
(1991) 06 MAD CK 0030

In the Madras High Court

Case No : Tax Case No. 640 of 1980 (Reference No. 260 of 1980)

Commissioner of Income Tax

APPELLANT

Vs

Prema Ramannujam

RESPONDENT

Date of Decision : 11-06-1991

Acts Referred:

Income Tax Act, 1961 — Section 45, 48, 55(2)

Citation : (1991) 96 CTR 101 : (1991) 192 ITR 692

Hon'ble Judges : V. Ratnam, J;T. Somasundaram, J

Bench : Division Bench

Advocate : C.V. Rajan, for the Appellant; S.A. Balasubramanian, for the Respondent

Judgement

Ratnam, J.—The assessed is an individual. During the previous year ending on March 31, 1975, relevant to the assessment year 1975-76,

the assessee sold 675 shares held by her in a private limited company for Rs. 89,661. In computing the capital gains, the Income Tax Officer,

after noticing the total shareholding of the assessee, include the original holding and also all the bonus shares issued subsequently, worked out the

average cost per share at Rs. 47.17, which was adopted as the cost of acquisition of the shares sold by the assessee and computed the long-term

capital gains at Rs. 57,820 and subjected it to tax. In so doing, the Income Tax Officer supported to follow the decision in Commissioner of

Income Tax, Bihar Vs. Dalmia Investment Co. Ltd., , as, in his view, the decision in Shekhawati General Traders Ltd. etc. Vs. Income Tax

Officer, Company Circle-1, Jaipur, , was inapplicable in that, on the issue of bonus shares, the original shares were split up, totally losing their

identity. On appeal by the assessee before the Appellate Assistant Commissioner,

she, after adverting to the history of the shares holding of the assessee and referring to the decisions of Commissioner of Income Tax, Bihar Vs. Dalmia Investment Co. Ltd., and Shekhawati General Traders Ltd. etc. Vs. Income Tax Officer, Company Circle-1, Jaipur, , took the view that the method adopted by the Income Tax Officer in spreading over the cost of the original shares, whose fair market value on January 1, 1954, had been fixed at the option of the assessee, after taking in to account the whole of the subsequently issued bonus shares, to arrive at the cost of acquisition of the shares sold by the assessee was erroneous and upheld the stand of the assessee that the capital gains exigible to tax would only be Rs. 2,261. On further appeal to the Tribunal by the Revenue, it found that the assessee had elected to opt for the fixation of the fair market value in respect of the shares originally held by her, which was unalterable in view of the decision in Shekhawati General Traders Ltd. etc. Vs. Income Tax Officer, Company Circle-1, Jaipur, and that, out of the 675 shares sold by the assessee, 375 shares formed part of the original holding and 300 shares were comprised in the bonus shares issued subsequently. In that view, the Tribunal proceeded to compute the cost of acquisition in respect of the 375 shares at the fair market value opted by the assessee as on January 1, 1954. Regarding the sale of 300 bonus shares, the Tribunal found that the shares so sold formed part of the bonus shares issued during the year ended March 31, 1967, and applied the method of spreading over the cost in respect of the shares originally held by the assessee and also the bonus shares issued up to March 31, 1967, and not the subsequent issue of bonus shares, to arrive at the cost of acquisition of 300 bonus shares sold by the assessee. So computing the cost of acquisition of shares sold by the assessee, the Tribunal affirmed the order of the Appellate Assistant Commissioner and dismissed the appeal. That has given rise to this reference u/s 256(1) of the Income Tax Act 1961 (hereinafter referred to as "the Act"), at the instance of the Revenue, on the following question of law :

Whether, on the facts and in the circumstances of the case, the method adopted by the Tribunal for valuing the cost of shares for purposes of arriving at the taxable capital gains is correct in law ?

2. A brief reference may now be made to the mode of acquisition of shares by

the assessee. The assessee had received from her father a gift of 3,000 shares. Later, she sold 125 shares leaving a balance of 2,875 shares. Since the shares became the property of the assessee by way of gift, the cost to the previous owner had to be taken or the value as on January 1, 1954, and, in this case, there is no dispute that the assessee chose to have the value as on January 1, 1954 at Rs. 184 per share. Thus, the value of 2,875 shares at the fair market value opted by the assessee at Rs. 184 per share worked out to Rs. 5,29,000. The assessee obtained 5,750, 1,725 and 1,380 bonus shares on March 31, 1967, March 31, 1968, and March 31, 1970, respectively. Later, the assessee also acquired 358 shares for Rs. 41,200. The Tribunal had found as a fact that 375 shares sold with distinctive numbers 20,011 to 20,385 formed part of the original shareholding of the assessee, referable to the gift by her father in her favour and that 300 bonus shares issued on July 4, 1966, bearing distinctive numbers 80,706 to 81,005 had been sold by the assessee during the previous year relevant to the assessment year 1975-76 for Rs. 89,661. In computing the capital gains, the Income Tax Officer, with a view to ascertain the cost of acquisition of shares held by the assessee, spread the entire cost, viz., Rs. 5,29,000 plus Rs. 41,200 over the total holdings of the assessee in respect of 12,088 shares and arrived at the average cost of acquisition at Rs. 47.17 per share. This method adopted by the Income Tax Officer was plainly erroneous. In respect of the 375 shares out of 675 shares sold, which formed part of the original shareholding of the assessee, u/s 55(2)(ii) of the Act, at the option of the assessee, the fair market value of the assets on January 1, 1954, had been determined at Rs.184 per share. Thus, with reference to the ascertainment of the cost of acquisition of 375 shares out of 675 shares sold by the assessee, the cost of acquisition has to be worked out on the basis of the unalterable fair market value fixed at the option of the assessee as on January 1, 1954, and that has to be adopted. This is clearly established by the decision of the Supreme Court in Shekhawati General Traders Ltd. etc. Vs. Income Tax Officer, Company Circle-1, Jaipur, , where it has been pointed out that the cost of acquisition u/s 55(2) of the Act is the cost of the asset of the assessee or the fair market value of the asset as on January 1, 1954, at the option of the assessee and if the assessee had exercised an option

and the fair market value is duly determined, it is wrong to hold that, for purposes of computing the capital gains, the cost had to be worked out by averaging the cost of the original shares among the original shares and the bonus shares taken together, ignoring the statutory provisions of sections 48 and 55(2) of the Act and that, for the ascertainment of the fair market value of the shares as on January 1, 1954, events prior to or subsequent to that date would be extraneous and irrelevant. In view of this clear pronouncement of the Supreme Court and the undisputed exercise of option by the assessee to adopt the fair market value of the shares originally held at Rs. 184 per share, the cost of acquisition of 375 shares had to be computed on the basis of the fair market value fixed on the basis of the exercise of option by the assessee and the issue of bonus shares subsequently cannot, in any manner, affect or alter the determination of the fair market value as provided u/s 55(2)(ii) of the Act in this case. That leaves for consideration the determination of the cost of acquisition of the bonus shares issued to the assessee. Earlier, it has been seen that the assessee had received bonus shares on March 31, 1967, March 31, 1968 and March 31, 1970. However, the Tribunal has found as a fact that out of 5,750 bonus shares issued on July 4, 1966 (for the year ending March 31, 1967), the assessee had sold 300 bonus shares bearing distinctive numbers 80,706 to 81,005. To ascertain the cost of acquisition of 300 bonus shares sold by the assessee, the cost of 2,875 shares at the rate of Rs. 184 per share as opted by the assessee has to be taken into account and that cost spread over the original shareholding of the assessee, viz., 2,875 shares, as well as the bonus shares issued during the year ended March 31, 1967, viz., 5,750 shares, in order to ascertain the cost of acquisition of the bonus shares issued during the year ended March 31, 1967, out of which 300 shares had been disposed of by the assessee. That this is the proper method of ascertaining the cost of acquisition of the bonus shares is laid down by the Supreme Court in the decision in Commissioner of Income Tax, Bihar Vs. Dalmia Investment Co. Ltd., . Considering the different methods available for the purpose of ascertaining the value of bonus shares, the Supreme Court pointed out that the amount spent by the shareholder in acquiring the original shares and to spread it over the original shares and the new shares, treating the new as accretions to the old and to treat the cost price of the original shares as

the cost price of the old shares and the bonus shares taken together, would be a simple method, even as suggested by the Revenue in the case, where the bonus shares rank *pari passu* with the old shares. It is not the case of the Revenue that the bonus shares issued to the assessee did not rank *pari passu* with the shares originally held by her and, therefore, there is no difficulty in adopting the method of spreading the original cost over the old and new bonus shares held by the assessee. But, even while working out the cost of acquisition of the bonus shares, it has to be determined with reference to the particular point of time when shares had been acquired. In this case, on the factual finding of the Tribunal that 300 out of 5,750 bonus shares obtained by the assessee on July 4, 1966 (for the year ending March 31, 1967), had been sold by the assessee, it would suffice to ascertain the cost of acquisition of the bonus shares so sold and, for that purpose, the subsequent issue of bonus shares on March 31, 1968, and March 31, 1970, would not be relevant. u/s 48(ii) of the Act, the income chargeable under the head ""Capital gains"" shall be computed by deducting from the full value of the consideration received or accruing as a result of the transfer of the capital asset, the cost of acquisition of the capital asset and the cost of any improvement thereto. In this case, there is no question of cost of any improvement and necessarily, the cost of acquisition of 675 shares sold alone has to be deducted from the full value of the consideration of Rs. 89,661 and, in respect of ascertainment of the cost of acquisition of the 675 shares sold, the exercise of option as per section 55(2)(ii) of the Act in respect of 375 shares at the fair market price at Rs. 184 per share as on January 1, 1954, and the averaging method indicated in the decision of the Supreme Court in Commissioner of Income Tax, Bihar Vs. Dalmia Investment Co. Ltd., in respect of 300 bonus shares have to be given effect to and, if so done, the assessable capital gains arising out of the sale of 675 shares by the assessee would only be Rs. 2,260 as claimed by her, and the Tribunal was, therefore, right in its conclusion. We, therefore, answer the question referred to us in the affirmative and against the Revenue. The assessee will be entitled to the costs of this reference. Counsel's fee Rs. 500.