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IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO. 2886 OF 2009

The Commissioner of Income Tax - 3 **...Appellant**

Versus

M/s. Darshan Securities Pvt. Ltd. **...Respondent**

Mr. Suresh Kumar for Appellant.

Mr. Jehangir D. Mistri, Sr. Adv with Mr. P.C.Tripathi and Mr. Raj
Darak for Respondent.

**CORAM: DR. D.Y. CHANDRACHUD &
M.S. SANKLECHA, JJ.**

DATE : 02 FEBRUARY 2012.

ORAL JUDGMENT (PER DR.D.Y.CHANDRACHUD,J.)

1. In this Appeal by the Revenue, there was a delay of 366 days. By the order of a Division Bench dated 10 December 2007, the Motion taken out by the Revenue for condoning the delay, was dismissed. The Revenue carried the matter in Appeal before the Supreme Court. By a Judgment dated 30 November 2009, the Supreme Court allowed the Civil Appeal, which arose

out of the Judgment of the Division Bench in the Motion for condonation in the following terms.

“ In our view, this a fit case for the High Court to decide the matter on the question of law which basically also requires interpretation of Explanation to Section 73 of the Income Tax Act, 1961. The High Court has dismissed the appeal filed by the Department only on the ground of delay. No doubt, there was a delay. However, looking to the importance of the question of law involved in this matter and looking to the stakes involved, we are of the view that the High Court should consider the matter for admission and thereafter decide the matter on merits in accordance with law.

The Civil appeal stands, accordingly allowed.”

2. The appeal by the Revenue raises the following substantial question of law:

“Whether on the facts and in the circumstances of the case and in law the ITAT was justified in holding that the case of the respondent is not covered by explanation to section 73 as it falls within the first limb of exception to the explanation and therefore the assessee’s loss should not be treated as speculative loss?”

The appeal is admitted and is by consent taken up for hearing and final disposal.

3. The Appeal relates to Assessment Year 1996-97. An order of Assessment was passed under Section 143 (3) of the

Income Tax Act, 1961 on 30 December 1998 by which *inter alia* the Assessing Officer disallowed a share trading loss, which was held to be a speculation loss, in the amount of Rs.02,23,32,127/-. The Assessee preferred an Appeal, which was allowed by the Commissioner (Appeals) on 14 January 2000. The Tribunal in an Appeal by the Revenue confirmed the decision of the Commissioner following its earlier Judgment in Assistant Commissioner of Income Tax, Special Circle 18(1) V/s Concord Commercials Pvt. Ltd.¹

4. In order to appreciate the issue, which arises in the Appeal, a reference briefly to the relevant facts would be in order. During the assessment year, the assessee returned an Income of Rs.2,25,04,588 from service charges. The assessee had a loss of Rs.02,23,32,127 in share trading. The assessee had a dividend income of Rs.4,79,325/-. The assessee claimed that in computing the gross total income for the purpose of the explanation to Section 73, the income from service charges had to be adjusted against the loss in share trading. This contention of the assessee has found acceptance by the Commissioner (Appeals) and the

¹ (ITA No.5220/MUM/1994) decided on 28 January 2005.

Tribunal. The provision of the explanation to Section 73 falls for determination in the Appeal.

5. Under Section 28, income which is chargeable to income tax under the head of profits and gains of business or profession includes the profits and gains of any business or profession, which was carried on by the assessee at any time during the previous year. Explanation (2) to Section 28 provides that where speculative transactions carried on by an assessee are of such a nature as to constitute a business, the business shall be deemed to be distinct and separate from any other business. Section 43 which contains a statutory dictionary of definitions of certain terms relevant to income from profits and gains of business or profession defines the expression “speculative transaction” in sub section (5). That expression is defined to mean a transaction in which a contract for the purchase or sale of any commodity, including stocks and shares, is periodically or ultimately settled, otherwise than by the actual delivery or transfer of the commodity or scrips. Consequently, where a contract for purchase or sale of shares is settled by actual delivery, it does not fall within the definition of the expression. Section

70(1) provides for a setting off of loss from one source against income from another source under the same head. Section 72 makes provision for carry forward and set off of business losses, under the head of profits and gains of business or profession other than a loss sustained in a speculation business. Sub Section (1) of Section 73 provides that any loss, computed in respect of a speculation business carried on by the assessee, shall not be set off except against profits and gains, if any, of another speculation business. As a result of the provision of Sub Section (1) of Section 73, a bar is introduced against the setting off of a loss which has arisen in respect of speculation business carried on by the assessee save and accept against the profits and gains of another speculation business. The explanation to Section 73 provides as follows :

“ Where any part of the business of a company ([other than a company whose gross total income consists mainly of income which is chargeable under the heads “Interest on securities”, “Income from house property”, “Capital gains” and “Income from other sources”], or a company principal business of which is the business of banking or the granting of loans and advances) consists in the purchase and sale of shares of other companies, such company shall, for the purpose of this section, be deemed to be carrying on a speculation business to the extent to which the business consists of the purchase and sale of such shares.”

6. The explanation to Section 73 introduces a deeming fiction. The deeming fiction stipulates that where any part of the business of a company consists in the purchase and sale of shares of other companies, such company shall, for the purposes of the section be deemed to be carrying on a speculation business to the extent to which the business consists of the purchase and sales of such shares. The deeming fiction applies only to a company and the provision makes it clear that the deeming fixation extends only for the purposes of the section. The bracketed portion of the explanation, however carves out an exception. The exception is that the provision of the explanation shall not apply to a company whose gross total income consists mainly of income which is chargeable under the heads “Interest on securities”, “Income from house property”, “Capital gains” and “Income from other sources” or a company whose principal business is of banking or the granting of loans and advances.

7. The submission which has been urged on behalf of the Revenue is that in computing the gross total income for the purpose of the explanation to Section 73, income under the heads of profits and gains of business or profession must be ignored.

Alternatively, it has been urged that where the income from business includes a loss in the trading of shares, such a loss should not be allowed to be set off against the income from any other source under the head of profits and gains of business or profession.

8. In our view, the submission which has been urged on behalf of the Revenue cannot be accepted. Leaving aside for a moment, the exception, which is carved out by the explanation to Section 73, the explanation creates a deeming fiction by which a company is deemed to be carrying on a speculation business where any part of its business consists in the purchase and sale of shares of other companies. Now, the exception which is carved out applies to a situation where the gross total income of a company consists mainly of income which is chargeable under the heads "Interest on securities", "Income from house property", "Capital gains" and "Income from other sources". Now, ordinarily income which arises from one source which falls under the head of profits and gains of business or profession can be set off against the loss which arises from another source under the same head. Sub Section (1) of Section 73 however sets up a bar to the

setting off of a loss which arises in respect of speculation business against the profits and gains of any other business. Consequently, a loss which has arisen on account of speculation business can be set off only against the profits and gains of another speculation business. However, for Sub Section (1) of Section 73 to apply the loss must arise in relation to a speculation business. The explanation provides a deeming definition of when a company is deemed to be carrying on a speculation business. If, the submission of the Revenue is accepted, it would lead to an incongruous situation, where in determining as to whether a company is carrying on a speculation business within the meaning of the explanation, sub section (1) of Section 73 is applied in the first instance. This would in our view not be permissible as a matter of statutory interpretation, because the explanation is designed to define a situation where a company is deemed to carry on speculation business. It is only thereafter that sub section (1) of section 73 can apply. Applying the provisions of Section 73(1) to determine whether a company is carrying on speculation business would reverse the order of application. That would be impermissible, nor, is it contemplated by Parliament. For, the ambit of Sub Section (1) of Section 73 is only to prohibit

the setting off of a loss which has resulted from a speculation business, save and accept against the profits and gains of another speculation business. In order to determine whether the exception that is carved out by the explanation applies, the legislature has first mandated a computation of the gross total income of the Company. The words “consists mainly” are indicative of the fact that the legislature had in its contemplation that the gross total income consists predominantly of income from the four heads that are referred to therein. Obviously, in computing the gross total income the normal provisions of the Act must be applied and it is only thereafter, that it has to be determined as to whether the gross total income so computed consists mainly of income which is chargeable under the heads referred to in the explanation.

9. Consequently, in the present case the gross total income of the assessee was required to be computed *inter alia* by computing the income under the head of profits and gains of business or profession as well. Both the income from service charges in the amount of Rs.2.25 crores and the loss in share trading of Rs.2.23 crores, would have to be taken into account in

computing the income under that head, both being sources under the same head. The assessee had a dividend income of Rs.4.7 lacs (income from other sources). The Tribunal was justified, in coming to the conclusion that the assessee fell within the purview of the exception carved out in the explanation to Section 73 and that consequently the assessee would not be deemed to be carrying on a speculation business for the purpose of Sec. 73(1).

10. The view, which we have taken, also accords with the judgments of this Court in C.I.T. V/s. M/s. Hero Textiles and Trading Ltd. (Income Tax Appeal No. 296 of 2001 decided on 29 January, 2008) and in C.I.T. V/s. Maansi Trading Pvt. Ltd. (Income Tax Appeal No.47 of 2001, decided on 29 January, 2008). The Tribunal has relied upon its earlier decision in the case of Concord Commercial Pvt. Ltd. of 18 March 2008. A Division Bench of this Court had dismissed Notice of Motion no. 1921 of 2007 in Income Tax Appeal (Lodging) No.852 of 2007 for condonation of delay against the decision of Concord Commercial Pvt. Ltd. holding that even otherwise on merits, the issue was covered by the decision rendered by the Division Bench in Hero Textiles and Trading Ltd.

11. For the aforesaid reasons, we answer the question of law in the affirmative. The Appeal is accordingly disposed of. There shall be no orders as to costs.

(DR. D.Y. CHANDRACHUD, J)

(M.S. SANKLECHA, J)