1. **<u>Questionnaire No. 4 of notice dated 23.10.2019:</u>**

1.1. In this regards, your goodself had asked to furnish details regarding the further shares issued and allotted during the year to Mr. ABC and compliance of same with the provisions of section 56(2)(viib) of the Income Tax Act, 1961.

1.2. In this regard, it is submitted that the assessee company had issues 10,000 shares to Mr. ABC on 01.04.2019 at a total consideration of Rs. 250 per share including face value of Rs. 10 each and securities premium of Rs. 240 each. We hereby attach copy of Board Resolution passed by the Board of Directors on 21.03.2019 and Special Resolution passed by the company in its extraordinary general meeting on 01.04.2019 is attached herewith on page no. …………… Further, copy of relevant extract of the bank statement indicating such receipt from Mr. ABC and copy of share certificate issued in such regards are attached herewith on page no. ……….. for your kind perusal.

1.3. In respect of determining the consideration for issuance and allotment of shares, the assessee company had obtained valuation report from the Registered Valuer as mandatorily required under Companies Act, 2013. The Registered Valuer determined the value as per discounted cash flow method in such valuation report and the value of share determined therein was Rs. 285 per share. ***(Copy of such valuation report is attached herewith on page no. …………)***

1.4. In this regard, we most humbly draw your kind attention to provisions of section 56(2)(viib) of the act read with rule 11UA(2) of the Income Tax Rules, 1962 wherein, it has been provided that no private limited company except venture capitalist or specified companies as notified by CG, shall issue shares to a resident at a consideration higher than the fair market value of such share as computed in accordance with the manner prescribed u/r 11UA of the rules. Whereas, provisions of rule 11UA prescribes two method of computation of fair market value of shares and any of such prescribed method can be applied at the option of the assessee for determining the fair market value of the shares in hand. Relevant extract of the said rule is reproduced hereunder for your ready reference:

> ***Provisions of Section 56(2)(viib)***
>
> ***(viib) where a company, not being a company in which the public are substantially interested, receives, in any previous year, from any person being a resident, any consideration for issue of shares that exceeds the face value of***

such shares, the aggregate consideration received for such shares as exceeds the fair market value of the shares:

Provided that this clause shall not apply where the consideration for issue of shares is received—

(i) by a venture capital undertaking from a venture capital company or a venture capital fund 9[or a specified fund]; or

(ii) by a company from a class or classes of persons as may be notified by the Central Government in this behalf:

Provided further that where the provisions of this clause have not been applied to a company on account of fulfilment of conditions specified in the notification issued under clause (ii) of the first proviso and such company fails to comply with any of those conditions, then, any consideration received for issue of share that exceeds the fair market value of such share shall be deemed to be the income of that company chargeable to income-tax for the previous year in which such failure has taken place and, it shall also be deemed that the company has under reported the said income in consequence of the misreporting referred to in sub-section (8) and sub-section (9) of section 270A for the said previous year.

Explanation.—For the purposes of this clause,—

(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) as may be substantiated by the company to the satisfaction of the Assessing Officer, based on the value, on the date of issue of shares, of its assets, including intangible assets being goodwill, know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature,

whichever is higher;

(aa) "specified fund" means a fund established or incorporated in India in the form of a trust or a company or a limited liability partnership or a body corporate which has been granted a certificate of registration as a Category I or a Category II Alternative Investment Fund and is regulated under the Securities and Exchange Board of India (Alternative Investment Fund) Regulations, 2012 made under the Securities and Exchange Board of India Act, 1992 (15 of 1992);

(ab) "trust" means a trust established under the Indian Trusts Act, 1882 (2 of 1882) or under any other law for the time being in force;

(b) "venture capital company", "venture capital fund" and "venture capital undertaking" shall have the meanings respectively assigned to them in clause (a), clause (b) and clause (c) of Explanation to clause (23FB) of section 10;

Provisions of Rule 11UA

*(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* $= \frac{(A-L)}{(PE)} \times (PV)$,

where,

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 balance-sheet, 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;*

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

PV = *the paid up value of such equity shares; or*

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

1.5. In light of the aforesaid legal provisions, it is pertinent to note that in case of further issue of shares by a private limited company, valuation of fair market value as per discounted cash flow method as computed by a merchant banker is permissible to be considered as fair market value of such shares. In the instant matter of the assessee company, the shares were issued at total consideration of Rs. 250 per share whereas the fair market value determined in accordance with Rule 11UA(2) of the rules i.e. value determined by merchant banker (being registered valuer mentioned at Para 1.3 above) as per discounted cash flow method is Rs. 285 per share. As such, the impugned transaction of issue of fresh shares to Mr. ABC at a total consideration of Rs. 250 per share is in due compliance with provisions of section 56(2)(viib) of the act and no addition is required to be made in such regards.