

JUGGILAL KAMLAPAT, KANPUR

v.

COMMISSIONER OF INCOME-TAX, LUCKNOW

July 31, 1969

[J. C. SHAH, ACTING C.J., V. RAMASWAMI AND A. N. GROVER, JJ.]

Income-tax—Dealing in shares—Whether capital investment or trading activity.

The assessee firm used to promote companies. It purchased all the shares of a Company at the ruling rates with borrowed money and very soon thereafter disposed of all of them at a profit. Before the Income-tax authorities the assessee claimed that it had taken over the shares with a view to secure the managing agency of that Company and had thereafter distributed the shares to its allied concerns, that the transaction was only to facilitate acquisition of a capital asset and the profit realised from the sale of such a capital investment was a capital gain. It was, found by the Departmental authority and the Tribunal that the shares were not merely 'distributed' to the assessee's associates, but that, some of the shares were sold to its allied concerns and others to strangers, through brokers, in small lots and at a profit. Also, the interest which the assessee had to pay for the amount borrowed for purchasing the shares was debited in its revenue account and was claimed before the Income-tax authorities as a revenue allowance.

The assessee also purchased shares of two other Companies which were its allied concerns, and commenced selling them soon after at a profit. It was claimed before the Income-tax authorities, with respect to these transactions that when a part of the new issue of capital of those two Companies was not taken over by the public, the assessee, as the financiers of those two companies took over the shares, that they were in the nature of a capital investment and the shares were sold on account of 'financial embarrassment' and not with the object of earning income and so, the profit realised by the sale did not attract income tax. The Departmental authorities and the Tribunal found that the first lot of shares in one of these two Companies was purchased in January, 1945 and the firm went on purchasing and selling the shares of that Company thereafter from February, 1945 and hence, there could not have been any 'financial embarrassment'. As regards the shares in the second company they were purchased in February, 1945 and sold in August, 1945. The sales were all through brokers and at a profit.

On the question whether the total profits realised by the assessee was a capital gain or revenue income,

HELD : Whether a transaction is or is not an adventure in the nature of trade is a mixed question of law and fact : in each case, the legal effect of the facts found by the Tribunal on which the tax-payer could be treated as a dealer or an investor in shares has to be determined. [724 C-D]

In the present case, on the facts found, there was a well planned scheme for earning profit. Therefore, all the transactions were impressed with the character of a commercial transaction entered into with a view to earn profits and were not capital investments, and hence, were liable to tax [724 D; 725 A-B]

- A *Ram Narain Sons (P) Ltd. v. C. I. T., Bombay*, 41 I.T.R. 534, (S.C.) explained.

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 1953 of 1968.

- B Appeal by special leave from the judgment and order dated September 17, 1962 of the Allahabad High Court in Misc. I.T. Application No. 167 of 1955.

A. K. Sen, G. L. Sanghi and *B. R. Agarwal*, for the appellant.

Jagdish Swarup, Solicitor-General, S. K. Iyer, R. N. Sachthey and *B. D. Sharma*, for the respondent.

- C The Judgment of the Court was delivered by

Shah, Ag. C.J. In proceedings for assessment to income-tax for the year 1946-47, the appellant firm was assessed to tax in respect of an amount of Rs. 3,99,587 received by it as profit on sale of shares. The plea of the firm that the amount was

- D "capital gain" and was on that account not taxable was rejected. In the view of the Income-tax Officer the profit arose from "a well planned business activity in which the assessee had fully utilised its resources". The Appellate Assistant Commissioner affirmed the decision of the Income-tax Officer. The Income-tax Appellate Tribunal dismissed the appeal filed by the firm.

- E The Tribunal, amongst others, referred the following question to the High Court of Allahabad for opinion :

- F "Whether the surplus realised by the sale of the shares of Aluminium Corporation of India Ltd., J. K. Investment Trust and Raymond Woollen Mills amounting in aggregate to Rs. 3,99,587 or any part thereof was the revenue income of the assessee liable to tax under the Income Tax Act, 1922 ?"

The High Court answered the question in the affirmative. The firm has appealed to this Court with special leave.

- G In 1944 the firm purchased 50,000 ordinary shares of Raymond Woollen Mills Ltd. (hereinafter called "Raymond") for Rs. 69,75,255. The firm paid Rs. 7,00,000 on November 4, 1944 and the balance on December 6, 1944. The transaction was financed with the aid of a loan of Rs. 70 lakhs borrowed from the Hindustan Commercial Bank Ltd. The firm sold those shares through brokers between November 23, 1944 and April 2, 1946 and realised Rs. 72,42,200, the transaction resulting in a net profit of Rs. 2,66,945. Between January 26, 1945 and April 5, 1946 the firm also purchased 67 debentures, 5,582 preference shares and 18,576 ordinary shares of the Aluminium Corporation

Ltd.—(hereinafter called “Aluminium”) for Rs. 8,57,480. Except 2118 preference shares, the entire lot of shares with the debentures was sold for Rs. 7,05,957 between February 1, 1945 and August 13, 1945. Adjusting the cost of shares left on hand the firm realised a net profit of Rs. 60,278 in that transaction. The firm also purchased 290 “A” Class shares of J. K. Investment Trust Ltd.—(hereinafter called “J. K. Trust”) on February 4, 1945 for Rs. 1,45,000 and sold the same on August 22, 1945 for Rs. 2,17,264, the transaction resulting in a net profit of Rs. 72,364.

Before the departmental authorities the firm claimed that it had taken over the entire share capital issued by Raymond with a view to secure its managing agency and had thereafter distributed the shares of Raymond to the various associates of the firm, and the transaction being one to facilitate acquisition of a capital asset being a capital investment, the profit realised by sale of the shares was not liable to be assessed to income-tax. The firm also claimed that when a part of the new issue of capital of Aluminium was not taken over by the public, the firm as financiers of the J.K. Group of Industries took over the shares and the debentures not subscribed within the time allowed. This transaction, it was contended, was also of the nature of capital investment. It was explained that the shares were sold on account of “financial embarrassment” and not with the object of earning income, and the profit realised by the sale did not attract tax. Similar contentions were also raised in respect of the shares of J.K. Trust. The departmental authorities rejected the contentions. The Tribunal agreed with them.

From the facts found by the Tribunal it is clear that for purchasing the Raymond shares, the firm paid Rs. 7,00,000 on November 4, 1944, and the balance on December 6, 1944, and commenced selling the shares on November 23, 1944. The contention that the shares were only distributed to the “allied concerns” is contrary to the findings of the Tribunal. Some of the shares were sold through brokers to outsiders. It is a significant circumstance that the firm parted with all the Raymond shares by April 2, 1946 and did not retain a single share after that date. It is true that some of the shares were held by J.K. Industries Ltd. and other J.K. concerns. But the transfer even to the J.K. concerns was in all cases for a profit. Within a few days after purchasing the Raymond shares, the “firm started unloading them”, and the shares were never sold without making profit. The interest paid for the loan borrowed from the Hindustan Commercial Bank Ltd. for financing the purchase of Raymond shares was debited in the accounts as a revenue expenditure, and it was claimed as a permissible allowance. The firm used to promote Companies.

- A One of its activities was to finance "sister concerns" known as J.K. Industries. The case of the firm that the shares had to be sold on account of "financial embarrassment" was plainly untrue. The Tribunal was, in our judgment, right in inferring that the "purchase and sale of shares was a business activity which was continuous", and since the firm "had entered upon a well-planned
- B scheme for earning profit and that in furtherance and execution of that profit making scheme they sold the shares at the opportune time" and that "the sale of the shares was not merely on account of pecuniary embarrassment" as claimed, the profit realised by the firm by the sales of shares could not be characterised as a casual receipt, nor could it be treated as accretion to a capital asset.

- C Strong reliance was, however, placed on a somewhat obscure statement in the order of the Appellate Assistant Commissioner :

- "In the case of Raymond Woollen Mills shares it is clear beyond doubt that the purchase of the shares was a first rate business deal and that it was motivated by the desire and intention to acquire the Managing Agency of the Mills. If this is not an operation in the scheme of profit-making, it is not known what will constitute such a transaction."
- D

- E Apparently there is a typographical error in the second clause of the first sentence, and the word "not" has by inadvertence been omitted; otherwise in the context in which it occurs the clause has no meaning whatever. In any event as rightly pointed out by the High Court the reasons given by the Tribunal and the conclusion recorded by it are inconsistent with the finding that the shares were purchased with the sole object of acquiring the Managing Agency of the Raymond Woollen Mills and not with
- F a view to make profits.

- G Counsel for the firm invited our attention to the decision of this Court in *Ramanarain Sons (P) Ltd. v. Commissioner of Income-tax, Bombay*⁽¹⁾ in support of his contention that a transaction for purchasing shares with the object of acquiring the managing agency of a Company will be regarded as capital investment and not a business in share. In *Ramnarain Sons' case*⁽¹⁾ the appellant Company was a dealer in shares and securities and also carried on business as managing agents of other companies. With a view to acquire the managing agency of a company, the appellant Company purchased from the managing agents a large block of shares at a rate approximately 50% above the ruling market rate. Two months later the appellant Company sold a small lot out of those shares at a loss and claimed the loss as a
- H

(1) 41 I.T.R. 534.

trading loss. It was found in that case by the Tribunal that the intention of purchasing the shares was not to acquire them as part of the stock-in-trade of tax-payer's business in shares, but to facilitate the acquisition of the managing agency of the Company which was in fact acquired, and on that account loss incurred by the sale of a small lot could be regarded only as a loss of capital nature. The Court observed in that case that the circumstance that the tax-payer had borrowed loans at interest to purchase the shares or that it was a dealer in shares and was authorised by its memorandum of association to deal in shares was of no effect. On a review of the evidence the Tribunal held that the shares were purchased with the object of acquiring the managing agency and with that view the High Court agreed.

Whether a transaction is or is not an adventure in the nature of trade is question of mixed law and fact : in each case the legal effect of the facts found by the Tribunal on which the tax-payer could be treated as a dealer or an investor in shares, has to be determined. In the present case the transaction since the inception appears to be impressed with the character of a commercial transaction entered with a view to earn profit. Large block of shares was purchased at the ruling rates with borrowed money, and soon thereafter the shares were disposed of at a profit in small lots. Some of the shares were sold through brokers to strangers. The story of the firm that some or all the shares were merely "distributed" to its associates is not proved. The interest which the firm had to pay for the amount borrowed for purchasing the shares was acted in the revenue account and was claimed as a revenue allowance.

It was not the case of the firm that Aluminium and J.K. Trust shares were purchased for acquiring the managing agency. It was claimed that the shares were taken over because the public did not accept those shares. It was one of the objects of the firm to finance its allied concerns and in taking over shares which the public did not subscribe the firm was acting in the course of its business. The firm commenced selling the shares soon after they were purchased. Aluminium shares were purchased between January 26, 1945 and April 5, 1946 (except a few which were retained) and sold at profit. Whereas the first lot was purchased on January 26, 1945, the first sale was made on February 1, 1945. It could not be said that this was an investment in shares independent of the trading activity of the firm. The story that the shares had to be sold on account of financial difficulties is plainly belied by the circumstance that the firm went on purchasing and selling the Aluminium shares. J.K. Trust shares were purchased on February 14, 1945 and were sold on August 22, 1945. Aluminium shares as well as J.K. Trust shares were sold at a profit

- A and through brokers. These transactions were also stamped with the character of commercial transactions entered into with a profit motive and were not transactions in the nature of capital investments. The answer recorded by the High Court is therefore correct.
- B The appeal fails and is dismissed with costs.

V.P.S.

Appeal dismissed.