

**IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH “F”, MUMBAI**

**BEFORE SHRI ABY T VARKEY (JUDICIAL MEMBER)
AND
MS. PADMAVATHY S. (ACCOUNTANT MEMBER)**

**I.T.A. No.3987/Mum/2015
(Assessment year : 2008-09)**

M/s J.M. Financial Ltd 141, Maker Chambers, 11, Nariman Point, Mumbai-400 021 PAN : AAACJ2590B	vs	Deputy Commissioner of Income-tax- 4(3)(1), Mumbai 6 th Floor, Room No.649, Aayakar Bhavan, Mumbai-400
APPELLANT		RESPONDENT

**I.T.A. No.3925/Mum/2015
(Assessment year : 2008-09)**

Deputy Commissioner of Income-tax- 4(3)(1), Mumbai 6 th Floor, Room No.649, Aayakar Bhavan, Mumbai-400 020	vs	M/s J.M. Financial Ltd 141, Maker Chambers, 11, Nariman Point, Mumbai-400 021 PAN : AAACJ2590B
APPELLANT		RESPONDENT

Assessee represented by	Dr K Shivram
Department represented by	Shri Ankush Kapoor CIT DR

Date of hearing	12 -06-2023
Date of pronouncement	04-08-2023

ORDER**PER : MS PADMAVATHY S. (AM)**

These cross appeals by the assessee and the Revenue are against the order of the Commissioner of Income-tax (Appeals)-9, Mumbai (in short, 'the CIT(A)') dated 30/04/2015 for assessment year 2008-09.

2. The assessee is a holding company and has made investment in the joint venture in JM Morgan Stanley Security Pvt Ltd (JMMSSPL) in which the assessee is holding 49% (49 lakhs equity shares) along with Morgan Stanley (India) Securities Pvt Ltd (MSSPL) which holds 51% share. The assessee filed return of income for A.Y. 2008-09 declaring total income at Rs.1191,60,94,839/-. The case was selected for scrutiny and the assessment order under section 143(3) was passed on 06/12/2010 assessing the total income at Rs.1761,62,51,490/-. During the year under consideration, the assessee has shown long term capital gain of Rs.1730,58,51,513/- on sale of shares in JMMSSPL to MSSPL. The Assessing Officer proceeded to treat this gain as the business income of the assessee for the reason that the assessee was in the business of shares and securities as a broker and was also involved in share trading business. The Ld.CIT(A) upheld the order of assessment by holding that the termination of the joint venture was to avoid commercial inconvenience accruing in the future as a joint venture and that termination was a result of split of business arrangement between the assessee and its partners. Aggrieved, the assessee preferred appeal before the Tribunal. The Tribunal remitted the issue back to the Assessing Officer by holding that –

“We have considered the rival arguments made by both the sides, perused the orders of the AO and the ld.CIT(A) and the paper book filed on behalf of the appellant. We have also considered the various decisions cited before us. The question to be decided in the impugned ground is regarding the treatment of consideration received on sale of 49 lakh equity shares of JMMS Securities to Morgan Stanley or a gross consideration of ₹ 1771.32

crores. According to the appellant since these shares were held as capital asset for more than 8 years therefore, the gain on sale has to be treated as LTCG. According to the revenue the same has to be treated as LTCG of business or profession. Both the parties filed elaborate written submissions and relied on various case laws to support their stand. The Id.Counsel for the assessee while concluding his arguments filed a copy of the decision of Hon'ble Supreme Court in the case of Vodafone International Holding B.V. and submitted that all points have been answered in the elaborate decision of the Hon'ble Apex Court running in to more than 250 pages. Since admittedly this decision was not available either before the AO or before the Id.CIT(A), therefore, considering the totality of the facts of the case and in the interest of justice we deem it proper to restore the issue to the file of the AO with a direction to adjudicate the issues afresh in the light of the decision of the Hon'ble Apex Court cites supra and in accordance with law after giving due opportunity of being heard to the appellant. The AO shall also give opportunity to the appellant to furnish the details of the nature of services rendered by JMFCPL to it and show the nexus of expenses incurred in connection with the transfer of the shares. We hold and direct accordingly. The ground of appeal No.1 by the appellant is accordingly allowed for statistical purpose.”

3. In the second round of proceedings, the Assessing Officer held the gain on sale of shares be business income by stating that assessee's case is distinguishable from the case of Vodafone International Holdings B.V. vs UOI 341 ITR 1 (SC). The Ld.CIT(A) in the second round allowed the appeal in favour of the assessee by holding that the income arising out of the sale of shares is to be taxed under the head, 'capital gains'. The assessing Officer in addition to the above did not allow the loss arising out of sale of shares of JM Financial Products Pvt Ltd and did not allow the same to be set off against the long term capital gain declared by the assessee. This issue was also remitted back by the Tribunal in the first round of appeal to the Assessing Officer. The Assessing Officer in the second round retained the disallowance of set off of short term capital loss against the long term capital gain by holding the same to be non genuine. The CIT(A) upheld the order of the Assessing Officer in the second round of appellate proceedings also. Therefore, both the assessee and the revenue are in appeal before the Tribunal raising the following grounds of appeal –

Assessee

“1. Ground I: Treatment of the transaction of Sale of shares of JM Financial Products Pvt. Ltd, as a colourable device and non-genuine and consequently Disallowance of Claim for Set-off of Long-Term Capital Loss on the same: Rs.54,90,36,870 (Rs.54.90 crores)

(Page 104 of the Order)

On the facts and circumstances of the case, the Appellant prays that the conclusion reached by the learned Commissioner of Income-tax (Appeals) - 9, ("CIT(A)") that the Appellant has entered into a transaction for sale of shares of JM Financial Products Pvt. Ltd. with the object of tax avoidance and it is a colorable device is erroneous and contrary to the facts. The Appellant prays that the claim of long term capital loss of Rs.54,90,36,870/- be accepted as a genuine long term capital loss.

2. Ground II: Treatment of the transaction of Sale of shares of JM Financial Products Pvt. Ltd, as a colourable device and non-genuine and consequently Disallowance of Claim for Set-off of Short-Term Capital Loss on the same: Rs.465,44,19,508 (Rs.465.44 crores)

(Page 104 of the Order)

On the facts and circumstances of the case, the Appellant prays that the conclusion reached by the learned CIT(A) that the Appellant has entered into a transaction for sale of shares of JM Financial Products Pvt. Ltd. with the object of tax avoidance and it is a colorable device is erroneous and contrary to the facts. The Appellant prays that the claim of short term short term capital loss of Rs.465,44, 19.508/- be accepted as a genuine short term capital loss.

Ground III; Applicability of Section 55(2)(aa) for calculating the amount of Long-term capital loss and Short-term capital loss on sale of shares of JM Financial Products Pvt. Ltd.

(Page 104 of the Order)

On the facts and circumstances of the case, the Appellant prays that the conclusion reached by the learned CIT (A) on the non-applicability of the provisions of Section 55(2)(aa) of the Income-tax Act, 1961 to the shares of a private limited company is not correct and that such loss is determined by spreading the original cost to the total number of shares including the bonus shares is erroneous and contrary to the law. On the facts and circumstances of the case, the Appellant prays that the calculation of the amount of long-term capital loss and the amount of short-term capital loss as derived by the Appellant by applying the provisions of section 55(2)(aa) of the Income-tax t. Act, 1961 be accepted and that the long-term capital loss be accepted at Rs.54,90,36,870/- and the short-term capital loss be accepted at Rs.465,44,19,508/-.

Ground IV: Set-off of Long-Term Capital Loss on sale of shares of JM Financial Products Pvt. Ltd.: Rs.54,90,36,870 (Rs.54.90 crores)

(Page 104 of the Order)

On the facts and circumstances of the case, the Appellant prays that the long term capital loss of Rs.54,90,36.870/- be set off against the other long term capital gain ^ earned by the Appellant during the assessment year 2008-09.

Ground V: Set-off of Short-Term Capital Loss on sale of shares of JM Financial Products Pvt. Ltd.: Rs.465,44,19,508 (Rs.465.44 crores)

(Page 104 of the Order)

On the facts and circumstances of the case, the Appellant prays that the short term capital loss of Rs.465, 44, 19,5087- be set off against the other long term capital gain earned by the Appellant during the assessment year 2008-09."

Revenue

1. *"On the facts and in the circumstances of the case and in law, the Ld. CIT(A) erred in directing the AO to Charge gain of Rs. 1771,36,61,381/-on transfer of 49,00,000 equity shares as Long Term Capital Gain instead of Business Income".*
2. *"On the facts and in the circumstances of the case in law, the Ld. CIT(A) also erred in not appreciating the fact that the consideration was actually received for the premature termination of Joint venture, foregone future profit and goodwill of the business, not for the value of the share".*
3. *"On the facts and in the circumstances of the case and in law, the Ld. CIT(A) further erred in not appreciating the fact that the assessee failed to establish the valuation of shares done on the basis of the net worth of the joint venture and that the consideration was for the worth of the shares, not for the loss of further business."*
4. *The appellant craves leave to amend or alter any grounds or add a new ground which may be necessary*

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Sale of Shares – Long Term Capital Gain or Business Income

4. The assessee has made an investment in joint venture in JMMSSPL on 01/04/1999. The assessee has sold these investments in shares to MSSPL on

18/05/2007. The Assessing Officer in the remanded proceedings held after considering the Vodafone International Holdings B.V. vs UOI [(2012) 341 ITR 1] that the consideration is to be taxed in terms of section 28(2) of the Income-tax Act, 1961 for the reason that –

- Case of Vodafone was for taxability of capital gains in India when non-resident company transferred the underlying assets in Indian territory in guise of shares in territories outside India.
- In Vodafone's case the applicability of Sec.28(ii) has never been adjudicated.
- The assessee failed to show that valuation was done on the basis of the net worth of the joint venture.

5. The assessee in the second round of appellate proceedings submitted before the CIT(A) that -

1. The Assessee was a 49% shareholder in the Company JM Morgan Stanley, the shares of which were sold by the Assessee to Morgan Stanley. **(Pg. 8 PB1);**

2. The Assessee did not participate in the day to day operations of the Company, however it had a right **as a shareholder** to nominate 4 members to the board of the Company while Morgan Stanley could nominate 6. The Executive committee would have one executive to be appointed by the Assessee in the Company while MS would appoint two. The compensation committee would similarly have 2 members designated by the Assessee while MS would have three. **(Pg. 30 - 31 PB1);**

3. The Company would have its own team of management including its own CEO who would be appointed by the board of the Company where the Assessee had only 40% representation. **(Pg. 53 - 54 PB1). There would be a separate executive committee for the management of the Company in accordance with the business plan (Pg. 38 - 39 PB1).** The principal officers of the Company would be designated by MS while the Assessee would only be consulted for the same **(Pg. 39 PB1). This clearly shows that the Assessee was not managing the Company but was merely given rights to be consulted in the appointments of the principal officers;**

4. The Company had **purchased for a consideration** the existing business of the Assessee's Institutional Equity Sales and Trading Business Assets and customer accounts. **(Pg. 44 - 45 PB1).** The Assessee therefore was not carrying out the business of broking of shares and securities from the inception of the Company until the sale of the shares in the Company. There was a specific non-compete clause in the agreement on

both the parties. **(Pg. 58 PB1)**. In fact, even as of date the Assessee is not carrying the business of broking of shares and securities;

5. The Assessee has obtained substantial dividend income from the JV company **(Pg. 694 PB2)**, the shares were held as Investments **(Pg. 347 PB1)** and **there were no shares held as stock in trade**. 14A disallowance was made in AY 2007-08 on dividend received from the Company **(Pg. 845 PB2)**;

6. The Joint venture was not envisaged for any particular term but was in effect brought about to lay down the rights and duties of the Assessee and MS in the newly formed company. **(Pg. 106 PB1)**;

7. The Assessee had exited the broking business is clearly brought out in the terms of the non-compete clause and the fact that during the year, Income was earned mainly on sale of long term investments, short term investments, Interest, lease rent and dividend received **(Pg. 352 PB1)**. The name of the Assessee was also changed from J.M. Share and Stock Brokers Limited to JM Financial Ltd. to better reflect the change; and

8. The Agreement for sale of shares of the Company expressly states that the consideration received by the Appellant is for the sale of shares. It does not state that the consideration is paid as a compensation for the future profits. **(Pg. 250 PB1)**

6. The Ld.CIT(A) held the gains earned by the assessee on transfer of shares of JMMSSPL to be charged as long term capital gain by observing that –

- (i) The assessee has set up the broking business during the year 1999.
- (ii) The shares in the company were held by the assessee for a period of 8 years and were shown in the balance-sheet of the assessee as long term investments;
- (iii) The assessee was neither a trader in the shares of JM Morgan Stanley Securities Pvt Ltd nor were the shares held as stock in trade

7. The Ld.AR submitted that the shares are held as investments and reflected under the head “investments” in the financials of the assessee from year to year and that the assessee has earned substantial dividend on the said investments. Accordingly, the assessee is an investor and not a trader in respect of shares shown under the head ‘investments’ and, therefore, the gain arising out of the sale of the said investments should be taxed under the head ‘capital gains’. The Ld.AR also submitted that the assessee was not a trader in shares of JMMSSPL nor were the shares held as stock in

trade. The assessee was also not involved in the captive management of the company and, therefore, the consideration from sale of shares should be taxed under the head 'capital gain'. The Ld.AR argued that the Assessing Officer has erroneously treated amount received as a compensation for loss resulting from split of joint venture whereas in reality, the shares held were sold to the partner in the joint venture and as a result of the sale, the stock of the partner goes up from 51% to 100%. Therefore, the consideration received by the assessee is very much in the nature of capital gains from sale of shares. It is further submitted that the Assessing Officer treated the gain as a business income for the reason that the basis or arriving at the consideration is not on net worth of the joint venture. In this regard, the Ld.AR submitted that the valuation of consideration for sale of shares was not challenged by the department but the revenue has merely ascribed motive for the same saying that it was a transaction in the nature of ordinary business of the assessee incurred to avoid commercial inconvenience with no foundation and facts and with disregard for evidence on record. Another argument presented by the Ld.AR is that section 50CA of the Act has been inserted by the Finance Act, 2017 with effect from 02/04/2018 and therefore, the said insertion for valuation of capital asset transferred being shares of a company other than equity shares or the purpose of section 48 being "fair market value" determined as prescribed, is not applicable to the assessee for the year under consideration. The Ld.AR also relied on the decision of the Hon'ble Supreme Court in the case of Vodafone International Holdings B.V. vs UOI (supra) to submit that sale of shares of joint venture company is a transfer of capital asset and liable to capital gain tax. The Ld.AR without prejudice submitted that the amount received towards future profits or deprivation of future profit for the assessee is received not in the ordinary course of business and, therefore, is a capital receipt.

8. The Ld.DR, on the other hand, submitted that –
- Ld. CIT(A) has not appreciated the fact that at the very outset when the assessee entered in the Joint Venture with the Morgan Stanley Group in the year 1999, it was its "**institutional equity business**" (including the existing institutional equity sales and trading business assets of the assessee) which had been transferred by it to the Joint Venture Company, namely, J.M. Morgan Stanley Securities Pvt. Ltd. This fact is duly mentioned in Article 4 Section 4.01 (a) of the JV Agreement dated 21.01.1999 (**Pg. Nos. 44 & 45 of the Paper book**) It is therefore, logical to infer that finally, on 18.05.2007, when the assessee has exited this Joint Venture, the consideration received by the assessee is in fact the value of the assessee's stake in the Joint Venture business which had increased substantially in the 8 years during which the assessee was in this JV.
 - From the correspondence of the J.V. Company, namely, J.M. Morgan Stanley Securities Pvt. Ltd. (JMMSSPL) with Morgan Stanley placed by the assessee at Pg. Nos. 223 to 242 of this paper book, it is seen that the assessee had engaged in protracted negotiations to determine the amount receivable by it upon split of joint venture with Morgan Stanley Group. In this regard, from the letter dated 26.10.2006 (placed at **Pg. No. 223 to 230 of the Paper book**), written by Hans J. Schauettler addressed to Mr. Nimesh Kampani from the assessee group, it is seen that formal separation of **business** interest has been mentioned as the best way forward in view of the fundamental differences between these two groups.
 - Significantly, in Para 3 of this letter (placed at **Page Nos. 226 & 227 of the Paper book**) in which the Morgan Stanley reiterated the differences in the approach of the two groups during negotiations till that date i.e. till 26.10.2006, Morgan Stanley was willing to sell its shares in STJV & IBJV to J.M. Financial Ltd., (assessee) for US \$ 75 million whereas it offered to buy all the shares in STJV & IBJV from J.M. Financial Ltd. i.e. from the assessee for US \$ 125 million. It may be mentioned here that the shareholding of the assessee in J.M. Morgan Stanley Pvt. Ltd. was 49% while that of Morgan Stanley was 51%. This obviously shows substantially different rates for the same shares held by different price at the same time. Thus Morgan Stanley offered to sell its shareholding in the JV Company at a much lesser price and at the same time it offered to buy the assessee's shareholding in the JV company at a much higher price. It is, therefore, clear that had the negotiations been merely for determination of price of shares only, it would not have resulted in different rates for the same shares as the price of shares of a company at a particular time has necessarily to be the same in different hands.
 - Thus this offer by Morgan Stanley clearly establishes the fact that the amount of compensation negotiated was lumpsum since the very beginning of the negotiations and there was no indication that the payment was simply for the purchase of shares sold by the assessee.
 - It may also to be mentioned here that, the assessee itself had demanded from Morgan Stanley a sum of US \$ 540 million for the transfer of its stake in STJV being the "*loss*

resulting from split of consolidated businesses and pre-mature end' of the JV. This fact is clearly mentioned in Point No.3 in this letter (**Pg.No. 228 & 229 of the paper book**). Thus, later on also, the amount of US \$ 540 million asked by the assessee, the amount offered by Morgan Stanley and ultimately the amount paid by Morgan Stanley was for the value of the assessee's stake in the JV business and it was not the consideration received merely for the value of shares transferred/sold by the assessee.

- This fact is also evident from the mention by Hans J. Schauettler of Morgan Stanley to Mr. Nimesh Kampani in the above mentioned letter dated 26.10.2006 (at **Page 229 of the Paper book**) in which it was stated that the previous offer more than compensated J.M. Financial Ltd., for the *"value of the business and any risk it may face going forward"*.
- It may also be mentioned here that, as mentioned in the Agreement dated 18.05.2007 at Page No. 250 & 251 of the Paper Book, out of the total consideration agreed to be paid to the assessee, US \$50 million was agreed to be paid for obtaining of Qualified Merchant Banking Licence by MS (Morgan Stanley) Group. It is therefore, clear that consideration received by the assessee was not simply for the transfer of shares of the JV Company.
- It is thus amply clear from the above mentioned agreements and the correspondence that the negotiations between the assessee and the Morgan Stanley were never for determining the value of shares of the JV Company but for determining the value of the business as a whole and the potential loss suffered by the assessee by the assessee due to the loss of the future business profits and termination of the JV and the final consideration paid was also for the same.
- Further, it is also clear that the purpose for which whole exercise initiated was strategic end of JV as mentioned in pg. 5 in the above referred letter (**pg. no. 227 of the paper book**). It was in fact the payment for restructuring of all joint venture businesses including IVJV & STJV company and the transfer of shares of JMMSSPL by the assessee was only a modality adopted for such restructuring. In view of these facts, it will be a grossly erroneous interpretation that the sum of Rs. 1771.36 Cr. as sale consideration only for the sale of 49,00,000 shares of JM Morgan Stanley Securities Pvt. Ltd.
- 3.10 Hence it is obvious from the above facts that the amount of Rs. 1771.36 Cr. was assessee's claim of loss of resulting from split consolidated business and pre-mature end of JV business which makes it obvious that this amount was expected future profits which was loss to the assessee as a result of split of consolidated businesses and accordingly the same is revenue receipt and is accordingly to be treated as income from business as per the provisions of section 28 of I.T. Act, 1961.

9. We heard the parties and perused the material on record. The coordinate bench in the first round of appeal has remitted the issue back to the assessing officer to consider

the issue of treatment of gain on sale of shares in joint venture as capital gain or business income in the light of the decision of Hon'ble Supreme Court in the case of Vodafone (supra). The Assessing Officer in the remanded proceedings once again treated the income to be taxed as business income u/s.28 for the reason that the entire consideration received is not the value of the shares but for the value of business interest for which sale of shares is used as a medium. With regard to the applicability of the decision of the Apex Court in Vodafone (supra) to assessee, the Assessing Officer has held that –

- (i) In Vodafone case the parties involved were non-residents whereas in assessee's case the impugned transaction is between two entities
- (ii) In Vodafone case the issue of taxability u/s.28(ii) was not adjudicated
- (iii) In Vodafone case, the issue was with regard to the taxability of the profit whereas in assessee's case the taxability is not in dispute since the assessee itself has offered the income to tax
- (iv) In Vodafone case the main business of the parties involved was Telecommunication the transaction involved was to invest in the telecom business. In assessee's however the assessee is in the business of share trading, brokerage etc., and therefore the purchase of shares in joint venture company doing share trading business cannot be termed to be for the purpose of investment but only as part of business activity.

10. The Assessing Officer also held that it was the assessee who was conducting the business of the joint venture and the consideration received is for premature termination of joint venture, loss of future profit and renouncement of right to conduct business to MSSPL. It was further held that the investment in joint venture is part of the business of the assessee and the investment is done as businessman and not as investor. Another reason quoted by the Assessing Officer is that the valuation of the shares are not based on the net worth but based on the future business which is the assessee is losing due to the disinvestment and therefore the gain arising is a business income. Accordingly the

Assessing Officer sustained the treatment of gain arising on sale of shares as business income.

11. On further appeal the CIT(A) allowed the appeal in favour of the assessee. The CIT(A) held that –

- (i) The AO failed appreciate that the Hon'ble Supreme Court in Vodafone case has touched various factors relating to the share transfer transaction such as management control, transfer of business along with incidental rights, separate legal persona, indirect control, rights consisting of independent capital assets within the meaning of section 2(14), the aspect of control vis-à-vis the ownership of shares, control premium, legal relationship between a holding company and a subsidiary company, acquiring control on purchase of shares, transfer of controlling interest is incidental to the transfer of shares and that the two cannot be broken up etc.
- (ii) The AO has misconceived the applicability of Section 28(ii)(a) because it requires payment of compensation to a person who was managing the whole or substantially the whole of affairs of an Indian company in connection with the termination of his management.
- (iii) In Vodafone case the Hon'ble Supreme Court has held that to ascertain the legal nature of the transaction one has to look at the entire transaction as whole and not adopt dissecting approach by applying "look at" test.

12. Besides the CIT(A) also relied on various judicial pronouncements to hold that gain earned by the assessee on sale of shares is to taxed under the head Capital Gains. The main contention of the revenue for treating the gain on sale of shares as business income is that the assessee has a controlling interest in the business of JMMSSPL and consideration received is towards premature termination of joint venture where the assessee has transferred the said interest. JMMSSPL was formed as a JV to carry on the Institutional Equity and Trading business in which the assessee owns 49% of the shares of the company and the rest is owned by MSPPL. The assessee as per the non-compete clause in the agreement entered with MSPPL was not carrying on the business of broking of shares and securities post entering into the JV. From the perusal of the

records we notice that the assessee has been holding the shares of JMMSS from 01.04.1999 to 18.05.2007 i.e. more than 8 years and the same are reflected under the head Investments and not as stock-in-trade in the financials of the assessee (refer page 1722 of paper book). It is also noticed that the assessee has during the year under consideration has earned income mainly from sale of long term investments, short term investments interest, lease rent and dividend income from the investment made in JMMSSPL. Given this, it cannot be said that the shares in JMSSPL is held by the assessee for trading purposes. During the course of hearing the Id AR drew our attention to the corporate governance and management related documents to substantiate that the control and management of JMMSSPL is not held by the assessee and that the assessee is merely a shareholder not participating in the affairs of the company. In this regard it is relevant to take note of the following observations of the Hon'ble Supreme Court in the case of Vodafone (supra)

*At the outset, we need to reiterate that in this case we are concerned with the sale of shares and not with the sale of assets, item-wise. The facts of this case show sale of the entire investment made by HTIL, through a Top company, viz. CGP, in the Hutchison Structure. In this case we need to apply the "look at" test. In the impugned judgment, the High Court has rightly observed that the arguments advanced on behalf of the Department vacillated. The reason for such vacillation was adoption of "dissecting approach" by the Department in the course of its arguments. Ramsay (supra) enunciated the look at test. **According to that test, the task of the Revenue is to ascertain the legal nature of the transaction and, while doing so, it has to look at the entire transaction holistically and not to adopt a dissecting approach.** One more aspect needs to be reiterated. There is a conceptual difference between preordained transaction which is created for tax avoidance purposes, on the one hand, and a transaction which evidences investment to participate in India. **In order to find out whether a given transaction evidences a preordained transaction in the sense indicated above or investment to participate, one has to take into account the factors enumerated hereinabove, namely, duration of time during which the holding structure existed, the period of business operations in India, generation of taxable revenue in India during the period of***

business operations in India, the timing of the exit, the continuity of business on such exit, etc. Applying these tests to the facts of the present case, we find that the Hutchison structure has been in place since 1994. It operated during the period 1994 to 11.02.2007. It has paid income tax ranging from Rs. 3 crore to Rs. 250 crore per annum during the period 2002-03 to 2006-07. Even after 11.02.2007, taxes are being paid by VIH ranging from 394 crore to Rs. 962 crore per annum during the period 2007-08 to 2010-11 (these figures are apart from indirect taxes which also run in crores). Moreover, the SPA indicates “continuity” of the telecom business on the exit of its predecessor, namely, HTIL. Thus, it cannot be said that the structure was created or used as a sham or tax avoidant. It cannot be said that HTIL or VIH was a “fly by night” operator/ short time investor. If one applies the look at test discussed hereinabove, without invoking the dissecting approach, then, in our view, extinguishment took place because of the transfer of the CGP share and not by virtue of various clauses of SPA. In a case like the present one, where the structure has existed for a considerable length of time generating taxable revenues right from 1994 and where the court is satisfied that the transaction satisfies all the parameters of “participation in investment” then in such a case the court need not go into the questions such as de facto control vs. legal control, legal rights vs. practical rights, etc.

The House of Lords in IRC v. V.T. Bibby & Sons (1946) 14 ITR (Supp) 7 at 9-10, after examining the meaning of the expressions “control” and “interest”, held that controlling interest did not depend upon the extent to which they had the power of controlling votes. Principle that emerges is that where shares in large numbers are transferred, which result in shifting of “controlling interest”, it cannot be considered as two separate transactions namely transfer of shares and transfer of controlling interest. Controlling interest forms an inalienable part of the share itself and the same cannot be traded separately unless otherwise provided by the Statute. Of course, the Indian Company Law does not explicitly throw light on whether control or controlling interest is a part of or inextricably linked with a share of a company or otherwise, so also the Income Tax Act. In the impugned judgment, the High Court has taken the stand that controlling interest and shares are distinct assets.

Control, in our view, is an interest arising from holding a particular number of shares and the same cannot be separately acquired or transferred. Each share represents a vote in the management of the company and such a vote can be utilized to control the company. Controlling interest, therefore, is not an identifiable or distinct capital asset

*independent of holding of shares and the nature of the transaction has to be ascertained from the terms of the contract and the surrounding circumstances. Controlling interest is inherently contractual right and not property right and cannot be considered as transfer of property and hence a capital asset unless the Statute stipulates otherwise. **Acquisition of shares may carry the acquisition of controlling interest, which is purely a commercial concept and tax is levied on the transaction, not on its effect.***

13. When we look at the case in hand, it is noticed that the assessee had sold the investment which the assessee has been holding for long period of time from which the assessee has been earning dividend income. The impugned transaction, in assessee's case is sale of shares. Therefore applying the above ratio of the Hon'ble Supreme Court irrespective of whether the assessee was having a controlling interest (which according to the submissions, the assessee does not have) it is the transaction that needs to be looked into for the purpose of determining the taxability. Accordingly in our view the shares are held by the assessee as investment and the gain arising out of sale of such investment cannot be treated as a business income on the ground that the assessee was participating in the business of JMMSSPL and had had transferred the controlling/business interest.

14. The consideration for sale of shares is agreed between the assessee and MSPL as per the agreement of sale of shares in JMMSSPL. It is noticed that the assessee had negotiated the agreed price by producing before MSSSPL various prices which are paid in a similar transactions and final price was thus arrived at. The contention of the revenue is that the valuation is not done on the basis of net worth of JMMSSPL but based on the future business and therefore the consideration is for loss of business that cannot be treated as capital gains. From perusal of the method adopted for valuation of shares by the assessee, it is noticed that the assessee has agreed for a lump sum consideration without any breakup of what is attributable to assets, liabilities and future

business. It is to be noticed that the Act does not contain provisions to state that determination of the head of income under which the gain on sale of shares is to be taxed is based on the valuation used for arriving at sale consideration for transfer of shares. However the Assessing Officer has the right to question the correctness of the valuation and accordingly determine the treatment of the taxability of the amount which in his opinion is excess. In assessee's case the assessing officer did not question the method or basis of the valuation of shares and has not disputed the consideration received towards sale of shares but held the gain to be a business income on the ground that the valuation is arrived at based on future business. This in our opinion is not tenable since the treatment of shares in the books of accounts whether as stock-in-trade or investment is also one of the determining factor for taxation under capital gain or business income and it cannot be said that the method adopted for arriving at the sale consideration determines the nature of transaction. Further there is merit in the submission of the Id AR that since section 50CA of the Act is inserted by the Finance Act, 2017 with effect from 02/04/2018 and therefore, the said insertion for valuation of capital asset transferred being shares of a company other than equity shares or the purpose of section 48 being "fair market value" determined as prescribed, is not applicable to the assessee for the year under consideration. The intention of the assessee is to hold to the shares of JMMSSPL as investment is demonstrated by the reflection of the shares under investments in the financial statements and from the factual finding given by the CIT(A) that the Board Resolution dated 18.04.1998 passed while making the investment clearly mentions that the assessee has made a capital investment. Accordingly in our view treatment of the gain as business income on this ground is not sustainable. In view of these discussions we hold that that the gain arising on transfer of 49,00,000 equity shares of JMMSSPL by the assessee is chargeable to tax under the head capital gains and the assessee be allowed to claim the indexed cost of acquisition

considering the period of holding of the shares. In result the appeal of the revenue is dismissed.

I.T.A. No.3987/Mum/2015 – Assessee's appeal

15. The issue in assessee's appeal is disallowance of set off of short term capital gain / loss. During the year under consideration, the assessee had shown both, short term and long term capital loss on sale of shares of assessee's group company, JM Financial Product Pvt Ltd (JMFPPPL) which was a private limited company. Brief facts of the issue is that the assessee had claimed set off of long term capital loss of Rs.54,90,36,870/- and short term capital loss of Rs.4,65,44,19,508/- claimed to have been incurred on account of shares of assessee's group company namely, JMFPPPL. The assessee sold 54445 crore equity shares of JMFPPPL representing 10% of the equity share capital to JM Financial Group Employees Welfare Trust being a trust created for the benefit of employees of JM Financial Group. The assessee sold the said shares to JM Financial Group Welfare Trust in order to institute employee stock option plan for the benefit of the employees of entire JM Financials group. The assessee submitted that the shares sold included original shares as well as bonus shares. And that the trust would hold the shares until the shares were, purchased by the employees under the employee's stock option plan (ESOP) at the face value of Rs. 10/- per share. As regards sale price of Rs.10/- per share, it was explained that the shares were sold at the cost after ignoring rounding off which was Rs. 10.40 per share on 31.12.2007, The purpose for sale of shares to the trust was explained by the assessee as being administrative convenience and for grant of ESOP.

16. From the above details the AO observed that the total number of shares held by the assessee up to 29.10.2007 which included original investment, fresh issue and conversion of preference share was 1.75 crore. Further, 3.20 crore fresh shares were purchased on 31.10.2007 and 07.11.2007 at cost of Rs. 125/- per share taking the total holding of the assessee as on 07.11.2007 to 4.95 crore shares. Further, 49.50 crore bonus shares were issued on 14.12.2007, From these facts the A.O, observed that as a result of issue of bonus shares in the ratio of 9:1 on 14.12.2007, the average cost of the shares which was Rs. 114/- per share up to 07.11.2007 was reduced to Rs, 10.40 per share. The A.O. further observed that the assessee had sold 49% shares of J.M, Morgan Stanley Securities Pvt, Ltd, resulting in hook profit of Rs. 17,35,86,10.832/- on 05.10.2007. From these facts the A.O. concluded that the assessee, with the help of its own group company, made a colourable device to artificially create a loss to cancel part of profit earned on sale of 49% of joint venture and thereby evade the tax. The Assessing Officer held the transaction to be non-genuine and is merely a device to create a loss to cancel the part of profit earned on sale of the joint venture and evade the tax. The Assessing Officer relied upon the judgement of the Hon'ble Supreme Court in the case of McDowell & Co. Ltd 151 ITR 148 (SC) and rejected the assessee's claim of set off of short, term capital loss of Rs.465,44,19.508/- and long term capital loss of Rs.54,90,36,870/- as non-genuine camouflaged loss. The CIT(A) in the first round of appeal upheld the order of the Assessing Officer. The Tribunal remitted the issue back to the Assessing Officer to decide the issue in accordance with the decision in the issue pertaining to treatment of sale of shares in JM Morgan Stanley Securities Pvt Ltd to be assessable as capital gain or business income.

17. In the second round of proceedings, the Assessing Officer held that the assessee could not establish the genuineness of the transaction against the findings given by the

CIT(A) in the first round and that the onus was on the assessee to prove that the transaction was not a colourable transaction. The Ld.CIT(A) in the second time held that the entire transaction had taken place not for any commercial purposes but with a motive to create loss in books of account. Therefore, he relied on the order of CIT(A) in the earlier round of appellate proceedings and accordingly, disallowed the set off of losses.

18. The Ld.AR submitted that –

1. The assessee issued bonus shares of JMFPPPL for the reason that the assessee decided to include a large number of employees under the ESOP scheme and therefore large numbers of shares were issued at a lower price to make the ESOP scheme attractive.
2. Where shares have been actually sold, transferred and consideration has been received and details of sale of shares along with payment dates and other relevant details are already provided before the lower authorities.
3. The options have actually been granted and in a few cases actually exercised by the employees and therefore the said transaction cannot be said to be a sham transaction and the SEBI guidelines have been adhered to for the ESOP scheme.
4. The action of the CIT(A) (in Original Assessment Proceedings) in relying upon Wikipedia (**Pg. 815 PB2**) to ascertain the source of issue of bonus shares is erroneous and has no legal value as Wikipedia is openly editable. On the other hand the CIT(A) has also held that the said transaction is legally permissible (**Pg. 819 PB2**).
5. The AO and the CIT(A) have both proceeded on the assumption that the transfer was made by the Assessee in order to reduce the Capital gains on the sale of 49% shares in JM Morgan Stanley Securities Pvt. Ltd.; however the Assessee had also sold bonus shares in a short term capital gain. It is therefore clear that the intention of the Assessee was not to reduce tax liability but that the transaction of sale of shares was

on account of the need of the Assessee to put in place an ESOP scheme for the benefit of the employees of the JM group. The sale of bonus shares ensured that the employees would be able to get more shares at a more attractive price.

6. The Id AR relied on the following judicial pronouncements in this regard -

- CIT v. Sakarlal Balabhai [1968] 69 ITR 186 (Guj)(HC)
- ACIT v. Biraj Investments P. Ltd. [2012] 210 Taxman 418 (Guj.)(HC)
- UOI v. Azadi Bachao Andolan [2003] 263 ITR 706 (SC)

19. We heard the parties and perused the material on record. We notice that the AO rejected the claim of set off of short term capital loss of Rs. 4,65,44,19,508/- and long term capital loss of Rs. 54,90,36,870/- on the ground that the assessee with the help of its own group companies made a colourable device to artificially create loss to cancel profit earned on sale of 49% shares to the J.V. and thereby evade the tax. For this proposition, he relied on the decision of Hon'ble Apex Court in the case of McDowell & Co. (supra). In the first round of appeal, the CIT(A) while upholding the action of the AO in rejecting the claim- of set off of such long term capital loss and short term capital loss relied on the decision in the case of Jannhavi Investment Pvt, Ltd. (304 ITR 276 Bom.) and Dahiben Umedbhai Patel vs. Normal-Jeans Hamilton & Others reported in 57 Comp. Case 700 Bom. and held that the computation of such loss by applying the provisions of section 55(2)(aa) is not correct. Accordingly the CIT(A) held that such loss shall not be allowed to be deducted or set off from income. In the second round of proceedings the lower authorities sustained the disallowance on the same grounds as stated by their predecessors in the first round of appeal.

20. The main contention of the revenue for disallowing the set off of loss is that the loss is artificially created to reduce the tax payment on gain on sale of shares in

JMSSPL. The revenue came to the said conclusion based on the finding that huge bonus shares were issued by JMFPPL which reduced the value of the shares from Rs.114 to Rs.10.40. During the course of hearing the bench directed the Id AR to submit the financials of JMFPPL for three years i.e. 31.03.2006, 31.03.2007 and 31.03.2008 in order to examine the basis of issue of bonus shares. The various key parameters perused from the financials are as tabulated below –

(Amount Rs.in Crore)

Financial year	Net worth as at end of the Year	Profit Before Tax	Tax	Profit After Tax
2005-06	99.09 (Pg.1677 PB7)	5.95 (Pg.1678 PB7)	1.50 (Pge.1678 PB7)	4.45 (Pg.1678 PB7)
2006-07	190.88 (Pg.1691 PB7)	34.50 (Pg.1692 PB &)	7.71 (Pg.1692 PB 7)	16.79 (Pg.1692 PB 7)
2007-08	636.53 (Pg.1716 PB7)	77.41 (Pg.1717 PB7)	28.49 (Pg.1717 PB7)	48.92 (Pg.1717 PB 7)
2021-22	1951.95 (Pg.1755 PB 7)	165.48 (Pge.1756 PB 7)	36.90 (Pg.1756 PB 7)	128.58 (Pg.1756 PB 7)

21. From the above it is noticed that the performance of the company has been showing upward trend from 31.03.2006 and that the reserves and surplus position of the company out of which the bonus shares were issued stood at Rs.173,38,10,363 as of 31.03.2007 and after the issue of bonus shares it was at Rs.92,02,83,991. Therefore we see merit in the submissions of the Id AR that the financial position of the company fully justifies the issue of bonus shares out of the share premium account and the same was not done just to bring down the value of shares.

22. During the year under consideration the assessee has transferred 5.445 crores shares of JMFPPL to the Trust formed for the purpose of issuing ESOPs to the employees. It is noticed from the perusal of records that out the above 3.439 crore

shares have already been issued to employees under the ESOP scheme by the Trust. It is noticed that the employees have exercised options to the extent of 14.82% of the shares. The 1d AR during the course of hearing submitted that JMFPPL was the main profit making subsidiary company in the group having high credit rating and that is the reason the company was chosen for implementing ESOPs. The 1d AR further submitted that the issue of shares under ESOP scheme is a common business practice in order to retain talent and to provide opportunity to employees to grow with the company. It is also brought to our notice that JMFPPL had applied for banking license in 2013 which resulted in phenomenal growth of the company which resulted in wealth creation for employees. We also notice that these facts have not been considered by the lower authorities before concluding that the entire transaction to be non-genuine. It is relevant to consider the decision of the Hon'ble Supreme Court in the case of CIT Mumbai vs Walfort Share & Stock Brokers (P.) Ltd where it is held that –

*20. The real objection of the Department appears to be that the assessee is getting tax-free dividend; that at the same time it is claiming loss on the sale of the units; that the assessee had purposely and in a planned manner entered into a pre-meditated transaction of buying and selling units yielding exempted dividends with full knowledge about the fall in the NAV after the record date and the payment of tax-free dividend and, therefore, loss on sale was not genuine. We find no merit in the above argument of the Department. At the outset, we may state that we have two sets of cases before us. The lead matter covers assessment years before insertion of section 94(7) vide Finance Act, 2001 with effect from 1-4-2002. With regard to such cases we may state that on facts it is established that there was a "sale". The sale price was received, by the assessee. That, the assessee did receive dividend. The fact that the dividend received was tax-free is the position recognized under section 10(33) of the Act. The assessee had made use of the said provision of the Act. That such use cannot be called "abuse of law". Even assuming that the transaction was pre-planned there is nothing to "impeach the genuineness of the transaction. With regard to the ruling in *McDowell & Co. Ltd. v. CTO* [\[1985\] 154 ITR 148](#) (SC), it may be stated that in the later decision of this Court in *Union of India v. Azadi Bachao Andolan* [\[2003\] 263 ITR 706](#) it has been held that a citizen is free to carry on its business within the four corners of the law. That, mere tax planning, without any motive to evade taxes through colourable devices is not frowned upon even by the judgment of this Court in *McDowell & Co. Ltd.*'s case (*supra*). Hence, in the cases arising before 1-4-2002, losses pertaining to exempted income cannot be disallowed.*

23. It is observed by the Hon'ble Supreme Court in the case of Azadi Bachao Andolan (supra) that an act which is otherwise valid in law cannot be treated as to evade tax merely on the basis of some suspicious underlying motive supposedly resulting in some economic detriment or prejudice to the Revenue. In the present case genuineness of the claim cannot be impeached. In his regard, we notice that the shares were sold by the assessee from the Demat account for which the consideration is received by the assessee and that shares sold had been issued under the ESOP scheme of the Trust where the options are being exercised by the assessee. We further notice that the assessee has also shown short term capital gain of Rs.4,95,00,000 on sale of 49.50 lakh shares of JMFPPL which supports the submission of assessee that the intention of the assessee was not purposely to reduce the payment of tax. On the other hand the revenue has not brought any material to controvert the contention of assessee. So we cannot countenance the action of Ld.CIT(A)/AO on this issue and uphold the claim of assessee. In view of these discussion and considering the decisions of the Hon'ble Supreme Court, we see no infirmity. We therefore set aside the order of the CIT(A) disallowing the setoff of long term capital loss of Rs.54,90,36,870/- and short term capital loss of Rs.4,65,44,19,508/-.

24. The CIT(A) while upholding the disallowance of set off of losses has also held that the loss as computed by the assessee is not correct for the reason that the provisions of section 55(2)(aa)(ii) of the Act is not applicable in assessee's case. During the course of hearing the Id AR presented various arguments in this regard contending that the provisions of section 55(2)(aa)(ii) is applicable to the impugned transaction. Since we have already held that the set off of loss should allowed in the case of the assessee in the foregoing paras., the submissions of the Id AR and Id DR in this regard is left open.

25. In result the appeal of the assessee is allowed and the appeal of the revenue is dismissed.

Order pronounced in the open court on 04/08/2023.

Sd/-

sd/-

(ABY T VARKEY)	(PADMAVATHY S)
JUDICIAL MEMBER	ACCOUNTANT MEMBER

Mumbai, Dt : 04th August, 2023

Pavanan

प्रतिलिपि अग्रेषित Copy of the Order forwarded to :

1. अपीलार्थी/The Appellant ,
2. प्रतिवादी/ The Respondent.
3. आयकर आयुक्त CIT
4. विभागीय प्रतिनिधि, आय.अपी.अधि., मुंबई/DR, ITAT, Mumbai
6. गार्ड फाइल/Guard file.

BY ORDER,

Asstt. Registrar / Senior Private Secretary

ITAT, Mumbai

//True Copy//

		Date	Initial	
1.	Draft dictated on	27/06		Sr.PS
2.	Draft placed before author	28/06		Sr.PS
3.	Draft proposed & placed before the second member			JM/AM
4.	Draft discussed/approved by Second Member.			JM/AM
5.	Approved Draft comes to the Sr.PS/PS			Sr.PS/PS
6.	Kept for pronouncement on			Sr.PS
7.	File sent to the Bench Clerk			Sr.PS
8.	Date on which file goes to the AR			
9.	Date on which file goes to the Head Clerk.			
10.	Date of dispatch of Order.			
11.	Dictation Pad is enclosed	Yes		

