

**IN THE HIGH COURT OF JUDICATURE AT CALCUTTA**

**SPECIAL JURISDICTION (INCOME TAX)**

**ORIGINAL SIDE**

RESERVED ON: 02.02.2023

DELIVERED ON: 14.03.2023

**CORAM:**

**THE HON'BLE MR. JUSTICE T.S. SIVAGNAM**

**AND**

**THE HON'BLE MR. JUSTICE HIRANMAY BHATTACHARYYA**

**ITA/83/2010**

**COMMISSIONER OF INCOME TAX, KOLKATA-IV, KOLKATA**

**VERSUS**

**M/S. CENTURY PLYBOARDS (I) LTD.**

**Appearance:-**

**Mr. Om Narayan Rai, Adv.**

**.....For the Appellant.**

**Mr. J.P. Khaitan, Sr. Adv.**

**Ms. Swapna Das, Adv.**

**Mr. S. Bhowmik, Adv.**

**.....For the Respondent.**

**JUDGMENT**

***(Judgment of the Court was delivered by T.S.SIVAGNAM, J.)***

1. This appeal filed by the revenue under Section 260A of the Income Tax Act, 1961 (the Act) is directed against the order dated 04.09.2009 passed by the Income Tax Appellate Tribunal (C) Bench, Kolkata ITA No. 552 of 1060/Kol/2009 for the assessment year 2005-06. The appeal was admitted on 20<sup>th</sup> March, 2010 on the following substantial question of law:

*“Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal is correct in holding the profit of Rs. 4,32,09,144/- as long-term capital gain?”*

2. We have heard Mr. Om Narayan Rai, learned Advocate for the appellant and Mr. J.P. Khaitan, learned Senior Advocate assisted by Ms. Swapna Das and Mr. S. Bhowmik, learned Advocates for the respondent.
3. The assessee filed its original return of income on 30<sup>th</sup> October, 2005 declaring a total income of Rs. 3,41,56,466/-. The return was processed under Section 143(1) on 13<sup>th</sup> July, 2006. The case was selected for scrutiny and notice under Section 143(2) was issued on 20<sup>th</sup> October, 2006 subsequently, notice under Section 142(1) was issued. The assessee is in the business of manufacture and sale of plywood and related products having its registered office in Kolkata and four regional offices and seventeen branches. Several issues were discussed with the assessee and the assessment was completed under Section 143(3) by order dated 20<sup>th</sup> December, 2007. In this appeal we are concerned with only one issue namely, whether the profit of 4,33,09,144/- should be treated as long-term capital gains or business profit. The Assessing Officer pointed out that the

assessee has shown long-term and short-term capital gains from sale and purchase of shares and units of mutual funds. The assessee issued show-cause notice to justify as to why the profit of the sale of shares/ units be treated as business profit. In the show-cause notice it was stated that looking at the frequency of the transactions it is prima facie clear that the assessee was transacting in shares as a business and they were required to justify as to why the investment should not be assessed under the head "income from business" instead of capital gains as has been shown by them. The assessee in their reply contended that the investment transactions were shown in the books of accounts under the head "investments" and they had invested idle funds within the limit prescribed under Section 372A of the Companies Act, 1956 and the investments were with a long-term view which is evident from the fact that during the financial year in question the assessee has earned Rs. 406.51 lakhs as capital gain from investment activities out of which Rs. 432.09 lakhs was long-term capital gain. Further, the assessee stated that during the financial year under consideration they had made only a few investment transactions compared to several other normal business activities such as trading of plywood and other products etc. Therefore, the assessee requested that the investments should be assessed under the head "capital gain". The Assessing Officer while considering the response given by the assessee referred to the memorandum and articles of association of the assessee and stated that it is clear that the main objects of the company was to undertake business in shares and securities. That during the year under consideration the assessee had carried on in a systematic and in an organized manner several transactions

of buying and selling of shares/ units which constituted its business activities. On perusal of the capital gain statement, it was pointed out that not only the assessee company carried out large number of transactions where the volumes were also large and some of the transactions were completed in very short span of time of 4 to 5 days or even on the same day. Further, the assessee has engaged professional manager to manage its portfolio under Portfolio Management Scheme which would clearly establish that assessee was buying and selling the shares/ units with an intention to earn profits. Further, the frequency of the transactions establish that they were business activities and not capital investments as claimed by the assessee. Thus, the Assessing Officer concluded that the transactions is impressed with the character of commercial transactions entered into with a view to earn profits, the transactions were numerous, carried out in a planned, systematic and organized manner and, therefore, the profits arising therefrom should be treated as profits from business and not capital gains. In support of such conclusion the Assessing Officer referred to the decision of the Hon'ble Supreme Court in **CIT Versus Distributors (Baroda) (P) Ltd.**<sup>1</sup> and also the decision of the High Court of Madras in the case of **CIT Versus Amalgamation (P) Ltd.**<sup>2</sup> wherein it was held that the only requirement is that there must be a real substantial and systematic or organized course of activity or conduct with the purpose of earning profit which is the test for a business. Reliance was placed on the decision of the High Court of Madras in the case of **Commissioner of Income Tax Versus**

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<sup>1</sup>83 ITR 377 (SC)

<sup>2</sup>108 ITR 895 (Mad)

**K. S. Venkatasubbaiah Reddiar** <sup>3</sup>, wherein it was held that the two essential requirements for an activity to be considered as business are (i) it must be a continuous course of activity, and (ii) it must be carried on with a profit motive. To explain the expression “business” reference was made to the decision of the Hon’ble Supreme Court in **State of A.P. Versus H. Abdul Bakhi and Ors.**<sup>4</sup> After referring to these decisions the Assessing Officer held that one of the main objects of the assessee as per the memorandum is to undertake the business of shares and securities, it acquired large quantity of shares and subsequently, disposed the same in a systematic manner to earn profits and these activities were carried out not only in the assessment year under consideration but also during the prior years and subsequent years in a systematic and organized manner. Further, these activities have yielded huge profits to the assessee and, therefore, it has to be held that the assessee is engaged in the business of dealing in shares. The explanation offered by the assessee company that they held the shares as investments to earn dividends was rejected and an inference was drawn that the transactions in buying and selling the shares amounts to business activity with the motive to earn profit and it was held that this conclusion is supported by the decision of the Hon’ble Supreme Court in **Dalhousie Investment Trust Co. Ltd. Versus Commissioner of Income Tax** <sup>5</sup>.

4. Aggrieved by such order the assessee preferred appeal before the Commissioner of Income Tax (Appeals), XI, Kolkata {CIT(A)}. The assessee

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<sup>3</sup> 221 ITR 18

<sup>4</sup>1964 15 STC 644

<sup>5</sup>(1968) 68 ITR 486 (SC)

contended that the mention of the business of share trading was one of the main objects in the memorandum and articles of association of the assessee company is not sufficient to lead to the conclusion that such business was actually carried on by the assessee and the fact being that no such business was done. Referring to Clause 18 of the memorandum which dealt with ancillary objects, it was stated that the same permits the assessee to invest and deal with the monies of the company not immediately required, in securities and such manner as may from time to time be determined. It was stated that the surplus funds of the business which were not immediately required were invested in terms of Clause 18 of the memorandum in order to maximize the value for share holders. It was further submitted that the question whether the gains of profits or business or capital gains depends upon whether the shares were held as stock -in-trade or investment. For such proposition, reliance was placed on the decision of the Hon'ble Supreme Court in ***Raja Bahadur Kamakhya Narain Versus CIT*** <sup>6</sup>. Further, it was contended that whether the shares were held as investment or stock-in-trade is a mixed question of fact and law, it is a matter which is within the knowledge of the assessee who should be in a position to produce evidence as to whether he has maintained any distinction between those shares which are stock-in-trade and those which are held by way of investment. It was further contended that the assessee held the shares as investment which is evident from the facts that they are consistently shown as investment in the balance-sheet and the gains of transfer of the same are shown as capital gains year after year. Further, it was submitted that out of

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<sup>6</sup>77 ITR 253 (SC)

the total capital gains, the income by way of long-term capital gains was Rs. 4.39 crores that is about 95% and it cannot be said that the period of holding was small. Further, it was contended that the assessee being a listed company are expected to carry each and every activity in a systematic and organized manner, it is not expected to sit idle and watch the hard-earned money being washed away because of unsystematic investments and therefore, merely because investments were made in a systematic and organized manner, cannot make them as a business activity. Business is something which occupies time, attention and labour of a person. However, since, the assessee was busy with its plywood business and other related items it had engaged services of a professional portfolio manager to handle its share portfolio. Further, it was contended that the existence of profit motive in transaction alone does not make it a business as even in the case of investment there can be a motive that an assessee should be able to sell such investment at a premium. The assessee further contended that they have been investing their surplus funds in shares, it is an on-going activity and consequently investments were also made on an on-going basis and there was no intention to do business in shares. It is further contended that the number of transaction is not determinative and does not make it a business activity and it is the intention of the assessee which is important. For such contention, reliance was placed on the decision in the case of **CIT Versus Trishul Investments Ltd.**<sup>7</sup> Further, it was contended that short period of holding of shares is not a determinative factor in concluding that the assessee was doing business of shares, the statute itself prescribes that

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<sup>7</sup> 215 ITR 96, Madras

a capital was held for less than 12 months is a short-term capital asset and capital gains arising on transfer thereof is short-term capital gain. Hence, any period of less than 12 months or few days or few months of holding of shares does not make any difference as in any case the transaction would result in short-term capital gains. Further, it was contended that earlier short-term capital gains were taxed at normal rate and the deductions available in computation thereof were very limited. Even at that point of time the assessee showed the same as short-term capital gains and had the assessee shown the gain as its business income the rate of tax would have been same but the assessee would have been able to claim many more deduction. However, this was not done as such shares were held as investment and not as stock-in-trade. Further, the department having treated the shares as investments and the gains as capital gains in the past, there is no justification for the Assessing Officer to take a different view in the assessment year under consideration. Though the findings in the previous assessment years do not operate as res judicata, does not mean that in every assessment year the Assessing Officer will take a different view. Further, it was contended that the distinction between “investment” and “stock-in-trade” and consequently the one between “capital gains” and “profits and gains of business” is very thin. It was contended that the intention behind the investment is to earn return for the same and not to earn profit from its turnover, though investments are also reshuffled once in a while. Further, it was contended that the intention at the time of purchase of the shares is of material significance. If an asset was purchased not with the intention to earn return but to earn profit from its turnover, it would be



a business transaction. An asset which was acquired as an investment may subsequently be converted into stock-in-trade. The CIT(A) referred to the main objects of the assessee company, the source of funds, the frequency of transactions, number of transactions, number of scrips transacted, the number of brokers/ intermediaries through whom transactions were done, the manner of maintaining books of accounts and ratio between purchase/sale and holding and held that all ingredients which makes the transaction a business transaction are found in the assessee's case. It was observed that the entries in the books of accounts are not determinative of the real nature of the transactions and when the apparent is not the real, the revenue authorities are to go for the substance and ignore the apparent. The CIT(A) agreed with the contention that once the department has given a particular treatment to a particular type of transaction, it should not normally deviate from such treatment in a subsequent year. However, it is a settled law that finding for one previous year does not operate as res judicata for another previous year and that even though the department has expected to maintain consistency in assessment, different views can be taken if some fresh material comes on record and the facts and circumstances justify such departure. The CIT(A) then proceeded to analyze the source of funds, and held that the assessee did not have any savings or surplus funds of its own which it could invest in shares and securities. The share capital was raised for purposes of doing business and has been applied fully for that purpose. The average funds of share capital as reserves and surplus combined was Rs. 41.37 crores which was grossly inadequate compared to the application of Rs. 68.94 crores in fixed and net current

assets. Therefore, the CIT(A) opined that even for it is normal business transaction of plywood and related items, the assessee had to resort to borrowing to the tune of Rs. 27.57 crores. Further, it was observed that the fund flow took place mainly through a bank account with State Bank of India which is a cash credit account in which there was a debit balance of Rs. 6.36 crores as on 31<sup>st</sup> March, 2005 which clearly shows that the funds were not the assessee's own but were borrowed, that there is no truth in the assertion of the assessee that surplus funds of business were invested in shares and securities. Further, it was observed that the assessee had incurred substantial expenditure by way of interest on borrowed fund and the said expenditure has been consistently claimed as business expenditure, suggesting thereby that they were utilized wholly and exclusively for purposes of business. Therefore, the CIT(A) held that the interest on borrowed capital has been claimed as expenditure against business income but income from share transactions is being shown as capital gains and this is incorrect in law and even if the department had accepted in the past, the same cannot be a bar to take a correct decision in the assessment year under consideration. The CIT(A) next dealt with the substantial part of the gains which was shown as the long-term capital gains which pertained to scrips of six companies and stated that these gains resulted from transfer of shares of companies which were thinly traded and were highly illiquid and they are called as penny stocks. The period of holding of the shares is just above 12 months and the appreciation in price during this period was phenomenal. On an average transaction in the shares are shown to have been yielded 1129% returns during the period of just above 12 months and

none of the companies is shown to have declared any dividend. Thus, the only motive in effecting such transactions was not to earn dividend but to earn profit on the appreciation of the share price. Further, the volume and frequency of transactions also leads to the conclusion that it is apparent that the transactions are not one of investment but it is that of trading. Dealing with the argument of the assessee that 95% of its gains were by way of long-term capital gains, the CIT(A) held that the motive of those transactions was to earn profit on turnover rather than return on investment and the period of holding of more than 12 months was also part of the strategy to make high profits tax free. Further, the CIT(A) commented that the assessee was dealing with as many as 12 brokers/ intermediaries and the bulk of the transactions were done through them and the assessee has a full-fledged share department. With regard to the plea of the assessee that it could have claimed various deductions, had the share transactions being shown as business activity was rejected by the CIT(A) stating that deductions which could be claimed under the head "profits and gains of business" have actually been claimed by the assessee in connection with its main business of plywood and related items and not relating to share transactions. Thus, the CIT(A) held that on an overall analysis of facts and circumstances of the case leads to the clear and inevitable conclusion that the intention of the assessee in the subject transactions was to earn profit from turnover and not by way of return on investment. The transactions were done in a systematic and organized manner with an intention to make profit. The assessee had no savings or surplus fund which could be invested in shares; the source of fund deployed in share transaction is directly seen

to the borrowed fund of the business, volume and frequency of the transactions, the number of varieties of scrip transacted, the number of intermediaries through whom transactions were done and the stock-to-turnover ratio too were too high for an investor. It is further stated that the profit from business from plywood and related items has been shown as Rs. 2,27,43,483/- while the gains from shares transactions is Rs. 4,51,37,343/- . Thus, the CIT(A) affirmed the order passed by the assessing officer treating the profits arising from transactions of shares and units as profits and gains of business.

5. Aggrieved by such order, the assessee preferred appeal before the Tribunal. The assessee contended that during the year under consideration the assessee had disclosed the total capital gains of Rs. 4,51,37,343/- which included long term capital gains of Rs. 4,32,09,144/- and short-term capital gain of Rs. 19,28,199/- that the assessee is a listed company which derives income from the manufacturing of plywood and the other related items and the turnover of the assessee from manufacture is more than Rs. 160 crores during the year under consideration. The assessee has made investments in shares and mutual funds and on the realization of investment, whatever profit or loss was incurred by the assessee was offered as long term/short term capital gains/loss. The assessee referred to a chart of long-term capital gain which was prepared for the transaction in respect of which the Security Transactions Tax (STT) was paid and in respect of transactions for which STT is not paid. It is pointed out by referring to the capital gains where STT is paid that the entire gains of Rs. 3,31,01,360/- arose from the sale of shares of four companies. No shares were purchased by the assessee during

the year under consideration. It was further contended that in respect of long-term capital gains wherein STT was not paid, the capital gains of Rs. 1,01,07,784/- arose out of the sale of shares of two companies namely *Arihant Enterprises Limited* and *Limtex Investment Limited* and no purchase of shares of any of the companies was made during the year under consideration and the assessee only sold shares. Therefore, it was contended that the allegations of the revenue that there was frequency of transactions is factually incorrect. The assessee referred to the balance sheet as on 31.03.2004 and pointed out that the capital and reserve of the assessee was Rs. 31.62 crores while as on 31.03.2005 it increased to Rs. 51.11 crores, on the other hand the total investment of the assessee was Rs. 5.01 crores as on 31.03.2004 and it reduced to Rs. 2.18 crores as on 31.03.2005. Thus, it was contended that the capital and reserve of the assessee was several times more than the investment in shares which will show that the investment in shares was out of assessee's own funds and it has not been pointed out by the revenue that borrowed money was utilized for investment in shares. Further it was submitted that in the immediate preceding year the assessee had received the dividend income of Rs. 3.80 crores and in the year under consideration it was Rs. 14.25 lakhs. With regard to the short-term capital gains, the assessee stated that they engaged the services of a portfolio manager who would indulge in day to day purchase and sale of shares and it is not done by the assessee themselves. Therefore, it was submitted that the surplus received by the assessee during the year under consideration from the realization of the investments should not be treated as business income. It was further contended that the

Memorandum and Articles of Association of the assessee company are very widely couched and merely because the memorandum permits the assessee to undertake business in shares does not mean that the investment in shares should be treated as adventure in the nature of trade. It was further contended that it has to be decided on facts of the case as to whether transactions of purchase and sale of shares was business of the assessee or investment in shares and realization thereof. However, referring to clause 18 of the Memorandum and Articles of Association, it was submitted that it permits the assessee to make investment in shares. Further it was pointed out that the CIT(A) in his order has accepted that the capital and free reserve of the assessee is much more than investment in shares. With regard to the frequency of transactions and the number of scripts transacted, it was stated that the figures mentioned in the order passed by the CIT(A) are factually incorrect and such observations is related to only short-term capital gain disclosed by the assessee and not long-term capital gains and therefore the capital gains as disclosed by the assessee should be accepted. The revenue placed reliance on the findings and observations in the order passed by the CIT(A) with particular reference to the paragraphs where the CIT(A) has summarized the reasons why the purchase and sell of shares was treated as business of the assessee. Further it was contended that the CIT(A) has considered the main object of the assessee as per Memorandum and Articles of Association, the source of funds, the frequency of transaction, number of scripts dealt with maintenance of books of accounts etc. and has come to the conclusion that the assessee was engaged in the business of trading in shares and units. Further it was contended

that the CIT(A) has also pointed out the shares wherein capital gain was disclosed were penny stocks.

6. The learned tribunal proceeded to examine the facts of the case. Firstly, with regard to the long-term capital gains amounting Rs. 3,31,01,360/- were STT was paid. After noting dates of purchase, names of the companies, the quantity of the shares and the amounts the tribunal held that the purchase of shares was of four companies that to was made in the preceding financial year (i.e.) F.Y.- 2002-2003. The purchase of shares of each of the companies was made in one block and during the year under consideration the entire shares of three such companies were sold out of which 50,000 shares of one of the companies 46,600 shares were sold and only 3400 shares remained in stock. Therefore, the tribunal held that the claim of the revenue that there was regular systematic and organized activity with regard to the purchase and sale of shares of the assessee is not applicable in the case of the purchase and sale of shares of those three companies as also, the findings of the CIT(A) that there was frequency in transactions that to in large numbers is also incorrect. Further the tribunal noted that the total investment in the shares is less than Rs. 50 lakhs while the capital and reserve of the assessee as on 31.03.2004 (preceding year) was Rs. 31.62 crores and as on 31.03.2005, it was Rs. 51.11 crores. The net profit of the assessee as per the profit and loss account for the year ended on 31.03.2004 was Rs. 9.01 crores while for the year ended 31.03.2005, it was Rs. 9.47 crores. Thus, the tribunal came to the conclusion that the capital and reserve of the assessee was many more times more than the investment in the shares in respect of which STT was paid and even the

profit of one year was several times more than the investment. Further the tribunal held that no evidence has been brought on record by the revenue that any borrowed funds were utilized for investment in shares. In the light of the above factual conclusion, the tribunal opined that the investment in shares was out of the assessee's own capital and not out of borrowed money. The turnover of the assessee from the manufacturing and trading activities was noted by the tribunal to be Rs. 128 crores for the year ended 31.03.2004 and Rs. 167.06 crores for the year ended on 31.03.2005. Further it was noted that the Memorandum and Articles of Association permitted the assessee to carry on business of purchase and sale of shares and also make investment therein. Taking note of the main business of the assessee and considering the facts relating to purchase and sale of shares, the tribunal opined that the same was investment in shares and realization thereof cannot be said to be business income of the assessee. Further while dealing with the observations of the CIT(A) stating that the shares were penny stocks, the tribunal observed that the CIT(A) has not doubted the genuineness of transactions and therefore the limited issue would be whether the transactions is in the nature of investment in shares or trading in shares. After considering the facts of the case, the tribunal was convinced to hold that the transactions were the investment in shares and the realization thereof and any surplus arising out of the sale of the shares has to be treated as capital gains and not business income. Accordingly, the tribunal held that the sum of Rs. 3,31,01,360/- should be assessed as long-term capital gains.



7. Nextly, the tribunal proceeded to consider the long-term capital gains of Rs. 1,01,07,784/- on which the STT was not paid. The details of the purchase and sale of the shares were noted and the tribunal held that there was no purchase during the year under consideration and the entire shares were sold during the accounting year relevant to the assessment year under consideration and having found the transactions to be similar to the transactions with regard to the purchase and sale on which STT was paid, it was held that the findings with regard to the long term capital gains on which STT was paid would be squarely applicable for long term capital gains on which STT was not paid and accordingly it held that the sum of Rs. 1,01,07,784/- should be treated as long term capital gains. With regard to the short-term capital gains, the learned tribunal noted the large number of transactions of purchase and sale and the facts that the services of an expert was utilized and that the shares/mutual funds were sold after short duration of its purchase, the number of companies and mutual funds whose shares were purchased and sold during the year under consideration held that the short term capital gain offered by the assessee at Rs. 19,28,199/- cannot be accepted as short-term capital gains but it should be assessed as business income of the assessee. This finding of the learned tribunal has not been challenged by the assessee and therefore we are not required to examine the correctness of such findings.

8. Mr. Om Narayan Rai, learned senior standing counsel appearing for the appellant revenue contended that the learned tribunal has accepted the assessee's assertion that it purchased the shares out of his own funds and while doing so, the learned tribunal glossed over the pertinent finding of the

CIT(Appeals) as regards the application of funds by the assessee in the business of investment and therefore the learned tribunal fell in error in not advertent to the findings rendered by the CIT(Appeals) on the said issue. It is submitted that the tribunal has observed that no evidence has been brought on record by the revenue that any money borrowed had been utilized for investment ignoring the findings of the CIT(A) that the bank account through which transactions were made was a cash credit account which will clearly show the funds were not the assessee's own funds but were borrowed funds. It is further submitted that since the assessee has sought for exemption from payment of tax the burden would be on the assessee to prove that they are entitled for exemption. The CIT(A) having clearly pointed out that the funds from the cash credit account had been utilized for the purpose of purchasing shares, the burden is on the assessee to show that the funds utilized for purchase were not borrowed fund. However, the learned tribunal had mistakenly treated the cash credit account to be a current account. Further it is submitted that the assessee having purchased shares by employing the borrowed funds, that is, by withdrawing sums from the cash credit account as found by the CIT(A), the learned tribunal could not have held that as profit of one year was several times more than investment, the shares could not have been purchased by borrowed funds. In this regard, reliance was placed on the decision of the Hon'ble Supreme Court in ***East India Pharmaceuticals Works Limited Versus Commissioner of Income Tax, West Bengal***<sup>8</sup> and also the decision of the division bench of this Court in ***C.E.S.C. Limited Versus Commissioner of***

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<sup>8</sup>1997 4 SCC 96

**Income Tax, Kolkata-II** in **ITA No. 105 of 2004** dated 26.11.2004 which was relied on by the learned senior advocate appearing for the respondent assessee. Thus, it is submitted that the judgment in **East India Pharmaceuticals Works Limited** and also **C.E.S.C. Limited** concluded that for the purpose of assuming that the investments have been made from out of the profits the twin conditions must be namely : (a)the profit of entire business including the sale proceeds should be deposited in the mixed overdraft accounts and(b) the investment should be less than the amount of profit earned or which could reasonably be deemed to have been earned, regard being to the date of expenditure. It is submitted that in the instant case, it has not been averred nor shown that the profits have been deposited in the cash credit account were from borrowing/withdrawals had been done for purchasing shares. It is further submitted that the assessee had relied upon the decision of the Hon'ble Supreme Court in **South Indian Bank Limited Versus Commissioner of Income Tax** <sup>9</sup> however the facts of the said case are strikingly different from that of the present case in as much as it was a case where the source of funds for investment had not been identified or was not identifiable contrary to the categorical un-rebutted findings rendered by the CIT(A) that the fund flow took place through a cash credit account. Further it is contended that the CIT(A) while using the expression mixed account has explained it further to mean that it is the regular business transactions of plywood and other products as well as transactions routed through the said cash credit account. Therefore, the expression mixed account which was mentioned in the decision of the Hon'ble Supreme

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<sup>9</sup>2021 438 ITR Page 1 (SC)

Court in **South Indian Bank Limited** is different from the expression to be employed in the instant case which has been clearly brought out by the CIT(A). It is further contended that it is the duty of the assessee to demonstrate before the tribunal that the factual findings rendered by the CIT(A) was incorrect. More so when CIT(A) has taken this as one of the grounds to hold that the assessee had not purchased the shares by way of investment and the learned tribunal misdirected itself in not even remotely alluding to the aforesaid aspect and holding against the revenue. With regard to the principles of consistency, it is submitted that no firm conclusion can be drawn from the method of keeping of accounts and description of a commodity under a particular head which is not a decisive factor. In this regard, reliance was placed on the decision of the Hon'ble Supreme Court in **M/s. Investment Limited Versus Commissioner of Income Tax, Kolkata** <sup>10</sup>. Reliance was also placed on the decision of this Court in **Shyam Burlap Company Limited Versus Commissioner of Income Tax, Central - 1, Kolkata** <sup>11</sup>. It is argued that the principle of consistency would mean happening of same set of events periodically or successively during a span of time and accordingly the law will have to be applied and if not the principle of consistency is not applicable. Reliance was also placed on the decision of the High Court of Delhi in **Shri Rakesh Kumar Gupta Versus Commissioner of Income Tax-XIII and Another** <sup>12</sup> wherein it was the case where the assessee maintained a separate portfolio for business and investment and the court held in favour of the revenue. It

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<sup>10</sup>1970 3 SCC 333

<sup>11</sup>2016 380 ITR 151 (Kolkata)

<sup>12</sup>2018 SCC Online Delhi 7907

is further submitted that both the assessing officer and the CIT (A) have referred to and relied upon the main objects of the business of the assessee company as provided in the Memorandum and Articles of Association and in fact, the CIT(A) has analyzed the source for the purchase of shares and found it to be flowing from a cash credit account, further the CIT(A), found that the companies whose shares were purchased had not declared any dividend and these facts will be more or less identical to the facts of the case which was considered by the Hon'ble Supreme Court, in the case of **Commissioner of Income Tax, Nagpur Versus M/s. Sutlej Cotton Mills Supply Agency Limited** <sup>13</sup>. Reliance was placed on the decision of the Hon'ble Supreme Court in **Dalhousie Investment Trust Company Limited Versus Commissioner of Income Tax (Central), Calcutta** <sup>14</sup> wherein the Hon'ble Supreme Court after noting the facts pertaining to the share transactions held that the income derived by the assessee from the sale of its shares and securities was a revenue receipt. Reliance was also placed on the decision of the Hon'ble Supreme Court in the case of **Commissioner of Customs (Import), Mumbai Versus Dilip Kumar and Company and Others** <sup>15</sup> for the proposition that if the benefit which accrues in favour of the assessee is in the nature of an exemption the onus is on the assessee to establish that they are entitled to the benefit. With the above submission, the learned senior standing counsel prayed for restoring the order passed by the CIT(A).

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<sup>13</sup>1975 2 SCC 538

<sup>14</sup>1968 68 ITR 486 (SC)

<sup>15</sup>2018 9 SCC Page 1

9. Mr. J.P. Khaitan, learned senior advocate appearing for the respondent assessee submitted that the only question involved in the appeal is as to whether the tribunal was correct in holding the profit of Rs. 4,32,09,144/- on the sale of shares of six companies held over from earlier years as long-term capital gains. It is submitted that in the previous assessment years as well as the subsequent years, the assessee's activities in respect of shares and securities were treated as investment activities and gains from sale thereof were treated as capital gains. Shares and securities purchased by the assessee are shown in its books of accounts as investments and accounted for accordingly. For the assessment year under consideration, A.Y. 2005-2006, the assessee claimed that the gains of Rs. 4,51,37,343/- from the sale of shares and securities were capital gains comprising long term capital gains of Rs. 4,32,09,144/- and net short term capital gains of Rs. 19,28,199/-. The assessing officer treated the entire capital gains as business income which order was upheld by the CIT(A). On further appeal to the tribunal, it agreed with the authorities below that having regard to the number of scrips transacted, the number of transactions made, the frequency of transactions, sale of shares within a short duration from the purchase thereof and transactions through portfolio manager, the assessee had engaged itself in an adventure in the nature of trade in a systematic and organized manner in so far as the activities resulting in net gains of Rs. 19,28,199/- were concerned and the said amount was business income. The assessee's activities in respect of long-term shares held over from the earlier years were separately examined by the tribunal and it accepted the contention of the assessee that gains of Rs. 4,32,09,144/- from the sale of

long-term shares were long term capital gains. Aggrieved over such findings, the revenue has preferred this appeal.

10. It is submitted that the shares in three companies were purchased during the financial year 2002-2003 relevant to the assessment year 2003-2004 and shares in other three companies were purchased during the financial year 2003-2004 relevant to the assessment year 2004-2005 and the total cost was Rs. 38,86,896/-. The long-term shares were listed on the stock exchange. It is submitted that all the shares in the five companies and most of the shares in the sixth company totally costing approximately Rs. 38,00,000/- were sold during the financial year 2004-2005 relevant to the assessment year 2005-2006 (year under consideration) resulting in gain of Rs. 4,32,09,144/-. Some of the shares were sold before October 01, 2004 giving rise to long term capital gains of Rs. 1,01,07,784/- chargeable to tax at 10% inserted by the Finance (No. II) Act, 2004 on Securities Transaction Tax (STT) introduced by the Finance (No. II) Act, 2004 with effect from October 01, 2004. It is submitted that though the assessing officer referred to the assessee's activities in the earlier, current and subsequent years did not separately examine the activities of the assessee in respect of long term shares. However, CIT(A) had considered this aspect which would be evident from the various paragraphs of the order passed by the CIT(A). It is submitted that the CIT(A) in his order has stated that the shares which were traded, were highly illiquid and were so called penny stocks. However, no material has been cited or referred to come to such a finding. The learned tribunal while examining the correctness of the same had rightly held that the CIT(A) has not doubted the genuineness of the transactions and

therefore the only question would be whether the transaction is in the nature of investment in shares or trading in shares. Further the findings of the CIT(A) that there was no likelihood of the companies declaring dividend in future is based on presumptions and merely because the companies were not shown to have declared dividend, it cannot be presumed that there was no likelihood of the companies declaring dividend in future. However, as a matter of fact the assessee was in receipt of the dividend on its investment and a sum of Rs. 3.80 crores was received in the preceding year i.e. 2003-2004 and Rs. 14.25 lakhs during the previous year, 2004-2005. Thus, it is submitted that the assessee made the investments expecting return by way of dividend and capital appreciation. The CIT(A) committed an error in holding that if dividend is not declared by a company its shares cannot be treated as investment and such findings/approach of the CIT(A) cannot be considered as reasonable. Furthermore, the findings of the CIT(A) that the only motive of the assessee was not to earn dividend but to earn profit is not based on any material and such findings were not accepted by the tribunal in the impugned order. The other observations made by the CIT(A) were uncalled and unreasonable which were rightly rejected by the learned tribunal. Furthermore, the CIT(A) failed to take note of the fact that long term shares were purchased during the financial years 2002-2003 and 2003-2004 when long term capital gains were taxable. STT and exemption in respect of long-term capital gains came into effect only from October 01, 2004. It cannot be disputed that the assessee sold long term shares in two of the companies prior to October 01, 2004 giving rise to long term capital gains of Rs. 1,01,07,784/- which was chargeable to tax at the rate of 10%. It



was only the long-term shares which the assessee sold on or after October 01, 2004 that enjoyed tax exemption. The CIT(A) failed to consider that in terms of clauses 29A, 29B, 42A and 42B of Section 2 of the Act, shares held for more than 12 months were long term capital assets giving rise to long term capital gains and those held for not more than 12 months were short term capital assets giving rise to short term capital gains and the assessee cannot be put to prejudice or faulted for availing exemption in accordance with the statutory provisions. It is submitted that the CIT(A) mis-directed itself in holding that whether the assessee was doing business or not was required to be decided by the overall transactions and not scrip wise transactions. The CIT(A) sought to term the transactions in long term shares as “isolated transactions”. This view of the CIT(A) is contrary to the settled law. In support of such contention, reliance was placed on the decision of the Hon’ble Supreme Court in **Commissioner of Income Tax Versus Associated Industrial Development Company Private Limited** <sup>16</sup>. It is submitted that the said decision was followed by this Court in **Jet Age Securities Private Limited Versus Commissioner of Income Tax** in <sup>17</sup> dated September 15, 2022 in which, the court considered Circular No. 04 of 2007 dated June 15, 2007 where the CBDT emphasized that it is possible for a taxpayer to have two portfolios i.e. an investment portfolio comprising of securities which are to be treated as capital assets and a trading portfolio comprising of stock-in-trade which are to be treated as trading assets and consequently when the assessee has two portfolios, the assessee may have

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<sup>16</sup>1971 82 ITR 586 (SC)

<sup>17</sup>ITA No. 79 of 2010

income under both the heads i.e. capital gains as well as business income. Therefore, the CIT(A) committed an error in not considering the transactions in long term shares separately from the other transactions. Further it is submitted that the transactions in long term shares held over from earlier years were required to be separately considered on their own merit to decide whether the same were on investment account and it was not permissible to treat the sale as business transactions merely because the transaction of purchase of shares and securities and the sale thereof made during the previous year relevant to the assessment year 2005-2006 were held to be on business account. It is further submitted that the learned tribunal separately examined the transactions in respect of long-term shares to determine whether the same were on investment account or business account. In this regard, the learned senior advocate has drawn our attention to various paragraphs of the impugned order.

11. It was argued by the revenue that bank account used to make purchase and sales was a cash credit account and not a current account as erroneously observed by the tribunal. Further that the CIT(A) had arrived at a finding that the assessee had used borrowed funds to purchase the shares. It is submitted that on a perusal of the order passed by the CIT(A) it would clearly show that the cash credit account is a mixed/composite account through which the regular business transactions of plywood and allied products as well as shares transactions were routed. Though the CIT(A) has mentioned that the cash credit account had a debit balance of Rs. 6.36 crores as on March 31, 2005 no mention has been made of any debit balance on any other day. Thus, the CIT(A) proceeded on the

assumption that the average of share capital and reserves and surplus of Rs. 41.37 crores was entirely used for funding the fixed and net current assets of Rs. 68.94 crores and the assessee had to resort to borrowing to the tune of Rs. 27.57 crores even for its normal business transaction of plywood and allied products. The CIT(A) completely mis-directed itself in arriving at the aforementioned finding. It is not in dispute that the assessee's shares, capital and reserves amounted to Rs. 41.37 crores on an average whereas the amount invested in long term shares was less than Rs. 50 lakhs. Further it is not in dispute that not only during the assessment year 2005-2006 even for the assessment years 2003-2004 and 2004-2005 during which long term shares were purchased, the assessee earned profits. In this regard, the assessment order dated March 31, 2006 for the assessment year 2003-2004 and the order dated February 14, 2014 for the assessment year 2004-2005 were referred. That apart, the tribunal had noted that the profit as per the Profit and Loss Account for the year ended March 31, 2004 was Rs. 9.01 crores and for the year ended March 31, 2005 it was Rs. 9.47 crores. Referring to the decision of this Court in **C.E.S.C Limited Versus Commissioner of Income Tax** in<sup>18</sup> dated November 26, 2014, it is submitted that where the profit of the entire business including the sale proceeds were deposited in the mixed overdraft account and in case, the investment was less than the amount of profit earned, it had to be presumed that the investment was from out of the profits. Reliance was placed on the decision of the Hon'ble Supreme Court in **South Indian Bank Limited**

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<sup>18</sup>ITA No. 105 of 2004

***Versus Commissioner of Income Tax*** <sup>19</sup> wherein it was held that in a situation where the assessee had mixed funds and payment is made out of that mixed funds the investment must be considered to have been made out of the interest free funds. In the assessee's case the profits as well as interest free funds in the form of capital and reserves were far in excess of the amount invested and therefore the investment must be taken to have been made out of the assessee's own funds. It is further submitted that it is not in dispute that the long-term shares held over from the earlier years were shown as investments in the assessee's books of accounts. It was accepted in the assessment years 2003-2004 and 2004-2005 during which period the shares were purchased to be long term shares held as investments. The assessment orders for those years show that the assessee was charged to tax in respect of long-term capital gains. The CIT(A) accepted the assessee's stand that long-term shares were shown as investment and the profits were shown as capital gains consistently and that such treatment was accepted by the department in the past. However, the CIT(A) held that even though the department was expected to maintain consistency in assessment, different view can be taken if some fresh material comes on record and the facts and circumstances justify such departure. It is submitted that it would be impermissible for the revenue to contend that the shares which were held as investment and accepted as such for the assessment years 2003-2004 and 2004-2005 were not investments when it came to the assessment year 2005-2006 (year under consideration). There is no new or fresh material in respect of long-term shares on the basis of

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<sup>19</sup>2021 438 ITR (page 1) (SC)

which the consistent finding of the earlier years in respect of such shares can be reversed for the assessment year under consideration. To support such contention, reliance was placed on the decision in **Commissioner of Income Tax Versus Srideb Enterprises** <sup>20</sup>. Further it is submitted that the gains from the remaining long-term shares of the 6<sup>th</sup> company sold during the previous year relevant to the assessment year 2006-2007 were treated by the assessing officer as business income but this order was reversed on appeal. The revenue's appeal before the tribunal against the said order was dismissed by order dated February 11, 2011 in ITA No. 134/Kol/2010. For the assessment years 2007-2008 and 2008-2009, the assessing officer treated the income from sale of shares as business income but this order was reversed by the CIT(A) and the tribunal dismissed the revenue's appeal in ITA No. 1727/Kol/2010 and ITA No. 1728/Kol/2010 by orders dated May 11, 2011 and August 18, 2011 respectively and till date the assessee has not been served with any notice of any appeal preferred by the revenue before this Court.

12. It is submitted by the learned senior advocate that the learned senior standing counsel had been fair in placing the Circular No. 4 of 2007 dated June 15, 2007 and Circular No. 06 of 2016 dated February 29, 2016 but contended that the said circulars cannot have any retrospective effect. It is submitted that in paragraph 10 of the Circular No. 04 of 2007 the Board had accepted the position that an assessee can have both investment portfolio in respect of capital assets and trading portfolio comprising of stock-in-trade and such made have income under the head capital gains as

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<sup>20</sup>1991 192 ITR 165 (Kar)

well as business income. In the Circular No. 6 of 2016, the Board directed that in respect of listed shares and securities held for a period of more than twelve months immediately preceding the date of its transfer, if the assessee desires to treat the income arising from transfer thereof as capital gains, the same shall not be put to dispute by the assessing officer. However, this stand once taken by the assessee in a particular assessment year, shall remain applicable in subsequent assessment years also and the tax payers shall not be allowed to adopt a different/contrary stand in this regard in subsequent years. It is submitted that the circulars being beneficial circulars to the assessee have to be given retrospective effect and would apply to the assessment years under consideration. In support of such contention, reliance was placed on the judgment of the Hon'ble Supreme Court in **Director of Income Tax Versus SRMB Dairy Farming Private Limited**<sup>21</sup>. It is further submitted that if for any reason any matter for a year prior to the issue of the said circulars is remanded for a fresh decision, the assessee can certainly claim the benefit of the said circular in such proceeding. It is further submitted that it is well settled that the legal pursuit of a remedy, suit, appeal and second appeal are really but still in a series of proceedings all connected by an intrinsic unity and are to be recorded as one legal proceeding and therefore such beneficial circulars can be availed of by the assessee even at this stage.

13. It is further submitted that the decision to be taken in such matters depends on the facts of each case and it is not possible to evolve a single legal test or formula which could be applied in determining whether the

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<sup>21</sup>2018 400 ITR Page 9 (SC)

transaction was an adventure in the nature of trade or not and the answer to the question would depend in each case on the relevant factors and circumstances proved therein which will determine the character of the transactions. In support of such contention, reliance was placed on the decision of this Court in **Gyan Traders Limited Versus Commissioner of Income Tax**, <sup>22</sup>. It is submitted that in the decision in **Gyan Traders Limited** this Court has considered its previous decision in **Commissioner of Income Tax Versus Merlin Holding Private Limited** <sup>23</sup>, **Jet Age Securities Private Limited Versus Commissioner of Income Tax** in<sup>24</sup>dated September 15, 2022 and **Principal Commissioner of Income Tax Versus Purvanchal Leasing Limited** <sup>25</sup>.

14. Adverting to the decisions relied on by the revenue in case of **Dalhousie Investment Trust Company** and **Investment Limited**, was a case relating to the assessment year 1953-1954 and the decision in **Sutlej Cotton Mills** pertaining to the assessment year 1956-1957 where the statutory framework for taxation was quite different as during those years, there was no tax on capital gains. It is submitted that in the current economic scenario, investment in shares is recognised mode of investment as opposed to the olden times when recognised investment option were investing in properties and precious metals/jewellery. In this regard, the learned senior advocate referred to the various notifications which were issued by the Government to promote the primary and secondary market and the legislative changes which was brought about. The learned senior

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<sup>22</sup>2022 143 Taxman.com 42 (Cal)

<sup>23</sup>2015 375 ITR 118 (Cal)

<sup>24</sup>ITA No. 79 of 2010

<sup>25</sup>2022 287 Taxman 20 (Cal)

advocate referred to the facts in all the decisions relied on by the revenue and sought to distinguish the same. With regard to the decision in **Sri Rakesh Kumar Gupta**, relied on by the revenue, it is submitted that the assessee had purchased and sold shares either the same day or after a few days and in most cases they were intra-day transactions not involving delivery of shares and the said assessee's plea based on past assessment was not accepted as it was not shown that the transactions were identical. With regard to the decision in **Shyam Burlabh Company Limited**, relied on by the revenue, the principle of consistency was held not applicable in view of the changed fact situation. However, such is not the position in the assessee's case as there is no change in the facts in so far as the long-term shares are concerned. Further in **Shyam's Burlabh's** case claim for assessment under the head "business" was made for the first time in the assessment year 1996-1997 because it entailed a lower tax liability and there was no prior claim for adjudication with regard to the said head. In so far as the assessee's case is concerned, in the past the assessee claimed, the claimed assessment under the head capital gains which entailed lower taxation. The assessments for the years 2003-2004 and 2004-2005 were made under Section 143(3) of the Act and the assessing officer accepted that the income was properly offered under the head the capital gains. Therefore, the principle of consistency squarely applies to the case of the assessee. With the above submissions, the learned senior advocate sought to sustain the order passed by the learned tribunal.

15. Mr. Om Narain Rai, learned senior standing counsel by way of reply submitted that the CIT(A) had clarified that he has taken a holistic view of



all the shares dealings with the same wholesomely and merely because at the end of one of the sentences, the CIT(A) has referred to the then obtaining debit balance in the account, there is no reason to discredit the CIT(A) earlier observation where he has rendered a specific finding. It is reiterated that since the assessee was claiming exemption, the burden is on the assessee to establish the case. It is further submitted that the assessee had contended that the question as to whether a transaction is an investment or business is required to be decided script wise and not holistically may be relevant in a case where the assessee maintains two portfolios and in the instant case, the assessee has maintained a single portfolio in respect of all shares which fell for consideration before the authorities. On this ground, the learned senior standing counsel sought to distinguish the decision in ***Associated Industrial Development Company***. With regard to the argument that both the circulars are to apply retrospectively, it is submitted that the object of the circular could be culled out from the circular itself which clearly reveals that the same was for reducing litigation and maintaining consistency in approach on the issue of treatment of income derived from the transfer of shares and securities and there is no such benefit like exemption or otherwise given to the assessee by the said circular. Further in the decision in ***S.R.M.B. Dairy Farming Private Limited***, it is clarified that a circular cannot be applied *ipso facto*. In this regard, paragraphs 19, 20 and 25 of the said judgment were referred to wherein liberty was given to the department to move the High Court pointing out that the circular should not be applied *ipso facto* particularly, when the matter has a cascading effect. With the above submission, the learned

senior standing counsel prayed for allowing the appeal and answering the substantial questions of law in favour of the revenue.

16. The assessee company filed their return of income on 31 October 2005 declaring a total income of Rs 3,41,56,466/- for the assessment year 2005-2006. The return was processed under section 143 (1) on 13 July 2006. The case was selected for scrutiny and notice under section 143 (2) was issued on 20 October 2006. Thereafter notices under section 142 (1) was issued on several dates and the case was discussed with the authorised representative of the assessee. During the course of assessment proceedings several queries were raised by the assessing officer and in this appeal we are concerned about the issue as to whether the profit of Rs 4,32,09,144/- on sale of shares in six companies was long-term capital gains or was it business income. In this regard a show cause notice was issued to the assessee stating that on going through the return of income it was found that the assessee had entered into numerous transactions in a systematic and organised manner of buying and selling shares and securities and units of mutual fund during the assessment year under consideration, 2005-2006. It was stated that the assessee has shown the buying and selling of shares and securities as investment and offered the income from the sale as long-term capital gain or short-term capital gain and on going through the frequency of the transactions, it was alleged that the transactions wherein the nature of a business and therefore the assessee was called upon to justify the transactions as investment and as to why the same should not be assessed under the head "income from business" and not as long term capital gains as claimed by the assessee in the return of income.

17. The assessee in their reply contended that they have accounted for the transactions as investment transactions in its books of accounts and has been specifically shown as such in the schedule. That the assessee has been investing idle funds within the limit prescribed under section 372A of the Companies Act, 1956. That the assessee has been investing funds with long-term view which is evident from the fact that during the financial year in question the assessee has yearned Rs. 460.09 lakhs as capital gains from the investment activities out of which Rs. 432.09 lakhs was long-term capital gain. That during the whole financial year the assessee has made only a few investments in shares compared to several other transactions relating to its normal business activities namely trading of plywood and other products and therefore requested that the investment income should be assessed under the head capital gains.

18. The assessing officer after taking note of the stand taken by the assessee in the reply to the show cause notice, perused the Memorandum and Articles of Association of the assessee company, one of which being to carry on and undertake the business in shares, securities, mutual funds etc, to Act as brokers, sub-brokers to carry on inter-market transactions and to acquire by way of purchase or otherwise stock exchange membership card subscribing to new issues of shares, debentures and mutual funds. Taking note of the said clause in the Memorandum the assessing officer opined that business in shares and securities is one of the main business of the assessee company. Further the assessing officer opined that the assessee had carried on in a systematic and an organised manner, numerous transactions of buying and selling of shares which constituted its

business activities. Assessing officer further held that some of the transactions are completed in a very short period, within 4 to 5 days or even on the same day, the assessee company has also engaged professional manager to manage its portfolio under portfolio management scheme which clearly indicates the motive of the assessee while buying and selling the shares was only with a view to earn profits. Therefore it was held that the frequency of transactions carried out by the assessee are in the nature of business activities and not investment as claimed by them. Further the assessing officer opined that the transactions undertaken by the assessee is impressed with the character of commercial transactions entered into with a view to earn profits, the transactions were numerous and carried out in a planned, systematic and organised manner and therefore the profits arising to the assessee company from purchase and sale of shares should be treated as profits from business and not capital gains. In support of such conclusion the assessing officer referred to certain decisions of the Hon'ble Supreme Court and proceeded to hold that it is beyond doubt that the transactions done by the assessee of buying and selling of shares and securities were undertaken with a profit motive and at regular intervals. Had the motive of investment in shares been to earn dividends, the assessee company would not have entered into such frequent buying and selling the book profits on appreciation. Thus the assessing officer concluded that the assessee had purchased and sold shares with a view of yearning profit by such purchase and not with the object of investing its capital in the shares in order to derive income from that investment. Further the assessing officer held that the volume of transactions, the frequency of transactions, the

systematic and organised manner of undertaking the transactions strongly lead to the conclusion that the shares could not have been purchased as an investment to earn income from dividends and that the purchase of the shares were with the object of selling them subsequently at profit and in fact the shares were sold at considerable profits subsequently. The assessing officer rejected the stand taken by the assessee that the shares were held as investment to earn dividends.

19. Aggrieved by the assessment order dated 28th of December 2007 the assessee filed appeal before the Commissioner of Income Tax (Appeals)-X I, Kolkata [CIT(A)] contending that the assessing officer committed gross error in assessing the gains arising from the purchase and sale of shares/units under the head business. The assessee contended that mention of business of share trading as one of the main objects in the Memorandum and Articles of Association of the company is not sufficient to lead to the conclusion that such business was actually carried on by the assessee, but the fact being that no such business was done by the assessee. The assessee referred to clause 18 of the ancillary objects in the Memorandum of Articles of Association of the company which allows the assessee to invest and deal with the money of the company not immediately required, in such securities and in such manner as may from time to time be determined. The assessee therefore contended that the surplus funds of the business which were not immediately required were invested in terms of clause 18 of the ancillary objects with the view to maximise the value for shareholders. The assessee further contended that the issue as to whether the gains are profits of business or capital gains depends upon whether the shares were held as

stock in trade or investment. The assessee held the shares as investment which is evident from the fact that they are consistently shown as investment in the balance sheet and the gains on transfer of the same are shown as capital gains year after year. Further by referring to the computation of capital gains it was submitted that it is about 95% and the same cannot be said that the period of holding was small. Further with regard to the opinion of the assessing officer that the assessee conducted its activities in a systematic and organised manner, the assessee stated that they being a listed company are expected to carry on their activities in a systematic and organised manner and therefore the same cannot be construed to be a business activity. Further the assessee contended that existence of profit motive in transactions cannot be the sole determinative factor to treat the same as a business transaction. The assessee has been investing its surplus funds in shares. The said business was an ongoing activity, surplus therefrom also arose on an ongoing basis and consequently, investments were also made on an ongoing basis and there was no intention to do business in shares. Further the assessee stated that the number of transactions is not determinative and does not make it a business activity. Further short period of holding of shares is also not determinative in concluding that the assessee was doing business of shares. The Income Tax Act itself provides that a investment held for less than 12 months is a short-term investment and capital gains arising on transfer thereof is short-term capital gains. Hence any period of less than 12 months, be it a few days or few months is of holding the shares does not make any difference, in any case, the transaction would result in short-term capital gains. Further the

assessee contended that short-term capital gains tax at normal rate and the deduction is available in computation thereof where limited and even at the relevant time the assessee showed such gains as short-term capital gains and the assessee would have benefited if they had shown it as business income as they would have been able to claim several other deductions but the same was not done as the shares were held by the assessee as investment and not as stock-in-trade. The assessee further contended that the department having treated the shares as investment and the gains as capital gains in the past there is no justification for the assessing officer to take a different view in the year under consideration and the assessing officer ought to have maintained consistency. Further the assessee contended that the intention of the assessee at the time of purchase of the shares is of material significance as, if the shares were purchased not with an intention to earn return on the investment but to earn profit from its turnover it would be a business transaction. Then an asset which was acquired as an investment may subsequently be converted into stock-in-trade. Even if the asset is not shown as stock-in-trade or having been shown as investment, it is not converted into stock-in-trade, it may still be a business transaction, if the facts and circumstances so warrant. In so deciding, the factors that would be relevant are the volume and frequency of transactions, holding, source of funds (own or borrowed) and therefore the relevant facts and circumstances of each case ought to be considered. The CIT(A) examined the source of funds, the frequency of transactions, the number of transactions, number of scripts transacted the number of brokers who were involved, the manner in which the assessee had

maintained its accounts and the ratio between purchase/sale and holding and proceeded to form his opinion that all the ingredients to make the transaction as business transaction was found in the assessee's case. While analysing the source of funds the CIT(A) held that the fund flow took place mainly through its bank account with State Bank of India which was a cash credited account in which there was a debit balance of Rs 6.36 crores as on 31 March 2005 which would show that the funds were not the assessee's own funds but were borrowed funds and disbelieved the stand taken by the assessee that they have utilise the surplus funds for investment in shares and securities. The CIT(A) partially agree with the assessee that intention of the assessee is material factor but however held that the issue is not tax neutral and that taxation of capital gains on shares and securities is highly subsidised as compared to profits and gains of business. Thereafter the CIT(A) examined as to how the services of a prominent share broker was utilised by the assessee and other transactions in mutual funds. While dealing with the issue relating to long-term capital gains, the CIT(A) noted the transactions done by the assessee with the scrips of six companies and held that the shares were thinly traded and were highly illiquid. The period of holding of the shares is just about 12 months and the appreciation in price during this period was phenomenal and none of the companies have declared any dividend. The CIT(A) drew adverse inference against the assessee noting the volume and frequency of the transactions. The CIT(A) came to the conclusion that the assessee was actually engaged actively in share transactions, they had a full-fledged shares Department and it is the assessee who has been taking decisions in respect of high-volume, high



frequency as well as high-stakes transactions. With regard to the plea of the assessee that if they had shown the share transactions as business activity they could have claimed various deductions, the CIT(A) rejected such a plea as lacking in substance because all the deductions which could be claimed under the head profits and gains of business have actually been claimed by it in connection with the business of plywood and related items and not a single instance of deduction relating to share transactions has been shown which could be claimed as additional deductions, had the income been shown as profits of business, but has not been claimed. Thus the CIT(A) concluded that on the overall assessment of the facts and circumstances of the case leads to the clear and inevitable conclusion that the intention of the assessee was clear in making profit from turnover and not by way of return on investment. The CIT(A) held that the profit from the business of plywood and related item was far less from the gains from share transactions and therefore agreed with the assessing officer in treating the profits arising from share transactions and mutual fund units as profits and gains of business. Aggrieved by the order passed by Commissioner dated 23 March 2009, the assessee preferred appeal before the Tribunal.

20. Upon perusal of the order passed by the learned Tribunal we find that, the learned Tribunal rightly segregate the two claims, namely, the one claimed as long-term capital gain and the one claimed as short-term capital gain. In the category of long-term capital gain as well as short-term capital gain the learned Tribunal further segregated the issues under two heads namely where the assessee had paid STT and where STT was not paid. The first issue which was considered was with regard to the long-term capital

gain on which STT was paid.

21. The tribunal examined the facts of the case and found that the capital gains arose from the sale of shares of four companies and the purchase of those shares were made in the preceding financial year namely the financial year 2002-2003. The number of shares purchased was considered the total investment made, net profit of the assessee and held that there is no evidence brought on record by the revenue that any borrowed money was utilised for investment in the shares. The tribunal was of the view that the transactions were done through the assessee's current account which is maintained for the purpose of its plywood business and opined that the shares were not purchased out of the borrowed funds. The turnover of the assessee's main business was taken note of, the relevant clause in the Memorandum and Articles of Association of the assessee and considering the totality of the facts held that the purchase and sale of shares was an investment in shares and realisation thereof. Further the tribunal held that the authorities have not doubted the genuineness of the transactions and therefore the limited issue would be whether the transaction is in the nature of investment in shares or trading in shares. Similarly, the facts pertaining to long term capital gains where STT was not paid was considered. The tribunal after noting the relevant details held that the findings with regard to the long-term capital gains on which STT was paid will be equally applicable to the long term capital gains where STT was not paid and accordingly decided the issue in favour of the assessee. The correctness of the orders passed by the learned tribunal is being questioned by the revenue in this appeal. The of the case of the revenue was that findings rendered by

the CIT(A) that the account being a current account and set aside the order passed by the CIT(A) which is incorrect as it is factually wrong. It is no doubt true that the learned tribunal committed a mistake in referring to the said account as a current account, the fact being it is a cash credit account. The question would be whether if it is a cash credit account, will it lead to the automatic presumption that the funds which were utilised were borrowed funds. While we examine the issue, it has to be borne in mind that the long-term capital gains amounting to Rs. 3,31,01,360/- wherein STT was paid arose out of sale of shares of four companies and the purchase of those shares of the four companies were made in the preceding financial year i.e. 2002-2003. This is an important fact which needs to be borne in mind which appears to have been brushed aside by the CIT(A). Reverting back to the issue as to the nature of the bank account qua whether the funds were assessee's own surplus funds or borrowed funds. It is seen that during the year under consideration, the entire shares of M/s. Ankit Prachi Trading Company Limited, Globe Stock and M.P. Investments and Constructions were sold and out of the 50,000 shares of Bakra Limited, 46,600 shares were sold and 3400 shares remained in stock. The issue is can these transactions be said to be an organised activity, a systematic activity intended only to make profit and not as an investment. The facts clearly show that the purchase and sale of the shares of these four companies has not been shown by the revenue to be part of a systematic and organised activity. That apart, there was nothing on record to show that there was frequency in transactions, large number of shares were purchased and sold. The tribunal noted that the total investment in the shares of those

four companies is less than Rs. 50,00,000/-, while the capital and reserve of the assessee as on 31.03.2004 was Rs. 31.62 crores and as on 31.03.2005, it was Rs. 5.11 crores. The net profit of the assessee as per Profit and Loss Account for the year ended 31.03.2004 was Rs. 9.01 crores while for the year ended on 31.03.2005, it was Rs. 9.47 crores. Thus, noting these undisputed facts, the tribunal concluded that not only the capital and reserve of the assessee was many times more than the investment in shares in respect of which STT was paid, but even the profit of one year, was several times more than the investment. The tribunal held that there is no evidence brought on record by the revenue that any borrowed money was utilised for investment in the abovementioned shares. We fully agree with such a finding rendered by the tribunal as the CIT(A) concluded that the borrowed funds had been utilised solely for the reason that the funds flow was from a bank account which was a cash credit account. As the assessee has been able to demonstrate that the cash credit account is a mixed/composite account through which regular business transactions of plywood and allied products as well as shares transactions were routed. Furthermore, as rightly contended on behalf of the assessee, the CIT(A) had mentioned that the cash credit had a debit balance of Rs. 6.93 crores as on March 31, 2005 but there was no mention made of any debit balance on any other day. The revenue does not dispute that the assessee's share capital and reserve is Rs. 41.37 crores on an average whereas the amount invested in long term shares was less than Rs. 50,00,000/- and it was disputed only during the assessment year 2005-2006.

The learned senior advocate for the assessee referred to the assessment order dated 31.03.2006 for the assessment year 2003-2004 which was a scrutiny assessment under Section 143 (3) of the Act wherein the assessee's total income was Rs. 7,08,30,550/-. Similarly, by referring to the assessment order dated 14.02.2014 for the assessment year 2004-2005, it was shown that the total income of the assessee was Rs. 4,38,22,890/-. As already pointed out the tribunal also noted that as per the Profit and Loss Account for the year ended 31.03.2004, the profit was Rs. 9.01 crores and for the year ended March 31, 2005, it was Rs. 9.47 crores. These undisputed facts should enure in favour of the assessee. More or less an identical question was considered by the Hon'ble Division Bench of this court in the case of **C.E.S.C Limited Versus Commissioner of Income Tax, Kolkata – II** in **ITA No. 105 of 2004** dated 26.11.2014. In the said case, the assessee invested in share capital of a 100% subsidy company during the assessment year 1992-1993. The assessing officer held that borrowed funds were utilised for the purpose of the aforesaid investment and therefore interest at the rate of 18% was disallowed. On appeal before the CIT(A), the finding of the assessing officer was reversed. On appeal by the revenue before the tribunal, the findings of the CIT(A) was reversed on the ground that the said assessee failed to furnish any evidence or material to show that the assessee's own money accumulated out of the profits and being utilised in making investments in shares of its subsidiaries companies and that the assessee therein failed to establish or prove that the investment was made in shares by the assessee has been made out of the profits generated by the assessee company. The said order of the tribunal was subject matter of

challenge in the appeal before this court, and reliance was placed on the decision of the Division Bench in the case of **Woolcombers of India Limited Versus Commissioner of Income Tax** <sup>26</sup>. In the said case, the payment of advance tax from an overdraft account was held to be not business expense and the assessing officer disallowed the same. When the matter reached the Division Bench of this court, it was noted that the profits were sufficient to meet the advance tax liability, the profits were deposited with the overdraft account and it should be presumed that in its essence and true character the taxes were paid out of the profits of the year and not out of the overdraft account for the running of the business. After taking note of the decision, the Division Bench in the case of **C.E.S.C Limited** held that where the profits of the entire business including the sale proceeds were deposited in the mixed overdraft account and in the case the investment is less than the amount of profit earned or which could reasonably be deemed to have been earned, regard being had to the date of expenditure, it has to be presumed that the investment was made from out of the profits. In our considered view, the decision in **C.E.S.C Limited** will squarely apply to the facts and circumstances of the case on hand.

22. At this juncture, it would be beneficial to refer to the decision of the Hon'ble Supreme Court in **South Indian Bank Limited**. The question of law which arose for consideration before the Hon'ble Supreme Court was whether proportionate disallowance of interest paid by the banks is called for under Section 14A of the Act for investments made in tax free bonds/securities which yield tax free dividend and interest to assessee

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<sup>26</sup> 134 ITR 219

banks when the assessee had sufficient interest free own funds which was more than the investment made? The assessee's before the Hon'ble Supreme Court were scheduled banks and in the course of their banking business, they also engaged in business of investments in bonds, securities and shares which earn interest for the assessee. While completing the assessment, the assessing officer made proportionate disallowance of interest attributable to the funds investment to earn tax free income as separate accounts for investment was not maintained. The order was affirmed by the CIT(A). The tribunal considered the absence of separate identifiable funds utilised by the assessee for making investments in tax free bonds and shares but found that the assessee bank is having indivisible business and considering their nature of business, the investment made in tax free bonds and shares were held to be in the nature of stock-in-trade. The tribunal then noticed that the assessee bank is having surplus funds and reserves from which investments can be made and accordingly accepted the assessee's case that investments were not made out of the interest or cost bearing funds alone. Consequently, the disallowance under Section 14A was held to be not warranted in the absence of clear identity of funds. The decision of the tribunal was reversed by the High Court which decision was challenged before the Hon'ble Supreme Court. The Hon'ble Supreme Court while dealing with the fact situation decided how the issue has to be considered when the assessee has mixed funds that is partly of interest free funds and partly of interest-bearing funds and when payment is made out of the mixed funds. The said question was answered by the Hon'ble Supreme Court holding that when the assessee has mixed funds and payment is

made out of that mixed funds, the investment must be considered to have been made out of the interest free funds. The following paragraphs of the said judgment would be relevant:

*17. In a situation where the Assessee has mixed fund (made up partly of interest free funds and partly of interest-bearing funds) and payment is made out of that mixed fund, the investment must be considered to have been made out of the interest free fund. To put it another way, in respect of payment made out of mixed fund, it is the Assessee who has such right of appropriation and also the right to assert from what part of the fund a particular investment is made and it may not be permissible for the Revenue to make an estimation of a proportionate figure. For accepting such a proposition, it would be helpful to refer to the decision of the Bombay High Court in Pr. CIT v. Bombay Dyeing and Mfg. Co. Ltd.<sup>1</sup> where the answer was in favour of the Assessee on the question, whether the Tribunal was justified in deleting the disallowance Under Section 80M of the Act on the presumption that when the funds available to the Assessee were both interest free and loans, the investments made would be out of the interest free funds available with the Assessee, provided the interest free funds were sufficient to meet the investments. The resultant SLP of the Revenue challenging the Bombay High Court judgment was dismissed both on merit and on delay by this Court. The merit of the above proposition of law of the Bombay High Court would now be appreciated in the following discussion.*

*19. In HDFC Bank Ltd. v. Deputy Commissioner of Income Tax MANU/MH/0208/2016 : (2016) 383 ITR 529 (Bom), the Assessee was a Scheduled Bank and the issue therein also pertained to disallowance Under Section 14A. In this case, the Bombay High Court even while remanding the case back to Tribunal for adjudicating afresh observed (relying on its own previous judgment in same Assessee's case*



*for a different Assessment Year) that, if Assessee possesses sufficient interest free funds as against investment in tax free securities then, there is a presumption that investment which has been made in tax free securities, has come out of interest free funds available with Assessee. In such situation Section 14A of the Act would not be applicable. Similar views have been expressed by other High Courts in CIT v. Suzlon Energy Ltd. MANU/GJ/0279/2013 : (2013) 354 ITR 630 (Guj), CIT v. Microlabs Ltd. MANU/KA/0526/2016 : (2016) 383 ITR 490 (Karn) and CIT v. Max India Ltd. MANU/PH/1743/2016 : (2016) 388 ITR 81 (P & H) Mr. S Ganesh the learned Senior Counsel while citing these cases from the High Courts have further pointed out that those judgments have attained finality. On reading of these judgments, we are of the considered opinion that the High Courts have correctly interpreted the scope of Section 14A of the Act in their decisions favouring the Assesseees.*

23. The learned senior standing counsel for the revenue sought to distinguish the decision by referring to the paragraph 7 of the decision wherein the Hon'ble Supreme Court noted that the expenditure incurred towards interest paid on funds borrowed such as deposits utilised for investments in securities, bonds and shares which yielded the tax free income cannot be conveniently be related to a separate account, maintained for the purpose. In fact noting this factual position in paragraphs 27 and 28 of the decision the Hon'ble Supreme Court held that the proportionate disallowance of interest is not warranted under Section 14A of the Act. It was pointed out that the said conclusion is reached because nexus has not been established between expenditure disallowed and earning of exempt income. The revenue failed to substantiate their argument that the assessee was required to maintain separate accounts and that the revenue has failed

to refer to any statutory provisions which obligate the assessee to maintain separate accounts which might justify proportionate disallowance. Thus, holding that in taxation regime there is no room for presumption and nothing can be taken to be implied. The issue was answered in favour of the assessee and against the revenue. In the case on hand, the revenue does not state that the assessee was bound to maintain separate accounts. In such circumstances, the decision will assist the case of the respondent assessee.

At this juncture, it would be of relevance to take note of the decision cited by the revenue in the case of **East India Pharmaceuticals Works Limited** wherein the Hon'ble Supreme Court held that the question whether a presumption can be drawn that the taxes were paid out of the profits of the relevant year and not out of the overdraft account for the running of the business as was drawn in **Woolcombers** case by the Calcutta High Court and was followed in three other cases of the same High Court, would essentially depend upon the fact as to whether the entire profits have been pumped into the overdraft account, whether such profits were more than the tax amount paid for the relevant year and all other germane factors. It is an argument of the revenue that in both the decision namely in **East India Pharmaceuticals Works Limited** and **C.E.S.C Limited** for the purpose of presuming that investments have been made from out of the profits, two conditions are to be satisfied that the profit of the entire business including the sale proceeds should be deposited in the mixed overdraft account and investment should be less than the amount of profits earned or which could reasonably be deemed to have been earned, regard being had to the date of

expenditure. The revenue's case before us is that the assessee has not shown that profits have been deposited in the cash credit account wherefrom borrowing/withdrawals had been done for purchasing shares.

In the preceding paragraphs, we have noted that the CIT(A) came to the conclusion that borrowed funds were utilised for the purchase of shares for the sole reason that the funds flow was from a cash credit account. The question would be whether such a presumption can be drawn without noting the facts. Admittedly there is nothing on record that borrowed funds were utilised for the purpose of investment in shares. As already pointed out, the tribunal has noted the total investment in the shares of the four companies on which long term capital gains arises is less than Rs. 50,00,000/- while the capital and reserve of the assessee as on 31.03.2004 was Rs. 31.62 crores and as on 31.03.2005, it was Rs. 5.11 crores. The net profit of the assessee was Rs. 9.01 crores for the year ended 31.03.2004 and Rs. 9.47 crores for the year ended on 31.03.2005. Therefore, the tribunal was fully justified in coming to the conclusion that not only capital and reserve of the assessee was several times more than the investment in shares in respect of which STT was paid, but even the profit of one year was several times more than the investment. Therefore, in our view, the fact situation has been clearly brought on record by the tribunal which was failed to be taken into consideration by the CIT(A). Therefore, the conclusion arrived at by the tribunal in this regard cannot be faulted. Consequently, we hold that the CIT(A) would not have drawn a presumption that merely because the fund flow was from a cash credit account, it pre-supposes that

borrowed funds were utilised for the purchase of shares especially when it is a specific case of the assessee that it is a mixed account which has not been shown to be wrong by the revenue.

24. The next issue would be as regards the correctness of the observations of the CIT(A) that the shares were thinly traded and highly illiquid and that the companies have not declared dividends. In our view, these aspects need not be gone into as the assessing officer did not doubt the genuineness of the transactions. It is only when the genuineness of the transactions is doubted, there would be an occasion to examine whether the shares were penny stocks or not, what was the percentage of appreciation, the period during which the appreciation took place and was the appreciation beyond the normal person's expectations etc. Thus, in the absence of any doubt raised either by the assessing officer or by the CIT(A) as regards the genuineness of the transactions, the CIT(A) could not have held that the transaction was in the nature of business transaction as the companies have not declared dividend. Such finding rendered by the CIT(A) in our opinion was rightly reversed by the tribunal.

25. The next aspect is with regard to the principle of consistency. It is an undisputed fact that the long-term shares were held over for earlier years and were shown as investments in the books of account. This was accepted by the department in the years in which the shares were purchased namely 2003-2004 and 2004-2005. The assessment orders were placed which shows that for those years the assessee was charged to tax in respect of long term capital gains. The CIT(A) accepted the assessee's stand that long term

shares were shown as investment and profits were shown as capital gains and consistently the department meted out the same treatment to the said investment and the case of the assessee was accepted. The CIT(A) does not dispute the facts that in the previous years, the transactions was shown as an investment and accepted by the department as an investment. But would state that different view can be taken if some fresh material comes on record and facts and circumstances justifies such a departure. Thus, the principle of consistency required to be firmly maintained has been accepted by the CIT(A) but would state that a departure can be made if there are some fresh materials. Thus, it is to be seen that any fresh materials as brought on record by the CIT(A) or even the assessing officer.

26. The learned senior standing counsel referred to the decision in the case of **Investments Limited, Shyam Burlap Company Limited** and **Sri Rakesh Kumar Gupta** for the proposition that no firm conclusion can be drawn from the method of keeping accounts and the description of a commodity under a particular head is not decisive. In our view, we need not travel thus far to find an answer to the issue before us as no case law is required to arrive at a conclusion because the facts are required to be examined before we refer to the decisions which may or may not support either of the parties. As noted above, for the assessment years 2003-2004 and 2004-2005 orders were passed by the assessing officer charging the assessee to tax in respect of long-term capital gains. The CIT(A) also accepted the assessee's stand that long term shares were shown as investment and profits were shown as capital gains consistently. Thus, when the shares were held to be investments and accepted as such for the

assessment years 2003-2004 and 2004-2005, can it be held to be not an investment when it comes to the assessment year under consideration 2005-2006. On a careful reading of the orders passed by the assessing officer as well as the CIT(A), there is nothing to indicate that there was any fresh material to come to a different conclusion. If such fresh material was available with the department, the same should have been brought on record. The observations of the CIT(A) to get over the consistent view of the department is by making an observation which at best can be treated to be a statement of law namely if there are fresh materials a departure from a consistent view is permissible. However, to apply such legal principle, facts have to be brought on record, and in the absence of facts or fresh materials the conclusion of the CIT(A) has to be termed as perverse.

27. Interestingly, the gains from the remaining long-term shares of the sixth company sold during the previous year relevant to the assessment year 2006-2007 was treated as business income by the assessing officer which order was reversed by the CIT(A) and affirmed by the tribunal by order dated 11.02.2011. The assessing officer once again for the assessment years 2007-2008 and 2008-2009 sought to treat the same as business income which was reversed by the CIT(A) and the tribunal dismissed the revenue's appeal by the orders dated 11.05.2011 and 18.08.2011 and those orders have attained finality. Therefore, for the solitary year, the year under consideration, a departure from the consistent manner in which the department viewed the transactions, cannot be disturbed. The decision in the case of **Gyan Traders Limited** would also aid and assist the case on hand wherein it was pointed out as under:

*The legal principle that is deduceable from the above decisions are that in considering whether a transaction was or was not an adventure in the nature of trade, the problem must be approached in the light of the intention of the assessee having regard to the legal requirements which were associated with the concept of trade or business. That is not possible to evolve a single legal test or formula which could be applied in determining whether a transaction was an adventure in the nature of trade or not and the answer to the question would depend in each case on the relevant factors and circumstances proved therein which will determine the character of the transaction. Further the distinction between the two types of transactions is not always easy to make.*

27. In the absence of any doubt raised by the department with regard to the purchase of shares treated as investment for the preceding years and the subsequent years, a departure cannot be made by the department for the year under consideration. The decision in **Jet Age Securities Private Limited** considered as to how the volume of transactions has to be viewed and taking note of the earlier decisions of this court, it was held as follows:

*11. In Commissioner of Income Tax Vs. Merlin Holding Private Limited MANU/WB/0417/2015 : (2015) 375 ITR 118 (Cal), the Hon'ble Division Bench of this Court held that an investor can have shares transactions with a motive of making investment as well as trading if they are separately shown in books of accounts. It was further held that the volume of transactions can only be an indicative factor but it cannot be a determinative factor in analysing any transactions. The decision in Merlin Holding Private limited was followed in Principal Commissioner of Income Tax, Central-1, Kolkata Vs. Purvanchal Leasing Limited MANU/WB/0052/2022 : (2022) 287 Taxman 20/137 taxmann.com 253 (Calcutta) wherein it was held as follows:*

*"The second submission is with regard to the volume of transaction which, according to the*

*revenue, is to be noted to ascertain the intention of the assessee. It was pointed out by the learned senior counsel for the respondent that only less than 1/3rd of the total transactions was held for a short period. That apart, the volume of transaction cannot have any impact to consider as to whether the transaction would give rise to short-term capital gain or not."*

*"..... in the case of CIT v. Merlin Holding (P.) Ltd. MANU/WB/0417/2015 : [2016] 65 taxmann.com 37/[2015] 375 ITR 118 (Cal.). In the said case the Court found that the frequency cannot alone go to show the intention was not to make an investment."*

*12. At this juncture, it will be useful to refer to the decision of the Hon'ble Supreme Court in CIT Vs. Associated Development Company Private Limited MANU/SC/0268/1971 : 82 ITR 586 (SC) wherein it was held that the issue regarding the holding of shares is by way of investment or forming part of stocks in trade is a matter within the knowledge of assessee and if produces evidence to show he had maintained the distinction between the shares which are held as stock in trade and which are by way of investment, then the intention of the assessee is a main criteria to be judged.*

28. Circular No. 4 of 2007 dated 15.06.2007 was issued with regard to the distinction between shares held as stock-in-trade and shares held as investment and the tests for such a distinction were laid down. The following paragraphs of the circular would be relevant:-

*10. CBDT also wishes to emphasise that it is possible for a tax payer to have two portfolios, i.e., an investment portfolio comprising of securities which are to be treated as capital assets and a trading portfolio comprising of stock-in-trade which are to be treated as trading assets. Where an assessee has two portfolios, the assessee may have income under both heads i.e., capital gains as well as business income.*



*11. Assessing officers are advised that the above principles should guide them in determining whether, in a given case, the shares are held by the assessee as investment (and therefore giving rise to capital gains) or as stock-in-trade (and therefore giving rise to business profits). The assessing officers are further advised that no single principle would be decisive and the total effect of all the principles should be considered to determine whether, in a given case, the shares are held by the assessee as investment or stock-in-trade.*

29. This brings us to the last issue as to the effects of the circulars issued by the CBDT dated 29.02.2016 and 02.05.2016. Circulars dated 29.02.2016 was with regard to the issues of taxability of surplus on sale of shares and securities-capital gains of business income-instruction in order to reduce the litigation. The need for issuing such a circular arose on account of a disputes on the applications of the principles laid down by the courts mentioning different parameters to distinguish the shares held as investments from the shares held as stock-in-trade. Thus, with a view to reduce the litigation the circular was issued and the following would be relevant:-

- (a) Where the assessee itself, irrespective of the period of holding the listed shares and securities, opts to treat them as stock-in-trade, the income arising from transfer of such shares/securities would be treated as its business income,*
- (b) In respect of listed shares and securities held for a period of more than 12 months immediately preceding the date of its transfer, if the assessee desires to treat the income arising from the transfer thereof as Capital Gain, the same shall not be put to dispute by the Assessing Officer. However, this stand, once taken by the assessee in a particular Assessment Year, shall remain applicable in subsequent Assessment Years also and the taxpayers shall not be allowed to*

*adopt a different/contrary stand in this regard in subsequent years.*

30. The circular dated 02.05.2016 was with regard to the consistency and taxability of income/loss arising from transfer of unlisted shares under the Act and the following instructions was issued:-

*Regarding characterisation of income from transaction in listed shares and securities, Central Board of Direct Taxes (CBDT) had issued a clarificatory Circular No. 6/2016 dated 29<sup>th</sup> February, 2016, wherein with a view to reduce litigation and maintain consistency in approach in assessments, it was instructed that income arising from transfer of listed shares and securities, which are held for more than twelve months would be taxed under the head 'Capital Gain' unless the tax-payer itself treats these as its stock-in-trade and transfer thereof as its business income. It was further stated that in other situations, the issue was to be decided on the basis of existing Circulars issued by the CBDT on this subject.*

*Similarly, for determining the tax-treatment of income arising from transfer of unlisted shares for which no formal exists for trading, a need has been felt to have a consistent view in assessments pertaining to such income. It has, accordingly been decided that the income arising from transfer of unlisted shares would be considered under the head 'Capital Gain', irrespective of period of holding, with a view to avoid disputes/litigations and to maintain uniform approach.*

*It is, however, clarified that the above would not be necessarily applied in the situations where:*

- (i) the genuineness of transactions in unlisted shares itself is questionable; or*
- (ii) the transfer of unlisted shares is related to an issue pertaining to lifting of corporate veil; or*
- (iii) the transfer of unlisted shares is made along with the control and management of underlying business.*

*And the Assessing Officer would take appropriate view in such situations.*

31. It is the argued by Mr. Roy that the circulars cannot be applied *ipso facto* when the matter has a cascading effect. We are of the view that there can be no quarrel as to such proposition. Equally well settled is that the benefit of the circular should be extended to the assessee especially when it is a beneficial circular in favour of the assessee. As noticed from the relevant paragraphs of the circular, the department has clarified that the assessee can have investment portfolio and also a trading portfolio and may have income under the head capital gains as well as business income. The circular dated 29.02.2016 clarifies that in respect of listed shares and securities held for a period of more than 12 months immediately preceding the date of its transfer if the assessee desires to treat the income arising from transfer thereof as capital gains, the same shall not be put to dispute by the assessing officer. It is further stated that once such stand is taken by the assessee in a particular assessment year, shall remain applicable in subsequent assessment years also and the taxpayers shall not be allowed to adopt a different/contrary stand in this regard in subsequent years. In the instant case, the assessee had treated the income arising from transfer thereof as capital gains consistently, accepted by the department. In terms of the circular the assessee's precluded from taking a contrary stand in the subsequent years. If that be so, the same embargo can also be placed on the department, by holding that the department cannot take a different view in the subsequent years in the absence of any fresh materials warranting such departure. Reading the circular in its entirety will show that on account of dispute which had arisen while interpreting the directions issued by the courts and tribunal the Board thought fit to issue appropriate instructions

to the field formation. Therefore, it is to be understood that the circular would be retrospective in operation. In any event, as rightly contended by the learned senior advocate for the assessee in the event the matter is remanded for fresh consideration to the assessing officer either by the CIT(A) or by the tribunal nothing prevents the assessee from referring to the circulars and the theory of prospectivity or retrospectivity loses its significance.

32. Thus, we hold that the circulars can be referred to by the assessee and they being at least partially beneficial to the assessee has to be held to be retrospectively applicable in so far as the instructions/clarifications which enure in favour of the assessee's.

33. Thus, for all the above reasons, we hold that the revenue has not made out any case for interference with the order passed by the tribunal.

34. In the result, the appeal fails and the substantial questions of law are answered against the revenue. No costs.

**(T.S. SIVAGNANAM, J.)**

**I Agree**

**(HIRANMAY BHATTACHARYYA, J.)**