

(2007) 08 GAU CK 0071
In the Gauhati High Court

Bhikamchand Betala and Sons

APPELLANT

Vs

Income Tax Officer

RESPONDENT

Date of Decision : 21-08-2007

Acts Referred:

Income Tax Act, 1961 — Section 10, 24, 260A, 28, 29

Citation : (2007) 294 ITR 10

Hon'ble Judges : D. Biswas, J;A. Hazarika, J

Bench : Division Bench

Judgement

A. Hazarika, J.—This is an appeal u/s 260A of the Income Tax Act, 1961. By this appeal, the appellant has challenged the legality and validity of the order dated January 24, 2003, passed by the Income Tax Appellate Tribunal, Gauhati Bench, Guwahati in Income Tax Appeal No. 118(Gau)/99 for the assessment year 1995-96.

2. The facts of the present appeal may be briefly stated at the very outset.

The appellant is an assessee under the Income Tax Act, 1961 (for short "the Act"), assessed to tax by the Income Tax Officer, Ward 1(5), Guwahati. The status of the assessee is that of Hindu undivided family and the assessment year under consideration is 1995-96. During the assessment proceeding a claim was made by the assessee of share business loss amounting to Rs. 3,99,860. On various grounds mentioned in the assessment order dated March 31, 1998, the Assessing Officer concluded that the transaction in shares as claimed by the assessee cannot be treated as genuine. Accordingly, the share business loss of Rs. 3,99,860 was not allowed and the same was added back to the total income of the assessee for the said year.

3. The assessee preferred an appeal before the Commissioner Income Tax (Appeals), Guwahati, questioning the addition of the aforesaid amount to its income. The appellate authority, vide order dated October 30, 1998, allowed the said appeal of the assessee by holding that the disallowance of the loss of share

business amounting to Rs. 3,99,860 was based on a wrong perception of the facts. The Assessing Officer was directed to allow the loss so claimed.

4. Against the aforesaid order, the Revenue came up in appeal before the Income Tax Appellate Tribunal, Gauhati Bench, Guwahati ("the Tribunal" for short). The said appeal was registered as I.T.A. No. 118(Gau)/99. The Tribunal, vide its order dated January 24, 2003, allowed the said appeal of the Revenue. Though the Tribunal held that there was no cogent material to show that the said share transactions were not genuine, the Tribunal observed that the assessee had purchased the share from M/s. R.K. Associates on principal to principal basis and resold the shares to the same M/s. R.K. Associates without taking physical delivery of the shares and also paid only the difference amount of purchase and sale value of the said M/s. R.K. Associates. In view of the provisions contained in Section 43(5) of the Act, the Tribunal took the view that the loss of Rs. 3,99,860 so suffered by the assessee was speculation loss and accordingly, modified the appellate order dated October 30, 1998.

5. The above order of the Tribunal is under challenge in the present appeal.

The appeal was admitted by this Court on April 25, 2003, on the following substantial questions of law:

1. Whether the Tribunal was justified in applying the provisions of Section 43(5) when broker being the agent of the appellant was in custody of the shares on behalf of the appellant?

2. Whether the Tribunal was justified in holding the transaction to be speculative when the shares were directed to be sold to avoid further loss as the value of shares of steel companies were in downward trend?

6. I have heard Mr. G.N. Sahewalla learned senior Counsel assisted by Md. Aslam and Ms. M. Jain learned Counsel for the appellant. Also heard Mr. U. Bhuyan learned standing Counsel appearing for the respondent-income tax Department.

7. Mr. Sahewalla learned senior Counsel submitted that the Tribunal erred in holding the loss in share transaction amounting to Rs. 3,99,860 as speculation loss. According to him, after recording the finding that there was no cogent material to show that the share transactions were not genuine, there was no justification for the Tribunal to proceed further to hold the said loss as speculation loss. He asserted that the Tribunal has committed a manifest error in holding the said loss suffered by the assessee as speculation loss as it was nobody's case that the transactions entered into by the assessee were speculative transactions and the loss suffered was speculation loss.

8. Countering the arguments of Mr. Sahewalla learned senior Counsel, Mr. U. Bhuyan learned standing Counsel for the Revenue has submitted that there is no infirmity in the order of the Tribunal and the Tribunal was correct and justified in treating the said share transaction loss as speculation loss. Referring to the provisions of Explanation 2 to Section 28, Section 43(5) and Section 73 of the

Act, learned standing counsel asserted that the said transactions came within the ambit of the meaning of speculative transaction and, therefore, the Tribunal was justified in treating the said loss as speculation loss.

9. Before proceeding further it would be apposite to note down the relevant provisions of the Act relating to speculative transaction and speculation loss:

Section 28, Explanation 2.--Where speculative transactions carried on by an assessee are of such a nature as to constitute business, the business (hereinafter referred to as the "speculation business"), shall be deemed to be distinct and separate from any other business.

Section 43. In Sections 28 to 41 and in this section, unless the context otherwise requires--....

(5) "Speculative transaction" means a transaction in which a contract for the purchase or sale of any commodity, including stocks and shares, is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scrips:

Provided that for the purposes of this clause--

(a) A contract in respect of raw materials or merchandise entered into by a person in the course of his manufacturing or merchanting business to guard against loss through future price fluctuations in respect of his contracts for actual delivery of goods manufactured by him or merchandise sold by him; or

(b) a contract in respect of stocks and shares entered into by a dealer or investor therein to guard against loss in his holdings of stocks and shares through price fluctuations; or....

shall not be deemed to be a speculative transaction.

Section 73(1) Any loss, computed in respect of a speculation business carried on by the assessee, shall not be set off except against profits and gains, if any, of other speculation business....

Explanation.--....

10. Now, let us have a look upon the decisions relied upon by the respective counsel. Mr. Sahewalla, learned senior Counsel appearing on behalf of the assessee has relied upon the following decisions:

(i) CIT v. Kamani Tubes Ltd. [1994] 207 ITR 298;

(ii) Commissioner of Income Tax, Jodhpur Vs. Mangal Chand, and

(iii) Commissioner of Income Tax, Bombay City-III Vs. Shantilal P. Ltd., .

11. In CIT v. Kamani Tubes Ltd. [1994] 207 ITR 298 the court after referring to various decisions of the apex court as well as the High Courts, held that a transaction cannot be described as a "speculative transaction" within the

meaning of Section 43(5) of the Income Tax Act, 1961, where there is a breach of the contract and on a dispute between the parties damages are awarded as compensation. The court further held that in deciding the character of the transactions, what is important to consider is the distinctive character of such transactions. In each case it is the total effect of all the relevant facts and circumstances that determines the character of the transaction. Moreover, the burden of proving that the transactions carried on by an assessee were of such a nature as to constitute "speculation business" is on the taxing authorities. If the authorities come to a conclusion without making necessary investigation in that regard such an inference cannot be sustained. The court thus held that the Income Tax Officer was not justified in disallowing the deduction by referring to Section 43(5) of the Act.

12. In the case of Commissioner of Income Tax, Jodhpur Vs. Mangal Chand, , the court held that if the assessee has concluded the transaction by taking delivery of shares and has sold the same by giving delivery along with blank transfer forms it is immaterial whether the shares were not registered in the name of the assessee or dividend were not paid to the assessee. The court further held that delivery of blank transfer form along with share certificates results in completing transaction between the transferee and transferor notwithstanding that the same may not be registered in the register of members, thus the transaction of purchase and sale of shares were conducted by actual delivery of scrips. Therefore, such transactions were not speculative transactions within the meaning of Section 43(5) and the consequential loss was not speculative loss.

13. In Commissioner of Income Tax, Bombay City-III Vs. Shantilal P. Ltd., , the apex court held that a transactions cannot be described as a "speculative transaction" within the meaning of Sub-section (5) of Section 43 of the Income Tax Act, 1961, where there is breach of contract and on a dispute between the parties damages are a, warded as compensation by an arbitration award.

14. There is no dispute with the above proposition arrived at by the courts in the aforesaid cases referred to and relied upon by learned Counsel appearing for the appellant. However, on the facts of the present case, the aforesaid cases do not help the assessee and the Tribunal has rightly held that the loss suffered by the assessee was speculation loss.

15. In support of his submission, Mr. Bhuyan learned standing counsel relies on the following decisions:

(i) HOOSEN KASAM DADA (INDIA) LTD. Vs. COMMISSIONER OF Income Tax, CALCUTTA., ;

(ii) Commissioner of Income Tax Vs. Maya Ram Jia Lal,

(iii) V.N. Sarsetty Vs. Commissioner of Income Tax, ;

(iv) Abdul Gani Haji Habib and Others Vs. Commissioner of Income Tax, ; and

(v) Commissioner of Income Tax, U.P. Vs. Jagannath Mahadeo Prasad,

16. In HOOSEN KASAM DADA (INDIA) LTD. Vs. COMMISSIONER OF Income Tax, CALCUTTA., , the court held that under Explanation 2 to Section 24, a transaction in which a contract for purchase and sale of any commodity is settled otherwise than by delivery, is a speculative transaction irrespective of whether the parties initially intended to give delivery or not and the Tribunal rightly held that, under the proviso to Section 24(1), the loss in contracts in which delivery was not given could not be allowed to be set off. The court further held that the definition contained in Explanation 2 has severely restricted the meaning of the expression "speculative transaction" and in a sense simplified it for the purpose of computation of Income Tax. Thus, where there is no delivery under a settlement contract, it is a speculative transaction. On the other hand, however, speculative transaction might be, if there is delivery, it cannot be considered as a speculative transaction for the purpose of Section 24.

17. In Commissioner of Income Tax Vs. Maya Ram Jia Lal, the assessee, which carried on business in the sale of wool-tops and manufacture of yarn, entered into contracts with various parties for the supply of goods to them. Since the assessee could not fulfil the contract in time, the assessee settled the contracts by paying compensation to the parties. The assessee claimed the compensation paid as a business loss. The Income Tax Officer took the view that the compensation paid for the non-fulfilment of the contracts was speculative in nature within the meaning of Section 43(5) of the Income Tax Act, 1961, as there were no written agreements between the assessee and various parties. The Appellate Assistant Commissioner upheld the claim of the assessee. The Tribunal found that in respect of almost all transactions, the settlement was made long after the date of delivery as contemplated in the contracts, that the claim of the assessee was based on breach of contract and did not come within the meaning of a contract "settled" as used in Section 43(5) and that the loss was allowable as a trading liability. The court on the reference made, after detailed deliberation held that compensation paid by the assessee to the various parties for non-fulfilment of the contracts was a speculative transaction within the meaning of Section 43(5).

18. While arriving as above, the court in Commissioner of Income Tax Vs. Maya Ram Jia Lal, relied upon the two decisions of the Supreme Court rendered in Nirmal Trading Co. Vs. Commissioner of Income Tax (Central), Calcutta, and Jute Investment Co. Ltd. Vs. Commissioner of Income Tax, West Bengal, for the proposition that if the delivery of the goods is not made and it is not shown that there was any dispute between the contracting parties, then it is to be held that the settlement arrived at between the parties would be deemed to be a settlement by a contract which transaction has to be held to be speculative and thereby, in Commissioner of Income Tax Vs. Maya Ram Jia Lal, held that as no delivery was made and it is also apparent that the contracts between the parties were settled by payment and, therefore, such payment cannot be allowed and

have to be disallowed being a speculative nature as they clearly come within the ambit of Section 43(5) of the Act. In Commissioner of Income Tax Vs. Maya Ram Jia Lal, the court further held that to find out whether a transaction is speculative or not, the following are the criteria.

19. If the dispute is settled between the parties then it is not a speculative transaction, but if the contract is settled and under the settlement of the contract, damages are paid, it would be a speculative transaction.

20. In the case of V.N. Sarsetty Vs. Commissioner of Income Tax, the assessee entered into a contract with the buyer for supply of cotton within the stipulated time. The buyer was given option to extend the time for delivery of goods but not delivered within the stipulated time even after repeated demands and extension of time for performance of contract. However, the goods could not be delivered within time. Thereafter, the assessee paid Rs. 35,000 by way of loss on account of non-delivery of goods in full settlement of the contract. The amount so paid to the buyer by way of loss for non-delivery of goods in full settlement of contract, held, is not damages for breach of contract but the transaction is speculative transaction and the payment so made to the buyer is speculative loss.

21. In the case of V.N. Sarsetty Vs. Commissioner of Income Tax, , the court relied upon the decisions in Bhandari Rajmal Kushalraj Vs. Commissioner of Income Tax, Mysore, and Commissioner of Income Tax, Bombay City-III Vs. Shantilal P. Ltd., .

22. In Abdul Gani Haji Habib and Others Vs. Commissioner of Income Tax, the court relying upon the decisions in HOUSEN KASAM DADA (INDIA) LTD. Vs. COMMISSIONER OF Income Tax, CALCUTTA., , D. M. WADHWANA Vs. COMMISSIONER OF Income Tax, WEST BENGAL., and SAHU JAIN LTD. Vs. COMMISSIONER OF Income Tax., , held that the transactions which were settled by payment of differences must be treated as speculative transactions even though the assessee did not intend when the contract were entered into to settle them by payment of differences inasmuch as the intention of the parties has no place in the scheme of Section 24.

23. In Commissioner of Income Tax, U.P. Vs. Jagannath Mahadeo Prasad, the question that arises in the appeals was whether speculative loss can be set off against profit from any other business activity u/s 10 in spite of the first proviso to Section 24(1) of the Indian Income Tax Act, 1922.

24. After elaborate discussion, the apex court held that the assessee is not entitled to set off speculative losses against profits from other business" activities of the same year, for the purpose of computing the income, profits and gains u/s 10(1) of the Indian Income Tax Act, 1922; the second proviso to Section 24(1) of the Act prior to the amendment of the Section by the Taxation Laws (Extension to Jammu and Kashmir) Act, 1954, or the first proviso after that amendment applies. It provides in unmistakable and unequivocal terms that any losses sustained in speculative transactions which are in the nature of a business

shall not be taken into account except to the extent of the amount of profits or gains in any other business consisting of speculative transactions.

25. On the above authorities cited by Mr. Bhuyan learned standing Counsel, we have to overrule the arguments advanced on behalf of the assessee that in spite of holding by the learned Appellate Tribunal that no cogent material could be brought on record by the Revenue to show that the share transactions were not genuine and merely by observing that the assessee purchased the share from M/s. R.K. Associates on principal to principal basis and resold the shares to the same M/s. R.K. Associates without taking the physical delivery of the shares and also paid only the difference amount of purchase and sale value to the said M/s. R.K. Associates and thereby holding that loss of Rs. 3,99,860 so suffered by the assessee was speculation loss is based on wrong perception of laws and not justified.

26. Therefore, the contention made on behalf of the assessee that as there was no initial intention on his part to settle the contract in question, by payment of difference but he was only forced by the subsequent circumstances to do so, the transactions were not speculative in nature, cannot be accepted in the facts and circumstances of the case.

27. In the result, the argument advanced by the assessee failed and we answer the question formulated by this Court in the affirmative and in favour of the Revenue. The loss of Rs. 3,99,860 held to be speculation loss and, therefore, there shall be no deduction of tax on the aforesaid amount.