

Profit from sale of shares from investment portfolio taxable as “Capital Gains” and not as “Business Income”

The Hon’ble ITAT, Ahmedabad in *Swatiben Anilbhai Shah v. DCIT [Income Tax Appeal Nos. 1513, 1514 and 1515/Ahd/2019 decided on January 29, 2021]* held that where assessee purchased shares and recorded them in investment portfolio and it was justified that the intention of the assessee was to purchase the shares as capital asset, then income arising out of such shares was to be taxed as ‘short term capital gain’ (“**STCG**”) under the head 'Capital Gains' and not as business income under the head 'Profit and Gains from Business or Profession' (“**PGBP**”).

Facts:-

A return of income was filed by Swatiben Anilbhai Shah (“**the Appellant**”) on November 7, 2007 declaring a total income of Rs. 1,41,20,990/-. Search and seizure was conducted on February 02, 2008 under Section 132 of the Income Tax Act, 1961 (“**the IT Act**”) and a notice dated August 01, 2008 was issued under Section 153A of the IT Act.

In response to the above notice dated August 01, 2008 the Appellant filed another return of income under Section 153A of the IT Act declaring total income at Rs. 1,58,02,820/- which was revised to Rs. 1,54,88,670/- thereafter. As per the returns filed under Section 153A of the IT Act, the Appellant inter alia declared income under the head 'Capital Gains' as STCG of Rs. 1,40,01,808/-

An order dated May 05, 2009 was passed under Section 153A read with Section 143(3) of the IT Act wherein STCG of Rs. 1,40,01,808/- was treated as 'business income' by the Assessing Officer (“**AO**”) as against the claim of the Appellant to be assessed as STCG.

The matter travelled up to the Hon’ble ITAT, Ahmedabad but they set aside the issue regarding the nature and character of gains arising to the Appellant amounting to ₹ 1,40,01,808/- for re-examination through an order dated May 19, 2016.

The AO, once again called for the details of borrowed funds and details of transactions of purchase and sales of shares of Pyramid Siamira Theater Ltd. (“**PSTL**”) wherefrom the capital gain was mainly derived and passed the order concluding that in the absence of utilization of own funds for purchase of shares and in the absence of separate de-mat account maintained for purchase and sale of shares in investment account vis-a-vis trading account, the gains arising on sale of shares are required to be treated as 'business income'.

Aggrieved by the Impugned order, the Appellant preferred an appeal before the CIT(Appeals) but the appeal was rejected.

Flat no. 34B, Ground Floor, Pocket -1, Mayur Vihar, Phase -I, Delhi - 110091

Email: bimaljain@a2ztaxcorp.com; Web: www.a2ztaxcorp.com; Tel: +91 11 4242 7056

Further aggrieved, the Appellant preferred an appeal before the Hon'ble ITAT, Ahmedabad.

Issue:-

Whether the gains arising on sale of shares be treated as STCG and taxed under the head 'Capital Gains' or Business Income and taxed under the head 'PGBP'?

Held:-

The Hon'ble ITAT, Ahmedabad in ***Income Tax Appeal Nos. 1513, 1514 and 1515/Ahd/2019 decided on January 29, 2021*** has held as under:

- Found that, the gains in question have arisen on sale of shares of one company only by the Appellant i.e. PSTL. The Appellant has purchased 215802 shares and sold 167000 shares during the year. The total number of transactions of purchase is barely 5 and that of corresponding sale is only 7.
- Noted that, the Appellant has maintained capital and trading transactions as a separate category in books of account.
- Observed that, the order of the AO is cryptic without any proper verification of books of accounts. The AO merely deemed the borrowed funds to have been utilized for investment purposes.
- Further observed that, it was upon the Appellant to demonstrate that his intention for earning investment income and share trading income are well differentiated.
- Said that, the law has considerably evolved on the point and continuing. The Courts have laid down several tests for ascertaining the nature of transaction. The Central Board of Direct Taxes ("**CBDT**") itself has also laid down parameters by way of ***Circular No.4/2007 dated June 15, 2007***.
- Held that the cumulative effect of all factors need to be weighed and a mere involvement of borrowed funds in some instances would not *per se* denude the transactions of its character of capital assets. The issue is essentially factual and depends of peculiar facts of each case.
- In the absence of any straight jacket formula, the lack of regularity and isolated instances of capital transactions would vindicate the stand of the Appellant that

Flat no. 34B, Ground Floor, Pocket -1, Mayur Vihar, Phase -I, Delhi - 110091

Email: bimaljain@a2ztaxcorp.com; Web: www.a2ztaxcorp.com; Tel: +91 11 4242 7056

income/loss from 7 transactions have been rightly regarded as capital gains. As stated above, the Appellant has taken delivery of shares before sale. While maintenance of capital and trading transactions as a separate category in books can be insisted upon in practice to ascertain the underlying intentions, the maintenance of separate D-mat account separately is not necessarily in conformity with usage of share trade and thus cannot be insisted upon.

- Held that the income arising out of these shares will be taxed as STCG under the head 'Capital Gains' and not as business income under the head 'PGBP'.

Our Comments:-

The CBDT had issued an Office Memorandum dated December 13, 2005 to clarify the basis of difference between shares held as stock in trade and shares held as investments. Circumstances that need to be considered by the AO in determining whether a person is a trader or an investor in stocks are as follows:

- 1) Whether the purchase and sale of securities was allied to his usual trade or business/was incidental to it or was an occasional independent activity.
- 2) Whether, the purchase is made solely with the intention of resale at a profit or for long-term appreciation and/or for earning dividends and interest.
- 3) Whether scale of activity is substantial.

Online GST Course by Bimal Jain

Recorded: Certified Advanced GST Course

Course Details: Certificate of Participation will be Provided, Free GST Updates on E-mail, WhatsApp, Telegram for 1 Year, Background Material and PPT will be Provided on the downloadable basis, Total 21 Recorded Sessions (60 Hours), will be available for 120 hours or 60 Days whichever expires earlier.

For Registration:- <https://cutt.ly/hxjI5Cu>

Recorded: GST Course on Exports, Deemed Exports, SEZ, Imports, Merchandise Exports, Inverted Duty Structure (including Refunds)

Course Details: 6 Online Recorded Sessions of 2.30Hrs each with Background Material (BGM)

For Registration:- <https://cutt.ly/pvw7mzl>

For more details, Call: +91-8076563802, **E-mail:** intern@a2ztaxcorp.com, **Web:** www.a2ztaxcorp.in

DISCLAIMER: The views expressed are strictly of the author and A2Z Taxcorp LLP. The contents of this article are solely for informational purpose. It does not constitute professional advice or recommendation of firm. Neither the author nor firm and its affiliates accepts any liabilities for any loss or damage of any kind arising out of any information in this article nor for any actions taken in reliance thereon.