



IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED : 07.09.2021

CORAM

The Honourable Mr. Justice T.S. SIVAGNANAM
and

The Honourable Mr. Justice SATHI KUMAR SUKUMARA KURUP

T.C.A.No.78 of 2016

Commissioner of Income Tax,
Trichy.

.. Appellant/Appellant

-vs-

M/s.Exim Rajathi India Pvt. Ltd.,
No.11, First Line Beach Road,
Nagapattinam.

.. Respondent/Respondent

Appeal under Section 260A of the Income Tax Act, 1961 against the order dated 07.04.2014 made in I.T.A.No.1584/Mds/2012 on the file of the Income Tax Appellate Tribunal 'D' Bench, Chennai for the assessment year 2007-08, against the order of the Commissioner of Income Tax III (Appeals) Tiruchirapalli, dated.25.05.2012 in ITA No.294/2011-12 pertaining to Assessment Year 2007-2008 against the order of the Joint Commissioner of Income Tax, Thanjavur Range, Thanjavur, dated 30.12.2011 in PAN No./GIR No.AABCE1762D.

For Appellant : Mr.M.Swaminathan,
Senior Standing Counsel
assisted by Ms.V.Pushpa,
Standing Counsel

For Respondent : Mr.B.Ramanakumar

JUDGMENT

(Delivered by T.S.Sivagnanam, J.)

This appeal, by the Revenue, filed under Section 260A of the Income Tax Act, 1961 (hereinafter referred to as "the Act") is directed against the order dated 07.04.2014 made in I.T.A.No.1584/Mds/2012 on the file of the Income Tax Appellate Tribunal 'D' Bench, Chennai (for brevity "the Tribunal") for the assessment year 2007-08.



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2.The appeal was admitted on 02.02.2016, on the following substantial question of law:-

"Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that the shares/debentures not listed in the recognized stock exchange could be treated as a long term capital asset as per Section 2(42A) read with its proviso?"

3.We have heard Mr.M.Swaminathan, learned Senior Standing Counsel assisted by Ms.V.Pushpa, learned Standing Counsel for the appellant-Revenue and Mr.B.Ramanakumar, learned counsel appearing for the respondent-assessee.

4.The assessee is an exporter of agricultural commodities and also dealing in iron ore. The assessee filed their return of income for the assessment year 2007-08 on 31.10.2007, declaring total income of Rs.7,93,48,354/-. The return was duly processed under Section 143(1) of the Act. Subsequently, the case was selected for scrutiny, the assessee was called upon to furnish details and the case was discussed with the Authorized Representative of the assessee.

5.On going through the books of accounts and other documents produced by the assessee, the Assessing Officer pointed out various issues and ultimately, the assessment was completed under Section 143(3) of the Act by order dated 30.12.2009. The Commissioner of Income Tax-II, Tiruchirappalli (for brevity "the CIT") exercised his power under Section 263 of the Act on the ground that the Assessing Officer failed to find out how many shares were acquired by the assessee from a hotel, which is a company registered under the Indian Companies act and how many shares were acquired by another company, which owned a hotel in Trichy. Further, the Assessing Officer has not ascertained at what price and when the shares were acquired. After noting certain facts, the CIT was of the opinion that the order of assessment is erroneous and prejudicial to the interest of Revenue and accordingly, proceeded with the matter under Section 263 of the Act. After hearing the assessee, an order was passed by the CIT dated 15.02.2011 by directing the Assessing Officer to workout the short term capital gains keeping in mind the rate of interest. The said order was given effect to by the Assessing Officer by order dated 30.12.2011. Aggrieved by the same, the assessee preferred appeal to the Commissioner of Income Tax (Appeals), Tiruchirappalli (for brevity "the CIT (A)"). The assessee contended that the Revenue has made a mistake by treating the shares held for more than twelve months as short term capital assets whereas, the proviso to Section 2 (42A) clearly defines an asset as a long term capital asset and



therefore, the gain should be taxed at the special rate of 20%. The CIT(A) after taking into consideration the factual and legal submissions made by the assessee, noted that the shares need not be one of a company, which is listed in its stock exchange and even shares of private limited companies are eligible to be treated as long term asset, if it is held for more than twelve months. Accordingly, the appeal was partly allowed by order dated 25.05.2012, directing the Assessing Officer to treat the sale of shares as long term capital asset, allowing the indexation and tax the resultant capital gain at the special rate of 20%. Aggrieved by the same, the Revenue was on appeal before the Tribunal contending that the proviso to Section 2(42A) of the Act would apply only to shares listed in a recognized stock exchange which shall be treated as long term capital asset which are held for more than twelve months. It was further contended that the CIT(A) ought to have seen that the shares which were sold by the assessee were unquoted and not listed in a registered stock exchange and were held for less than thirty six months and therefore, would not be covered by the proviso to Section 2(42A) of the Act. The Tribunal after considering the submissions on either side, the definition of "short-term capital asset" as defined under Section 2(42A), the amendment brought out by Finance Act, 1994 with effect from 01.04.1995, the relevant extracts of the explanatory notes on the provision of the Finance Act and the definition of the term "securities" as defined in Section 2(h) of the Securities Contracts (Regulation) Act, 1956 (hereinafter referred to as "the Securities Contracts Act"), held that the intention of the Legislature while introducing the amendment to the Act was very much clear not to include shares in the term "security" and therefore, concluded that there is no distinction between unlisted and listed shares for classifying them as short term capital asset under the Act. Thus, the only issue involved in the instant case is whether the shares held by the assessee in a company, which is not a listed company when sold, can be brought under the definition of "short-term capital asset" as defined under Section 2(42A) of the Act or whether it should be treated as a "long term capital asset".

6.The explanatory notes on the provisions of the Finance Act, 1994 would make the situation lucid and clear, which read as follows:-

"There are many financial instruments, other than company shares, through which the investors are entering the capital market. The units of the Unit Trust of India and Mutual Funds specified under section 10(23D) of the Income-tax Act are the instruments through which the small investors are increasingly getting the



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benefit of investment in the capital market. In order to provide such units and all the securities traded in the recognised stock exchanges a level playing field with company shares, the Finance Act has amended the provisions of Section 2(42A) so that the maximum holding period for which such instruments are to be considered as short-term will be 12 months in place of 36 months. In other words, such assets are to be considered long-term capital assets if they are held for more than 12 months. The expression "securities" will have the meaning assigned to it in clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956.

This amendment takes effect from 1st April, 1995 and will, accordingly, apply in relation to assessment year 1995-96 and subsequent years."

7.The above amendment came into effect from 01.04.1995. In the case on hand, the assessee purchased the shares during November, 1993, as stated, in a company which was not listed. The sale of shares took place in 1996 and the amendment would apply.

8.To be noted that between 1978-79 to 1987-88, there is no differential period mentioned in Section 2(42A) and the period was thirty six months both for shares and other securities. From the assessment year 1988-89, the period of holding was reduced to twelve months in respect of shares alone and not extended to other security and the position remained till the assessment year 1994-95, when the present amendment was introduced with effect from 01.04.1995 bringing other securities also on par with the shares.

9.The definition of "short-term capital asset" as defined under Section 2(42A) as it stood at the material time reads as follows:-

"Section 2(42A):

"Short-term capital asset" means a capital asset held by an assessee for not more than (thirty-six) months immediately preceding the date of transfer.

Provided that in the case of a share held in a company (or any other security listed in a recognised stock exchange in India or a unit of the Unit Trust of India established under the Unit Trust of India Act, 1963 (52 of 1963) or a unit of a Mutual Fund specified under clause



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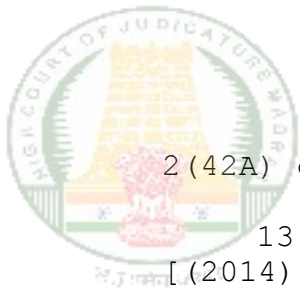
(23D) of Section 10 (or a zero coupon bond), the provisions of this clause shall have effect as if for the words "thirty-six months", the words "twelve months" had been substituted.

Explanation (1). -

10. In terms of the above definition, short term capital asset would mean a capital asset held by an assessee for not more than 36 months immediately preceding the transfer. The interplay of the provision in Section 2(42A) would be relevant for the case on hand, which states that in case of a share held in a company or any other security listed in a recognized stock exchange in India or a unit of the Unit Trust of India or a unit of a Mutual Fund or a zero coupon bond, the provisions of the clause shall have effect as if for the words "thirty-six months", the words "twelve months" had been substituted.

11. What is important to note is to use the word "or" in between each of the categories of items mentioned in the proviso. The first of which being shares held in company. The provision does not make a distinction between a public company, a private company, a listed company or an unlisted company. The second category is "other securities" and a condition has been imposed under the statute that for the benefit of the reduced period of twelve months, the other securities should be listed in a recognized stock exchange in India. This is precisely the reason for which the amendment has been brought above and this is clear on a reading of the explanatory notes, which states that in order to provide such units and all the securities traded in the recognized stock exchanges a level playing field with company shares, the Finance Act has amended the provisions of Section 2(42A) so that the maximum holding period for which such instruments are to be considered as short term will be twelve months in the place of thirty six months.

12. The argument of Mr. M. Swaminathan, learned Senior Standing Counsel is that the definition of "securities" as defined under Section 2(h) of the Securities Contracts Act should be taken note of. This aspect has also been dealt with by the Tribunal and it was held that although under the Securities Contracts Act, the term "securities" includes shares, but in Section 2(42A) of the Act, shares have been mentioned separately. As pointed out earlier, the use of the word "or" in between each of the categories of holding is very important and such distinction needs to be borne in mind. It may be true that "securities" as defined under Section 2(h) of the Securities Contracts Act includes shares, scripts, stocks, bonds etc., that by itself cannot have an impact to give a different interpretation to the distinction of "short-term capital asset" as defined in Section



2(42A) of the Act.

13. In Mohan Virwani vs. Deputy Commissioner of Income Tax [(2014) 51 taxmann.com 43 (Kar.)], the question which fell for consideration was whether the shares held by the assessee is a short term capital asset or a long term capital asset. The assessee in the said case, acquired shares in November 1993 and sold the shares in June, 1996, the period of holding was less than thirty six months. The assessee claimed benefit under Section 2(14) of the Act claiming that the shares is a long term capital asset. All the three authorities held that the period of holding for thirty six months would apply in the case of shares for a company listed in the stock exchange in India and the shares of the said assessee are of a private limited companies, which are not listed shares in the stock exchange. Therefore, all the shares of a private limited company would have to be construed as thirty six months only and therefore, the shares cannot be treated as short term capital gain and accordingly, taxed. Aggrieved by the same, the assessee approached the High Court of Karnataka. While answering the question, the Court took into consideration the definition of "short-term capital asset" as defined under Section 2(42A), the circular issued by the Central Board of Direct Taxes (CBDT) bearing Circular No.684 dated 10.06.1994 and pointed out that the shares held in a company, which may be a private limited company, a public limited company or a listed company or any other security other than those shares listed in a recognized stock exchange in India, if it is held for a period of twelve months, then it ceased to be a short term capital asset and it becomes a long term capital asset. Therefore, the Court pointed out that the authorities have not kept this distinction in mind and they have misread the section and accordingly, the appeal filed by the assessee was allowed. The above decision would apply with full force to the case on hand warranting answering of the substantial question of law in favour of the respondent-assessee.

14. Identical issue came up for consideration before the Income Tax Appellate Tribunal (ITAT), Delhi Bench in the case of Analjit Singh vs. Deputy Commissioner of Income Tax, Circle-16 (2), Delhi [2017 SCC OnLine ITAT 18870]. Two of the issues, which were framed for consideration by the ITAT were (i) whether the CIT(A) erred on facts and in law in observing that for unlisted shares to qualify as "long term capital asset", the period of holding was 36 months and not 12 months as per the first proviso to Section 2(42A) (as applicable during the year under consideration) read with Section 2(29A) of the Act; and (ii) Whether the CIT(A) erred on facts and in law in holding that the shorter period of 12 months to qualify as "long term



capital asset" was only applicable to unlisted shares sold during the period 01.04.2014 to 10.07.2014, in terms of second proviso to Section 2(42A), which was inserted by the Finance (No.2) Act, 2014, with effect from 01.04.2015.

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15. We find from paragraphs 85 to 87 of the order, which have crystallized the arguments of the learned counsel appearing for the assessee and the Revenue and we find those arguments to be substantially similarly to the arguments, which were advanced before us. The ultimate conclusion arrived at by the ITAT was that so far as the term used 'shares held in a company' is concerned, there is no category mentioned as listed or unlisted shares, albeit the condition for being listed in recognized stock exchange in India is for 'any other security'. The expression listed in a recognized stock exchange in India is only used for category of 'any other security' and not for the category of 'share held in a company'. Further after taking into consideration that the condition for the period of holding was curtailed from 36 months to 12 months by the Finance Act, 1987, it was only for 'share held in a company'. Further, when the amendment by the Finance Act 1994 was brought in the statute so far as the category 'shares held in a company' was concerned, the same was not disturbed, albeit, new category was included like 'any other security listed in recognized stock exchange in India'. Further, the ITAT took note of the Memorandum explaining the provision in the Finance Bill and observed that the Memorandum clearly makes a distinction that there are many financial instruments other than the company shares through which the investor are entering capital market and in order to provide such units and all securities traded in the recognized stock exchange, a level playing field with the company's share is proposed to be amended and thus, the said Memorandum clearly makes a distinction between the company shares and other than company shares.

16. In our considered view, the above decision of the ITAT has laid down the correct legal principle which we have discussed in the preceding paragraphs.

17. On a search made, we find that the Revenue has not challenged the order of the ITAT before the Court, but it is the assessee, who has challenged it before the High Court of Delhi and obviously not against the above finding, which was rendered in favour of the assessee.

18. Further, we take note of the Explanatory Notes to the Provisions of the Finance (No.2) Act, 2014 vide Circular No.01/2014, dated 21.01.2015. In paragraph 5.2 of the Circular, it has been stated as follows:-



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"5.2.The shorter period of holding of not more than twelve months for consideration as short-term capital asset was introduced for encouraging investment on stock market where prices of the securities are market determined. However, all shares whether listed or unlisted have enjoyed the benefit of short period of holding and even any investment in shares of private limited companies enjoyed long-term capital gains on its transfer after twelve months."

19.The above Circular issued by the CBDT will clearly indicate that all shares whether listed or unlisted have enjoyed the benefit of shorter period of holding and even any investment in shares of private limited companies enjoyed long-term capital gains on its transfer after twelve months.

20.For all the above reasons, the appeal filed by the Revenue is dismissed and the substantial question of law is answered against the Revenue and in favour of the assessee. No costs.

Sd/-
Assistant Registrar(CO)
//True Copy//

Sub Assistant Registrar

abr

To

1. The Income Tax Appellate Tribunal 'D' Bench,
Chennai.
2. The Joint Commissioner of Income Tax,
Thanjavur Range,
Thanjavur
3. The Commissioner of Income Tax II (Appeals)
Trichy

+1CC to Mr.M.Swaminathan, Advocate, Sr.No.45635

T.C.A.No.78 of 2016

SRA (CO)
K.RK. (27.09.2021)