

ITA No. 2307/KOL/2018
A.Y. 2015-2016
&
C.O. No. 16/KOL/2021
(in ITA No. 2307/KOL/2018)
Godhuli Dealcom LLP

**IN THE INCOME TAX APPELLATE TRIBUNAL,
KOLKATA 'A' BENCH, KOLKATA**

**Before Shri Rajpal Yadav, Vice-President (KZ)
&
Shri Manish Borad, Accountant Member**

**I.T.A. No. 2307/KOL/2018
Assessment Year: 2015-2016**

Income Tax Officer,.....Appellant
Ward-34(4), Kolkata,
Aayakar Bhawan, Purba,
110, Shanti Pally, 7th Floor, Room No. 712,
Kolkata-700107

-Vs.-

M/s. Godhuli Dealcom LLP,.....Respondent
A/213, Shanti Gopal Chamber,
Vikas Marg, Shakarpur,
Delhi-110092
[PAN:AANFG1802H]

&

C.O. No. 16KOL/2021
(in ITA No. 2307/KOL/2018)
Assessment Year: 2015-2016

M/s. Godhuli Dealcom LLP,.....Cross Objector
A/213, Shanti Gopal Chamber,
Vikas Marg, Shakarpur,

Delhi-110092
[PAN:AANFG1802H]

-Vs.-

Income Tax Officer,.....Respondent
Ward-34(4), Kolkata,
Aayakar Bhawan, Purba,
110, Shanti Pally, 7th Floor, Room No. 712,
Kolkata-700107

Appearances by:

Md. Ghayas Uddin, CIT(DR), appeared on behalf of the Revenue

Shri A.K. Tibrewal, FCA & Shri Amit Agarwal, Advocate, appeared on behalf of the assessee

Date of concluding the hearing : March 30th, 2022

Date of pronouncing the order : June 28, 2022

ORDER

Per Manish Borad, Accountant Member:-

This appeal filed by the Revenue and the Cross Objection filed by the assessee pertaining to the Assessment Year (in short “AY”) 2015-16 are directed against the order of Id. Commissioner of Income-tax (Appeals)-10, Kolkata [in short Id. “CIT(A)”] dated 24 08.2018 vide Appeal No. 843/CIT(A)- 10/W34(4)/ 15-16/2017-18/Kol., which is arising out of the assessment order framed u/s 143(3) of the Income Tax Act, 1961 (in short the “Act”) dated 28.12.2017.

2. Registry has informed that the Cross Objection filed by the assessee is time-barred by 996 days. On perusal of the condonation application filed by the assessee dated 09.09.2021, we observe that the Revenue's appeal came for hearing before this Tribunal on 17.08.2020 and directions were given to the Id. D.R. to produce the assessment records and the order of the competent authority shows that the scope of limited scrutiny was large in view of the instructions of Central Board of Direct Taxes. The matter was adjourned to 01.10.2020, 01.01.2021 and 09.02.2021 to produce the assessment records. On 2nd August, 2021, the case was fixed for hearing and further adjourned with the verbal direction. In compliance thereto, the assessee has filed the Cross Objection. On going through the order-sheet dated 02.08.2021, we find that there is no specific direction by this Tribunal directing the assessee to file the Cross Objection. However, looking to the flow of events and the issue involved, we are satisfied with the assessee's submission that delay in filing the Cross Objection is not intentional and the assessee was under the bonafide belief that it was not required to file the Cross Objection. We, therefore, condone the delay of 996 days in filing of the Cross Objection and admit the same for adjudication.

3. The Revenue has raised the following grounds of appeal:-

"1. On the facts and circumstances of the case, the Id. CIT(A) erred in deleting the securities premium reserve of Rs. 12,87,23,000/- which stood transferred by the

erstwhile company to the assessee-LLP upon conversion as a taxable profit.

2. Moreover there was no substantial increase in business activity. But there were substantial increase in salary and rent without deduction of any professional tax or no tax deducted at source. ”

4. The assessee in its Cross Objection before the Tribunal has raised the following grounds:

“1. That Id. CIT(A) erred in not adjudicating the additional ground taken by the appellant-LLP.

2. That the case of the assessee was selected for limited scrutiny but the AO made additions beyond the scope of limited scrutiny without taking approval of the competent authority and therefore the Id. CIT(A) should have quashed those additions made beyond the scope of limited scrutiny.”

5. Brief facts of the case are that the assessee is a Limited liability Partnership (in short ‘LLP’) and stated to be engaged in the business of buying and selling of merchandise and commission agent. The LLP was incorporated during the year under appeal and its first return of income was filed on 07.09.2015 declaring income of Rs.12,616/-. The case of the assessee was selected for limited scrutiny through CASS for the following two reasons:-

- (i) Low income in comparison to High Loan/Advances/investment in shares;

(ii) High interest expenditure against new capital added in work-in-progress or addition made to fixed assets.

Notices under section 143(2) and 142(1) of the Act duly served upon the assessee along with the questionnaire. Ld. Assessing Officer examined the various details and while going through the source of the investment details, also went on to examine the security premium and share capital transferred from the Private Limited Company namely Godhuli Dealcom Pvt. Limited. After observing the issues in detail, the Assessing Officer came to a conclusion that the security premium of Rs.12,87,23,000/- which was received in the Pvt. Limited Company before being converted into M/s. Godhuli Dealcom LLP, i.e. the assessee, cannot be transferred under the head "Reserve & Surplus" of the newly incorporated LLP and since the assessee transferred to reserve and surplus, the security premium reserve of Rs.12,87,23,000/- is to be considered as income of the LLP and accordingly added the same to the income of the assessee. The ld. Assessing Officer also disallowed the expenses at Rs.10,00,000/- and the income assessed at Rs.12,97,63,830/-.

6. Aggrieved, the assessee preferred appeal before the ld. CIT(Appeals) raising the issues on merits as well as also raising legal issue through an additional ground that the assessment order framed under section 143(3) of the Act is void, *ab initio* and illegal as there was no sanction to do the assessment *qua* the complete scrutiny. However, the ld. CIT(Appeals) did not dealt with the legal issue raised by the assessee. So far as the merits of the case are concerned, ld. CIT(Appeals) deleted both the additions made by the ld. Assessing Officer.

7. Aggrieved, the Revenue is now in appeal before the Tribunal, whereas the assessee has raised the legal ground through its Cross Objection.

8. We will first take up the legal ground raised in the Cross Objection through which the assessee has contended that the case of the assessee was selected for limited scrutiny but the ld. Assessing Officer made the additions beyond the scope of limited scrutiny without taking approval of the competent authority and, therefore, the ld. CIT(Appeals) should have quashed assessment proceeding carried out beyond the scope of limited scrutiny.

9. Ld. counsel for the assessee referred to paper book dated 29.06.2021, the Instruction No.20/2015 dated 29.12.2015, Instruction No. 5/2016 dated 14.07.2016 and Notification No. DGIT(Viz.)/HQ/81/2017-18 dated 30.11.2017. Reliance has also been placed on the following four decisions in support of the contention that without necessary approval, the ld. Assessing Officer cannot go for complete scrutiny as the instant case is selected for limited scrutiny:-

(1) Sanjeev Kumar Khemka -vs.- Pr. CIT

ITA No.1361/KOL/2016 (Judgment dated 02.06.2017) at pages 1-12;

(2) Chengamari Tea Co. Ltd. -vs.- ACIT

(ITA No.812/KOL/2019 (Judgment dated 31.01.2020) at pages 13-21;

(3) JDB Finance -vs.- DCIT

(ITA No.127/GAU/2019 (judgment dated 16.09.2020) at pages 22-28;

(4) Sonali Hemant Bhavsar -vs.- Pr. CIT

(ITA No.742/M/2019 (Judgment dated 17.05.2019) at pages 29-42

10. Per contra, learned Departmental Representative (in short ld. D.R.) referred to the paper book dated 17.02.2022 in which a letter dated 05.04.2021 issued by the ITO, Ward-34(1), Kolkata addressing the ld. CIT(DR), ITAT-1, Kolkata is enclosed stating that the Assessing Officer raised the inquiry only with regard to

the reasons for which the limited scrutiny was initiated and, therefore, there was no requirement of taking approval from the competent authority. Reference was also made to the written submissions filed by the ITO, Ward-34(1), Kolkata through the ld. CIT(DR).

11. We have heard the rival contentions, perused the relevant material available on record. The legal ground raised in the Cross Objection by the assessee is that the ld. Assessing Officer exceeded the jurisdiction while framing the assessment under section 143(3) of the Act by going for complete scrutiny in place of the limited scrutiny without taking approval of the competent authority. Though this legal issue was raised by the assessee before the ld. CIT(Appeals) but the same has not been adjudicated by the ld. CIT(Appeals). However, since the issue is a legal issue and can be raised at any stage, we are adjudicating the same in view of the ratio laid down by the Hon'ble Supreme Court in the case of NTPC Limited -vs.- CIT (1998) 229 ITR 383.

12. All the submissions and decisions relied by the ld. Counsel for the assessee only revolve around the ratio that if an Assessing Officer converts the scrutiny from limited scrutiny to complete scrutiny, the same can be done only after getting the necessary approval from the authorities prescribed under the Act. Various circulars cited by the ld. Counsel for the assessee also support this contention.

13. Now before us, the first issue is that whether the ld. Assessing Officer travelled beyond the scope of limited scrutiny or not. In case, the Assessing Officer has not travelled beyond the limited scrutiny, then the issue of getting approval from the competent authority will end and in case it is otherwise, then it needs to be examined that whether the ld. Assessing Officer took approval from the competent authority.

14. Now to examine that whether ld. Assessing Officer exceeded the jurisdiction beyond the scope provided for Limited Scrutiny, we observe that the assessee-LLP filed its first return of income in A.Y. 2015-16 on being converted from Private Limited Company to Limited Liability Partnership, which is the year under appeal. The return of income is filed electronically and all the datas in this return of income are captured online in a soft form. The case of the assessee is selected for limited scrutiny for the following two reasons:-

(i) Low income in comparison to High Loan/Advances/investment in shares;

(ii) High interest expenditure against new capital added in work-in-progress or addition made to fixed assets.

15. We need to appreciate the fact that limited scrutiny is carried out with the assistance of computers and is based on the data filled by the assessee in their IT return certain parameters inserted by the Department in the computer software, which helps to pin points/captures certain aspects of the financial transactions of an assessee, comparing the same with the previous years' data like increase and decrease in turnover/profits/loans/fixed assets/capital, low profit rates, vis-a-vis high turnover and various other permutations. Based on such information through the computer software, the case is selected for limited scrutiny.

16. Once a case is selected for limited scrutiny, though the role of the ld. Assessing Officer is confined to examine the issues for which the case is selected for limited scrutiny but then the Assessing Officer has to go into the depth of such issue and minutely examine the facts attached thereto. The ld. Assessing Officer just cannot casually examine the issue and come to the conclusion because the reasons are just indicative in nature and to reach the depth of the issue raised in the limited scrutiny, the Assessing Officer has to make the examination deeper and deeper examining all the aspects linked to such reason. In case of the complete scrutiny,

1d. Assessing Officer has to examine all the financial transactions carried out by the assessee during the year, whereas in limited scrutiny's issues are limited but the same needs more intense, accurate and deep examination of the issue and facts attached to it.

17. Now coming to the fact of the present case, we notice that the assessee-LLP was converted from the Private Limited to LLP and this was the first year of its incorporation and the return was e-filed submitting various financial datas. In the LLP, which is newly incorporated and there is no past history and showing a meagre income of Rs.40,826.50 during the year, has shown partner's capital contribution at Rs.27,00,000/-, reserve & surplus of Rs.12.88 crores (Approx.), unsecured loan of Rs.1.30 crores, investments at Rs.43.90 lakhs, loans and advances at Rs.13.97 crores (approx.) and other current assets and liabilities. In the Profit & Loss Account, only income is interest of Rs.14.29 lakhs and after claiming expenses, net profit of Rs.40,826.50 has been shown. Based on such datas and the certain parameters of the computer system of the Department, assessee's case was selected for limited scrutiny.

18. The first issue is low income in comparison to high loans/advances/investment in shares. The reason is just an indication for the ld. Assessing Officer to examine various aspects. Once the low income is to be examined, it has to be seen in consonance of the higher loans standing in the balance-sheet and in the present case, the interest income is shown only at Rs.14.29 lakhs, whereas the loans and advances are standing to the tune of Rs.13.97 crores. When the ld. Assessing Officer went on to examine this aspect of low income, he then asked the assessee about the investment made during the year because the ld. Assessing Officer wanted to see why the assessee has earned low income when there are huge loans and advances. When the Assessing Officer was examining the loans and advances, he came to know that this is the first year of incorporation and the LLP has been converted from the company. Ld. Assessing Officer asked the assessee about the source of investment. Then based on this question, the assessee submitted that the source is the share capital and security premium of the erstwhile company before being converted to LLP and the ld. Assessing Officer went on to examine the issue of security premium reserve.

19. Similar is the case for the second reason for high interest expenditure against new capital added in work-

in-progress or addition made to fixed assets and the catch words are high interest expenditure, new capital added which in this case is partner's capital and Reserve & Surplus (Security Premium Reserve). Though the reasons are not very specific but it is also a fact that any detailed questionnaire is not supplied to the Assessing Officer as to what he needs to examine for a particular reason. There are few catchy words in the reasons which are only supplied to the ld. Assessing Officer and thereafter ld. Assessing Officer needs to decide at his own end to examine a particular reason. On overall examining the financial statements of the LLP, erstwhile Private Limited Company, the reasons for selecting the case for limited scrutiny which covers various aspects of the assessee including low income, high loans, advances, investment in shares, high interest expenditure, new assets added in work-in-progress and additions in fixed assets, we find that the ld. Assessing Officer has carried out the assessment proceedings only within the parameters provided under "limited scrutiny" and has fairly done well by reaching to the depth of the issue and was well within the jurisdiction to examine the source of investment i.e. share capital, Security Premium and unsecured loan of erstwhile Private Limited Company made during the year which were the source of investments fetching very low income. The source of

investment as evident from the balance-sheet of LLP, is the share capital and security premium which was carried over from the Private Limited Company.

20. We are, therefore, of the considered view that the ld. Assessing Officer has not exceeded the jurisdiction and has not travelled beyond the reasons for selecting the case of the limited scrutiny and ld. Assessing Officer has not done complete scrutiny of the case and has restricted his scrutiny proceedings only with regard to the two reasons mentioned hereinabove for carrying out limited scrutiny. We, therefore, find no merit in the legal issue raised by the assessee in the Cross Objection. The decisions referred and relied upon by the ld. counsel for the assessee and the Instruction of the CBDT referred in the paper book could have been of any help to the assessee only if Assessing Officer has converted the scrutiny from limited to complete scrutiny, which is not the case before us. The legal issue raised in the Cross Objection filed by the assessee is dismissed.

21. Now we come to the Revenue's appeal. The first issue raised in the Revenue's appeal is that the ld. CIT(Appeals) has erred in deleting the addition for securities premium reserve of Rs.12,87,23,000/-, which is transferred by the erstwhile company to the assessee-LLP upon conversion as a Reserve & Surplus.

22. Brief facts related to the issue are that the assessee-LLP was converted from a Private Limited Company during the financial year 2014-15, i.e. the first year after incorporation of LLP. In the balance-sheet, reserve and surplus of Rs.12,87,23,000/- is appearing. The said reserve and surplus was security premium reserve of the erstwhile Private Limited Company namely Godhuli Dealcom Private Limited (in short GDPL). Ld. Assessing Officer has treated the same as income of the assessee for the year under appeal.

23. Before us, ld. D.R. vehemently argued supporting the order of the ld. Assessing Officer.

24. Per contra, ld. counsel for the assessee relied on the submissions made before the ld. CIT(Appeals), referred to the paper book containing 39 pages filed on 14.07.2020 and heavily relied on the following finding of the ld. CIT(Appeals), who has deleted the said addition observing as follows:-

“1. I have carefully considered the submissions furnished by the Ld. AR of the appellant and the observations & findings recorded by the Ld. AO. The facts involved in this case are in narrow compass. The assessee-LLP was formed by virtue of LLP agreement dated 02.05.2014. M/s Godhuli Dealcom Pvt Ltd, an erstwhile company was converted into the assessee-LLP. In terms of the LLP agreement all the assets & liabilities of the erstwhile company was transferred to the converted LLP and the shareholders of the company continued as the Partners of the LLP. For the relevant year the assessee filed its return of income

declaring total income of Rs. 12,616/-. The conversion of the company into LLP was claimed as exempt in terms of the provisions of Section 47(xiiib) of the Act. The Ld. AO however was of the view that the assessee-LLP did not satisfy the conditions prescribed in Section 47(xiiib) and therefore taxed the securities premium balance of the erstwhile company as the taxable income of the assessee-LLP.

2. In the appellate proceedings the Ld. AR of the appellant assailed the order of the Ld. AO on several fronts. The Ld. AR contended that all the conditions prescribed in Section 47(xiiib) stood satisfied and in that view of the matter the benefit of exemption could not be denied. The Ld. AR further argued that even if the benefit of exemption was to be denied then the tax liability, if any, would arise in the hands of the transferor i.e. the erstwhile company and not the transferee i.e. the assessee LLP. The Ld. AR further submitted in the alternate that the gain arising on transfer ought to be computed to be the difference between the value recorded in the appellant's books and the value appearing in the erstwhile company's books. It was claimed that on mere conversion of company into LLP, the entire securities premium of the company could not be brought to tax. It was submitted that even the Ld. AO was unable to justify the basis & manner of taxing the entire sum in as much as the relevant provision of the Act under which he sought to tax the entire securities premium of the LLP.

3. On giving due consideration to the facts of the case and the averments made by the Ld. AR of the appellant, I find sufficient force in the arguments put forth by him. It is noted that the erstwhile company M/s Godhuli Dealcom Pvt Ltd was formed in the FY 2007-08. From the financial statements of the M/s Godhuli Dealcom Pvt Ltd it is observed that the said company had assets & liabilities remained the same upon conversion. The said erstwhile company was thereafter converted by virtue of the LLP agreement dated 02.05.2014 whereby all the assets & liabilities of the erstwhile company vested with the newly formed LLP and the existing shareholders of the company became the partners of the LLP. In this factual background, it would now be relevant to examine the provisions of Section 47(xiiib) which read as follows:

(xiiib) any transfer of a capital asset or intangible asset by a private company or unlisted public company (hereafter in this clause referred to as the company) to a limited liability partnership or any transfer of a share or shares held in the company by a shareholder as a result of conversion of the

company into a limited liability partnership in accordance with the provisions of section 56 or section 57 of the Limited Liability Partnership Act, 2008 (6 of 2009):

Provided that—

- (a) all the assets and liabilities of the company immediately before the conversion become the assets and liabilities of the limited liability partnership;*
- (b) all the shareholders of the company immediately before the conversion become the partners of the limited liability partnership and their capital contribution and profit sharing ratio in the limited liability partnership are in the same proportion as their shareholding in the company on the date of conversion;*
- (c) the shareholders of the company do not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of share in profit and capital contribution in the limited liability partnership;*
- (d) the aggregate of the profit sharing ratio of the shareholders of the company in the limited liability partnership shall not be less than fifty per cent at any time during the period of five years from the date of conversion;*
- (e) the total sales, turnover or gross receipts in the business of the company in any of the three previous years preceding the previous year in which the conversion takes place does not exceed sixty lakh rupees; and*
- (f) no amount is paid, either directly or indirectly, to any partner out of balance of accumulated profit standing in the accounts of the company on the date of conversion for a period of three years from the date of conversion.*

Explanation.—For the purposes of this clause, the expressions "private company" and "unlisted public company" shall have the meanings⁵² respectively assigned to them in the Limited Liability Partnership Act, 2008 (6 of 2009))

4. From the facts on record it is observed that the assessee-LLP indeed satisfied all the conditions as laid down in Section 47(xiiib) and in that view of the matter the transfer of assets & liabilities to the LLP was exempt and not liable to tax. It is noted that the Ld. AO in his impugned order has made various irrelevant observations with regard to the past history of the erstwhile company which has no bearing whatsoever on the tax liability of the appellant-LLP. From the above provision, it is apparent that in order to avail the benefit of exemption of Section 47(xiiib), the shareholders of the company preceding the conversion has to continue to be the partners of the LLP and their profit sharing ratio should also continue in the same proportion. In the facts involved

in the present the case, this fact that the shareholders of the erstwhile company had only continued as partners of LLP remains undisputed by the Ld. AO. Instead it is noted that the Ld. AO has emphasized on irrelevant considerations such as the manner in which the shareholders purchased the shares & the non-availability of particulars of earlier shareholders of the company to deny the benefit of exemption, which in my considered view is wholly immaterial to ascertain the compliance of the provisions of Section 47(xiiib) in the tax assessment of the appellant-LLP.

5. *For the reasons set out above I find sufficient merit in the claim of the Ld. AR of the appellant that the Ld. AO's action of assessing the securities premium of Rs. 12,87,23,000/- by denying the benefit of exemption u/s 47(xiiib) was wholly untenable on facts & in law. I also find force in the alternate claim of the Ld. AR that under no circumstance could any adverse view be drawn in the hands of the appellant who was the transferee in the present case. Undeniably the transferor was the erstwhile company and therefore no adverse view could be drawn against the appellant-LLP even if the exemption u/s 47(xiiib) was denied.*

6. *Overall therefore, I hold that the Ld. AO gross erred in assessing the securities premium reserve of Rs. 12,87,23,000/- which stood transferred by the erstwhile company to the appellant-LLP upon conversion as the taxable profit of the appellant and the same is hereby deleted. This ground is therefore allowed”.*

25. We have heard the rival contentions, perused the relevant records placed before us. In Ground No. 1, the grievance of the revenue is that the ld. CIT(Appeals) has erred in deleting the addition made by the Assessing Officer taxing the reserve and surplus as income of the LLP, which was previously shown as security premium reserve in the erstwhile Private Limited Company ‘GDPL’ before being converted to LLP.

26. We find that the company named Godhuli Dealcom Private Limited (in short 'GDPL') was incorporated on 05.03.2008 and regularly filed return of income till A.Y. 2014-15. On 16.04.2014, GDPL was converted to Godhuli Dealcom LLP (in short 'GDLLP') and a Certificate of Registration on conversion was issued by the Ministry of Corporate Affairs and all the assets and liabilities of the GDPL became the assets and liabilities of Godhuli Dealcom LLP. On such transaction of conversion of Private Limited Company to a Limited liability partnership is governed by the provision of section 47(xiii b) of the Act and for the sake of convenience, the provision of section 47(xiii b) of the Act is reproduced below:-

“Section 47 (xiii b) :- any transfer of a capital asset or intangible asset by a private company or unlisted public company (hereafter in this clause referred to as the company) to a limited liability partnership or any transfer of a share or shares held in the company by a shareholder as a result of conversion of the company into a limited liability partnership in accordance with the provisions of section 56 or section 57 of the Limited Liability Partnership Act, 2008 (6 of 2009):

Provided that—

(a) all the assets and liabilities of the company immediately before the conversion become the assets and liabilities of the limited liability partnership;

(b) all the shareholders of the company immediately before the conversion become the partners of the limited liability partnership and their capital contribution and profit sharing ratio in the limited liability partnership are in the same proportion as their shareholding in the company on the date of conversion;

(c) *the shareholders of the company do not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of share in profit and capital contribution in the limited liability partnership;*

(d) *the aggregate of the profit sharing ratio of the shareholders of the company in the limited liability partnership shall not be less than fifty per cent at any time during the period of five years from the date of conversion;*

(e) *the total sales, turnover or gross receipts in the business of the company in any of the three previous years preceding the previous year in which the conversion takes place does not exceed sixty lakh rupees; [***]*

(ea) *the total value of the assets as appearing in the books of account of the company in any of the three previous years preceding the previous year in which the conversion takes place does not exceed five crore rupees; and*

(f) *no amount is paid, either directly or indirectly, to any partner out of balance of accumulated profit standing in the accounts of the company on the date of conversion for a period of three years from the date of conversion.*

27. So far as the case in hand is concerned, we find that if the case of assessee does not fall under the proviso (a) to (f), then the said transaction is not to be treated as transfer u/s. 2(47) of the Act. But in case, any of the conditions is not fulfilled, then the said transfer will have to be examined in the light of 2(47) r.w.r.t. section 45 of the Act. On perusal of the above exceptions in light of the facts of the instant case, we find that exception (a) is worth examining. Exception (a) in proviso to section 47(xiii b) of the Act contemplates that all the assets and liabilities of the company immediately before the conversion become

the assets and liabilities of the Limited liability partnership. Now looking to the balance-sheet as on 31.03.2014 of GDPL, we find that under the head “reserve and surplus’, there are two items i.e. (a) security premium reserve of Rs.12,87,23,000/- and (ii) surplus in the statement of profit and loss account at Rs.41,137.68. We are concerned here with the amount of security premium reserve. This amount was standing as on 31.03.2014 and it was brought forward from preceding year. So far as the genuineness of the security premium reserve is concerned, the same is not in dispute before us. The said security premium reserve has been shown as “Reserve and Surplus” in the newly formed LLP in the subsequent year. Now Exception (a) says that all the assets and liabilities of the company before the conversion become assets and liabilities of the limited liability partnership. Now security premium reserve has been treated as reserve and surplus. As far as security premium reserve is concerned, section 52 of the Companies Act, 2013 (Chapter IV Share Capital and Debenture) deals with application of premium received on the issue of shares and the same reads as follow:-

(1) Where a company issues shares at a premium, whether for cash or otherwise, a sum equal to the aggregate amount of the premium received on those shares shall be transferred to a

“securities premium account” and the provisions of this Act relating to reduction of share capital of a company shall, except as provided in this section, apply as if the securities premium account were the paid-up share capital of the company.

(2) Notwithstanding anything contained in sub-section (1), the securities premium account may be applied by the company—

(a) towards the issue of unissued shares of the company to the members of the company as fully paid bonus shares;

(b) in writing off the preliminary expenses of the company;

(c) in writing off the expenses of, or the commission paid or discount allowed on, any issue of shares or debenture of the company;

(d) in providing for the premium payable on the redemption of any redeemable preference shares or of any debentures of the company; or

(e) for the purchase of its own shares or other securities under section 68.

(3) The securities premium account may, notwithstanding anything contained in sub-sections (1) and (2), be applied by such class of companies, as may be prescribed and whose financial statement comply with the Accounting Standards prescribed for such class of companies under section 133,—

(a) in paying up unissued equity shares of the company to be issued to members of the company as fully paid bonus shares; or

(b) in writing off the expenses of or the commission paid or discount allowed on any issue of equity shares of the company; or

(c) for the purchase of its own shares or other securities under section 68.

28. On going through section 52 of the Companies Act, 2013, we find that there are specific provisions for the application of Security Premium received by the Company on the issue of its share capital, but nowhere in the provision of section 52 of the Companies Act, 2013 states that the Security Premium can be distributed as income to its shareholders. Now in the instant case, the assessee has claimed that all the assets and liabilities of the erstwhile Private Limited Company 'GDPL' has been converted into assets and liabilities of newly incorporated 'GDLLP' and the said conversion is not a transfer u/s. 2(47) of the Act as the proviso (a) to (e) of section 47(xiii b) of the Act are not attracted. In the instant case, clause (a) of the proviso to section 47(xiii b) needs to be examined. Since the Security Premium Reserve of the erstwhile Company was a liability and not eligible to be distributed as dividend to its shareholders, the same needs to carry the same characteristic in the converted LLP. But in the newly formed LLP, the Security Premium Reserve has been shown under the head "Reserve & Surplus", which for the purpose of 'GDLLP' is a profit available for distribution to its designated partners after three years from the date of said conversion. Now since the nature of liability of Security Premium Reserve is not the same to the nature of liability shown in Reserve & Surplus in the newly formed LLP, in our considered view, the assessee's case falls under the proviso (a) and since all the assets and liabilities are not converted into assets and liabilities of the Limited Liability Partnership, the said conversion

is a transfer u/s. 2(47) of the Act and provision of section 45 of the Act needs to come into operation.

29. As far as treatment of Security Premium Reserve in the books of newly incorporated LLP is concerned, we observe that Security Premium is not accumulated profit but it is a part of share capital to the extent it was received while issuing in shares by the erstwhile Private Limited Company. Since the Private Limited Company has been converted into a LLP, the only option left for the treatment of the Security Premium Reserve is to bring it to tax in the year in which the Company is converted into LLP. Such Security Premium standing in the balance-sheet at the close of the year before being converted first needs to be brought to tax under the provision of section 56(1) of the Act and then the amount needs to be transferred to Reserve & Surplus and which will thereafter be free for withdrawal by the designated partners of the LLP as per the provision of the Act.

30. We find that the ld. CIT(Appeals) failed to examine this aspect of the Security Premium Reserve, which the ld. Assessing Officer has rightly observed in the assessment order. We also find merit in the finding of the ld. Assessing Officer for the reason that this issue of examining the treatment of Security Premium Reserve is possible only while examining the case of the assessee for the year in which such conversion takes place. Because if it is not examined in the year of conversion and the balance of Reserve & Surplus converted from the Security Premium Reserve

is transferred to Reserve & Surplus Account and carried forward to subsequent years, then it will not be easy for the revenue authorities to track such adjustment.

31. We, therefore, under the given facts and circumstances of the case in view of the options available for utilization of Security Premium Reserve as per the provision of section 52 of the Companies Act, 2013, absence of clear-cut provisions for treatment of such Security Premium Reserve which though is a liability not available for distribution to shareholders of the Private Limited Company, but once the conversion takes place, its treatment in the LLP is only possible by way of treating such Security Premium as income of the LLP under section 56(1) of the Act as “income from the other sources” and to be brought to tax by crediting it in the Profit & Loss Account and debiting the Security Premium Reserve Account, which will bring the Security Premium Reserve balance as NIL and the Reserve & Surplus will be the income shown under section 56(1) of the Act and it will be brought to tax in the year when the Private Limited Company is converted into LLP and in the instant case, i.e. A.Y. 2015-16 for which the ld. Assessing Officer has rightly made the addition for the Security Premium Reserve of the erstwhile Private Limited at Rs.12,87,23,000/- as income of the newly incorporated LLP. We, therefore, reverse the finding of the ld. CIT(Appeals) and confirm the addition made by the ld. Assessing Officer and allow Ground No. 1 raised by the Revenue.

32. As far as Ground No. 2 is concerned challenging the action of the ld. CIT(Appeals) deleting the disallowance of expenses of Rs.10,00,000/-, we find that this disallowance includes disallowance of rent at Rs.1,80,000/- and the remaining balance towards salary and other expenditure. So far as the rent expenditure is concerned, the assessee has filed the details of rent paid to Munush Chand HUF which are incurred in cash at Rs.1,72,000/- , which is below the limit provided u/s 194I of the Act. This disallowance of rent expenditure is deleted. As regards the remaining sum is concerned, the same relates to salary expenditure but no details of the same have been filed before the lower authorities. We direct the assessee to furnish the necessary details before the ld. Assessing Officer and if ld. Assessing Officer is satisfied, he can allow the claim in accordance with law. Thus Ground No. 2 is partly allowed for statistical purposes.

33. In the result, the appeal of the Revenue is partly allowed for statistical purposes and the Cross Objection raised by the assessee is dismissed.

Order pronounced in the open Court on June 28, 2022.

Sd/-
(Rajpal Yadav)
Vice-President (KZ)

Sd/-
(Manish Borad)
Accountant Member

Kolkata, the 28th day of June, 2022

ITA No. 2307/KOL/2018
A.Y. 2015-2016
&
C.O. No. 16/KOL/2021
(in ITA No. 2307/KOL/2018)
Godhuli Dealcom LLP

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- (3) *Commissioner of Income Tax- Kolkata,*
- (4) *The Departmental Representative*
- (5) *Guard File*

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By order

Assistant Registrar,
Income Tax Appellate Tribunal,
Kolkata Benches, Kolkata

Laha/Sr. P.S.