



Past litigations

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Past litigations...

✦ Section 88E

- Whether apportionment of expenses to be done to find income from taxable securities transactions
- Whether rebate allowed on tax under MAT
- Whether rebate allowed on speculation loss, which do not form part of income for the year

✦ Rule 8D – whether retrospective

✦ Dividend stripping – whether colorful devise

Past litigations(2)

✦ S.43(5)(d) – whether retrospective

- Mumbai ITAT *in DCIT v. SSKI Investors Services Pvt. Ltd.*, (2008) 113 TTJ (Mumbai) 511
 - Held not speculative
 - Nirmal Trading Co 82 ITR 382 (Kolkata)
 - Compound Financials 67 ITD 304 (Bangalore)
 - ANZ Grindlays Bank 88 ITD 53 (Del)
- Kolkata ITAT in *Shree Capital Services Ltd. v. ACIT* – held prospective
 - Held speculative prior to 25.01.2006



•Securities— Other issues

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A typical financial company a/c..

Issues involved - legal

- Speculation vs. non- speculation
- Valuation
 - Stock
 - Derivatives /M2M
- Can a broker/finance company have investments and stock in trade side by side – Is it at his sweet whim
- Conversion
 - Stock in trade into investments and vice-versa
- Cost of purchase -Right shares, bonus shares

A typical financial company a/c..


✦ Issues involved – legal (2)

- Expenses apportionment
 - Exempt income
 - Capital Gains or speculation
- Deemed income u/s 56 – Acquisition of unquoted shares below book value
- Deemed dividend u/s 2(22)(e) – Loan received from group co or shareholder
- Dividend stripping u/s 94(7)
- Bonus stripping u/s 94(8)

Securities transactions....

✦ Investigation Issues

- Creating Exempt LTCG on listed securities (Penny stocks)
 - Creating loss
 - Penny Stocks (listed)
 - Unquoted shares
 - Derivative transactions
 - Creating profits
 - Commodities exchange transactions



Capital Gains Vs. Business

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Adventure or CG

✱ Business as per s.2(13) includes 'adventure in the nature of trade'

✱ Business vs. Capital Gains

- No well- defined demarcation between investment activity and business activity
- Even a single transaction could be a business transaction
- Intention vital

Adventure or CG? – Case study 1

Investment Ltd vs. CIT[77 ITR 533(SC)]

- Assessee co. claimed loss suffered in the sale of securities as a business loss, disallowed by ITO on the ground that in the Balance Sheet, it was shown as investments
- SC allowed as business loss- Held description in the Balance Sheet not relevant.
- Tests:
 - Memorandum of Association
 - Past transactions – large magnitude of tr. Trans
 - Shares held in stock in trade as in the past.

Adventure or CG? – Case study 2

• CIT vs. Sulej Cotton Mills Supply Agency Ltd [100 ITR 706(SC)]

- Co. subscribed for 349000 shares of a group co., viz. Gwalior Rayon in the year ending 31.12.1951
- In year ending 31.03.56, sold part of it at a profit.
- SC held it to be ‘adventure.....’
- Tests:
 - In the past, similar transactions were treated as business
 - Resolution authorised one of the director to deal in share
 - No dividend was declared by Gwalior
 - Money was borrowed for purchase of shares

Adventure or CG? – Case study 3

✦ Dalhousie Investment Trust Co. Ltd v. CIT [68 ITR 486(SC)]

- Assessee purchased and sold **large** quantity of shares of one company only
- Motive of earning profits
- **Held**
 - Adventure in the nature of trade

Adventure or CG? – Case study 4

✦ Neerja Birla Vs. ACIT[62 ITD 39(Mum)]

- Purchased and sold shares of Indo-gulf fertilizers Ltd
- Claimed long term capital gains

✦ Held:

- ‘adventure in the nature of trade’
 - Only one shares – large quantity
 - Loan taken to purchase the shares

Adventure or CG? – Court observes

- In **Raja Bahadur Kamakhya Narain Singh [77 ITR 253]**, SC held ‘the distinction between the two types of transactions is not always easy to make’
- In **Venkataswami Naidu & Co. Vs. CIT [35 ITR 594]**, SC held that a single plunge in waters of trade may partake of character of an adventure in nature of trade.
- In **CIT vs. Central Kurkhend Coal Co. Ltd [113 ITR 483(SC)]**, a solitary transaction was held to be adventure in the nature of trade.

Adventure or CG? - Tests

✿ CIT vs. Holck Larsen [160 ITR 67(SC)]

- The subject matter of the realization
 - Commodities, regular yield or personal enjoyment
- The length of the period of ownership
- Frequency of similar transactions by same person
- Supplementary work on or in connection with property realized
- Circumstances that were resp. for realization
 - Emergency, utilization of funds, etc
- Motive
 - Transaction of purchase and sale clearly discernible

Adventure or CG? - Tests

Associated Industrial Development Case 82 ITR 586 (SC)

- Stock and Investment
- Domain of the assessee
- Distinction by the assessee
- Evidence – failure by assessee
- ITAT – final fact finding authority

Business or CG – CBDT Circular.

✱ Instruction no. 1827 dated 31st August 1989

✱ Draft Instruction dated 16th May 2006

✱ Circular no 4/2007 dated 15th June 2007

✱ Held

- Stock in trade or capital asset
- Treatment in books
- Volume
- Ratio of purchase to sale
- Motive – profit or dividend
- MOA/AOA not conclusive
- Cumulative Tests
- Relevance of decisions

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● Adventure or CG? – Recent judgments

✦ Held investments

– DCIT v. Bharat Kunverji Kenia ITA No. 929/Mum./2010
[BCAJ]

- Assessee's favour because
 - The shares held were all along treated as an investment;
 - The assessee had not borrowed funds for making investments;
 - Shares once sold were not purchased again;
 - Average holding period of the shares sold was of 181 days.

Adventure or CG? – recent judgments

Held Business

– Deepaben A. Shah 99 ITD 219 (Ahd)

- Assessee engaged in the business of applying in IPO out of own funds, regularly and continuously and selling on allotments
- Held business income by looking at Volume, frequency, continuity and regularity



• **Preponderance
of probability**

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● Principle of 'Preponderance of probabilities'

- Mere furnishing of the particulars is not enough and mere payment by a/c payee cheque is not sacrosanct nor can it make a non-genuine transaction a genuine one.
 - *Precision Finance Pvt. Ltd [208 ITR 465(Cal)]*
- Science has not invented any instrument to test the reliability of the evidence placed before a court of Tribunal. Therefore, the courts and tribunals have to judge the evidence before them by applying the test of human probabilities.
 - *Sumati Dayal V. CIT [214 ITR 801 (SC)]*
 - *CIT V. Durga Prasad More [82 ITR 540(SC)]*