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### Capital Gains on buyback of equity shares by subsidiary company taxable u/s 46A as not covered as exempt transfer u/s 47(iv) of the Act

Buyback of equity shares by subsidiary company u/s 46A does not get covered u/s 47(iv) and conditions u/s 47(iv) should be fulfilled by the holding company or its nominees.

The Bangalore Tribunal has held that capital gains arising on buyback of shares by the subsidiary company is taxable under section 46A of the Act, as section 45 and Section 46A of the Income tax Act, 1961 operate in different fields and are independent. Section 45 covers actual capital gains on transfer of capital asset while section 46A deals with deemed capital gains on buyback of shares. Section 47(iv) of the Act relating to transactions not regarded as taxable transfer is not applicable as (i) the subsidiary company was not wholly owned by the parent company or its nominees and (ii) Section 47 (iv) is regarding non applicability of section 45 to a transfer of a capital asset by a company to its subsidiary company and regarding buyback of shares.

#### Facts of the case:

Acciona Wind Energy Private Limited<sup>1</sup> (taxpayer) is a company incorporated in India with M/s Acciona Energia International S.A. Spain holding 99.99 percent of the equity share capital and Acciona Energia S.A Spain holding remaining 0.01 percent of the equity share capital of the taxpayer. During the financial year relevant to the assessment year 2014-15, the taxpayer bought back equity shares from the holding company at a price in excess of the issue price and did not withhold tax on the payment of consideration to the foreign parent company.

The Tax Officer passed orders under section 201(1) and 201(1A) of the Act for the default in withholding tax and consequent interest thereon. The CIT(A) held that taxpayer is in default for failing to withhold taxes on buyback of shares by the subsidiary company. Section 46A of the Income tax Act, 1961 (the Act) is a charging provision for gains arising from buyback of shares and would prevail over the general provision of Section 45 of the Act. Section 47 of the Act is limited in its application only to section 45 of the Act and does not apply to buyback of shares to which Section 46A of the Act applies.

#### Decision of ITAT:

##### Whether the condition mentioned under section 47(iv) is fulfilled

The Tribunal discussed that Section 47(iv) of the Income tax Act does not require that parent company should hold the entire share capital of the subsidiary company in its own name as it requires that shares should be held by the parent company and its nominees. Further as per Companies Act, 2013, it is legally impossible to hold whole share capital of subsidiary company by a single holding company. The Tribunal distinguished the decision in the case of Papilion Investments (P.) Ltd<sup>2</sup> relied upon by the taxpayer as in that case, the second shareholder was the director of the Company and held shares jointly with the company. However, in the present case two separate foreign companies hold the shares of the taxpayer, with the second shareholder not being the nominee of the other shareholder. Accordingly, the Tribunal held that the conditions of Section 47(iv) are not fulfilled.

<sup>1</sup> Order dated 20.12.2019 in ITA Nos. 1783 and 1784/Bang/2018 for AY 2014-15

<sup>2</sup> 206 taxman 142

## Whether Section 47(iv) should apply to buyback transaction covered under section 46A?

The Tribunal discussed that Section 45 of the Act is the section regarding profits or gains arising from transfer of the capital asset. Section 46A of the Act was inserted by the Finance Act, 1999 w.e.f 1 April 2000 to enjoin that any consideration received by the shareholder or holder of other specified securities from any company on purchase of its own shares or specified securities held by such shareholder. The difference between the cost of acquisition and the value of consideration received by the shareholder is deemed to be capital gains. There is no requirement of transfer of any capital asset in case of buyback of shares. There is no mention of the term "Transfer" in Section 46A of the Act. Section 47(iv) of the Act is regarding non-applicability of Section 45 of the Act to a transfer of capital asset by a company to its subsidiary company, if the parent company or its nominees hold the whole of share capital.

Further, the Tribunal discussed the following judicial precedents:

- Cadell Wvg. Mill Co. (P.) Ltd.<sup>3</sup> relied upon by the taxpayer, was rejected as the issues involved were different and was for the assessment year 1990-91 i.e., before introduction of section 46A of the Act from the financial year 2000-01.
- Goldman Sachs<sup>4</sup> relied upon by the tax department. The Tribunal observed that this judgment is an authority regarding applicability of section 46A in respect of receipt by shareholder on account of buy back of shares from the concerned company but observed that there was no argument or decision about applicability of section 47 (iv) of the Act in that decision.

The Tribunal held that Section 46A is specifically applicable to buyback of shares and Section 45 and Section 46A operate in different fields and should be read independently, accordingly the Tribunal upheld the order of CIT(A) applying section 46A of the Act to the facts of the case.

### Comments:

The Authority for Advance Ruling (AAR) in *Re RST*<sup>5</sup> and in *Armstrong World Industries Mauritius Multiconsult Ltd., In re*<sup>6</sup> had similarly ruled that the proposed transaction of buyback of shares by subsidiary company is not exempt by virtue of section 47(iv) of the Act.

The shareholder of the taxpayer is from Spain. However, relief under the provisions of the India Spain Double Taxation Avoidance Agreement (DTAA) have not been discussed in the ITAT order, likely, as the gains for the alienation of shares, forms part of a participation of at least 10 percent of the capital stock of the Indian company.

Section 115QA of the Act has been introduced, whereby with effect from 1 June 2013, tax should be payable by the domestic company on the income distributed for buyback of shares.

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<sup>3</sup> 116 Taxmann 77 (Bom)

<sup>4</sup> 70 taxmann.com 46 (Mumbai – Trib.)

<sup>5</sup> AAR 1067 of 2011

<sup>6</sup> A.A.R. NO. 1044 of 2011



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