आयकर अपीलीय अधिकरण, मुंबई न्यायपीठ 'ई' मुंबई

IN THE INCOME TAX APPELLATE TRIBUNAL
"E" BENCH, MUMBAI

श्री बी. रामकोटय्य, लेखा सदस्य, एवं श्री अमित शुक्ला, न्यायिक सदस्य के समक्ष

BEFORE SHRI B. RAMAKOTAIAH, ACCOUNTANT MEMBER AND
SHRI AMIT SHUKLA, JUDICIAL MEMBER

आयकर अपील सं. / ITA no. 3063/Mum./2011
(निर्धारण वर्ष / Assessment Year : 2006–07)

आयकर अपील सं. / ITA no. 3064/Mum./2011
(निर्धारण वर्ष / Assessment Year : 2007–08)

M/s. Trinetram Consultants P. Ltd.
601/602, Vinayak Aangan
Old Prabhadevi Road
Mumbai 400 025

……….……… अपीलार्थी / Appellant

बनाम v/s

Dy. Commissioner of Income Tax
Ward–8(3), Mumbai

.………..…… प्रत्यर्थी / Respondent

स्थायी लेखा सं./ Permanent Account Number – AAACT72200

राजस्व की ओर से / Assessee by : Mr. Vijay Mehta
निर्धारिती की ओर से / Revenue by : Mr. Manoj Kumar

सुनवाई की तारीख / Date of Hearing – 05.02.2013	आदेश घोषणा की तारीख / Date of Order – 05.04.2013

आदेश / ORDER

अमित शुक्ला, न्यायिक सदस्य के द्वारा /
PER AMIT SHUKLA, J.M.

The present appeals preferred by the Assessee, are against the impugned orders of even date 25th March 2011, passed by the learned

Commissioner (Appeals)–XVIII, Mumbai, for the quantum of assessment passed under section 143(3) of the Income Tax Act, 1961 (for short *"the Act"*), for the assessment years 2006–07 and 2007–08 respectively. Since both these appeals pertain to the same assessee involving common issues arising out of identical set of facts and circumstances, therefore, as a matter of convenience, these appeals were heard together and are being disposed off by way of this consolidated order. However, in order to understand the implication, it would be necessary to take note of the facts of one appeal. We are, accordingly, narrating the facts, as they appear in the appeal in ITA no. 3063/Mum./2011, for assessment year 2006–07.

2. The sole common dispute which we need to adjudicate in these appeals is with regard to the direction of the learned Commissioner (Appeals) in treating the short term capital gain on shares and mutual funds aggregating to ₹ 1,83,55,523 for assessment year 2006–07 and ₹ 58,57,807 for assessment year 2007–08 as business income.

3. <u>Facts in brief</u>:– The assessee is a private limited company and the nature of business is stated to be consultancy relating to tours and travels and allied service. The Assessing Officer noted that the assessee had shown income of ₹ 39.75 lacs under the head *"Income From Interest"* and ₹ 3.93 lacs under the head *"Income From Other Sources"*. On a perusal of the details of *"Income From Other Sources"*, he observed that it mainly consist of gain on sale of shares at ₹ 3.29 crores, dividend income on shares of mutual fund at ₹ 30.59 lacs and commission received at ₹ 15.31 lacs. Against these receipts, the assessee had claimed expenses of ₹ 86.40 lacs consisting of tour and travel expenses and administrative expenses. It was further observed by the Assessing Officer that the receipts in the year were mainly on account of transaction in shares and on perusal of the Balance Sheet revealed that the major portion of the funds available at ₹ 20.51 crores have been invested in shares / units at ₹ 16.99 crores. Besides this, unsecured loan taken during the year at ₹ 1.55 crores have also deployed in purchase of shares and units. After verifying the transactions and the activities of the

assessee, he came to the conclusion that the short term capital gains and long term capital gains declared by the assessee is nothing but *"Income From Business"*. The Assessing Officer's finding has been summarized by the Commissioner (Appeals) in Para–3.1 in the following manner:–

(i) The details of purchase and sale shows that there were regular and numerous transactions;

(ii) The major activity of the Assessee is dealing in shares and the activity stated to be the business activity of the Assessee has not contributed any receipts for the year;

(iii) The expenses claimed including staff expenses and other administrative expenses have mainly been channelised towards the share trading activity;

(iv) It cannot be accepted that merely because the shares / units have been shown as investment in the balance sheet and not as stock–in–trade it has to be inferred that the activity has to be considered as investment & gain should be taxed as capital gain;

(v) For obtaining capital gains and dividend is a fact based interpretation as the transactions can be given both the colour of investment and as a business. Courts of the land is helpful to draw inference as to whether the intention of the Assessee was to trade in shares or was merely to hold it as a capital for earning dividend;

(vi) The decision of the Hon'ble Madras High Court in the case of CIT v/s N.S.S. Investment P. Ltd. reported at 277 ITR 149, wherein a company can hold some shares as stock–in–trade for the purpose of doing business of buying and sale of such shares, while at the same time it can also hold some other shares as its capital for the purpose of earning dividend income;

(vii) The dividend earned by the Assessee is only ₹ 38.75 lakhs against total investment of ₹ 16.99 crores made during the year including the shares purchased and sold during the year. It cannot be the case of the Assessee that it had invested ₹ 16.99 crores for earning a return of ₹ 30.59 lakhs i.e., a yield of 1.8% when it could have cooly earned a safe return of around 10% in a nationalized bank without taking any risk and efforts. Accordingly, the intention of the Assessee fails on this ground to prove that the investments are solely for investment and earning of dividend and not for trading;

(viii) The Assessee has entered into numerous transactions in this year also involving sale of shares of substantial value and number of other transactions as seen from the details filed and these frequency of transactions clearly indicate that there was no intention for keeping it as an investment;

(ix) In this case, though the Assessee has treated the shares as investment in its balance sheet, it cannot form a conclusive evidence to prove that the Assessee had actually intended it to be an investment with the sole intention to earn dividend and selling it only when it intends to bring a change in its port folio;

(x) It can be seen from the MoU and Articles of Association that the Assessee company is an investment company authorised for dealing in shares and that it itself does not lend much prudence to the Assessee’s arguments that its activity is in the nature of investment and not as a business activity. Moreover, on this test it is also relevant to cite the decision of the Hon'ble M.P. High Court in CIT v/s Motlay Finance P. Ltd., 290 ITR 719 (M.P); and

(xi) In this case the facts clearly indicate that the investment is not to derive income by way of dividend but is for earning profit from sale of the shares.

Thus, the entire income from purchase and sale of shares was treated under the head *"Income From Business"*.

4. Being aggrieved by the stand so taken by the Assessing Officer, the assessee went in appeal before the first appellate authority, whrein it was submitted that out of total gains of ₹ 3,29,28,126, ₹ 1,20,07,344, constituted long term capital gains which was exempt under section 10(38) of the Act and ₹ 2,09,20,782, was on account of short term capital gains chargeable @ 10%. The only motive and intention of the assessee was to earn dividend income and to reap the benefits of appreciation in prices of shares occasionally as an investor. Looking to volatility in the share market, the assessee had many times dispose off its investment in shares but this only for the purpose of minimizing the loss and to maximize the gain. All the transactions undertaken by the assessee in equity shares were delivery based which reflects the intention of the assessee of being an investor. The assessee has also earned sufficient dividend which is at ₹ 30.59 lacs which goes to show that the main purpose was for earning of dividend as investor in shares. The assessee was in the business of consultancy and not in the business of trading of shares. It was also clarified that the Assessing Officer's observation that the assessee has diverted interest bearing loans to the purchase of shares is incorrect as the assessee has interest free loan from its directors and no interest has been paid. Details regarding holding periods of the shares shown under the head long term capital gains and short term capital gains was also furnished to show that average period of holding was quite substantial. Lastly, it was brought to the notice that in the earlier

assessment years, assessee's case was selected for scrutiny and the similar nature of gain in the sale of shares was accepted to be assessable under the head *"Capital Gain"* and not under the head *"Income From Business"*.

5. The Commissioner (Appeals) rejected the assessee's contention on the ground that principle of estoppel does not apply in the income tax proceedings and even though in the earlier years such a nature of transactions have been accepted to be assessable under the head *"Capital Gains"* will not preclude in taking different stand in this year. CBDT circular no.4 of 2007 dated 15th June 2007, was also relied upon by him. Based on this CBDT instruction and various case laws cited by him, he held that profit motive was paramount aspect in the transactions undertaken by the assessee and, therefore, the Assessing Officer was right in treating the income from transaction of shares under the head *"Income From Business"*. While coming to this conclusion, the Commissioner (Appeals) has made following observations:–

> *"3.3.3 The appellant has shown the shares held by it as investment in the books of account and in the balance sheet. The Supreme Court has held that the manner of entry in the books of account is not decisive (82 ITR 363 (SC). Therefore, the share shown as investment does not mean that they are investment; one has to see the substance of the conduct of the appellant.*
>
> *3.3.4 The appellant's average of investment of 31.03.2005 & 31.33.2006 is ₹ 9.14 crores and it had its own fun at ₹ 16.49 crores on 31.3.2005 and ₹ 18.79 crores as on 31.3.2006, the borrowed funds at 27.62 lakhs 31.3.2006 & ₹ 1.71 crores on 31.3.3006.*
>
> *3.3.5 The volume and frequency of transaction with respect to the transactions shown by the appellant as short term capital gain are very high with short holding period.*
>
> *3.3.5 The volume of transaction with respect to long term capital gain shown by the appellant are high but the number of transactions are very small with long holding periods.*
>
> *3.3.6 the Apex Court in the case of Karanpura Development Co. Ltd. v/s CIT, 44 TR 362 states that substance of transaction would prevail over form. The essential characteristic of the business are (a) continuous and systematic exercise of activity, (b) profit motive. The activity of appellant has been continuous and systematic and frequent sale and purchases have been made with the intention to earn profit*

> *with respect to the transactions shown as short term capital gains. The facts of the transactions of the shares & units by appellant clearly indicate that it has been purchasing and selling shares with the intention of making profit and not with the intention to invest and the activity of the appellant has been that of an adventure in the nature of trade as the appellant has been constantly looking at the rise and fall of price of shares and units with the intention to earn profit. As the profit motive is paramount with respect to the transactions shown as short term capital gain by the appellant, the action of A.O. to treat the transactions of shares and in mutual funds shown as short term capital gain as business income is correct."*

6. However, with regard to the transactions of shares under the head long term capital gains, he held that number of transactions was only ten and the period of holding was also substantial, therefore, the assessee was correct in showing the gains from such transactions of long term capital gains.

7. It is very pertinent to note here that earlier, this issue had come up for consideration before the Tribunal wherein the Tribunal has decided the issue against the assessee, vide order dated 16th December 2011. However, against the said decision, the assessee has preferred miscellaneous application pointing out that the primary basis on which the Tribunal has decided the issue against the assessee i.e., the *"notes on accounts"* given in the audit report was not confronted to the assessee at the time of hearing. The Tribunal, after hearing both the parties, has recalled the entire order for hearing it afresh. It is now after recalling of the order, we have heard the matter afresh.

8. Before us, the learned Counsel, Mr. Vijay Mehta, representing the assessee, after referring to the relevant facts of the case, first of all, drew our attention to the summary of transactions and details of shares shown under the head *"Short Term Capital Gains*" which are appearing in the paper book from Pages–82 to 88. From these details, he pointed out the name of scrips, date of purchase, quantity of shares, date of purchase and sale, quantity sold, amount received and the period of holding. From these details, he pointed out that there are three categories of transaction under the head

"Short Term Capital Gain" – (i) there is one purchase and one sale of scrip and most of them fall in this category; (ii) one or more instance of sale but no repetitive transactions and (iii) there is a repetitive transactions, however, such transactions are very few. The number of scrips undertaken under the head *"Short Term Capital Gain"*, was 74 and likewise short term capital gains through PMS were 11 and in mutual funds, it was 18. Thus, it cannot be held that the assessee was doing regular trading of shares. He further submitted that all the transactions were delivery based and there was no speculation or derivative transaction. The average period of holding even under head *"Short Term Capital Gain"* is 107 days and the average period of mutual fund holding was 152 days. He also pointed out that in the assessment year 2004–05 and 2005–06, the assessee's case was selected for scrutiny under section 143(3) and similar nature of transactions have been accepted to be assessable under the head *"Capital Gain"* and not under the head *"Income From Business"*. He also pointed out the computation of income and relevant balance sheet for the respective assessment years of 2004–05 and 2005–06. At Page–91 of the paper book, he also referred to the history of the assessment and also pointed out that in assessment year 2008–09, the Commissioner (Appeals) has treated the similar nature of transaction to be assessed under the head *"Short Term Capital Gain"*. Thus, looking to the history of assessment, it can very well be said that income from sale of shares is to be treated under the head *"Capital Gain"* and not under the head *"Income From Business"*. While referring to the entries made in the balance sheet, he submitted that the entire shares have been shown under the head *"Investment"* and no borrowed funds have been utilized for purchasing these investments. He clarified that the assessee had own sufficient funds in the form of reserve and surplus funds and interest free funds and, therefore, there was no occasion to divert any interest bearing funds for purchase of shares. Moreover, the only interest bearing loan was car loan of ₹ 16,00,000 and other unsecured loans were taken from the directors which were interest free. He also referred to the object clause of the MoU of the company that it was not authorized to do trading in shares and as per the object 29, the assessee can only invest in shares.

9. Coming to the notes on accounts as given in annexure to audit report of 31st March 2006, specifically clause (xiv), wherein the auditor has given a remark that in his opinion, the company is dealing in or trading in securities which was the main basis for the Tribunal to decide the issue against the assessee in the first round, he submitted that such a remark will have no bearing looking to the actual nature of transaction, past history of the earlier years and the nature of entries in the books of account. He clarified that even in the earlier years, wherein the assessment was completed under section 143(3), similar note was given by the auditor and still the Assessing Officer has accepted the fact that the assessee is not dealing in trading of shares. Such kind of note is in fact as per the ICAI guidelines wherein there is a standard remark which has been incorporated by the auditor. This does not mean that the assessee is actually trading in shares. To clarify this that this remark does not describe the activity of the business carried on by the assessee, he has filed a certificate from the auditors namely Mr. Rajesh Rajeev & Associates, C.A., wherein they have certified that clause xiv given in the financial statement does not describe the activity of the business carried on by the assessee but is a format extracted from the report prescribed under the ICAI guidelines. Lastly, he relied upon various case laws, compilation of which has been filed before us. This compilation also includes the judgment of Hon'ble Jurisdictional High Court in CIT v/s Gopal Purohit, [2011] 336 ITR 287 (Bom.).

10. On the other hand, the learned Departmental Representative strictly relying upon the findings of the Commissioner (Appeals) and the Assessing Officer, submitted that the Commissioner (Appeals) has taken note of a number of scrips, volume and frequency of transaction undertaken by the assessee which shows that the assessee's intention was to earn maximum profit and has to be treated under the head *"Income From Business"*. He further submitted that the acceptance by the Department in the earlier year cannot be held as resjudicata in this year also as the Assessing Officer has examined the issue in detail and has come to the conclusion that the nature

of transaction in shares undertaken by the assessee shows that it is in the nature of business income.

11. We have heard the rival contentions, perused the orders of the authorities below and the material available on record. The issue of assessability of income under the head *"Capital Gains"* and *"Income From Business"* in such kind of transactions have come up for consideration in large number of cases. However, there is a very thin line of distinction between the activities which can be considered purely for investment purpose and for trading purpose in such kind of cases. The parameters like volume, frequency of transactions, continuity, holding period, the intention of the assessee, treatment given in the books of account and host of other factors, though are very relevant for judging a transaction like this, whether it is purely for investment purpose or for trading activities. However, these parameters may, at times, break down in certain cases as there cannot be any all embracing formula to judge these kinds of transactions. It has been quite a phenomenon in the last decade that many people in the country had invested in the equity shares and mutual funds to maximise their investment within a short period. Even transactions are being entered for a brief period. To judge such transactions, one has to adopt a pragmatic approach looking to the facts, circumstances and merits of the case, keeping in mind the intention of the assessee and whole gamut of transactions, whether it is for commercial consideration or not. In the present case, similar issue is involved i.e., the treatment of short term capital gains on sale of shares and mutual fund aggregating ₹ 1,83,55,523, is whether assessable under the head *"Income From Business"* or under the head *"Short Term Capital Gain"*. The Revenue's case is that looking to the volume and frequency of the transactions which are quite high and the period of holding is also short, therefore, gain from such transactions has to be treated under the head *"Income from Business".* On a perusal of the transaction, it is seen that the assessee has shown gain on sale of equity shares at ₹ 91,32,471, and gain on sale of mutual fund of ₹ 92,23,053. For short term capital gains, the number of scrip entered into are 74, however, in most of the cases, the

average holding period is far more than 100 days. The over all average of period of holding is around 184 days. Insofar as the allegation of the Revenue is concerned that the number of transactions have been undertaken in the sale of 74 scrips, the same cannot be taken as primary parameter to hold that it should be treated as business activity because it is a known phenomenon in Stock Exchange that a single transaction is split into many smaller transactions while trading in the Stock Exchange through computers. Such transactions, at times, give unrealistic figures of number of transactions. In this case, following important facts are relevant while adjudicating the issue as to whether the gains from the transactions of shares is to be assessed under the head *"Short Term Capital Gain"* or under the head *"Income From Business"*. Firstly, the assessee has, all throughout, been showing purchase of shares as investment in the books of account and the same has been classified in the balance sheet under the head *"Investment"*; secondly, such a nature of transaction shown under the head *"Investment"* has been treated to be capital gain in the assessment years 2004–05 and 2005–06 by the Assessing Officer under scrutiny proceedings wherein the order has been passed u/s 143(3). In the assessment year 2008–09, the Commissioner (Appeals) has accepted the gain from transactions of shares to be assessable under the head *"Short term Capital Gain"*. Thus, if the same facts are permeating through all the assessment years, it cannot be held that on similar nature of transactions, the income from shares has to be assessed as *"Income From Business"*; thirdly, all the transactions undertaken by the assessee are delivery based and the assessee has not undertaken any speculative or derivative trading of shares. This shows that the assessee's intention was never to indulge in trading of shares; and fourthly, as clarified by the learned Counsel, no interest bearing borrowed funds or loans have been diverted for purchase of shares rather they have been purchased from the surplus funds available with the assessee. Lastly, from the details of short term capital gain, it is seen that most of the gain has come from sale of mutual funds, which cannot be traded in Stock Exchange. This also goes to prove that the assessee is mainly an investor. From these facts, it can be very well concluded that the assessee's intention was to purchase the shares for holding it as investment.

12. Now coming to the remark of the auditor in the financial statement, it is seen from the certificate given by the Chartered Accountant that it was solely on account of extraction from the report prescribed by the ICAI guidelines and it is not descriptive of activity or business carried on by the assessee company. Moreover, such a noting is also there in the earlier financial statements in the assessment years 2004–05 and 2005–06, wherein the Revenue has accepted that the Assessee is not engaged in the trading of shares. Thus, such a remark cannot be adversely viewed for drawing adverse conclusion against the assessee. Lastly, the principle laid down by the Hon'ble Jurisdictional High Court in Gopal Purohit (supra) is also applicable in the facts of the present case inasmuch as the assessee has shown these shares as investment and in the earlier years, similar nature of transactions have been accepted by the Revenue. In view of the aforesaid findings and the facts and circumstances of the case, we hold that the gain arising from sale of shares is assessable under the head *"Short Term Capital Gain"* and not under the head *"Income From Business"* as held by the Assessing Officer and the CIT(A). Consequently, the impugned orders passed by the CIT(A) are hereby set aside and the ground raised by the assessee in the appeals under consideration is treated as allowed.

13. परिणामतः निर्धारिती की अपील स्वीकृत मानी जाती है ।

13. In the result, assessee's appeals are treated as allowed.

आदेश की घोषणा खुले न्यायालय में दिनांकः 5th April 2013 को की गई ।
Order pronounced in the open Court on 5th April 2013

Sd/-	**Sd/-**
बी. रामकोटय्य	**अमित शुक्ला**
लेखा सदस्य	**न्यायिक सदस्य**
B. RAMAKOTAIAH	**AMIT SHUKLA**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

मुंबई MUMBAI, दिनांक DATED: 5th April 2013

<u>आदेश की प्रतिलिपि अग्रेषित / Copy of the order forwarded to</u>:

(1) निर्धारिती / The Assessee;

(2) राजस्व / The Revenue;

(3) आयकर आयुक्त(अपील)/ The CIT(A);

(4) आयकर आयुक्त / The CIT, Mumbai City concerned;

(5) विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, मुंबई / The DR, ITAT, Mumbai;

(6) गार्ड फाईल / Guard file.

सत्यापित प्रति / True Copy

आदेशानुसार / By Order

प्रदीप जे. चौधरी / Pradeep J. Chowdhury

वरिष्ठ निजी सचिव / Sr. Private Secretary

उप / सहायक पंजीकार / (Dy./Asstt. Registrar)

आयकर अपीलीय अधिकरण, मुंबई / ITAT, Mumbai