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INTRODUCTION

A negotiated control acquisition of listed shares can produce an unmodelled tax cost for the acquirer. The parties may negotiate a price reflecting a control premium, diligence findings, deal risk and transfer restrictions. Yet, where the acquisition is completed off-market and the quoted price appreciates between signing and closing, tax law may treat that appreciation as a benefit received by the buyer, even where the buyer has neither negotiated nor economically captured that increase.

This potential outcome arises from section 56(2)(x) of the Income-tax Act, 1961 ("**ITA 1961**"). The provision taxes, subject to specified exceptions and thresholds, property received for inadequate consideration by reference to its prescribed fair market value ("**FMV**"). Under the Income-tax Act, 2025 ("**ITA 2025**"), applicable with effect from 1 April 2026, the corresponding provision is section 92(2)(m), with the valuation methodology now prescribed in Rules 56 and 57 of the Income-tax Rules, 2026 ("**IT Rules 2026**").

The provision has a clear anti-abuse rationale: addressing transfers of wealth through gifts and undervalued transactions. The difficulty arises when a mechanical rule deems the quoted price to be value, notwithstanding that commercial circumstances or regulatory requirements dictated a different transaction price.

The issue is not whether negotiated transactions should be insulated from section 56(2)(x) or section 92(2)(m), or whether contractual price should displace the statutory valuation rule. It is whether the FMV mechanism should apply where the difference from quoted price reflects signing-to-closing drift, regulatory conditionality, market microstructure or other commercial factors, rather than an economic benefit conferred on the recipient.

**From Gift Tax to section 92(2)(m) of ITA 2025:
The Evolution of an Anti-Abuse Rule**

The present provision reflects a gradual expansion of the tax law's response to transfers below apparent market value. Following the abolition of the gift tax regime, section 56 was progressively expanded to cover specified receipts without or for inadequate consideration.

Provision	Broad Scope	Policy Context
Gift Tax		
Gift-Tax Act, 1958	Gift tax levied on the donor on taxable gifts	Complemented estate duty; abolished for gifts made on or after 1 October 1998
ITA 1961		
Section 56(2)(v)	Sums of money exceeding INR 25,000 received without consideration by an individual/ HUF	Reintroduced taxation of specified gift-like receipts after abolition of Gift Tax
Section 56(2)(vi)	Sums of money exceeding INR 50,000 in aggregate received without consideration by an individual/ Hindu Undivided Family (" HUF ")	Recalibrated threshold to an aggregate basis
Section 56(2)(vii)	Money, immovable property and specified movable property received by individuals/HUFs without or for inadequate consideration	Extended the anti-abuse framework from money to property
Section 56(2)(viii)	Shares of closely held companies received by firms/ closely held companies without or for inadequate consideration	Addressed undervalued transfers of unlisted shares
Section 56(2)(x)	Any person; specified money and property receipts	Finance Act 2017 consolidated and expanded the framework
ITA 2025		
Section 92(2)(m)	Any person; specified money and property receipts	Carries forward s. 56(2)(x) substantively unchanged under the new Act, effective 1 April 2026

The legislative history identifies the mischief at which the provisions were directed. The Central Board of Direct Taxes ("**CBDT**"), in Circular No. 1/2011¹ explaining section 56(2)(vii) of the ITA 1961, described the provision as a 'counter evasion mechanism' intended to prevent laundering of unaccounted income under the garb of gifts, and stated that the intention was not to tax transactions carried out in the normal course of business or trade.

Section 56(2)(x) of the ITA 1961 extended the rule to cover receipts by 'any person'. Section 92(2)(m) of the ITA 2025 retains this architecture: specified property received below prescribed FMV can give rise to 'Income from other sources'.

What does the Law treat as Fair Market Value?

For shares falling within the definition of 'quoted shares or securities', the statutory framework is apparently straightforward. Rule 57 of the IT Rules 2026 distinguishes

¹ F.No.142/1/2011-SO(TPL), dated 6 April 2011.

between transactions executed through and outside a recognised stock exchange.

Transaction	Statutory FMV	Practical Consequence
Through a recognised stock exchange	Transaction value recorded on the exchange	Actual exchange price is the statutory benchmark
Off-market, with trading on valuation date	Lowest quoted price on any recognised stock exchange on the valuation date	Negotiated price is displaced by an observable market price
Off-market, with no trading on valuation date	Lowest quoted price on the immediately preceding trading date	A prior market price becomes the benchmark

Rule 56 of the IT Rules 2026 defines 'quoted shares or securities' as shares or securities quoted on a recognised stock exchange with regularity from time to time, where the quotations are based on current transactions made in the ordinary course of business. It also defines the 'valuation date', for section 92 of the ITA 2025, by reference to the date on which the property or consideration is received by the assessee. Accordingly, in an off-market acquisition of quoted shares, the relevant date is ordinarily the date of receipt and not the date on which the acquisition agreement was signed.

The distinction assumes importance where regulatory approvals separate signing from closing: the price may be fixed at signing, but the shares are transferred only at closing, after the quoted price has moved materially.

When the Valuation Rule meets commercial reality

Control Acquisitions: Can a Screen Price Capture a Control Premium?

- ▶ A quoted market price indicates the price at which shares trade on-market; it may not reflect the negotiated price of a block carrying control, strategic influence, or attendant contractual rights and obligations.
- ▶ For an off-market transfer, however, the rule looks to the lowest quoted price on the valuation date, comparing a negotiated block price with a liquid public-market trade. The disconnect is most pronounced where free float is limited or market depth is thin, but it is not confined to such stocks: even in a liquid market, a control transaction and a screen trade may represent different economic propositions. The price negotiated in a control deal may reflect a control premium or liquidity discount, competing bids, diligence findings, representations and indemnities, financing constraints, transaction certainty and execution risk.
- ▶ The issue arose directly in *Vivira Investment and Trading Private Limited v. Assistant Commissioner of Income Tax*², involving an off-market acquisition of approximately 1.53 crore listed shares at INR 653.29 per share against the lowest quoted price of INR 873. The addition under section 56(2)(x) of the ITA 1961 was challenged, inter alia, on the basis that the negotiated price reflected a bona fide commercial transaction and should not be tested mechanically against the quoted price. The Mumbai Tribunal admitted additional pricing evidence and remanded the matter for fresh consideration without deciding the issue.

² 2025 SCC OnLine ITAT 7366.

The Signing-to-Closing Gap: Conditions Precedent and Interim-Period Price Drift

- ▶ Where price is fixed at signing but completion awaits regulatory requirements, an acquisition may require compliance with the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 ("**SEBI Takeover Code**") and competition, sectoral or foreign-exchange approvals. The buyer is meanwhile committed to the agreed price but cannot complete the transaction.
- ▶ Consider an SPA executed at INR 500 per share. Pending satisfaction of conditions precedent, the quoted price rises to INR 650 following an announcement or broader market movement. If the shares are received off-market at closing, the statutory FMV may be INR 650. The acquirer has therefore paid INR 500 per share but is potentially taxed on INR 150 per share of deemed income, with no ability to monetise the appreciation.
- ▶ Yet the increase may not represent a benefit transferred by the seller. The seller agreed INR 500, while the buyer could not sell at INR 650 before closing and may have been subject to standstill restrictions. The difference may therefore reflect market movement during the approval process and not a concession by the seller in the negotiated price.
- ▶ The point is stronger where standstill arrangements leave the economic and voting rights with the seller until completion: the distinction between contractual commitment and actual receipt then becomes critical.

SEBI Pricing: When the securities law has already determined the price

- ▶ Listed-share transactions are also subject to securities regulations. Regulation 8 of the SEBI Takeover Code prescribes pricing mechanisms for open offers, including reference to highest negotiated price, historical volume-weighted average prices and specified market measures. The resulting price may diverge from the screen price at closing.
- ▶ This raises a question of harmonious construction between the two statutes: where securities law requires a prescribed pricing methodology, should tax law treat the difference from a contemporaneous quoted price as a taxable benefit?
- ▶ Securities regulation does not determine income-tax liability; the regimes serve different purposes. Nevertheless, the ITA 1961 or ITA 2025 should not be construed in disregard of the regulatory framework within which the transaction had to be undertaken. Where price results from a mandatory or structured regulatory mechanism, that should inform whether the recipient was economically enriched.

Lock-in restrictions: When is a listed share not a 'quoted share'?

- ▶ Transfer restrictions sharpen the distinction between listing and marketability. In *Deputy Commissioner of Income Tax v. BPL Ltd.*³, the Supreme Court, in the context of the wealth-tax laws, treated locked-in shares as unquoted because they could not be traded and there were no current transactions in the ordinary course of business, recognising that transfer restrictions affect valuation.
- ▶ A similar approach was adopted in *Hero MotoCorp Ltd. v. Deputy Commissioner*

³ 2022 SCC OnLine SC 1405.

of *Income Tax*⁴, where the Delhi Tribunal declined to benchmark the off-market acquisition of Honda's 26% stake in Hero Honda against quoted market price, given the broader commercial arrangement and contractual transfer restrictions. Though decided under section 28(iv) of the ITA 1961, it reinforces that the quoted price may not reflect the value of a substantial negotiated block, particularly where the shares are subject to transfer restrictions.

- ▶ More recently, in *Assistant Commissioner of Income Tax v. Ajay Singh*⁵, involving the acquisition of a substantial block of SpiceJet shares subject to a lock-in, the Delhi Tribunal remanded the matter to the assessing officer to examine the appropriate valuation of the shares for purposes of section 56(2)(x) of the ITA 1961. The ruling nonetheless treats the lock-in as relevant, rather than quoted price as determinative.
- ▶ Where a legally enforceable restriction prevents the holder from realising the quoted price, the assumption that it represents the value of the property received requires closer scrutiny.

Is Section 56(2)(x) / Section 92(2)(m) intended to tax bona fide transactions?

The history of section 56(2) of the ITA 1961 and the CBDT's publications indicate that the provision targeted disguised transfers and laundering of unaccounted wealth, rather than every commercial transaction where prescribed FMV exceeds the negotiated price.

That purpose does not create a general 'commercial transaction' exemption. Section 56(2)(x) / section 92(2)(m) is a deeming provision that must be given effect according to its terms. Where the provision admits of more than one construction, the construction that advances the legislative purpose should ordinarily prevail over one that extends the provision beyond the mischief it was intended to address.

Judicial limits on the reach of anti-abuse provisions

In *K.P. Varghese v. Income Tax Officer*⁶, the Supreme Court rejected a literal application of the then section 52(2) of ITA 1961 that would have permitted substitution of fair market value merely because it exceeded the stated consideration. Having regard to the object of the provision, the Court held that it was intended to address cases involving understatement of consideration, and not bona fide transactions where the stated consideration reflected the actual bargain between the parties.

The decisions in *Sudhir Menon HUF v. Assistant Commissioner of Income Tax*⁷ and *Assistant Commissioner of Income Tax v. Subhodh Menon*⁸ are more directly relevant to the section 56 regime. In *Sudhir Menon HUF* (supra), the Mumbai Tribunal held that a proportionate rights issue did not give rise to taxable income, recognising that the value of the additional shares was offset by the corresponding dilution of the existing shareholding. *Subhodh Menon* (supra) followed this reasoning and, importantly, also referred to the CBDT's stated legislative intent that the provision was not intended to apply to transactions undertaken in the normal course of business.

These decisions do not establish a general exemption for bona fide or arm's-length

4 ITA 1053 (Del) / 2023.

5 2025 SCC OnLine ITAT 5238.

6 (1981) 4 SCC 173.

7 2014 SCC OnLine ITAT 118.

8 ITA 676 and 2776 (Mum) / 2015.

transactions. They support the narrower proposition that an anti-abuse provision must be construed having regard to the transaction, statutory language and the targeted mischief, and not by reference to a valuation differential alone.

The Central Question: What is the taxpayer actually receiving?

Section 56(2)(x) / Section 92(2)(m) is triggered by receipt of property for inadequate consideration; the valuation rules supply the measure of the deemed income and are not an independent charging mechanism. The question remains whether the taxpayer has received property within the charging provision.

For quoted shares, prescribed FMV can move independently of the bargain because of market sentiment, announcements, sector movements, liquidity or volatility. Price drift between signing and closing is not, without more, evidence of value transfer by the seller.

The stronger cases are not those where the taxpayer merely says the negotiated price was 'fair'; they are those where the facts show why quoted price is an imperfect proxy: an arm's-length price for a control block, unconnected parties, a competitive process with confirmatory diligence, closing deferred by regulatory conditionality outside the parties' control, and no ability for the acquirer to monetise the intervening appreciation.

The evidentiary record will matter. The SPA and shareholders' agreement, board and investment committee papers, valuation analysis, bid history, regulatory correspondence, standstill provisions and market data may all demonstrate the commercial basis for the price.

Recalibrating the Valuation Framework

The present framework could be strengthened without undermining the anti-abuse purpose of section 56(2)(x) / section 92(2)(m). Three changes merit consideration:

- ▶ **Execution-Date Valuation for Delayed Closings:** Where consideration is fixed under a binding agreement and closing is deferred solely on account of regulatory approvals or other conditions precedent, FMV could be determined by reference to the execution date. This would prevent interim-period market movements from creating a tax differential that formed no part of the agreed economics.
- ▶ **Safe Harbour for Market-Price Variations:** A tolerance band could be introduced for off-market transfers of quoted shares, recognising that market prices fluctuate and that a modest divergence from the statutory benchmark does not necessarily represent a transfer of economic benefit.
- ▶ **Recognition of Regulatory Pricing Mechanisms:** Where securities law prescribes a pricing mechanism, that price could carry a rebuttable presumption of arm's-length value without becoming conclusive for all tax purposes.

These changes would preserve the rule's anti-abuse efficacy while removing deal-timing noise, by distinguishing genuine valuation disputes from cases where the statutory benchmark is disconnected from transaction economics.

CONCLUSION

Taxing Value, Not Volatility

Section 56(2)(x) / Section 92(2)(m) addresses a real anti-abuse concern: property can be transferred at an artificial price. The difficulty lies not in the charging provision but in the application of a rigid valuation proxy where it ceases to reflect the economics of the property received.

Listed shares illustrate the problem well. An observable screen price is not necessarily the correct measure for every transaction: a control block carrying governance rights differs from a marginal screen trade, a locked-in share from a freely tradable share, and a signing price from one observed months later at closing.

The ITA 2025 and IT Rules 2026 preserve the earlier architecture. The interpretive question therefore remains: where statutory FMV materially differs from the price independently negotiated and paid, does the difference represent income, or merely movement in a market benchmark?

The answer turns on the statutory language and the facts of each case. The better approach keeps the anti-abuse purpose of section 56(2)(x) / section 92(2)(m) in view while recognising regulated capital-market realities. The objective is not to immunise negotiated prices, but to tax genuine economic benefit without mistaking market volatility, regulatory delay or transaction mechanics for one.

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