

## Honorable Delhi High Court Rules that Buy-back of Own Shares is a Capital Reduction and Not Acquisition of Property; Section 56(2)(x) Not Applicable

The Delhi High Court held that buy-back of a company's own shares amounts to reduction of share capital and does not constitute acquisition of property, rendering addition under section 56(2)(x) untenable. The Court affirmed that once shares are bought back and extinguished, no asset remains to trigger deemed income, and therefore the Assessing Officer's view treating the buy-back as generating profit was flawed and unsustainable in law.

### **Key Facts of the case:**

- The assessee company was engaged in the business of share broking and trade clearing. During AY 2018–19, it undertook a buy-back of 28.62 lakh equity shares at a price of INR 313.40 per share, resulting in a total outflow of approximately INR 89.71 crore. The company duly paid buy-back tax on the distributed income under section 115QA of the Income-tax Act.
- While completing assessment under sections 153A read with 143(3),

the Assessing Officer observed that the fair market value (FMV) of the shares as determined under Rule 11UA was INR 370.46 per share.

Treating the buy-back as an acquisition of “property,” the Assessing Officer invoked section 56(2)(x) and added the differential amount of around INR 16.33 crore as income.

- In appellate proceedings, the Commissioner (Appeals) held that the transaction was not a simple purchase of shares but a buy-back of the company’s own shares, which effectively resulted in reduction of share capital. Consequently, the provisions of section 56(2)(x) read with Rule 11UA were held to be inapplicable, and the addition was deleted.
- The Income Tax Appellate Tribunal, in second appeal, upheld the order of the Commissioner (Appeals) and dismissed the Department’s appeal.

### **Judgement (High Court): On appeal by the department before the Honorable High Court, the court observed as under;**

The case involves an important legal issue, where it is undisputed that the respondent-company had purchased its own shares under a buy-back scheme. The buyback was carried out in accordance with law at a price determined by the Board of Directors and duly approved by the shareholders, with consideration paid out of free reserves and securities premium. The Court



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observed that, under the framework of the Companies Act, a company can purchase its own shares only by following the procedure prescribed under section 68, as such a transaction is otherwise not permissible. Shares, though capable of being treated as property in certain contexts, represent capital contributed by shareholders in the case of the issuing company. Accordingly, a buy-back essentially results in reduction of share capital. Further, section 68 mandates that the shares so bought back must be extinguished and destroyed, reinforcing the position that no asset continues to exist thereafter. In this context, the Court held that once the shares are extinguished, it cannot be said that the company has acquired any property so as to give rise to deemed income. A person cannot be taxed for so-called deemed profit from the property (shares) which accrues to

it consequent to destruction of the very same property. Because, once the shares are bought back, the purported property extinguishes or vanishes. Hence, the very hypothesis that the respondent-company had acquired an asset at lesser rate than the fair market value has no legs to stand on. Buy-back of its own shares is antitheses to buying an asset. Therefore, the assumption that the company acquired shares at a value lower than fair market value is incorrect, as buy-back of own shares is fundamentally different from acquisition of an asset. The Court also observed that although the Department's interpretation of section 56(2)(x) may appear attractive at first, it does not stand scrutiny when tested against the principles of company law and the Income-tax Act. While it was noted that the Tribunal had incorrectly relied on a decision based on section 56(2)(viiia), this did not

affect the ultimate conclusion, as the Tribunal had otherwise properly examined the issue and upheld the well-reasoned order of the Commissioner (Appeals). Accordingly, the Court held that the Commissioner (Appeals) was justified in allowing the appeal and rejecting the addition made by the Assessing Officer.

### **Conclusion:**

The Delhi High Court's decision brings much-needed clarity to an area that has seen a lot of disputes. It emphasizes that tax implications under the Income-tax Act, 1961 should be determined based on the true nature of the transaction and not viewed in isolation. In the case of share buy-back, the Court has rightly treated it as a reduction of share capital rather than a purchase of property, which helps in better understanding the correct tax position.

**Source : High Court of Delhi (ITA 364/2024 dated 07.04.2026) in the case of PCIT, New DelhiVs M/s Globe Capital Market Ltd.**



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