumstances of the case by confirming the addition made by the learned Assessing Officer on account of conversion of Cumulative Compulsory Convertible Preference Shares (CCPS) into equity shares as transfer within the meaning of section 2(47) of the act and computing Long-term capital gains of ₹ 2,55,46,266/- as per section 45 of the Act on the said conversion."*

3. Briefly stated facts relating to this issue are that the AO noted from the schedule of non-current investment forming part of balance sheet of the assessee as on 31.03.2012 that during the previous year 2011-12 relevant to AY 2012-13, the assessee company held 51,634 number of CCPS series A of Trent Ltd. as investment and converted the same into equity shares. According to AO, the conversion of CCPS into equity shares is transfer within the meaning of the definition provided in section 2(47)(i) of the Act. According to AO, the amount of ₹ 2,85,01,968/- being difference of market value of 51,634 number of equity shares of Trent Ltd. as on 10.09.2011 and the cost of the acquisition of equal number of

CCPS A series of Trent Ltd., which were completed into equity shares are taxable capital gain on account of transfer of shares by way of exchange. The assessee contested the action of the AO but AO finally added the same as taxable long term capital gain amounting to ₹ 2,55,46,266/-. Aggrieved, assessee preferred the appeal before CIT(A).

4. The CIT(A) considered the assessment order and also the submissions of the assessee and noted that this issue is covered by the decision of Hon'ble Bombay High Court in the case of CIT vs. Santosh L.Chowgule and others [1998] 234 ITR 787 (Bom.), wherein Hon'ble Bombay High Court has categorically held that preference shares and equity shares are different. The CIT(A) further noted that in the said decision the court relied on the decision of Hon'ble Andhra Pradesh High Court in the case of Addl. CIT vs. Trustees of H.E.H. The Nizam's Second Supplementary Family Trust (1976) (102 ITR 248) (AP), in that decision Hon'ble Andhra Pradesh High Court has categorically held that conversion of preference shares into equity shares is nothing but bartar, which constitute transfer by way of exchange within the meaning of section 45 of the Act. The CIT(A) also noted that Hon'ble Andhra Pradesh High Court has further relied on the decision of Hon'ble Supreme Court in the case of CIT v. Motors & General Stores (P.) Ltd [1967] 66 ITR 692 (SC) and the ratio of the case is clearly applicable to the case of the assessee. Accordingly, the CIT(A) confirmed the action of the Assessing Officer. Aggrieved, now assessee is in second appeal before Tribunal.

5. Before us, the learned Counsel for the argued that the compulsory conversion of preference shares on a specific date into equity is without any further consideration and without any further action and the preference shares were listed on the stock exchange and were freely tradeable. The assessee could have sold the CCPS which the assessee has not done and choose to get converted into equity shares on the pre

specified date. The learned Counsel for the assessee drew our attention to circular issued by CBDT dated 12.05.1984 vide F No. 12/1/64-IT(A). Ld Senior Counsel Sh Pardiwala argued that this circular as, referred in case of ITO vs. Vijay M. Merchant (1986) 19 ITD 510 (Mum)] reads as under:

> *"Where one type of shares is converted into another type of share (including conversion of debentures into equity shares), there is, in fact, no 'transfer' of a capital asset within the meaning of section 2(47) of the Income Tax Act, 1961."*

6. Hence, any profits derived from such conversion are not liable to capital gains tax under section 45(1) of the Act. However, when such newly converted share is actually transferred at a later date, the cost of acquisition of such share for the purpose of computing the capital gains shall be calculated with reference to the cost of the acquisition of the original share of stock from which it is derived. At such, the circular being beneficial to the assessee, has to be adopted by the Income Tax Department without any option. Accordingly, no capita gain tax liability arose upon the conversion. In case, and otherwise also the circular is perfectly in consonance with the legislative intention as well as the legislative scheme of taxing capital gain. This is evident from section 55(2)(b)(v)(e). Simply put, it is provided that where the capital asset being share of company, became property of the asset on conversation of any kind of shares of the company into another kind the cost of acquisition for the purpose of computing capital gain would be the cost of acquisition calculated with reference to the cost of acquisition of shares from which such asset is derived. In other words, when the equity shares, so received by the assessee upon such conversion are sold later on, while computing capital gain tax liability, its cost of acquisition would be the

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cost of subscribing the CCPS and not intermediate value. Thus, it is clear that the legislature itself has chosen to ignore the intermediate even of conversion for taxation purposes. If there arises any capital gain tax event upon such conversion, then the cost of acquisition would be the consideration adopted while computed such capital gain. However, by specifically providing so in section 55(2)(b)(v)(e), the legislative intention is made clear to regard such conversion as tax neutral. It should be also appreciated that logically also this view is name more sound, specifically taking into account the peculiar facts that the conversion was automatic and mandatory and the entire price was paid at the time of application of CCPS itself. In other words, what the assessee paid at the time of application of CCPS was not merely towards subscription of CCPS but also towards the automatic and compulsory conversion of CCPS into equity share within such a short period after subscription of CCPS. In other words, the seed to get converted share was already sown at the time of subscription CCPS itself. So to say the equity shares was already embedded at the time of issue of CCPS itself, the conversion only blossomed that right into fully grown equity share in fact the consideration can said to be more towards such equity share. In view of these arguments and also refereed precedents which we will cites during our further discussion.

7. On the other hand, the ld. Senior DR relied on the assessment order and the order of the CIT(A).

8. We have heard the rival contentions and gone through the facts and circumstances of the case. The facts of the case are that the assessee-company is engaged in the business of investment activities and is also a partner in a registered partnership firm, M/s S.P. Corporation from which it receives share of profit. During the financial year 2010-11 relevant to the assessment year 2011-12, assessee made

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investment in 51634 Cumulative Convertible Preference Shares (CCPS) of Series A of Trent Ltd. amounting to Rs.2,83,98,700/- on a rights issue basis. The price of the above CCPS was at Rs.550/- per share and the entire issue price was paid on application itself. As per the terms of the Scheme for issue of CCPS, one CCPS of Series A will compulsorily and automatically get converted into one fully paid up equity share of Rs.10/-. Accordingly, in terms of the above Scheme, assessee was allotted one equity share of Trent Ltd. for every preference share held in Trent Ltd., i.e. 51634 CCPS. Such conversion was compulsory and automatic. There was neither any option with the assessee nor any further step that was required to be taken by the assessee for conversion, being compulsory and automatic. The Assessing Officer while framing the assessment considered the conversion of CCPS into equity shares as 'transfer' within the meaning of Sec. 2(47) of the Act and brought to tax under Long Term Capital Gains an amount of Rs.2,55,46,266/-. The CIT(A) also confirmed the action of the Assessing Officer exactly on the same reasoning. Now, we have to consider whether any transfer of a capital asset has taken place or not. The provisions of Sec. 45(1) of the Act bring into tax the profits or gains arising from transfer of a capital asset under the head 'Capital Gains' in case there is a capital asset, there is transfer of such capital asset and there is gain arising out of such transfer of such capital asset. The Assessing Officer relying on the definition of 'exchange' as per the Black's Law Dictionary, deluxe fourth edition held that conversion of preference shares into equity shares will be treated as 'transfer' within the meaning of Sec. 2(47) of the Act, whereas the assessee argued from the beginning that there has been a conversion of one type of share into other type of share and, as such, same cannot be stated as an 'exchange' of assets within the meaning of Sec. 2(47) of the Act as held by the Assessing Officer.

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9. Before us, the ld. Counsel for the assessee relied on the CBDT Circular F. No. 12/1/84-IT(AI) dated 12.05.1964 which states that where one type of share is converted into another type of share, there is no 'transfer' of capital asset within the meaning of Sec. 2(47) of the Act. The Circular also states that the same has been issued to clarify that there is no capital gain u/s 45(1) or u/s 45(2) of the Act on conversion of one type of share into another. It also states that where the newly converted share is transferred at a later date, then, the cost of acquisition of such share for the purpose of computing the capital gain tax shall be calculated with reference to the cost of acquisition of the original share from which it is derived. The ld. Counsel for the assessee before us cited the relevant portion of the said Circular, which reads as under:-

> *".....Section 14 of the Finance Act, 1964, introduces a new clause (v) in sub-section (2) of section 55 of the Income-tax Act, 1961, laying down the method for determining the cost of acquisition of a new share which becomes the property of the assessee on conversion of one type of share into another type of share. A question has been raised whether the transaction of conversion of one type of share into another attracts the capital gains tax under Section 45(1).... The position in this regard is as follows :*
>
> *(1) Where one type of share is converted into another type of share (including conversion of debentures into equity shares), there is, in fact, no 'transfer' of a capital asset within the meaning of section 2(47) of the Income-tax Act, 1961. Hence, any profits derived from such conversion are not liable to capital gains tax under section 45(1) of the Income-tax Act. However, when such newly*

> *converted share is actually transferred at a later date, the cost of acquisition of such share for the purposes of computing the capital gains shall be calculated with reference to the cost of acquisition of the original share of stock from which it is derived."*

10. We have gone through the jurisdictional Tribunal's decision in the case of ITO vs Vijay M. Merchant, [1986] 19 ITD 510 (Bom.) and noted that the Tribunal placing reliance on the CBDT Circular (supra) held as under :-

> *"........according to the circular, when the shares which are converted and are sold, capital gains are to be calculated on the basis of cost of original shares. Thus, the factum of conversion does not make any material difference in calculating the capital gains....... the circular of the Government to which we have made reference above, clearly lays down that there is no transfer when one type of share is converted into another type of share...."*

11. We have gone through the provisions of Sec. 48 of the Act which specifies the mode of computation of capital gain, which makes it clear that the provision regarding computation of capital gain contemplates ascertainment of the full value of consideration received or accruing as a result of transfer of capital asset. The word 'received' means actually received and the word 'accruing' means the debt created in favour of the assessee as a result of the transfer. According to us, in any case, both the terms are used as actual and not estimated amounts. The provision does not contain words to the effect 'fair market value'. The Id. Counsel for the assessee before us has distinguished the case law of the Hon'ble Bombay High Court in the case of CIT vs Santosh L. Chowgule, 234 ITR

787 (Bom.) wherein it is stated that the preference shares and equity shares are held to be different. The ld. Counsel drew our attention to para 5 of the judgment of the Hon'ble Bombay High Court to narrate the facts, which read as under:-

> *5. We have carefully considered the rival submissions. The controversy in this case is whether the irredeemable preference shares issued by the company pursuant to its resolution dated 30-9-1971 are different from the equity shares in lieu whereof they were issued and whether they can be deemed to have been held by the assessee from the date of their issue or from the date of issue of the equity shares in lieu whereof they were issued. This controversy assumes importance because if the date of the issue of the irredeemable preference shares is regarded as the date of the acquisition of these shares by the assessee, the loss suffered by the assessee by the transfer thereof would be a short-term capital loss which can be set off against the income under any other head, whereas, if they are deemed to have been held by the assessee from the date of acquisition of the original equity shares in exchange for which they were issued, the date of acquisition would be the year 1965 and the loss suffered by the assessee on the transfer thereof would be a long-term capital loss which cannot be adjusted against the income under any other head of income."*

12. Subsequently, the ld. Counsel took us through para 7, wherein discussion regarding different kinds of shares held by the assessee and finally discussed the issue as under:-

> *"7. Equity share capital", on the other hand, has been defined to mean share capital which is not preference share capital. The rights and obligations attached to the two kinds of share capital are different. On the face of the above provisions of the Companies Act, it is not possible to hold that the equity shares held by the assessee since 1965 and the irredeemable preference shares acquired by the assessee in exchange thereof pursuant to the resolution dated 30-9-1971 were the same. That being so, the preference shares in question cannot be said to be acquired by the assessee prior to 30-9-1971, the date on which they came into existence. In fact, consequent to the resolution dated 30-9-1971, the equity share capital held by the assessee was exchanged for the three new types of equity shares and the irredeemable preference shares in question. It was not a case of change of nomenclature of the shares. It was an exchange of one kind of shares for another kind of shares, having different rights and liabilities."*

13. The ld. Counsel for the assessee in view of the above argued that the decision of the Hon'ble Bombay High Court in the case of Santosh L. Chowgule (supra) and the decision of the Hon'ble Andhra Pradesh High Court in the case of Addl. CIT vs. Trustees of H.E.H. The Nizam's Second Supplementary Family Trust, 102 ITR 248 (AP) are not applicable. The ld. Counsel further drew our attention to the decision of the Hon'ble Supreme Court in the case of CIT vs Gillanders Arbuthnot & Co., 66 ITR 622 (SC), wherein it is specifically held as under :-

> *"It is manifest that the consideration for the transfer of capital asset is what the transferor receives in lieu of the asset he parts with, namely, money or money's worth and,*

therefore, the very asset transferred or parted with cannot be the consideration for the transfer. It follows that the expression "full consideration" in the main part of section 12B(2) of 1922 Act cannot be construed as having a reference to the market value of the asset transferred but the expression only means the full value of the thing received by the transferor in exchange for the capital asset transferred by him. The consideration for the transfer is the thing received by the transferor in exchange for the asset transferred and it is not right to say that the asset transferred and parted with is itself the consideration for the transfer. The main part of section 12B(2) of 1922 Act provides that the amount of a capital gain shall be computed after making certain deductions from the "full value of the consideration for which the sale, exchange or transfer of the capital asset is made". In case of a sale, the full value of the consideration is the full sale price actually paid. The legislature had to use the words "full value of the consideration" because it was dealing not merely with sale but with other types of transfer, such as exchange, where the consideration would be other than money. If it was held in the present case that the actual price received by the respondent was at the rate the shares were transferred, the full value of the consideration must be taken at the same rate. In the first proviso to section 12B(2) of 1922 Act the expression "full value of the consideration" is used in contradistinction with "fair market value of the capital asset" and there is an express power granted to the ITO to "take the fair market value of the capital asset transferred" as "the full value of the consideration" in specified circumstances. It is evident that the legislature itself has made a distinction between

> *the two expressions "full value of the consideration" and "fair market value of the capital asset transferred" and it is provided that if certain conditions are satisfied as mentioned in the first proviso to section 12B(2) of 1922 Act, the market value of the asset transferred though not equivalent to the full value of the consideration for the transfer, may be deemed to be the full value of the consideration."*

14. The ld. Counsel also drew our attention to the decision of Hon'ble Bombay High Court in the case of CIT vs Texspin Engg. & Mfg. Works, 263 ITR 345 (Bom.), wherein the issue of full value of consideration received/accrued u/s 48 r.w.s 45(4) of the Act has been discussed and held as under :-

> *"Now, in the present case, it is argued on behalf of the department before the Tribunal, for the first time, that in this case, on vesting of the properties of the erstwhile Firm in the Limited Company, there was a transfer of capital assets and, therefore, it was chargeable to income-tax under the head "Capital gains" as, on such vesting, there was extinguishment of all right, title and interest in the capital assets qua the Firm. We do not find any merit in this argument. In the present case, we are concerned with a Partnership Firm being treated as a company under the statutory provisions of Part IX of the Companies Act. In such cases, the Company succeeds the Firm. Generally, in the case of a transfer of a capital asset, two important ingredients are : existence of a party and a counterparty and, secondly, incoming consideration qua the transferor. In our view, when a Firm is treated as a Company, the said two conditions are not attracted. There*

is no conveyance of the property executable in favour of the Limited Company. It is no doubt true that all properties of the Firm vests in the Limited Company on the Firm being treated as a Company under Part IX of the Companies Act, but that vesting is not consequent or incidental to a transfer. It is a statutory vesting of properties in the Company as the Firm is treated as a Limited Company. On vesting of all the properties statutorily in the Company, the cloak given to the Firm is replaced by a different cloak and the same Firm is now treated as a Company, after a given date. In the circumstances, in our view, there is no transfer of a capital asset as contemplated by Section 45(1) of the Act. Even assuming for the sake of argument that there is a transfer of a capital asset under Section 45(1) because of the definition of the word "transfer" in Section 2(47)(iii), even then we are of the view that liability to pay capital gains would not arise because Section 45(1) is required to be read with Section 48, which provides for mode of computation. These two sections are required to be read together as the charging section and the computation section constitute one package. Now, under Section 48 it is laid down, inter alia, that the income chargeable under the head "Capital gains" shall be computed by deducting from the full value of the consideration received or accrued as a result of the transfer, the cost of acquisition of the asset and the expenditure incurred in connection with the transfer. Section 45(4) is mutually exclusive to Section 45(1). Section 45(4)categorically states that where there is a transfer by way of distribution of capital assets and where such transfer is due to dissolution or otherwise of the firm, the Assessing Officer was entitled to

treat the market value of the asset on the date of the transfer as full value of the consideration received. This latter part of Section 45(4) is not there in Section 45(1). Therefore, one has to read the expression "full value of the consideration received/accruing" under Section 48 de hors Section 45(4) and if one reads Section 48 with Section 45(1) de hors Section 45(4) then the expression "full value of consideration" in Section 48 cannot be the market value of the capital asset on the date of transfer. In such a case, we have to read the said expression in the light of the two judgments of the Supreme Court in the cases of George Henderson & Co. Ltd. (supra) and Gillanders Arbuthnot & Co. (supra) in which it has been held that the expression "full value of the consideration" does not mean the market value of the asset transferred, but it shall mean the price bargained for by the parties to the transaction. It has been further held that consideration for the transfer of a capital asset is what the transferor receives in lieu of the assets he parts with viz. money or money's worth and, therefore, the very asset transferred or parted with cannot be the consideration for the transfer and, therefore, the expression "full value of the consideration" cannot be construed as having a reference to the market value of the asset transferred and that the said expression only means the full value of the things received by the transferor in exchange of the capital asset transferred by him. In the circumstances, even if we were to proceed on the basis that vesting in the company under Part IX constituted transfer under Section 45(1), still the assessee ought to succeed because the Firm can be assessed only if the full value of the consideration is received by the Firm or if it

accrues to the Firm. In the present case, the Company had allotted shares to the Partners of the erstwhile Firm, but that was in proportion to the capital of the Partners in the erstwhile Firm. That allotment of shares had no correlation with the vesting of the properties in the Limited Company under Part IX of the Act. Lastly, Section 45(1) and Section 45(4) are mutually exclusive. Under Section 45(4) in cases of transfer by way of distribution and where such transfer is as a result of dissolution, the department is certainly entitled to take the full market value of the asset as full value of consideration provided there is transfer by distribution of assets. In this case, we have held that there is no such transfer by way of distribution and, therefore, Section 45(4) is not applicable. This deeming provision, regarding full value of consideration, is not there in Section 45(1) read with Section 48. If one reads Section 45(1) with Section 48, it is clear that the former is a charging section and if that section is applicable, the computation has to be done under Section 48, which only refers to deductions from full value of consideration received or accruing. Section 48 does not empower the Assessing Officer to take market value as full value of consideration as in the case of Section 45. In the circumstances, even if we were to hold that vesting amounts to transfer, the computation is not possible because it has been laid down in the above judgment of the Supreme Court that full consideration cannot be construed to mean market value of the asset transferred. The Legislature, in its wisdom, has amended only Section 45(4) by which the market value of the asset on the date of the transfer is deemed to be the full value of

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> *consideration. However, such amendment is not there in Section 45(1).*
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> *In the circumstances, neither Section 45(1) nor Section 45(4) stand attracted*

15. Another aspect argued by the ld. Counsel for the assessee before us is that in case the assessee sells the equity shares of Trent Ltd. received pursuant to CCPS, then, as per the provisions of Sec. 55(2)(b)(v)(e) of the Act, the cost of acquisition would be the original cost of CCPS. He further submitted that as the Assessing Officer has also taxed the difference between the original cost of CCPS and the fair market value in the captioned year, thus, on actual sale of shares it would tantamount to double taxation considering the provisions of the Act. It was also explained that the CBDT vide its Circular (supra) has explained that legislature has chosen to ignore the intermediate event of conversion for taxation purposes. If there arises any capital gain event upon such conversion, then, the cost of acquisition would be the consideration adopted while computing such capital gain and the exercise in regard to such conversion will be tax-neutral. The decisions relied on by the Assessing Officer and the CIT(A) for taxing the CCPS to equity shares as being transfer of capital asset are distinguished by the ld. Counsel for the assessee particularly in the case of CIT vs Motors & General Stores Pvt. Ltd., 66 ITR 692 (SC) by stating that this judgment by the Hon'ble Supreme Court was delivered in the context of an assessment year prior to introduction of Sec. 55(2)(b)(v)(e) of the Act and also prior to the above CBDT Circular dated 12.05.1964. The ld. Counsel also explained in the case of Santosh L. Chowgule (supra), the Hon'ble Bombay High Court has discussed the issue without considering the provisions of Sec. 55(2)(b)(v)(e) of the Act, which section has a direct bearing on the case

of the assessee. According to him, neither this section was considered nor adjudicated.

16. We have considered the issue in hand and noted that the CBDT vide its Circular dated 12.05.1964 (supra) has clarified the position that where one type of share is converted into another type of share, there is no transfer of capital asset within the meaning of Sec. 2(47) of the Act. The present case before us is not a case where one form of share has been exchanged, bartered, swapped for other form of share. In the present case, one type of share has been converted into other type and the earlier type of share has ceased to exist. Thus, there is no exchange of any share as the pre-conversion security has ceased to exist. From the above, it is evident that mere conversion of one type of share to other type of share will not be a transfer of a capital asset within the meaning of Sec. 2(47) of the Act. Even the jurisdictional Tribunal in the case of Vijay M. Merchant (supra) has clearly laid down that when shares, which are converted, are sold; capital gain is to be calculated on the basis of cost of original shares. The factum of conversion does not make any material difference in calculating the capital gain. The Tribunal relying on the Circular held that there is no transfer when one type of share is converted into any type of share. The facts before the Hon'ble Supreme Court in the case of Motors & General Stores Pvt. Ltd. (supra) are that the assessee-company sold a cinema house and in lieu of the consideration, it had received 5% tax-free cumulative preference shares and the question before the Hon'ble Supreme Court was whether the above transaction would be treated as sale or exchange. The Hon'ble Supreme Court, in the above case, laid down the ratio that barter of one type of goods for other type of goods without consideration in monetary form will be treated as exchange and not as a sale. The Hon'ble Supreme Court held in favour of the assessee in that case stating that the exchange of cinema

house to preference shares is not to be considered as a transfer for the purpose of taxability considering the provisions of Sec. 10(2)(vii) of the Income Tax Act, 1922 corresponding to Sec. 41(2) of the present Income Tax Act, 1961. Accordingly, the decision of Hon'ble Supreme Court in the case of Motors & General Stores Pvt. Ltd. (supra) is entirely distinguishable on facts of the present case.

17. According to us, there is no leakage of revenue if such interpretation is adopted. Not only this interpretation would be in furtherance to the legislative intention but would also make the competition provision of capital gain work smoothly, in synchronization with other provisions, without any conflict with other provisions. On the other hand, if the view is adopted that capital gain tax liability arose upon conversion, the same would be not only against the legislative intention but also would make the composition of capital gain unworkable and would bring conflict with other provisions of the Act. In fact, the contrary interpretation would lead to double taxation in as much as, having taxed the capital gain upon such conversion, at the time of computing capital gain upon sale of such converted shares, the assessee would be still taxed again, as the cost of acquisition would still be adopted as the issue price of the CCPS and not the consideration adopted while levying capital gain upon such conversion. By so starch of imagination, such interpretation process is permissible.

18. In view of the above factual discussion and legal propositions, we are of the view that conversion of CCPS into equity shares cannot be treated as ‘transfer’ within the meaning of Sec. 2(47) of the Act and hence, we delete the addition and allow this issue of assessee’s appeal.

19. The next issue in this appeal of the assessee is against the order of the ITO confirming the action of the AO in making addition on account

of notional interest of ₹6,91,418/- @ 7% on capital balance in the partnership firm as income of the assessee.

20. We have heard rival contentions and gone through the facts and circumstances of the case. The facts of the case are that the assessee is a partner in partnership firm named under the name S.P. Corporation. The assessee receives share of profit from the firm which is exempt in the hands of the assessee. The capital balance of the assessee in the partnership firm is ₹25,000 as on 31.3.2012. The current account balance was ₹98,77,401/- and ₹1,55,68,356/- as on 1.4.2011 and 31.3.2012 respectively. As per clause (4) of partnership deed dtd. 15.7.1985, a registered partnership firm, provided interest @ 7% p,a, payable on the capital of any partner remaining to its credit in the books. However, the assessee entered into a supplementary partnership deed dtd 17.6.1986 wherein clause (4) was substituted as under :-

> *"the capital of the Partnership shall be a sum of Rs.1,25,000/- to be contributed hereto in the manner following that it is to say*
> *Capital*
> *The party of the First Part Rs.25,000*
> *The party of the Second Part Rs.1,25,000*
> *Interest at the rate of 7% p.a. shall be payable to any partner on the capital of the time being remaining to its credit in the Partnership books, as and when agreed by the partners."*

> *"Section 61 - Closing and Opening of branches*
> *Section 62 - Change in Name and Address of Partners*
> *Section 63 - Change in the Constitution and Dissolution of firms"*

However, the supplementary deed was not registered and it was mutually decided by the partners that no interest was provided for the capital balance during the year under reference in the books of the partnership firm. But the AO stated that the assessee is following mercantile system of accounting and accordingly, he computed notional interest @ 7% on the opening balance of current capital account as on 1.4.2011 and added an amount of ₹6,91,418/- to the returned income of the assessee. The CIT(A) also confirmed the action of the AO. Aggrieved now, assessee is now in second appeal before the Tribunal.

21. Before us, assessee contended that the deed was not modified pertaining to the below changes and thus, the same has not been registered with the Registrar of Firms.

But, the supplementary deed entered by the assessee was duly executed on a stamp paper and as such, holds legal validity. Now, before us, ld. Counsel stated that even under section 40(b) of the Act, which provides the allowance for remuneration and interest expense of partners for a partnership firm does not provide for a requirement to have the partnership firm registered in order to allow the expenses in the hands of the firm. Even otherwise, the income has not accrued to the assessee we find that these facts need verification and hence, the same are restored back to the file of the AO. This issue of the assessee's appeal is allowed for statistical purposes.

22. The next issue in this appeal is assessment under MAT computation under section 115JB of the Act in respect to long term capital gain added by AO on conversion of cumulative compulsory preference share into equity share and notional interest on capital balance. Since we have already adjudicated the first issue of long term capital gain in favour of assessee, gain not to be charged to capital gain

and the issue of notional interest set aside to the file of the AO, this issue has been academic and hence needs no adjudication.

23. **In the result, assessee's appeal is partly allowed.**

Order pronounced in the open court on 09-11-2018.

Sd/-	Sd/-
(एन. के. प्रधान /N.K. PRADHAN)	(महावीर सिंह /MAHAVIR SINGH)
(लेखा सदस्य / ACCOUNTANT MEMBER)	(न्यायिक सदस्य/ JUDICIAL MEMBER)

मुंबई, दिनांक/ Mumbai, Dated: 09-11-2018

सुदीप सरकार, व.निजी सचिव */ Sudip Sarkar, Sr.PS*

<u>आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to</u> :

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. आयकर आयुक्त(अपील) / The CIT(A)
4. आयकर आयुक्त / CIT
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, मुंबई / DR, ITAT, Mumbai
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

सत्यापित प्रति //True Copy//

उप/सहायक पंजीकार (Asstt. Registrar)

आयकर अपीलीय अधिकरण, मुंबई **/ ITAT, Mumbai**

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