IN THE INCOME TAX APPELLATE TRIBUNAL
"C''BENCH: BANGALORE

BEFORE SHRI N.V. VASUDEVAN, VICE PRESIDENTAND
SHRI B.R. BASKARAN, ACCOUTANT MEMBER

ITA No.1181/Bang/2018
Assessment Year: 2014-15

M/s. I-Exceed Technology Solutions Pvt. Ltd. SJR Padukone Plaza #51, II Floor 100 Ft. Road, Koramangala Bengaluru-569033 **PAN NO :AACCI6248K**	**Vs.**	Income Tax Officer Ward-3(1)(1) Bengaluru
APPELLANT		**RESPONDENT**

Appellant by	**:**	Shri V. Srinivasan, A.R.
Respondent by	**:**	Smt. R. Premi, D.R.

Date of Hearing	**:**	27.07.2020
Date of Pronouncement	**:**	14.08.2020

O R D E R

PER B.R. BASKARAN, ACCOUNTANT MEMBER:

The assessee has filed this appeal challenging the order dated 7.2.2018 passed by Ld. CIT(A)-3, Bengaluru and it relates to assessment year 2014-15.

2. All the grounds urged by the assessee relate to the addition made by the A.O. u/s 56(2)(viib) of the Income-tax Act,1961 ['the Act' for short] relating to share premium, which was partially confirmed by Ld CIT(A).

3. The facts relating to the case are stated in brief. The assessee company is engaged in the business of developing software products and providing consultancy services to customers in banking and financial services industry. The A.O. noticed that the assessee has issued 6,15,088 equity shares of Rs.10/- each at a premium of Rs.80/- per share to six persons. Accordingly, it has collected share premium of Rs.4,92,07,040/- Out of the above said amount, the AO noticed that the share premium received from resident shareholders was Rs.1,77,77,760/-. Accordingly, he proceeded to examine the collection of share premium in terms of sec.56(2)(viib) of the Act.

4. The assessee furnished a valuation certificate dated 15.12.2012 obtained from a Chartered Accountant in support of the price at which the shares were issued. The A.O. noticed that the C.A. has adopted discounted cash flow method (DCF Method) for valuation of shares. In the valuation report, the accountant had arrived at the value per share at Rs.87.56 per share. However, the assessee has issued shares @ Rs.90/- per share including share premium of Rs.80/- per share. Accordingly, the assessee justified the share premium collected by it.

5. The A.O. noticed that, under DCF method, the valuation has been arrived on the basis of projected figures. Further, it was noticed that the details of projected results have been furnished by the management only and the basis of projections was also not given. Accordingly, the AO rejected DCF method of valuation. The A.O. took the view that the share valuation has to be arrived on the basis of book value, i.e., Net Asset value (NAV) method. On the basis of assets and liabilities of the assessee, the AO worked out the value of per share @ Rs.6.04. Accordingly, the A.O. the view the share premium collected by the assessee is not justified. Since share premium amount collected from resident persons could alone be assessed u/s 56(2)(viib) of the Act, the AO assessed the share premium of Rs.1,77,77,760/- as the share premium collected from resident shareholders.

6. The Ld. CIT(A), in principle, agreed with the view taken by the AO. However, he noticed that the share premium received from resident shareholders is Rs.88,88,880/- only and not Rs.1,77,77,760/- as assessed by the A.O. Accordingly, he confirmed the addition to the extent of Rs.88,88,880/-. Aggrieved, the assessee has filed this appeal before us.

7. We heard the parties and perused the record. We notice that the A.O. did not examine the valuation report furnished by the assessee in which value of shares has been arrived under DCF method. The question as to whether the A.O. could reject the DCF valuation was examined by the Bengaluru Bench of Tribunal in the case of M/s. Futura Business Solutions Pvt. Ltd. (ITA No.3404/Bang/2018) relating to assessment year 2013-14 and the matter was restored to the file of the A.O. with the following observations by following decision rendered by another bench of Tribunal in the case of VBHC Value Homes in ITA No.2541/Bang/2019 order dated 12-06-2020, which in turn followed the decision rendered by Hon'ble Bombay High Court in the case of Vodafore m-pesa Ltd Vs Pr.CIT 164 DTR 257. For the sake of convenience, we extract below the relevant discussions made by the Tribunal in the case of Futura Business Solutions P Ltd (supra):-

"17. With regard to the correctness of DCF method adopted by the Assessee for valuing shares and the procedure to be followed when such method of valuation is not accepted by the AO, the ld. counsel for the Assessee has drawn our attention of the ITAT, Bangalore Bench in the case of VBHC Value Homes in ITA No.2541/Bang/2019 order dated 12-06-2020. The Tribunal, after relying on the decision of the Hon'ble Bombay High Court in the case of Vodafone M-Pesa Ltd Vs Pr.CIT 164 DTR 257 and decision of the ITAT, Bangalore Bench in the case of Innovit Payment Solutions Pvt. Ltd., Vs ITO (2019) 102 Taxmann.com 59. held as follows:

"9. We have considered the rival submissions. First of all, we reproduce paras 11 to 14 from the Tribunal order cited by learned AR of the assessee having been rendered in the case of Innoviti Payment Solutions Pvt. Ltd., Vs. ITO (supra). These paras are as follows:

"11. As per various tribunal orders cited by the learned AR of the assessee, it was held that as per Rule 11UA (2), the assessee can opt for DCF method and if the assessee has so opted for DCF method, the AO cannot discard the same and adopt other method i.e. NAV method of valuing shares. In the case of M/s. Rameshwaram Strong Glass (P) Ltd. vs. The ITO (Supra), the tribunal has reproduced relevant portion of another tribunal order rendered in the case of ITO vs. M/s Universal Polypack (India) Pvt. Ltd. in ITA No. 609/JP/2017 dated 31.01.2018. In this case, the tribunal held that if the assessee has opted for DCF method, the AO cannot challenge the same but the AO is well within his rights to examine the methodology adopted by the assessee and/or underlying assumptions and if he is not satisfied, he can challenge the same and suggest necessary modifications/alterations provided the same are based on sound reasoning and rationale basis. In the same tribunal order, a judgment of Hon'ble Bombay High Court is also taken note of having been rendered in the case of Vodafone M-Pesa Ltd. vs. PCIT as reported in 164 DTR 257. The tribunal has reproduced part of Para 9 of this judgment but we reproduce herein below full Para 9 of this judgment.

> *"9. We note that, the Commissioner of Income-Tax in the impugned order dated 23rd February, 2018 does not deal with the primary grievance of the petitioner. This, even after he concedes with the method of valuation namely, NAV Method or the DCF Method to determine the fair market value of shares has to be done/adopted at the Assessee's option. Nevertheless, he does not deal with the change in the method of valuation by the Assessing Officer which has resulted in the demand. There is certainly no immunity from scrutiny of the valuation report submitted by the Assessee. Therefore, the Assessing Officer is undoubtedly entitled to scrutinise the valuation report and determine a fresh valuation either by himself or by calling for a final determination from an independent valuer to confront the petitioner. However, the basis has to be the DCF Method and it is not open to him to change the method of valuation which has been opted for by the Assessee. If Mr. Mohanty is correct in his submission that a part of demand arising out of the assessment order dated 21st December, 2017 would on adoption of DCF Method will be sustained in part, the same is without working out the figures. This was an exercise which ought to have been done*

> *by the Assessing Officer and that has not been done by him. In fact, he has completely disregarded the DCF Method for arriving at the fair market value. Therefore, the demand in the facts need to be stayed."*

12. As per above Para of this judgment of Hon'ble Bombay High Court, it was held that the AO can scrutinize the valuation report and he can determine a fresh valuation either by himself or by calling a final determination from an independent valuer to confront the assessee. But the basis has to be DCF method and he cannot change the method of valuation which has been opted by the assessee. Hence, in our considered opinion, in the present case, when the guidance of Hon'ble Bombay high Court is available, we should follow this judgment of Hon'ble Bombay High Court in preference to various tribunal orders cited by both sides and therefore, we are not required to examine and consider these tribunal orders. Respectfully following this judgment of Hon'ble Bombay High Court, we set aside the order of CIT (A) and restore the matter to AO for a fresh decision in the light of this judgment of Hon'ble Bombay High Court. The AO should scrutinize the valuation report and he should determine a fresh valuation either by himself or by calling a final determination from an independent valuer and confront the same to the assessee. But the basis has to be DCF method and he cannot change the method of valuation which has been opted by the assessee. In our considered opinion and as per report of research committee of (ICAI) as reproduced above, most critical input of DCF model is the Cash Flow Projections. Hence, the assessee should be asked to establish that such projections by the assessee based on which, the valuation report is prepared by the Chartered accountant is estimated with reasonable certainty by showing that this is a reliable estimate achievable with reasonable certainty on the basis of facts available on the date of valuation and actual result of future cannot be a basis of saying that the estimates of the management are not reasonable and reliable.

13. Before parting, we want to observe that in the present case, past data are available and hence, the same can be used to make a reliable future estimate but in case of a start up where no past data is available, this view of us that the projection should be on the basis of reliable future estimate should not be insisted upon because in those cases, the projections may be on the basis of expectations and in such cases, it should be shown that such expectations are reasonable after considering various macro and micro economic factors affecting the business.

14. In nutshell, our conclusions are as under:-

> *(1) The AO can scrutinize the valuation report and the if the AO is not satisfied with the explanation of the assessee, he has to record the reasons and basis for not accepting the valuation report submitted by the assessee and only*

thereafter, he can go for own valuation or to obtain the fresh valuation report from an independent valuer and confront the same to the assessee. But the basis has to be DCF method and he cannot change the method of valuation which has been opted by the assessee.

(2) For scrutinizing the valuation report, the facts and data available on the date of valuation only has to be considered and actual result of future cannot be a basis to decide about reliability of the projections.

(3) The primary onus to prove the correctness of the valuation Report is on the assessee as he has special knowledge and he is privy to the facts of the company and only he has opted for this method. Hence, he has to satisfy about the correctness of the projections, Discounting factor and Terminal value etc. with the help of Empirical data or industry norm if any and/or Scientific Data, Scientific Method, scientific study and applicable Guidelines regarding DCF Method of Valuation."

10. From the paras reproduced above, it is seen that in this case, the Tribunal has followed the judgment of Hon'ble Bombay High Court rendered in the case of Vodafone M-Pesa Ltd., Vs. Pr. CIT (supra). The Tribunal has noted that as per the judgment of Hon'ble Bombay High Court, it was held that AO can scrutinize the valuation report and he can determine a fresh valuation either by himself or by calling a determination from an independent valuer to confront the assessee but the basis has to be DCF method and he cannot change the method of valuation which has been opted by the assessee. The Tribunal has followed the judgment of Hon'ble Bombay High Court and disregarded various other Tribunal orders against the assessee which were available at that point of time. In the present case also, we prefer to follow the judgment of Hon'ble Bombay High Court rendered in the case of Vodafone M-Pesa Ltd., Vs. Pr. CIT (supra) in preference to the judgment of the Hon'ble Kerala High Court cited by DR of the Revenue rendered in the case of Sunrise Academy of Medical Specialities (India) (P.) Ltd. Vs. ITO (supra) because this is settled position of law by now that if two views are possible then the view favourable to the assessee should be adopted and with regard to various Tribunal orders cited by learned DR of the Revenue which are against the assessee we hold that because we are following a judgment of Hon'ble Bombay High Court rendered in the case of Vodafone M-Pesa Ltd., Vs. Pr. CIT (supra), these tribunal orders are not relevant. In the case of Innoviti Payment Solutions Pvt. Ltd., Vs. ITO (supra), this judgment of Hon'ble Bombay High Court was followed and the matter was restored back to the file of AO for a fresh decision with a direction that AO should follow DCF method only and he cannot change the method opted by the assessee as has been held by the Hon'ble

> Bombay High Court. The relevant paras of this Tribunal order are already reproduced above which contain the directions given by the Tribunal to the AO in that case. In the present case also, we decide this issue on similar line and restore the matter back to the file of AO for a fresh decision with similar directions. Accordingly, ground No.3 of the assessee's appeal is allowed for statistical purposes.

18. The gist of the conclusion is that the law contemplates invoking provisions of section 56(2)(viib) of the Act only in situations where the shares are issued at a premium and at a value higher than the fair market value. The fair market value contemplated in the provisions above is as under: - (a) The fair market value of the shares shall be the value

> (i) As may be determined in accordance with such method as may be prescribed; or
>
> (ii) Any other value to the satisfaction of the Assessing Officer……..

The law provides that, the fair market value may be determined with such method as may be prescribed or the fair market value can be determined to the satisfaction of the Assessing Officer. The provision provides an Assessee two choices of adopting either NAV method or DCF method. If the Assessee determines the fair market value in a method as prescribed, the Assessing Officer does not have a choice to dispute the justification. The methods of valuation are prescribed in Rule 11UA(2) of the Rules. The provisions of Rule 11UA(2) reads as under:-

> "(2) Notwithstanding anything contained in sub-clause (b) of clause (c) of sub-rule (1), the fair market value of unquoted equity shares for the purposes of sub-clause (i) of clause (a) of Explanation to clause (viib) of sub-section (2) of section 56 shall be the value, on the valuation date, of such unquoted equity shares as determined in the following manner under clause (a) or clause (b), at the option of the assessee, namely:—
>
> (a) the fair market value of unquoted equity shares = where, (A–L) × (PV), (PE)

A = book value of the assets in the balance-sheet as reduced by any amount of tax paid as deduction or collection at source or as advance tax payment as reduced by the amount of tax claimed as refund under the Income-tax Act and any amount shown in the balance-sheet as asset including the unamortised amount of deferred expenditure which does not represent the value of any asset;

L = book value of liabilities shown in the balancesheet, but not including the following amounts, namely:—

(i) the paid-up capital in respect of equity shares;

(ii) the amount set apart for payment of dividends on preference shares and equity shares where such dividends have not been declared before the date of transfer at a general body meeting of the company;

(iii) reserves and surplus, by whatever name called, even if the resulting figure is negative, other than those set apart towards depreciation;

(iv) any amount representing provision for taxation, other than amount of tax paid as deduction or collection at source or as advance tax payment as reduced by the amount of tax claimed as refund under the Income-tax Act, to the extent of the excess over the tax payable with reference to the book profits in accordance with the law applicable thereto;

(v) any amount representing provisions made for meeting liabilities, other than ascertained liabilities;

(vi) any amount representing contingent liabilities other than arrears of dividends payable in respect of cumulative preference shares;

P E = total amount of paid up equity share capital as shown in the balance-sheet;

P V = the paid up value of such equity shares; or

(b) the fair market value of the unquoted equity shares determined by a merchant banker or an accountant as per the Discounted Free Cash Flow method.

19. The provisions of Rule 11UA(2)(b) of the Rules provides that, the Assessee can adopt the fair market value as per the above two methods and the choice of method is that of the Assessee. The Tribunal has followed the judgment of Hon'ble Bombay High Court rendered in the case of Vodafone M-Pesa Ltd., Vs. Pr. CIT (supra) and has taken the view that the AO can scrutinize the valuation report and he can determine a fresh valuation either by himself or by calling a determination from an independent valuer to confront the Assessee but the basis has to be DCF method and he cannot change the method of valuation which has been opted by the Assessee. The decision of ITAT, Delhi in the case of Agro Portfolio Ltd. 171 ITD 74 has also been considered by the ITAT, Bangalore in the case of VBHC Value Homes Pvt.Ltd.(supra).

20. The gist of the findings of the Assessing Officer and the ld. CIT(A) on the alleged discrepancies in the valuation report is as under:

1. Growth rate is taken at 12% year after year
2. WACC has been forecasted at 30%
3. The sales have been projected at Rs.2,36,54,400/- for the F.Y.2012-13, Rs.7,88,74,080/- for the F.Y.2013-14 and Rs.14,00,00,000/- for the F.Y.2014-15, whereas the actuals as per the returns filed are Rs.17,67,146/-, Rs.4,50,06,477/- and Rs.4,26,45,399/- only. In view of this, the growth rate of 12% is stated to be not acceptable.
4. The net profit has been projected at Rs.30,94,769/- for the F.Y.2012-13, Rs.1,29,86,330/- for the F.Y.2013-14 and Rs.2,16,06,523/- for the F.Y.2014-15, whereas the actuals as per the returns filed are (-) Rs.5,40,078/-, (-) Rs.1,25,58,421/- and (-) Rs.2,70,00,184/- only.

21. We are of the view that, the Assessing Officer has erred in considering the actuals of revenue and profits declared in the future years as a basis to dispute the projections. At the time of valuing the shares as on 16.04.2012, the actual results of the later years would not be available. What is required for arriving at the fair market value by following the DCF method are the expected and projected revenues. Accordingly the valuation is on the basis of estimates of future income contemplated at the point of time when the valuation was made. It has been clarified by the Assessee that the product which was being developed by the Assessee has substantial value and the Assessee was able to raise funds to the tune of Rs.50.13 crores from international market

22. In view of the above legal position, we are of view that the issue with regard to valuation has to be decided afresh by the AO on the lines indicated in the decision of ITAT, Bangalore in the case of VBHC Value Homes Pvt.Ltd., Vs ITO (supra) i.e.,

(i) the AO can scrutinize the valuation report and he can determine a fresh valuation either by himself or by calling a determination from an independent valuer to confront the assessee but the basis has to be DCF method and he cannot change the method of valuation which has been opted by the assessee.

(ii) For scrutinizing the valuation report, the facts and data available on the date of valuation only has to be considered and actual result of future cannot be a basis to decide about reliability of the projections. The primary onus to prove the correctness of the valuation Report is on the assessee as he has special knowledge and he is privy to the facts of the company and only he has opted for this method. Hence, he has to satisfy about the correctness of the projections, Discounting factor and Terminal value etc. with the help of Empirical data or industry norm if any and/or Scientific Data, Scientific Method, Scientific study and applicable Guidelines regarding DCF Method of Valuation.

The order of ld.CIT(A) is accordingly set aside for deciding the issue afresh after due opportunity of hearing to the Assessee.
23. In the result, the appeal is allowed for statistical purpose.

8. Since facts are identical, following the above said decision of the Bengaluru Bench of Tribunal, we set aside the order passed by Ld. CIT(A) and restore the issue to the file of the A.O. with identical directions as given in the above said case.

9. In the result, the appeal filed by the assessee is treated as allowed for statistical purposes.

Order pronounced in the open court on 14-08-2020.

Sd/-	**Sd/-**
(N.V. Vasudevan)	**(B.R. Baskaran)**
Vice President	**Accountant Member**

Bangalore,
Dated 14th Aug, 2020.
VG/SPS

Copy to:

1. The Applicant
2. The Respondent
3. The CIT
4. The CIT(A)
5. The DR, ITAT, Bangalore.
6. Guard file

By order

Asst. Registrar, ITAT, Bangalore