

AO was justified in rejecting DCF method to calculate FMV of shares if no evidence was produced for validity of data

Summary – The Delhi ITAT in a recent case of Agro Portfolio (P.) Ltd., (the Assessee) held that where assessee allotted shares to a company and fair market value of shares was done by a Merchant banker only on basis of Direct Cash Flow (DCF) method, only depending on data supplied by assessee and no evidence was produced for verifying correctness of data supplied by assessee, Assessing Officer was justified in rejecting DCF method and adopting Net Asset Value method

Facts

- The assessee company was engaged in the business to acquire by original subscription, tender, purchase, exchange or otherwise held shares, stocks, etc. The assessee allotted 3,15,000 equity shares of face value of Rs. 10 each at a premium of Rs. 40 per share. The said allotment was done by the assessee company in pursuance to provision of section 56(2)(viib). The fair market value of the share was determined at Rs. 50 on the basis of Discounted Cash Flow Method, which was done by one Merchant Banker. The assessee filed its return of income declaring loss of Rs. 53,083.
- The Assessing Officer made addition of Rs. 1.27 crores under section 56(2)(viib) rejecting the valuation report of the said Merchant Banker and independently determined the value of shares at Rs. 9.60 each. Amount over and above the value of share over Rs. 9.60 *i.e.* Rs. 40.40 each was added to the assessee's income. Thus, Rs. 1.27 crores (Rs. 40.40 x 3,15,000) was disallowed and added to assessee's income.
- On appeal, the Commissioner (Appeals) dismissed the contentions of assessee.
- On appeal to the High Court:

Held

- It is not possible to accept the contentions of the assessee that in view of the provisions under section 56(2)(viib), read with rule 11UA(2). Assessing Officer had no jurisdiction to adopt a different method than the one adopted by the assessee, and if for any reason the Assessing Officer has any doubt recording such valuation report and does not agree with the same is bound to make a reference to the Income Tax Department Valuation Officer to determine the fair market value of such capital asset. This is so because unless and until the assessee produces the evidences to substantiate the basis of projections in cash flow and provides reasonable connectivity between those projections in cash flow with the reality evidences by the material, it is not possible even for the Departmental Valuation Officer to conduct any exercise of verification of the acceptability of the value determined by the merchant banker. This is more particularly in view of the long disclaimer appended by the merchant banker in the paper book which clearly establishes that no independent

enquiry is caused by merchant banker to verify the truth or otherwise the figures furnished by the assessee at least on test basis. The merchant bankers solely relied upon an assumed without independent verification, the truthfulness accuracy and completeness of the information and the financial data provided by the company. A perusal of this long disclaimer clearly shows that the merchant banker did not do anything reflecting their expertise, except mere applying the formula to the data provided by the assessee. It is not possible to brush aside the contention of the revenue that the possibility of tailoring the data by applying the reverse engineering to the predetermined conclusions.

- There has not been any possibility of verifying the correctness or otherwise of the data supplied by the assessee to the merchant banker, in absence of which the correctness of the result of DCF method cannot be verified. This left no option to the Assessing Officer but to reject the DCF method and to go by NAV method to determine the FMV of the shares. Without such evidence, it serves no purpose even if the matter is referred to the Department's Valuation Officer. Therefore, there is not any illegality or irregularity in the approach or conclusions by the authorities below. While confirming the same, we dismissed the appeal as devoid of merits. In the result, the appeal of the assessee is dismissed.