

In the High Court of Judicature at Madras

Dated: 18.06.2013

Coram

The Honourable Mrs.JUSTICE CHITRA VENKATARAMAN
and
The Honourable Ms.JUSTICE K.B.K.VASUKI

Tax Case (Appeal) No.152 of 2010

Commissioner of Income Tax
Circle XIV, Chennai - 6

.... Appellant

Vs.

Vijay M.Mahtaney

.... Respondent

APPEAL under Section 260 A of the Income Tax Act against the order dated 4.9.2009 made in I.T.A.No.1017/Mds/2008 on the file of the Income Tax Appellate Tribunal 'C' Bench for the assessment year 2003-04.

For Appellant : Mr.J.Narayanaswamy
For Respondents: Mr.R.Vijayaraghavan for
M/s.Subbaraya Aiyar

J U D G M E N T

(Judgment of the Court was delivered by CHITRA VENKATARAMAN,J.)

The above Tax Case (Appeal) is filed at the instance of the Revenue against the order of the Income Tax Appellate Tribunal for the assessment year 2003-04 by raising following substantial question of law:

"Whether, on the facts and circumstances of the case, the Tribunal was right in deciding that, first, the computation of capital gain has to be given effect to and then only apply the provisions of Section 70 of the Income Tax Act?"

2. It is seen from the facts narrated that the assessee herein made a long term capital gain to the tune of Rs.6,42,22,435/- on the sale of shares. Admittedly, the assessee had invested the long

term capital gains in REC Bonds to the tune of Rs.6,50,00,000/-. Apart from this, there were long term capital loss on sale of shares and immovable properties which were claimed to be carried forward to the subsequent years. The Assessing Officer apparently agreed with the assessee on this state of affairs. However, in exercise of jurisdiction under Section 263 of the Income Tax Act, 1961, the Commissioner of Income Tax (Appeals) viewed that as per Section 74(1) of the Income Tax Act, the loss relating to the long term capital asset shall be first set off against income, if any, under the head "Capital gains" assessable for that assessment year in respect of any other capital asset not being a short term capital asset and then only the exemption under Section 54 EC would apply. He thus held that the assessment completed under Section 143(3) of the Income Tax Act is thus erroneous and prejudicial to the interest of the Revenue requiring revision of assessment. While summarily rejecting the assessee's reply based on Section 54 EC, the Commissioner of Income Tax (Appeals) directed the Assessing Officer to redo the assessment.

3. Aggrieved by the same, the assessee went on appeal before the Income Tax Appellate Tribunal. The Tribunal pointed out that even though Section 45(1) does not specify Section 54EC as had been done by erstwhile Sections 54, 54A, 54B, 54EA, 54EB and 54F, yet, going by the import of Section 54EC(1)(a) and (b), the assessee was entitled to take advantage of the said provisions even before working out Section 70. Pointing out to the scheme of Sections 45 to 55A which provide for the computation of capital gains, the Tribunal held that effect has to be given first to the provision of capital gains as given under the above scheme and then apply the provisions of Section 70. It viewed that Section 70 would come into play only when the capital gains have been computed in accordance with the provisions contained in Sections 45 to 55A. Irrespective of whether Section 54EC(1) is found in Section 45 or not, in terms of Section 54EC, the effect of it cannot be ignored, as the investment in REC bonds takes the capital gains out of the charging provision. Since the amount invested in REC bonds does not enter into the computation at all, the revision done was not sustainable in law. Consequently, the Tribunal set aside the order of the Commissioner of Income Tax (Appeals). Aggrieved by this, present appeal has been filed by the Revenue.

4. Before going into the contentions raised herein, the relevant provisions of Sections 45(1), 54EC and 70 of the Income Tax Act, relevant to the assessment years, have to be noted, which read as follows:-

Capital gains.

Section 45(1) Any profits or gains arising from the transfer of a capital asset effected in the previous year shall, save as otherwise provided in sections 54, 54B, 54D, 54E, 54 EA, 54 EB, 54F, 54G and 54H, be chargeable to income tax under the head "capital gains", and shall be deemed to be the income of the previous year in which the transfer took place.

Capital gain not to be charged on investment in certain bonds.

Section 54 EC (1) Where the capital gain arises from the transfer of a long term capital asset (the capital asset so transferred being hereafter in this section referred to as the original asset) and the assessee has, at any time within a period of six months after the date of such transfer, invested the whole or any part of the capital gains in the long term specified asset, the capital gain shall be dealt with in accordance with the following provisions of this Section, that is to say-

(a) if the cost of the long term specified asset is not less than the capital gain arising from the transfer of the original asset, the whole of such capital gain shall not be charged under Section 45.

(b) if the cost of the long term specified asset is less than the capital gain arising from the transfer of the original asset, so much of the capital gain as bears to the whole of the capital gain the same proportion as the cost of acquisition of the long term specified asset bears to the whole of the capital gain, shall not be charged under Section 45.

Set off, or carry forward and set off.

Set off of loss from one source against income from another source under the same head of income.

Section 70. (1) Save as otherwise provided in this Act, where the net result for any assessment year in respect of any source falling under any head of income, other than "Capital gains", is a loss, the assessee shall be entitled to have the amount of such loss set off against his income from any other source under the same head.

(2) Where the result of the computation made for any assessment year under Sections 48 to 55 in respect of any short term capital asset is a loss, the assessee shall be entitled to have the amount of such loss set off against the income, if any, as arrived at under a similar computation made for the assessment year in respect of any other capital asset.

(3) Where the result of the computation made for any assessment year under sections 48 to 55 in respect of any capital asset (other than a short term capital asset) is a loss, the assessee shall be entitled to have the amount of such loss set off against the income, if any, as arrived at under a similar computation made for the assessment year in respect of any other capital asset not being a short term capital asset.

5. Thus consequent on insertion of Section 54 EC, sunset clauses were inserted under the Finance Act, 2000 dated 1.4.2001 in Section 54 EA and Section 54 EB to cover cases of transfer of long term capital asset made before 01.04.2000. Explaining the introduction of the said provisions, the Board, by its Circular in Circular No.794 dated 9th August, 2000, in paragraph 30, stated as follows:-

30. Sunset Clauses to Sections 54EA and 54EB and introduction of a new Section 54EC to ensure focussed investment of capital gains in agricultural finance and highway infrastructure.

30.1 Under the existing provisions, sections 54EA and 54EB of the Income Tax Act offer a basket of investment options to absorb taxable capital gains arising from transfer of long term capital assets. The notified instruments providing the roll-over to capital gains include shares, bonds, units and deposits of banks and various other instruments. The two sections were introduced in 1996 to give an incentive to the development of infrastructure. However, the objective has been diluted in the presence of a large number of varied and diverse instruments. Further, incentives to infrastructure are also available under other sections of the Income Tax Act such as sections 80-IA, 80-IB and 10(23G). In a regime of low tax rate on long term capital gains, there is very little justification for having such an omnibus basket of exemptions. Therefore, it has been decided to insert sun-set clauses to sections 54EA and 54EB limiting their application to transfers of long term capital asset made on or before 31st March 2000. Where the capital gain has arisen on transfers made before 31st March, 2000, the investments in notified securities can be made under Sections 54EA and 54EB beyond that date but within the stipulated period.

30.2. In place of sections 54EA and 54EB, which are being terminated, a new section namely, 54EC, has been inserted for transfer of capital assets made on or after 1st April, 2000. The new section will allow exemption from tax on long term capital gains, if invested in bonds, targeted exclusively on

agricultural finance and highway infrastructure. The instruments in question shall be bonds, redeemable after three years, to be issued by the National Bank for Agriculture and Rural Development (NABARD) and the National Highway Authority of India (NHAI). The exemption from long term capital gains shall be to the extent of investment in these bonds.

30.3. These bonds will have a lock in period of three years. Any transfer or conversion of bonds into money during the lock-in period will make the amount so converted as deemed capital gains taxable in the year of transfer or conversion. Such deemed capital gain will also arise, if any loan or advance is taken on the security of these bonds. Further, any amount invested in these bonds will not be eligible for deduction under Section 88 of the Income Tax Act.

30.4 These amendments will take effect from 1st day of April, 2001 and will accordingly apply to the assessment year 2001-2002 and subsequent years.

6. Thus, going by the circular issued and the insertion of Section 54EC is only a substitute in the place of Section 54EA and Section 54EB to cover cases of transfer of long term capital asset on and from 01.04.2001, we do not find that the argument of the Revenue by reason of Section 45, not excluding the operation of Section 54EC, the other provisions under Section 54EC would stand at different footing from that of similarly worded other provisions under the said Chapter. It may further be seen that as per Section 54EC(1)(a) on the capital gains arising from the transfer of long term capital asset invested in accordance with the said Section, capital gains shall not be charged under Section 45.

7. Secondly, one may also note that Section 54EC does not specifically mention about specified nature of transfer or of any specified long term capital asset. On the other hand, it merely speaks about the "capital gain arising out of a long term capital asset".

8. Contrast this with Section 54 which deals with capital gains arising on sale of property used for residence. Section 54 specifically provides that in the case of capital gains arising from the transfer of long term capital asset, being a residential house, exemption would be available if the assessee has purchased within a period of one year before or two years after the date on which the transfer took place, a residential house or within a period of three years after that date, constructed the residential house. Section 54(2) provides that the amount of capital gains not appropriated by the assessee towards the purchase of the new asset or purchase and construction of the new asset before the date specified in Section 54(1), shall be deposited in the specified Bank or institution and utilised in accordance with any scheme which the Central Government may notify. Section 54B deals with capital gain on transfer of land used for agricultural purposes not to be charged. Section 54D deals with Capital gain on compulsory acquisition of lands and buildings not to be charged. Section 54E deals with capital gain on transfer of capital assets not to be charged. Section 54EA deals with Capital gain on transfer of long-term capital assets not to be charged in the case of investment in specified bonds or debentures and Section 54EB deals with capital gain on transfer of long-term capital assets not to be charged.

9. A reading of Section 54EC shows that it replaced Sections 54EA and 54EB by the Finance Act, 2000 with effect from 01.04.2001, with the result that the benefit of Section 54EA and 54EB ceased to be available with reference to transfer of long term capital assets before 01.04.2000. Thus relief of transfer under Section 54EC is available in respect of transfers from the accounting year relevant to

the assessment year 2001-02 to preserve the continuity of the benefit of deduction with the only difference that Section 54EC limits the available bonds for purposes of reinvestment benefit with the minimum lock in the period of three years. The bonds available for benefit under Section 54E are part of the statute itself. Thus Section 54EA and 54EB would have relevance to the transfer of long term capital before 01.04.2000 and Section 54EC, to the transfer made on or after 01.04.2001.

10. Thus, if, for working out the relief under Section 54, the Revenue does not insist upon the applicability of Section 70(3), we do not find any acceptable reason as to how Section 70(3) would stand attracted in the case of Section 54EC. Thus, we reject the argument of the Revenue that for the purpose of working out the relief under Section 54 EC, one has to take recourse first to Section 70(3) and then only look at Section 54 EC. A reading of Section 70(3) shows that the loss that has to be looked at first is not with reference to the loss arising in respect of any new capital asset, but in the totality of the loss suffered on the sale of capital asset chargeable to tax under Section 45. On the other hand, Section 54EC is specific with reference to investment in specified bonds as regards the capital gain arising from and out of a long term capital asset. Thus going by the scheme of the Act and the Board circular, we accept the plea of the assessee that for taking benefit under Section 54E, it is not necessary that one should first apply Section 70(3) and thereafter only, the assessee could invest the capital gain arising from the long term capital asset to any specified bond as specified under Section 54EC.

11. In the light of the above, we find no error in the order of the Tribunal in setting aside the order of the revision made by the Commissioner of Income Tax (Appeals). In the circumstances, we reject the appeal, thereby, confirm the order of the Tribunal. The above Tax Case (Appeal) is dismissed. No costs.

Index : Yes/No
Internet : Yes/No

(C.V.,J) (K.B.K.V,J)
18.06.2013

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To

Commissioner of Income Tax
Circle XIV, Chennai.
CHITRA VENKATARAMAN,J.
AND
K.B.K.VASUKI,J.

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T.C.(A) No.152 of 2010

Dated: 18.06.2013