Controversies

CA. Kaushik D. Shah
dshahco@gmail.com.

Issue

When there are number of transactions of purchase and sale of shares, whether profit or loss should be treated as Business Income or Capital Gain?

Proposition

The magnitude and frequencies and the ratio of sales to purchase is not decisive as to whether a particular holding of shares is by way of investment or it is adventure in the nature of trade. If the intention is to obtain a capital asset, the purchases and subsequent sales of shares to realize higher gain cannot be regarded as trading operations and the surplus has to be taxed as capital gains.

It is important to note that intention at the time of purchase is very relevant to decide whether surplus is required to be taxed as capital gain or as business income. However, if the intention is to hold the shares as investment and not as stock-in-trade and assesse also show such surplus in the return of income as capital gain then it has to be taxed as capital gain.

View against the Proposition

The surplus realized on the sale of shares would be capital, if the assessee is an ordinary investor realizing his holding; but it would be revenue, if he deals with them as an adventure in the nature of trade. The fact that the original purchase was made with the intention to resell at an enhanced price could be obtained by itself is not enough, but in conjunction with the conduct of the assessee and other circumstances it may invest his character of the transaction. For eg. , an assessee may invest his capital in shares with the intention to resell them, if in future their sale may bring in higher price. Such an investment, though motivated by a possibility of enhanced value, does not render the investment a transaction in the nature of trade. The test often applied is whether the assessee has made his shares and securities the stock-in-trade of business – *Raja Bahadur Kamkakhya Narain Singh v.*CIT (1970)77 ITR 253(SC).

View in favour of the Proposition

In order to determine whether one is a dealer in shares or an investor, the real question is not whether the transaction of buying and selling the shares lacks the element of trading but whether the later stage of the whole operations shows that the first step – purchase of shares – is not taken as, or in course of, a trading transaction. The fact that purchase of shares was motivated by a possibility of enhanced value, will not necessarily render the investment, a transaction in the nature of trade – CIT v. H. Holck Larsen (1986) 160 ITR 67 (SC).

Element of carrying on of business must be present. When an owner of an ordinary investment chooses to realize it and obtains a higher price for it than when he originally acquired it, the enhanced price is not a profit assessable to income-tax, but an act done in what is truly the carrying on of a business, the amount recovered as appreciation will be assessable – Raja Bahadur Visheshwar Singh v. CIT (1961) 41 ITR 685 (SC).

Thus, it is very clear that the frequency of transactions is not a relevant factor to decide whether the transactions are on capital account or are on trading account? There has to be a systematic business activity and also the intention to carry on

the business and also financing of such transactions, which will decide whether the result of the transaction should be taxed as business income or capital gain.

Summation

Let me refer to circular of CBDT dated 29th February 2016 , it has been clarified that 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 the transfer of such shares/securities would be treated as its business income.

When shares are disclosed in the balance sheet as investment and surplus is declared as capital gain then this circular squarely applies and such surplus has to be taxed as capital gain.

Let me now refer to the decision of honorable ITAT reported in ABCAUS Case Law Citation: 937 2016(06) ITAT. The honorable ITAT held as under "It is undisputed fact that the assessee had disclosed these transactions as investment in the return during the year under consideration. It is also a fact that the assessee was in investment in shares from 2000-01 to till date and in all the years, he has disclosed short term/ long term capital gain on account of investment in shares which has been accepted by the department. The Id Assessing Officer as well as Id CIT (A) has considered the various decisions on which they came to conclusion that these transactions are business transactions but latest circular issued by the CBDT No. 6/2016 dated 29/2/2016 and F.No. 225/12/2016/ITA.II dated 02/5/2016 has set guidelines to assess the share trading income from other sources. The share trading is not a main business of the assessee but he made investment in part time individually with his own fund without any assistance of the man power or office, which itself shows that the intention of the assessee was to invest in shares to gain in the return. After considering both sides, we have considered view that the assessee was in investment of shares not share trading.

Now let me refer to the decision ITAT Mumbai "B" Bench in the case of Manish Ajmera v. ITO 25(2)(2).ITA No. 5700/Mum/2013.A.Y 2010-11 decided on 26.08.2016. The honorable tribunal heeled as under in Para 4 "Revenue Authorities were not having any advantage of this circular and this Circular in Clause 3A has squarely mentioned that where assessee itself irrespective of the period of holding the listed shares and services, opts to treat them as stock-in-trade, the income arising from transfer of such shares/securities would be treated as its business income, driving spirit of a circular which is binding on Revenue Authorities, we direct the Assessing Officer to treat the income in question as Short Term Capital Gain instead of business made by the Assessing Officer.

Now I would like to refer to the recent decision of the lordships of Gujarat High Court in the case of Deepaben Amitbhai Shah v. Deputy Commissioner of Income –tax reported (2016) 72 taxmann.com 202 (Gujarat). The lordships have in Para 9 of their order has followed the circular no. 6 of 2016 dated 29.2.2016 and heeled that if the assessee has declared capital gain on sale of shares than the same has to be taxed as capital gain and not as business income.

Lastly, I would like to rely on the decision of Bombay High Court in the case of Godavari Saraf v. CIT (1978) 113 ITR 589. Where, it has been held that when there is only decision of one High Court (not jurisdictional High Court) Tribunal is bound to follow it on the reason of judicial discipline.

❊❊❊