

**IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION**

INCOME TAX APPEAL (IT) NO.1187 OF 2017

Pr.Commissioner of Income Tax-7 ... Appellant

V/s.

National Stock Exchange ... Respondent

Mr.Suresh Kumar with Ms.Priyanka Tiwary and
Ms.Sumandevi Yadav, Advocate for the Appellant.

Mr.J.D.Mistri, Senior Advocate with Mr.Atul K. Jasani for
the Respondent.

**CORAM : UJJAL BHUYAN &
MILIND N. JADHAV, JJ.
DATE : FEBRUARY 3, 2020**

P.C.:-

1. Heard Mr.Suresh Kumar, learned standing counsel,
Revenue for the appellant and Mr.J.D.Mistri, learned
senior counsel assisted by Mr.Atul K. Jasani, learned
counsel for the respondent.

2. This appeal has been preferred by the Revenue
under Section 260A of the Income Tax Act, 1961 (briefly
“the Act” hereinafter) against the order dated 4th April,

2016 passed by the Income Tax Appellate Tribunal, Mumbai Bench "B", Mumbai (briefly "the Tribunal" hereinafter) in Security Tax Appeal No.02/Mum/2010 for the financial year 2005-06.

3. In this appeal appellant has proposed the following questions as substantial questions of law:-

"(i) Whether in the facts and in the circumstances of the case and in law the Tribunal was correct in holding that under the statute National Stock Exchange (NSE) is not liable for any alleged short deduction of Security Transaction Tax (STT)?

(ii) Whether in the facts and in the circumstances of the case and in law the Tribunal was correct in holding that NSE had not committed any fault in collection of correct STT, when infact section 100(1) of Securities Transaction Tax mandates the recognized stock exchange for collection and recovery of STT at the rates specified in section 98 of STT Act?

(iii) Whether in the facts and in the circumstances of the case and in law the Tribunal was correct in holding that it was the responsibility of member brokers of NSE to collect the correct STT on the transactions, when infact these member brokers are of NSE itself and operate on NSE's platform?

(iv) Whether in the facts and in the circumstances of the case and in law the Tribunal was correct in deleting the penalty for failure to collect the said Security Transaction Tax?"

4. The appeal has arisen on the following facts :-

5. For the financial year 2005-06 respondent filed return of taxable securities transaction on 29th June, 2006 declaring the total taxable securities transaction at Rs.6,99,10,47,72,669.00. The case was selected for scrutiny, whereafter notices were issued to the respondent.

6. Be it stated that, respondent is the National Stock Exchange of India Limited (NSE). In the course of the assessment proceeding Assessing Officer expressed apprehension that there was some under-collection of Securities Transaction Tax (STT) by the respondent in respect of certain institutional investors like foreign institutional investors. Assessing Officer made an enquiry on sample basis amongst the brokers registered with the respondent. According to the Assessing Officer, there was discrepancy in the total amount of STT collected by the

brokers from their foreign institutional investors, atleast by nine brokers, and the amount of STT collected by the respondent. According to the Assessing Officer, the nine brokers had reported a total of Rs.2,80,78,444.00 as short collection of STT by the respondent from the brokers pertaining to transactions entered into by the foreign institutional investors (FIIs) through the brokers. According to them, the total amount of STT collected from their foreign institutional investor clients was Rs.2,79,27,48,914.00 whereas the total amount of STT recovered by the respondent was Rs.2,76,46,70,470.00, thus leading to a shortfall of Rs.2,80,78,444.00. It was observed that the figure of discrepancy pertaining to FIIs transaction was likely to be higher as the discrepancies noticed by the Assessing Officer was from amongst nine brokers which were only illustrative and not exhaustive. Assessing Officer therefore held that respondent had failed to take inbuilt measures to collect STT properly and accurately from the members (brokers) as per requirement of Section 100 of Chapter VII of Finance (No.2) Act, 2004. Taking the view that his

inquiry covered only 1/4th of the total number of brokers registered with the respondent, Assessing Officer called upon the respondent to explain as to why a bonafide estimate of Rs.5 crores of STT should not be paid by the respondent which had escaped collection in its hand from the brokers. After considering the response of the respondent Assessing Officer passed the assessment order dated 28th March, 2008 raising STT collectable by the respondent by an additional amount of Rs.5 crores over and above the STT collected and deposited by the respondent during the year under consideration. It was observed that Assessing Officer had kept the option open to continue with the inquiry and to amend the assessment order if necessary since there was likelihood that the actual figure of under collection of STT pertaining to the FII's transactions would be much more. Accordingly, an amount of Rs.5 crores was added as the additional STT payable by the respondent and together with the interest, the amount payable was estimated at Rs.6,14,21,680.00. Assessing Officer further directed

initiation of penalty proceedings under Section 105(a) of Chapter VII of the Finance (No.2) Act, 2004.

7. Respondent preferred appeal before the Commissioner of Income Tax (Appeals)-13, Mumbai. By the appellate order dated 1st December, 2009, Commissioner of Income Tax (Appeals) took the view that liability to collect STT and to credit the same to the account of Central Government was a strict liability which the respondent had failed to discharge. Respondent had failed to collect due STT as per Section 100 read with Section 98 of the Finance (No.2) Act, 2004. However, Commissioner of Income Tax (Appeals) noted that since the actual discrepancy noted by the Assessing Officer on account of shortfall of STT collected from the brokers was Rs.2,80,78,444.00, Assessing Officer was directed to restrict the addition on account of shortfall of STT to Rs.2,80,78,444.00. However, Assessing Officer was directed to collect information from other brokers to determine whether any further shortfall of collectable STT was there and to raise the same accordingly.

Regarding initiation of penalty proceedings, it was observed that the same would be decided at the time of penalty proceedings. Thus, appeal of the respondent was partially allowed.

8. Respondent carried the matter in further appeal before the Tribunal. The said appeal was heard with several other appeals of the respondent on the same issue for different financial years as well as on the incidental issue of imposition of penalty. In its appellate order dated 4th April, 2016, Tribunal posed a question to itself as to whether respondent could be held liable for the alleged short deduction of STT on certain transactions of FII's for which higher rates are applicable being delivery based transactions in respect of both purchases as well as sales. After considering relevant provisions of the Finance (No.2) Act, 2004, more particularly Sections 98, 99 and 100 as well as Explanation to Rule 3(a)(iv) of the Security Transaction Tax Rules, 2004, Tribunal held that all the STT were collected through and under the client codes of the

member brokers. Duty of the respondent was to collect the tax at the correct rate of purchase and sale of shares executed through a particular client code. If there is default by a member either at the time of collecting STT in accordance with the client code or certain additional amount of STT was to be collected which had not been done, then the respondent could not be held responsible or liability could not be fastened on the respondent. Respondent could only ensure the determination of value of taxable security transaction purchased and sold through a client code and in accordance with the prescribed rate. Beyond that there is no mechanism provided that respondent should mandatorily collect STT beyond the client codes. Though there could be default by member brokers for not taking two separate client codes for sale and purchase but in so far respondent is concerned, it had not committed any default under the law because what respondent was required to see was whether the transaction of purchase and sale was undertaken through a particular client code or not. Respondent had admittedly complied with the

statutory requirement. Therefore, no default could be ascribed to the respondent. Accordingly, the addition as modified by the Commissioner of Income Tax (Appeals) was deleted. In view of the finding given in the quantum proceedings that there was no shortfall of STT and that there was no further liability of STT to be paid by the respondent, penalty levied was deleted.

9. Aggrieved, Revenue has preferred the present appeal proposing the above questions for consideration.

10. Mr.Suresh Kumar, learned standing counsel, Revenue referred to the provisions of Sections 98, 99 and 100 of the Finance (No.2) Act, 2004 and submits that on a conjoint reading of the aforesaid provisions it is evident that the liability for payment of STT is squarely on the respondent. He has also referred to the table provided in Section 98 as well as the columns thereto and submits that STT is charged as per the rate provided in column (3) to the table having regard to the nature of transaction of equity shares and securities. Referring to Section 100 he

submits that every recognized stock exchange is mandatorily required to collect the STT from every person being a purchaser or a seller who enters into a taxable securities transaction in that stock exchange at the rate specified under Section 98 and failure to collect and deposit STT at the prescribed rate would invite the consequences as provided in sub-section (4) to Section 100. He also placed reliance on a circular dated 30.09.2004 issued by the respondent to its members asking them to use two trading client codes for those investors whose transactions are to be settled only by delivery basis and submits that respondent ought to have ensured that the members used the proper code for correct collection of STT. He therefore submits that order passed by the Assessing Officer as modified by the Commissioner of Income Tax (Appeals) is fully justified. Tribunal erred in interfering with the said decision.

11. On the other hand, Mr.Mistri, learned senior counsel appearing for the respondent submits that respondent only provides the platform for carrying on of trading in

shares by the registered brokers. Value of taxable securities transaction is settled as per client code and in so far allocation of client code is concerned, respondent has no role to play. FIs were not given a separate client code for intra-day buying and selling of the securities by the brokers who operated on their behalf. There was nothing that the respondent could do about it. According to him, the problem might have arisen because some brokers did not take two client codes separately for buying and selling of the same scrip in intra-day transactions and further in not making correction of the client codes in their respective system. He submits that in view of the provisions contained in Section 98 read with Sections 99 and 100 of the Finance (No.2) Act, 2004, respondent is a mere collector of STT. It is not the case of the Revenue that respondent had defaulted in depositing the STT collected to the credit of the Central Government account. He also submits that the entire STT collected by the respondent has been credited in the account of the Central Government. His contention is that millions of transactions take place in the platform of

the respondent during the day. It is simply not possible on the part of the respondent to monitor each transaction or identify each transaction undertaken digitally on the platform of the respondent. If there is underpayment of STT, the liability would be on the broker and not on the respondent. All that it ensures is that brokers pay the prescribed rate of STT as per the table to Section 98. He therefore submits that Tribunal had correctly decided the issue in favour of the respondent. That apart, finding returned by the Tribunal is a finding of fact and no substantial question of law arises therefrom. Therefore, the appeal at the instance of the Revenue should be dismissed.

12. Submissions made by learned counsel for the parties have been duly considered.

13. Chapter VII of Finance (No.2) Act, 2004 deals with Securities Transaction Tax (already referred to as the STT). Section 97(11) defines securities transaction tax to mean tax leviable on the taxable securities

transactions under the provisions of the said chapter. As per Section 97(13), taxable securities transaction has been defined to mean transaction of purchase or sale of equity shares in a company or a derivative or a unit of an equity oriented fund or a unit of a business trust entered into in a recognized stock exchange; sale of unlisted equity shares by any holder of such shares under an offer for sale to the public included in an initial public offer and where such shares are subsequently listed on a recognized stock exchange; or sale of unlisted units of a business trust by any holder of such units which were acquired in consideration of a transfer referred to in clause (xvii) of Section 47 of the Income Tax Act, 1961 under an offer for sale to the public included in an initial offer and where such units are subsequently listed on a recognized stock exchange; or sale of an unit or an equity oriented fund to the mutual fund.

14. Section 98 is the charging section providing for charge of STT. It says that on and from the commencement of the chapter dealing with STT, there

shall be a charge of STT in respect of taxable securities transactions specified in column (2) of the table forming part of Section 98 at the rate specified in the corresponding column (3) on the value of such transaction and such STT shall be paid either by the purchaser or by the seller as specified in the corresponding entry in column (4). A glance at the table would show that at Sr.No.1 is mentioned purchase of an equity share in a company or a unit of a business trust where the transaction of such purchase is entered into in a recognized stock exchange and the contract for the purchase of such share or unit is settled by the actual delivery or transfer of such share or unit. For this category of taxable securities transaction the rate is 0.1% which is to be paid by the purchaser. Similarly, at Sr.No. 2 the transaction is of sale of an equity share in a company or a unit of a business trust. Here also the rate is the same but is required to be paid by the seller. Sr.No.3 deals with sale of an equity share in a company or in an unit of an equity oriented fund or an unit of a business trust where the transaction of such

sale is entered into in a recognized stock exchange and the contract for the sale of such share or unit is settled otherwise than by the actual delivery or transfer of such share or unit. In case of such transaction the rate of STT is 0.025 % and is required to be paid by the seller.

15. From the above, it is seen that there is difference in the rate between the transactions at Sr.Nos.1 and 2 as above and Sr. No.3.

16. Before deliberating on this aspect further, we may also refer to the other provisions of Chapter VII of the Finance (No.2) Act, 2004.

17. Section 99 provides the value of taxable securities transaction.

18. Section 100 deals with collection and recovery of STT. Sub-section (1) says that every recognized stock exchange shall collect STT from every person being a purchaser or a seller, as the case may be, who enters

into a taxable securities transactions in that stock exchange at the rates specified in Section 98. As per subsection (3), STT collected during any calendar month shall be paid by every recognised stock exchange to the credit of the Central Government by the seventh day of the month immediately following the said calendar month. In case of failure to collect STT, it shall be liable to pay the same to the credit of the Central Government under subsection (4).

19. Section 101 requires every recognized stock exchange to file return within the prescribed period and in the prescribed manner setting forth such particulars as may be prescribed in respect of all taxable securities transactions entered into during such financial year in that stock exchange.

20. Section 102 provides for making of assessment order by the Assessing Officer. The recognized stock exchange who submits return under Section 101 is construed to be an assessee for this purpose.

21. Section 104 provides for interest on delayed payment of STT.

22. While as per Section 105 an assessee is liable to pay penalty for failure to collect or pay STT, Section 108 clarifies that no order imposing a penalty shall be made unless the assessee has been given a reasonable opportunity of being heard.

23. Section 114 empowers the Central Government to make Rules for carrying out the provisions of the chapter.

24. In exercise of the powers conferred by sub-section (1) read with sub-section (2) of Section 114 of the Finance (No.2) Act, 2004, the Central government has made a set of rules for carrying out the provisions of Chapter VII of the said Act relating to STT called the Securities Transaction Tax Rules, 2004 (briefly “the Rules” hereinafter). Rule 3 deals with value of taxable

securities transaction. As per the explanation to clause (a)(iv) of Rule 3, the determination of the value of taxable securities transaction in a case where the equity share or unit is purchased or sold through a member of the stock exchange shall be made with reference to the trades executed in the equity share or unit under a particular client code through that member.

25. A careful reading of the above explanation would indicate that for determination of the value of the taxable securities transaction what is relevant is that the determination would be with reference to the trades executed in the equity share or unit under a particular client code through the concerned member (broker).

26. Having noticed the relevant legal provisions as above, it would be apposite to examine as to how the Tribunal dealt with the matter.

27. After considering the entire gamut of facts Tribunal summed up the main issue as to whether

respondent could be held liable for alleged short deduction of STT on certain transactions of FIIs for which higher rates were applicable being delivery based transactions in respect of both purchases as well as sales. After referring to the various provisions, Tribunal summed up the legal propositions in the following manner:-

“11. Now, from the conjoint reading of aforesaid provisions, following proposition can be culled out:

(i) The security transaction tax is charged at a specified rate in accordance with section 98. Such security transaction tax is payable by the purchaser and / or seller and not by the Stock Exchange;

(ii) The value of taxable security transaction has to be determined in accordance with section 99 which provides that, the value of taxable security transaction shall be the price at which such securities are purchased or sold and same has to be determined, which is as per proviso;

(iii) The Proviso below clause (c) of section 99 in turn empowers the Board to notify the rules and the method for determining the price of such securities;

(iv) In pursuance and in accordance with section 99(c), Rule (3) has been notified which prescribes, how the security transaction tax is to be determined;

(v) Clause (a) of Rule 3 provides for determination of STT in case where the equity shares or unit is purchased or sold by a person

on a trading day in the netted settlement mode;

(vi) Explanation to clause (a) provides that, determination of STT which is purchased or sold through Member of stock exchange shall be made with reference to the trade executed in the equity share or unit under particular "client code" through that member."

28. Having culled out the propositions as above, Tribunal held as under:

"12. Here in this case, there cannot be any dispute that the assessee had collected the STT in accordance with the provisions specified in section 98, which has been determined as per the mechanism laid down in section 99(c) r.w. Rule 3 and Explanation thereto. This is evident from the fact that, all the STT have been collected through and under the client codes of the members. It is not the case that assessee has not collected the STT under the given client code. If a member / broker does not collect STT through client code or has not taken the separate client codes in case of FII's, then so far as assessee is concerned, no liability can be fastened on the NSE. The duty of the NSE so far as the provisions of Security Transaction Tax Act r.w. STT Rules are concerned, is to collect the tax at a correct rate of purchase and sale of shares executed through particular client code. If there is default by a member either at the time of collecting the STT in accordance with the client code; or certain additional amount of STT is to be collected on account of any compliance of SEBI Regulations, which has not been done without adherence of client code; then, the assessee cannot be held responsible

or liability can be fastened under the provisions of section 98 to 100 r.w. Rule 3. The assessee can only ensure the determination of value of taxable security transaction purchase and sold through a client code and in accordance with the prescribed rate. Beyond that, there is no mechanism provided under the Act or Rules that assessee should mandatorily collect STT beyond the client codes. The SEBI issued the Circular to the National Stock Exchange for using two client codes, One for sale and Second for purchase transaction for those investors whose transactions are to be settled through delivery only, specifically in the case of FIIs. If the broker or the member have not taken any separate client code, then the assessee cannot be held responsible, because the assessee has already intimated / circulated that each and every broker or member should in such case take two client codes. Any failure cannot be ascribed to the assessee, because, it is an undisputed fact that the client code is not provided by the assessee, but by the member brokers. In case where the two separate client codes have not been taken for purchase and sale of shares for the same day and there is only one client code, then transactions are settled in the netted settlement mode, that is, squaring of the transaction and STT is calculated as per the netted settlement mode as prescribed under Rule 3. This netting off mode is not applicable in the case of FIIs in terms of SEBI regulations and Circular. If in some cases, there has been default by the Members brokers for not taking two separate client codes, then so far as assessee is concerned, it has not committed any default under the provisions of the STT Act r.w. relevant rules, because what assessee is required to see is whether the transactions of purchase and sale has undertaken through particular client

codes or not. Here in this case, the assessee has admittedly complied with this statutory requirement hence, we do not find any reason to ascribe any fault to the assessee or hold that be assessee committed and default to collect the correct STT. Thus, it is under the Statute NSE is not liable for any alleged short-deduction of STT. Accordingly, the addition which has been sustained by the CIT(A) to the extent of Rs.2,80,78,444/- stands deleted.”

29. Thus Tribunal held that STT is charged at a specified rate in accordance with Section 98. STT is payable either by the purchaser or by the seller and not by the stock exchange. Value of taxable securities transaction has to be determined in accordance with Section 99 and as per proviso thereto. Rule 3 of the Rules including the Explanation thereto have been notified prescribing how value of STT is to be determined. For determination of STT which is purchased or sold through a broker registered with the stock exchange, reference has to be made to the trade executed under the particular client code of the member broker. Thus, the STT is collected through a member broker under a particular client code. The client code is provided by the brokers and not by the stock exchange. Responsibility of

the stock exchange is to ensure firstly that STT is collected as per Section 98; secondly, it has been determined in accordance with Section 99 read with Rule 3 and Explanation thereto; and lastly, such STT collected from the purchaser or seller is credited to the Central Government as provided under Section 100.

30. Tribunal further held that the stock exchange i.e. the respondent can only ensure determination of the value of taxable securities transaction purchased and sold through a client code at the prescribed rate. However, there is no mechanism provided enabling the respondent to collect STT beyond the client code.

31. Tribunal also noted that Securities Exchange Board of India (SEBI) had issued circular to the respondent for using two client codes, one for sale and the other for purchase in respect of those investors like FIIs whose transactions are to be settled through delivery mode only pursuant to which the respondent had issued circular dated 30.09.2004 to its member brokers to use the two

client codes. If a broker had not taken any separate client code then the stock exchange cannot be held responsible. Such failure could not be ascribed to the respondent because the client codes were not provided by the respondent but by the member brokers. If in some cases there had been default by the member brokers in not taking two separate client codes, then so far the respondent is concerned it had not committed any default because what the respondent was required to see was whether the transactions of purchase and sale were undertaken through particular client codes or not. Respondent had admittedly complied with the statutory requirement.

32. Tribunal also returned a finding of fact that the STT collected by the respondent were through and under the client codes of the member brokers and the collected STT had been credited into the account of the Central Government.

33. Holding that respondent had not committed any default and that under the statute respondent was not liable for any alleged short deduction of STT, Tribunal deleted the addition made on this count as modified by the first appellate authority. Consequently, levy of interest and penalty were deleted.

34. To buttress what has been discussed above, we may advert to the explanation provided by one of nine brokers before the Assessing Officer. Morgan Stanley India Company Private Limited which was one of the broking companies dealing with FIIs stated before the Assessing Officer that for institutional clients the stock exchange provided facility of different client codes for purchase and sale trade for the same client to ensure that such trades were not netted. On occasions where client codes for institutional trades were not modified by the broker, the trades were treated as squared off trades and a lower STT was levied. This resulted in the exchange charging a lower STT from the member broker

while the member broker collected a higher delivery based STT from the client.

35. In such circumstances and on thorough consideration, we find no error or infirmity in the view taken by the Tribunal that under the statute respondent was not liable for any alleged short deduction of STT and therefore, no fault can be prescribed to the respondent and to hold the respondent to be in default for short collection of STT.

36. Consequently, we do not find any merit in the appeal. No substantial question of law arises from the impugned order passed by the Tribunal.

37. Resultantly, the appeal is dismissed. No cost.

(MILIND N. JADHAV, J.)

(UJJAL BHUYAN, J.)

....