

[1969] 71 ITR 504 (MAD.)

HIGH COURT OF MADRAS

Mrs. Sarojini Rajah

v.

Commissioner of Income-tax

VEERASWAMI AND RAMAPRASADA RAO, JJ.

TAX CASE NO. 156 OF 1964 REFERENCE NO. 54 OF 1964

FEBRUARY 7, 1968

S. Swaminathan and K. Ramagopal for the Applicant.

V. Balasubrahmanyam and J. Jayaraman for the Respondent.

#### JUDGMENT

Veeraswami, J.— The matter relates to the assessment year 1953-54 and the material point turns on whether certain shares, which the assessee held in the Vanguard Fire and General Insurance Company Limited, were an investment or constituted her stock-in-trade. The revenue as well as the Tribunal have considered that they were purchases by her as an investment. This controversy as to the character of her shareholding became relevant in the context of her claim for allowance of Rs. 42,534 as business loss incurred by her on the sale of the shares during the accounting year ended March 31, 1952. The Income-tax Officer was of the opinion that, having regard to the circumstances, there was every possibility of the transaction being one to book a loss for the purpose of reducing the tax liability of the assessee and, apart from it, the transaction also should be regarded but as an investment. Out of the holding by one Udaya Limited, in which the assessee was a director and her husband was the managing director, she purchased on March 31, 1952, 32,850 shares at Rs. 3-13-0 each, and for a total consideration of Rs. 1,25,342-8-0. On January 13, 1953, she sold 20,000 out of them through a broker of Bombay by name Naraindas and Company at Rs. 2-8-0 per share. The sale proceeds of Rs. 50,000 were received by her by cheque on January 15, 1953. She endorsed this cheque the next day in favour of Udaya Limited. We may mention that when she purchased the shares from Udaya & Company the latter had owed her Rs. 98,375. After giving credit for this amount towards her purchase of the shares, the balance of the price of 32,850 shares remained due from her to Udaya Limited. On March 10, 1953, she sold the remaining 12,000 shares at the same rate per share through another broker. The shares would appear to have been delivered by her to the broker through the Indian Bank which realised Rs. 30,000, being the total sale price, to her credit two days later. That is how, according to the assessee, she incurred a loss in the transaction relating to the 32,850 shares of Vanguard. The Tribunal has noted in its order that, as on March 31, 1953, the market value of the shares was Rs. 2-10-0, which was less than the cost to the assessee. The Income-tax Officer determined the assessee's total income for the year at Rs. 36,114 and charged the same to tax after declining to allow the loss in the share transaction. The Appellate Assistant Commissioner agreed with him and

found that the sales effected by her were not real sales. The Tribunal confirmed the view of the revenue on both the aspects, viz., that the purchase by the assessee of 32,850 shares was but an investment and that the sales of those shares were not genuine. In support of its finding that the purchase was only an investment, the Tribunal said:

"We are not inclined to infer from these transactions in Government securities (in 1948-49) that the assessee was a dealer in shares. The long interval of time has also to be taken note of. As we had indicated, though the market value was less than the cost price, the assessee did not choose to revalue the shares as any ordinary share-dealer should have done. Moreover, looking to the large block of shares and the fact that they were the shares in a company in which the assessee's husband was an important official, it can safely be inferred that they had been acquired for the purposes other than in regularly dealing with them ; that the assessee's intention in acquiring the shares was generally one of investment could be gathered from the fact that she had 3,000 deferred shares of Rs. 15,000 in Oriental Mercantile Distributors Limited and 10,000 deferred shares of Rs. 15,500 in Vanguard Fire and General Insurance Company Limited".

The Tribunal's conclusion that the sales were not genuine was rested primarily on the fact that eventually the assessee's husband purchased 32,000 shares in January, 1953, through share-brokers and that the price realised by the assessee by sale of the shares went into the account with Udaya Limited, which was common to her and her husband. It was inclined to think that the sum of Rs. 98,000 to the credit of the assessee with Udaya Limited was a transfer apparently to her husband's account or payment by the company towards certain prior debts. It was also of the opinion that the names of the brokers had been interposed to make the sales appear real and they were in the course of dealing in shares. At the instance of the assessee the reference has been made to us under section 66(2) of the Indian Income-tax Act, 1922, of the following question:

"Whether, on the facts and in the circumstances of the case, the disallowance of the loss of Rs. 42,534 resulting from the sale of 32,000 shares held by the assessee in Vanguard Fire and General Insurance Company Limited is lawful?"

The answer to this question will ultimately depend on the character of the holding by the assessee of 32,000 shares, as an investment or as a stock-in-trade. Having regard to the frame of the question, it is argued for the revenue that it does not cover the factual findings of the Tribunal, as they are called, both as to the character of the holding and the reality of the sales. We do not agree. The question, in our opinion, is comprehensive enough to include these matters. The propriety of the disallowance of the loss cannot be dealt with independent of them. If the findings of the Tribunal are not covered, we fail to see what other purpose the question under reference will serve to the assessee. The whole point at issue is whether the disallowance of the loss is legal and that is necessarily and inevitably intertwined with those findings of the Tribunal.

We may point out that whether a question is comprehensive enough to include other questions not specifically raised will have to be decided in the light of the facts in each case. *A.V. Thomas & Company Ltd. v. Commissioner of Income-tax* [1963] 48 ITR (SC) 67, in our opinion, proceeded on the special facts in that case,

for the Supreme Court was of the view that the issue raised under section 10(1), in order to claim a deduction as an ordinary business loss, could not be gone into because the question as considered in the High Court did not embrace it. But that is not the case here. The only question before the Tribunal was as to the propriety of the disallowance of the loss and that necessarily, as we have already indicated, embraces the character of the stockholding and the genuineness of the sales of the shares.

Another objection for the revenue is that the findings of the Tribunal are factual and should, therefore, be conclusive in this reference. It is unnecessary to enquire in the abstract what constitutes a question of law. We think that the question whether a given transaction is an investment or a trading activity is not a pure question of fact but is a mixed question of law and fact. As to the other finding of the Tribunal, it will of course be conclusive unless, upon a comprehensive, fair and proper view of the primary facts found, it is not reasonably possible to deduce that conclusion. This approach is not the same as there being no material to support the factual finding, which is open as a question of law.

Let us now proceed to consider whether the Tribunal was right in its view that the assessee held the shares only as an investment. It seems to us that the Tribunal's view on the question is not based on relevant premises and also fails to take into account certain facts which ought to have entered into its consideration. Its conclusion on the character of the holding is based on the premises: (1) there was a long interval of time between the sale of Government securities by the assessee in 1949-50 and the purchase by her of the shares of Vanguard, (2) the assessee did not choose to revalue the shares as any ordinary share-dealer should have done at the end of the accounting year, and (3) her shareholding related to a large block of shares in a company in which her husband was an important official. In approaching the question in that manner we think the Tribunal misdirected itself as to the proper criteria with reference to which the character of the shareholding should be ascertained. What a trading activity is, it is not easy to define with any comprehensiveness or precision. It is one of those matters which has to be judged having regard to the totality of the impression the circumstances of the case taken together make on the mind of the court. There are, however, certain badges of trade which may generally serve to distinguish it and which are collected in the report of the Royal Commission on the Taxation of Profits and Income, 1955:

"We have drawn up and set out below a summary of what we regard as the major relevant considerations that bear upon the identification of these 'badges of trade'.

(1)The subject-matter of the realisation.—While almost any form of property can be acquired to be dealt in, those forms of property, such as commodities or manufactured articles, which are normally the subject of trading are only very exceptionally the subject of investment. Again property which does not yield to its owner an income or personal enjoyment merely by virtue of its ownership is more likely to have been acquired with the object of a deal than property that does.

(2)The length of the period of ownership.—Generally speaking, property meant to be dealt in is realised within a short time after acquisition. But there are many exceptions from this as a universal rule.

(3)The frequency or number of similar transactions by the same person.— If realisations of the same sort of property occur in succession over a period of years or there are several such realisations at about the same date a presumption arises that there has been dealing in respect of each.

(4)Supplementary work at or in connection with the property realised.— If the property is worked up in any way during the ownership so as to bring it into a more marketable condition ; or if any special exertions are made to find or attract purchasers, such as the opening of an office or large-scale advertising, there is some evidence of dealing. For when there is an organised effort to obtain profit there is a source of taxable income. But if nothing at all is done, the suggestion tends the other way.

(5)The circumstances that were responsible for the realisation.—There may be some explanation, such as a sudden emergency or opportunity calling for ready money, that negatives the idea that any plan of dealing prompted the original purchase.

(6)Motive.—There are cases in which the purpose of the transaction of purchase and sale is clearly discernible. Motive is never irrelevant in any of those cases. What is desirable is that it should be realised clearly that it can be inferred from surrounding circumstances in the absence of direct evidence of the seller's intentions and even, if necessary, in the face of his own evidence".

We do not desire to be understood that we accept these considerations as comprehensive or exhaustive. But they are, in our opinion, of considerable assistance in deciding the character of a transaction as of a commercial character.

In *Ramnarain Sons ( Pr.) Ltd. v. Commissioner of Income-tax* [1961] 41 ITR 534, 537; [1961] 3 SCR 904 the Supreme Court observed:

"In considering whether a transaction is or is not an adventure in the nature of trade, the problem must be approached in the light of the intention of the assessee having regard to the legal requirements which are associated with the concept of trade or business".

What are these legal requirements ? In *Griffiths v. J.P. Harrison (Watford ) Ltd.* [1965] 58 ITR 328, 347, 348 (PC) the House of Lords had occasion to consider whether a loss which was sought to be set off in purchase and sale of certain shares by an incorporated company was a business loss. Just before the purchase of shares, the company had taken power in the memorandum of association to deal in shares. The majority opinion in that case held that the loss was a business loss. In dealing with that question Lord Morris stated :

"In judging as to the essential nature of a transaction it will often be relevant and of assistance to consider the objects and intentions which are the inspiration of the transaction ....

It is doubtless true to say that, in general, a trader embarks upon trade with the intention of making a profit ; but it cannot be said that if this intention is lacking there is no carrying on of a trade. A trade may be carried on with the knowledge that losses will result. Equally it seems to me that if on any ordinary examination of them certain transactions must be regarded as trading transactions or adventures

in the nature of trade they do not cease to be such because those conducting them have embarked upon them with a view to obtaining some fiscal benefit. . . . The possibility of tax recovery may be a result made possible by the trading activity but I am unable to accept that if a transaction fairly judged has in reality and not fictitiously the features of an adventure in the nature of trade it must be denied any such description if those taking part in it had their eyes fixed upon some fiscal advantage".

There is a further observation of Lord Morris [1965] 58 ITR 328, 347, 349 :

"The company bought the shares, received a dividend and then sold the shares. These facts seem to me to point firmly to the conclusion that the transaction was entered into as part of a trade of dealing in shares or was an adventure in the nature of trade".

We may also usefully extract the following observation from Lord Guest [1965] 58 ITR 328, 347, 349 :

"But where the company has power under its memorandum of association to indulge in a particular activity, and the transaction contains otherwise all the indicia of trading in that line of business, the fact that it was an isolated transaction is, in my opinion, nihil ad rem. In any event, regard must be had to the subsequent dealings in shares by this company, and, so viewed, this was not an isolated transaction, but one of many. . .

I therefore conclude that neither the fact that the company intended to make a loss nor the fact that the company intended to make a fiscal advantage out of the transaction negatives trading".

Certain other cases have been cited before us each of which appears to have turned on the particular facts. We think that the presence of commercial motive is a primary legal requisite of trade. Purchase and sale as a business deal in the present context may be another requisite. Intention to make a profit normally inspires trade and commerce, but it seems it may not be the essence of trade. Likewise, habitual dealing is ordinarily indicative of trade or commerce, but is not necessarily so, as pointed out by Rowlatt J. in *Graham v. Green* [1925] 9 Tax Cas. 309. There may be other legal requisites which may have to be satisfied with reference to the character of particular transactions in different kinds of trade or businesses. But whether these legal requisites are satisfied or are present will themselves, in their turn, be a mixed question of law and fact. The character of the motive or intention with reference to a transaction is a matter of inference from the other facts. It is here the badges of trade indicated by the Royal Commission earlier referred to are of assistance. The subject-matter of a transaction may be such as is commonly or usually dealt with in trade or commerce. For instance, often stocks and shares by their nature are transacted as a commercial deal, though occasionally there may be investment as such in shares and stocks. The length of their holding may perhaps be suggestive of the character of the holding. If the stocks purchased are held over a long number of years, it may be reasonable to conclude that it is a case of investment. But if there is frequency in the purchase and sale of shares in the course of a person's activities, that may lead to a just inference that he does so as a commercial deal and in the course of his business. There may be cases where the

subject-matter itself may not suggest the intention. For instance, supposing a person buys a motor car, uses it for a number of years and then sells it, that is a clear case of not being in the course of business. On the other hand the same person while making use of a car for over a long time also indulges in purchase of cars and frequent sales thereof with or without putting them to his use in between the purchase and sale, it may be possible to infer in such a case that he is a dealer in motor cars.

What is the position in the present case? The assessee, as the record shows, has been in the habit of purchase of Government securities and other stocks and selling them and making a profit or loss. In 1948-49 she sold Government securities and made a profit. In March, 1952, she purchased the shares in Vanguard and sold the same in January and March, 1953. In 1953 she made further purchases of shares and by sale of some of them made a profit. She purchased and sold shares relating to different concerns in the years following up to 1959. It is, therefore, clear that the purchase and sale of Vanguard shares are not isolated transactions. Not that we say that even an isolated transaction may not, in particular circumstances, be an adventure in the nature of trade. Is it reasonable to infer from such course of dealing over a period of years that the assessee's intention was not to deal in shares as a business proposition but only to make an investment in shares? In our opinion, the only reasonable and necessary inference is that she traded in shares with a commercial motive of making profit. It is no doubt true that there was an interval between 1948-49 and 1953-54 during which there were no transactions in shares by the assessee, but that, as we think, can hardly make any difference to the fact that her purchase and sale of shares was and has been with a commercial motive. The Tribunal evidently noticed her dealing in shares in the subsequent years, but has not taken it into account in deciding the character of the holding of shares in Vanguard in her hands. Apart from the fact that the shares are usually the subject-matter of commercial dealing and the assessee has purchased and sold shares before and after the accounting year, in the particular instance of purchase of the shares of Vanguard she has disposed them of practically within months of acquiring them. If investment was the motive, we fail to see how, in spite of the fact that the market at the relevant time was lower than the cost price, she sold the same. Once the purchase of shares in Vanguard is held to be in the course of her business in shares and, therefore, the shares formed part of her stock-in-trade, the fact that she designed to book a loss by sale of the shares in the accounting year cannot, in our opinion, alter the true character of the holding, provided the sale is not a sham. In taking that view, we think, we are supported by the principle of *Griffiths v. J.P. Harrison (Watford) Ltd.* [1965] 58 ITR 328 (PC).

The further question is whether, on a proper view of the facts and circumstances of the case, the Tribunal could at all have reasonably come to the conclusion that the sales by the assessee of the shares in Vanguard were not genuine transactions. The only circumstances, which according to the Tribunal led it to that conclusion, are that eventually the assessee's husband purchased the shares shortly after the sales by the assessee and that the account with Udaya Limited was a common account between them into which the sale proceeds of the shares had been credited. But the approach of the Tribunal in that manner has entirely overlooked the other facts which have a clear bearing upon and are determinative of the genuineness of the

sales by the assessee. The first lot of 20,000 shares was sold to Naraindas and Company, a stock broker of Bombay, who passed a cheque for the full amount of the sale proceeds. This cheque was received by the assessee. She endorsed it in favour of Udaya Limited, which realised it and credited the amount in her favour in the common account. The second lot of 12,000 shares too was sold to a broker and the transaction took place through the Indian Bank which realised the sale proceeds and credited to her. It is true Naraindas and Company sold the shares, which it had purchased, to the assessee's husband at its cost price in January, 1953. It is also true that the other lot purchased by a share broker passed on to another broker by name Chockalingam from whom the assessee's husband purchased, which was also in January, 1953, at its cost price, and the Tribunal finds that this Chockalingam was a man of no means. But, to our minds, these two circumstances, beyond raising a suspicion, are not of positive evidentiary value leading to the necessary conclusion that the sales of shares by the assessee were not genuine. Their genuineness will have to be judged in the light of the circumstances attending on the sales themselves which justify only one conclusion that the sales were and ought to have been genuine. The Tribunal has not stated that Naraindas and Company is a non-existing entity or the cheque passed by it for Rs. 50,000 was a make believe and that actually no money passed under the sale of 20,000 shares to the assessee. This observation applies also to the sale of the other lot of 12,000 shares.

We have already indicated that we are not prepared to accept the argument for the revenue that the Tribunal's conclusion in respect of the genuineness of the sales is a factual one which should be taken as conclusive before us in this reference. We would reiterate that, as pointed out by *Griffiths v. J.P. Harrison (Watford) Ltd.* [1965] ITR 328 (PC) a factual finding of a Tribunal cannot be disturbed in a reference, but if, upon a reasonable view of the facts, that conclusion could not reasonably be entertained, the bar has no application.

We answer the question in favour of the assessee with costs Rs. 250.