

Government of India
Ministry of Finance
Department of Revenue
Central Board of Direct Taxes

North Block, New Delhi, the 26th of February, 2016

Subject: Clarification regarding nature of share Buy-back transactions under Income-tax Act, 1961 - regd.-

As per provisions of Section 46A of the Income-tax Act, 1961 ('Act'), applicable with effect from 01.04.2000, any consideration received by a shareholder or a holder of other specified securities from any company on purchase of its own shares/other specified securities shall be, subject to provisions contained in section 48, deemed to be capital gains. Further, sub-clause (iv) of clause (22) of section 2 of the Act excludes any payment made by a company on purchase of its own shares in accordance with the provisions contained in section 77A of the Companies Act from the ambit of 'dividend'. Finance Act, 2013 subsequently introduced section 115QA (w.e.f. 01.06.2013) to provide that any amount of distributed income by a company on buyback of unlisted shares shall be charged to tax and the company so distributing its income shall be liable to pay additional income-tax at the rate of twenty percent of the distributed income.

2. It has been brought to the notice of the Board that the provisions of law regarding buy-back of shares since introduction of dividend distribution tax ('DDT') under section 115O of the Act w.e.f. 01.04.2003 till 31.05.2013 are being interpreted in a conflicting manner by the tax authorities and taxpayers, thereby giving rise to disputes on this issue. It has been contended that subsequent to introduction of section 115QA in the Act and placing reliance on a decision of the Authority for Advance Ruling (AAR No. P of 2010), income-tax authorities, in some cases have sought to re-characterize the purchase consideration received on account of buy-back of shares, undertaken prior to 01.06.2013, as dividend and accordingly, subjecting the amounts so distributed by the companies to DDT.

3. The matter has been examined. Between the period 01.04.2000 till 31.05.2013 as mentioned in para 1 above, provisions of section 46A read with section 2(22)(iv) of the Act clearly provide that the income arising to a shareholder on buy-back of shares was to be treated as income from capital gains and not dividend income. Further clarity on this issue emerges on perusal of Circular No. 779 dated 14.09.1999 of CBDT, which in Para 28 has mentioned following reasons for introducing section 46A in the statute:

"28 Clarification of tax issues arising out of the provision to allow buy-back of shares by the companies -

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28.1 The Companies (Amendment) Ordinance, 1998 [subsequently enacted as the Companies (Amendment) Act, 1999], inserted section 77A in the Companies Act, 1956, which allows a company to purchase its own shares subject to certain conditions. The shares bought back have to be extinguished and physically destroyed and the company is precluded from making any further issue of securities within a period of 24 months from such buy-back.

28.2 The above newly introduced provisions of buy-back of shares threw up certain issues in relation to the existing provisions of the Income-tax Act. The two principal issues are whether it would give rise to deemed dividend under section 2(22) of the Income-tax Act and whether any capital gains would arise in the hands of the shareholder. The legal position on both the issues were far from clear and settled and there was apprehension that there will be unnecessary litigation unless the issues are clarified with finality.

28.3 The Act, therefore, has amended clause (22) of section 2 of the Income-tax Act by inserting a new clause to provide that dividend does not include any payment made by a company on purchase of its own shares in accordance with the provisions contained in section 77A of the Companies Act, 1956. It has also inserted a new section, namely, section 46A in the Income-tax Act, to provide that any consideration received by a shareholder, or a holder of other specified securities from any company on purchase of its own shares or other specified securities shall be, subject to provisions contained in section 48, deemed to be the capital gains."

(Emphasis supplied)

4. Accordingly, the CBDT hereby clarifies that consideration received on buyback of shares between the period 01.04.2000 till 31.05.2013 would be taxed as capital gains in the hands of the recipient in accordance with section 46A of the Act and no such amount shall be treated as dividend in view of provisions of section 2(22)(iv).

5. With a view to bring about further clarity on this issue as a step towards non-adversarial tax regime, the CBDT hereby directs that as a matter of general principle, no fresh notice for assessment/reassessment/non-deduction of TDS at source shall be issued where buyback of shares has taken place prior to 01.06.2013 and the case is covered under section 46A read with section 2(22)(iv) of the Act. In cases where notices have already been issued and assessment proceedings are pending, tax authorities shall complete the assessment keeping in view the above legal position.

6. The above may be brought to the notice of all for necessary compliance.

7. Hindi version to follow.

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(Rohit Garg)

Deputy Secretary to the Government of India

(F.No. 225/19/2016/ITA.II)

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