(1990) 04 CAL CK 0032

In the Calcutta High Court

Case No : IT Reference No. 71 of 1986

Commissioner of Income Tax APPELLANT

Vs

Sun Distributors and Mining Co. Ltd. RESPONDENT

Date of Decision : 25-04-1990

Acts Referred:
Income Tax Act, 1961 — Section 109, 256(1), 73, 73(4)

Citation : (1993) 68 TAXMAN 223

Hon'ble Judges : Suhas Chandra Sen, J;Bhagabati Prasad Banerjee, J

Bench : Division Bench

Advocate : J.P. Khaitan and A.K. De, for the Appellant;

Judgement

Sen, J.—The Tribunal has referred to this Court the following question of law u/s 256(1) of the income tax Act, 1961 (''the Act''):

Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was justified in holding that the Explanation to section 73 of the income tax Act, 1961 is not applicable when there was no purchase of shares by the assessee during the assessment year under consideration?

The assessment year involved is 1978-79 for which the relevant period of account is the year ended on 3-6-1977.

2. The facts found by the Tribunal are as under:

The assessee is a limited company. The assessment year involved in the case is 1978-79. The company during the relevant assessment year was engaged in dealing in paper, coal, chemicals, etc., and it was also engaged in coal handling.

In the assessment for the assessment year under reference, the ITO made an addition of Rs. 1,20.632 with the following observation:

Loss on share dealing to be considered later vide Explanation to section 73 of the IT Act, 1961 as speculation loss:

Rs.

Rs.

Opening stock

8,84.787

Less :

Sales

60.339

Closing stock

7.03.816

7.64,155

1,20,632

Against the above addition, the assessee filed an appeal before the Commissioner of income tax (Appeals). The Commissioner of income tax (Appeals) sustained the income tax Officer''s action on the point.

3. The Commissioner (Appeals) observed as follows:

The appellant deals in paper, coal, chemicals, etc. and is also engaged in business of coal handling. Besides it also deals in shares, debentures, etc. The major source of income during this year was no doubt from trading in coal, paper and from coal handling charges. During that year only 8 bonus shares of Hindusthan Sanitary Ltd. were sold and 500 debentures of Paresh Kothi Ltd. were redeemed. Otherwise there were no transactions in shares or debentures during the year under consideration. The loss in share dealings account as computed by the ITO exclusive of apportionment of Rs. 70,000, as mentioned earlier, mainly arose out of adjustment in the value of closing stock of shares.

Explanation to section 73(4) was added by Taxation Law (Amendment) Act, 1973 with effect from 1-4-1977. Under Explanation where any part of the business of a company (other than an investment company or a banking or a financing company) consists in the purchase and sale of shares, such company for the purpose of this section be deemed to be carrying on a speculation business to the extent to which the business consists of the purchase and sale of shares. There is no doubt that the fiction embodied in the Explanation is only ''for the purpose of this section'' that is, where losses are incurred in shares and are sought to be set off against other income. The ITO has worked out the loss at Rs. 1,20,632 exclusive of apportionment to the extent of Rs. 70.000 out of administrative expenses and interest charged to profits and loss account which is reproduced below:

Rs.

Rs.

Opening Stock

8,84,787

Less :

Sales:

60,339

Closing Stock

7,03,816

7,64,155

Loss

1,20,632

The fact that during the year there was sale of only 8 bonus shares in addition to redemption of 500 debentures and that there was no loss on either account does not make any difference to the position that there was loss in share account, as computed correctly by the ITO. The closing stock of shares was valued by the appellant at cost or market value, whichever is lower, whereas debentures were valued at cost. The loss, as correctly computed by the ITO at Rs. 1,20,632 arose mainly due to method of valuation of closing stock of shares adopted by the appellant-company. It is not the magnitude of transaction in shares which should decide as to whether the appellant is engaged in purchase or sale of shares. Besides. Explanation to section 73(4) makes it clear that where any part of the business of a company consists in the purchase or sale of shares such company shall, for the purpose of section 73, be deemed to be carrying on a speculation business to the extent to which the business consists of the purchase and sale of shares. It is also not necessary that there should be both purchase and sale of shares in a particular year. Even though there was no purchase of shares during the year, there was certainly sale of shares, may be bonus shares. The loss having arisen as a result of share dealings partakes the character of speculation loss by virtue of Explanation 73(4).

The Tribunal in further appeal held as follows:

In our opinion CIT (Appeals) came to a wrong conclusion because he misread the Explanation to section 73. In order to attract the Explanation it is necessary that there must be ''purchase and sale of shares''. As embodied in the Explanation, the CIT (Appeals) was wrong in his assumption that in order to attract the Explanation the business of the company is to consist either in the purchase or sale of shares. When Explanation uses the words purchase and sale of shares instead of the words ''purchase or sale of shares'' we do not think that the CIT (Appeals) was at liberty to change the word ''and'' to ''or''. He himself held that there was no purchase of shares during the year under examination. As such one of the conditions required under the Explanation was lacking in the instant case and as such the Explanation could not be used against the assessee-company. It is not the case of the department that without the help of the Explanation the assessee-company can be said to be carrying on a speculation business. As such we are of the opinion that section 73 could not be used to deny the deduction of the loss to the assessee-company. So, we are of the opinion that the disallowances could not have been made. As such, we allow this appeal and delete the said disallowance of Rs. 1,20,632.

Section 73 of the Act deals with loss in speculation business. It provides as follows:

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

4. Sub-section (2) of section 73 lays down that where any loss in respect of a speculation business has not been wholly set off under sub-section (1), so much of the loss as has not been set off shall be carried forward to the following assessment year. It is also further provided that such carried forward loss in speculation business shall be set off against profits and gains of any speculation business of the subsequent assessment year. No loss shall be carried forward under this section for more than succeeding eight assessment years. There is an Explanation to section 73 which provides as follows:

Explanation : Where any part of the business of a company (other than an investment company, as defined in clause (1) of section 109, or a company the principal business of which is the business of banking or the granting of loans and advances) consists in the purchase and sale of shares of other companies, such company shall, for the purposes of this section, be deemed to be carrying on a speculation business to the extent to which the business consists of the purchase and sale of such shares.

5. The section will apply where any part of the business of the company ''consists'' in the purchase and sale of shares of other companies. Therefore, it has to be seen whether the assessee-company has such a business. It may be that in a particular year shares were only sold or in a particular year the shares were only purchased. The section does not require that both sale and purchase should take place in the same year. What is to be seen is whether the business of the company consists in purchase and sale of shares. In the instant case, the assessee-company had a business of buying and selling the shares. The shares are treated as stock-in-trade. The closing stock of the shares have been valued just as any other stock-in-trade is valued by a company. There were small lots of sale of shares in this year. But that will not make any difference to the main question, which is, whether the company was engaged in the business of sale and purchase of shares. If it is found that any part of the business of the

company consists in the purchase and sale of shares, then for the purpose of section 73 such a company shall be deemed to be carrying on a speculation business to the extent the business consisted of purchase and sale of such shares. It is not the requirement of the section that both purchase and sale of shares should take place in the same year. But what the section requires is that there will be business of sale and purchase of shares and the assessee-company will carry on that business in the relevant year of account. The very fact that shares were valued as stock-in-trade and the loss was disclosed, as a result of the valuation of the shares, goes to show that the business of share purchase and sale of shares was carried on by the company. To the extent such business was carried on, the business of the assessee-company must be treated as speculation business. In that view of the matter, the question is answered in the negative and in favour of the revenue.

There will be no order as to costs.

Banerjee, J.

I agree.

