

Commissioner of Income-Tax (Central), Delhi

Vs

M/S. Harparsad & Co. (P) Ltd.

Civil Appeal No. 494 of 1970

(Y. V. Chandrachud, R. S. Sarkaria, A. C. Gupta JJ)

25.02.1975

JUDGMENT

SARKARIA, J. -

1. This appeal is directed against the judgment, dated January 24, 1969, of the High Court of Delhi answering in the affirmative the following question referred to it under Section 66(1) of the Indian Income-tax Act, 1922 (for short, the Act) by the Commissioner of Income-tax :

Whether on the facts and in the circumstances of the case the capital loss of Rs. 28,662 could be determined and carried forward in accordance with the provisions of Section 24 of the Indian Income-tax Act, 1922, when the provisions of Section 12B of the Income-tax Act, 1922 itself were not applicable in the assessment year 1955-56.

2. The assessee (respondent) is a private limited company. The assessment year under reference is 1955-56 and the relevant previous year is from May 1, 1953 to April 30, 1954. On January 10, 1952, the assessee purchased 1,124 shares of M/s. Intercontinent Travancore Pvt. Ltd. at a cost of Rs. 1,12,400 from M/s. Escorts (A & M) Ltd. In the relevant accounting year ending on April 30, 1953 the assessee received 562 bonus shares from the same company. It thus acquired a total number of 1,686 shares. On September 3, 1953, i.e. during the relevant previous year the assessee sold all these 1,686 shares to M/s. Escorts (Agents) Ltd. for Rs. 84,300 and claimed a loss of Rs. 84,862 in the income-tax return filed by it. The Income-tax Officer disallowed the entire loss of Rs. 84,862 on the ground that it was a loss of a capital nature.

3. The assessee carried on appeal to the Appellate Assistant Commissioner and contended that this loss of Rs. 84,862 was a revenue loss arising out of dealing in shares. The Appellate Assistant Commissioner found that the assessee's claim was exaggerated and that the actual loss was to the tune of Rs. 28,662 only. He further held that this loss of Rs. 28,662 was not a 'revenue loss' but a 'capital loss', arising out of change of investment.

4. Against the decision of the Appellate Assistant Commissioner the assessee preferred an appeal before the Tribunal, challenging the findings of the Commissioner both in regard to the amount of loss and its nature. At the stage of arguments before the Tribunal, the assessee's Counsel did not press these grounds of appeal but took up the plea that the amount of Rs. 28,662 which had been held to be a 'capital loss' by the authorities below, should be allowed to be carried forward and set-off against profits and gains, if any, under the head "capital gains" earned in future, as laid down in sub-section (2A) and (2B) of Section 24 of the Act. Despite objection from the Departmental

Representative, the Tribunal allowed this new ground to be raised with the observation that it was "a pure question of law and did not require investigation of any fresh fact". It further accepted the contention of the assessee and directed that the 'capital loss' of Rs. 28,662 should be carried forward and set-off against "capital gains" if any, in future.

5. At the instance of the Commissioner of Income-tax, the Tribunal referred the above question (set out at the commencement of this judgment) to the High Court under Section 66(1) of the 1922 Act.

6. It was contended before the High Court on behalf of the Revenue that the expression "capital gains" in sub-section (2A) of Section 24 has reference only to Section 12B so that the loss suffered in the year in which the profits under the head "capital gains" were not taxable, could not fall within sub-section (2A) of Section 24. S. K. Kapoor, J., speaking for the Division Bench, rejected this contention in these terms :

This argument overlooks the fact that the head of income chargeable to income-tax are set out in Section 6.

Section 12-B deals only with the computation of capital gains and with their taxability if they arise during a particular period. As a matter of fact, Section 12-B itself refers to Section 6 inasmuch as it says that "the tax shall be payable by an assessee under the head 'capital gains'". This obviously has reference to the sixth head in Section 6. The effect of sub-sections (2A) and (2B) of Section 24 read with Sections 6 and 12B, therefore, is that if a capital loss is incurred in a year in which a capital gain did not attract tax under Section 12B such loss would still be loss under the head "capital gains" and if in subsequent year the assessee has any profit under that head it can still be carried forward and set-off against the taxable capital gain. The Tribunal, was in my opinion, right in coming to the conclusion that it did.

Hence this appeal by the Commissioner of Income-tax (Central) Delhi.

7. Capital gains tax for the first time was introduced by the Income-tax and Excess Profit Tax (Amendment) Act, 1947 (No. 22 of 1947) which inserted section 12B in the Act. This section made taxable "capital gains" which arose after March 31, 1946. The same Act of 1947 added as the sixth head "capital gains" in Section 6 of the Act. It also inserted sub-sections (2A) and (2B) in Section 24 of the Act.

8. The Indian Finance Act, 1949 virtually abolished the levy and restricted the operation of Section 12B to "capital gains" arising before April 1, 1948. But Section 12B in its restricted form, and the sixth head, 'capital gains' in Section 6, and sub-sections (2A) and (2B) of Section 24 were not deleted and continued to form part of the Act. The Finance Act (No. 3), 1956 reintroduced the "capital gains" tax with effect from March 31, 1956. It substantially altered the old Section 12B and brought it into its present form. As a result of Finance Act (No. 3) of 1956 "capital gains" again became taxable in the assessment year 1957-58. The position that emerges is that "capital gains" arising between April 1, 1948 and March 31, 1956, were not taxable. The capital loss in question relates to this period.

9. Mr. V. S. Desai, learned Counsel for the appellant contends that according to the scheme of the act a 'capital loss' occurring in a previous year, could be allowed to be carried forward and set-off against the 'capital gains' of a subsequent year, only if the income under that head was taxable in the relevant previous and subsequent years. Since during the period from April 1, 1948 to March 31,

1956, capital gains (plus) or capital gains (minus) did not entire into computation of the total income of the assessee chargeable to tax under Section 3 read with Section 12B of the Act, the question of carrying forward of such loss did not arise, much less could such a loss be set-off against the profits of any subsequent year.

10. As against this, Shri Ashok Sen, learned Counsel for the assessee maintains that a right to carry forward a loss under any of the heads enumerated in Section 6, is not dependent upon the taxability of income under that head; it is sufficient if at the relevant time "capital gains" is one of the heads of income recognized by the charging Section 6 and the loss is adjustable against 'capital gains', if any, in future under Section 24. The argument proceeds, that Section 6(vi) was not lying inert on the statute book but was operative, throughout, for the purpose of calculating the losses under that head. Shri Sen compared the non-taxability of capital gains during the period from April 1, 1948 to March 31, 1956, to a tax holiday for those years. Another illustration given by the learned Counsel is of a person whose total income falls entirely on the negative side on account of losses suffered by him under any of the heads of income given in Section 6. Such a person notwithstanding the fact that he had no assessable income, has a right to file a return and get his losses computed by the Income-tax Officer merely for the purpose of carrying forward the loss. The Income-tax Officer, it is added, cannot ignore the return filed by the assessee voluntarily showing losses even though such a return is filed beyond time. In this connection, Shri Sen has referred to C. I. T. v. Kulu Valley Transport Co. (P) Ltd. (77 ITR 518 (SC) : (1970) 2 SCC 192), Jaikishan Gopikishan and Sons v. C. I. T. (84 ITR 645) and C. I. T. v. Khushal Chand Daga (42 ITR 177 (SC) : (1962) 1 SCR 186).

11. Before dealing with the contentions canvassed, it will be appropriate to have a clear idea of the terms 'income', 'total income', 'computation of total income', "'carrying forward' of a loss and its purpose", in the context of the scheme of the Act.

12. Section 2, clause (15) defines "total income" to mean total amount of income, profits and gains referred to in sub-section (1) of Section 4 computed in the manner laid down in this Act. Section 3, captioned as "Charge of Income-tax", emphasises that the income-tax shall be charged in respect of the total income of the previous year of every assessee. Section 4 defines the ambit of that total income. Section 6 enumerates six heads of income, profits and gains chargeable to income-tax. They are :

- (i) Salaries.
- (ii) Interest on securities.
- (iii) Income from property.
- (iv) Profits and gains of business, profession or vocation.
- (v) Income from other sources.
- (vi) Capital gains.

13. Sections 7, 8, 9, 10, 12 and 12B relate to payability and computation of tax under the various heads of income. The material part of Section 12B at the relevant time was a follows :

12B. (1) The tax shall be payable by an assessee under the head "Capital gains" in respect of any profits or gains arising from the sale, exchange or transfer of a capital

asset effected after the 31st day of March, 1946 and before the 1st day of April, 1948 and such profits and gains shall be deemed to be income of the previous year in which the sale, exchange or transfer took place.

14. Section 22(1) requires a general notice to be published requiring every person whose total income during the previous year exceeds the maximum non-taxable limit to file a return. Sub-section (2) of this section enables the Income-tax Officer to issue notice to any such person requiring him to furnish a return. Sub-section (2A) - which was inserted by the Income-tax Amendment Act 25 of 1953, with effect from April 1, 1952 - provides :

If any person, who has not been served with a notice under sub-section (2) has sustained a loss of profits or gains in any year under the head profits and gains of business, profession or vocation, and such loss or any part thereof would ordinarily have been carried forward under sub-section (2) of Section 24, he shall, if he is to be entitled to the benefit of the carry forward of loss in any subsequent assessment, furnish within the time specified in the general notice given under sub-section (1) all the particulars required under the prescribed form of return.

15. The material part of Section 24 runs thus :

24. (1) Where any assessee sustains a loss of profits or gains in any year under any of the heads mentioned in Section 6, he shall entitled to have the amount of the loss set off against his income, profits or gains under any other head in that year :

* * * *##

Provided that in computing the profits and gains chargeable under the head "Profits and Gains of business, profession or vocation", any loss sustained in speculative transactions which are in the nature of a business shall not be taken into account except to the extent of the amount of profits and gains, if any, in any other business consisting of speculative transactions :

* * * *##

(2) Where any assessee sustain a loss of profits or gains in any year, being a previous year not earlier than the previous year for the assessment for the year ending on the 31st day of March, 1940, in any business, profession or vocation, and the loss cannot be wholly set off under sub-section (1), so much of the loss as is not so set off or the whole loss where the assessee had no other head of income shall be carried forward to the following year, and

(i) where the loss was sustained by him in a business consisting of speculative transactions, it shall be set off only against the profits and gains, if any, of any business in speculative transactions carried on by him in that year;

(ii) where the loss was sustained by him in any other business, profession or vocation, it shall be set off against the profit and gains, if any, of any business, profession or vocation carried on by him in that year : Provided that the business, profession or vocation in which the loss was originally sustained continued to be carried on by him in that year; and

(iii) if the loss in either case cannot be wholly so set off, the amount of loss not so set off shall be carried forward to the following year and so on

* * * *##

2A. Notwithstanding anything contained in sub-section (1), where the loss sustained is also falling under the head "Capital gains", such loss shall not be set off except against any profits and gains falling under that head.

2B. Where an assessee sustains a loss such as is referred to in sub-section (2A) and the loss cannot be wholly set off in accordance with the provisions of that sub-section, the portion not so set off shall be carried forward to the following year and set off against capital gains for that year, and if it cannot be so set off, the amount thereof not so set-off shall be carried forward to the following year and so on, so however, that no such loss shall be so carried forward for more than six years :

Provided that where the loss sustained in any previous year does not exceed fifteen thousand rupees, it shall not be carried forward.

(3) When, in the course of the assessment of the total income of any assessee, it is established that a loss of profits or gains has taken place which he is entitled to have set-off under the provisions of this section, the Income-tax Officer shall notify to the assessee by order in writing the amount of the loss as computed by him for the purposes of this section.

16. Section 2(6C) provides that 'income' includes (among other things) :

(vi) any capital gain chargeable under Section 12B.

17. From the charging provisions of the Act, it is discernible that the words 'income' or 'profits and gains' should be understood as including losses also, so that, in one sense 'profits and gains' represent 'plus income' whereas losses represent 'minus income' (C. I. T. v. Karamchand Prem Chand, 40 ITR 106 (SC) : (1960) 3 SCR 727; C. I. T. v. Elphinstone Spinning and Weaving Mills, 40 ITR 142 (SC) : (1960) 3 SCR 953). In other words, loss is negative profit. Both positive and negative profits are of a revenue character. Both must enter into computation, wherever it becomes material, in the same mode of the taxable income of the assessee. Although Section 6 classifies income under six heads, the main charging provision is Section 3 which levies income-tax, as only one tax, on the 'total income' of the assessee as defined in Section 2(15). An income in order to come within the purview of that definition must satisfy two conditions : Firstly, it must comprise the "total amount of income, profits and gains referred to in Section 4(1)". Secondly, it must be "computed in the manner laid down in the Act". If either of these conditions fails, the income will not be a part of the 'total income' that can be brought to charge.

18. Now, 'capital gains' would be covered by the definition of 'income' in sub-section (6C) of Section 2, only if they were chargeable under Section 12B. As noticed already, Section 12B as modified by the Finance Act, 1949, did not charge any 'capital gains' arising between April 1, 1948 to April 1, 1957. Indeed, Section 12B was not operative in these years (1948-57). During this period, 'capital gains', whether on the positive or the negative side, could not be computed and charged under Section 12B or any other provisions of the act. In the instant case, the second condition, namely, "the manner of computation laid down in the Act" which - to use the words of

Stone, C.J. (In re Kandar, 1946 ITR 10, 21) - "forms an integral part of the definition of 'total income'" was not satisfied. Thus in the relevant previous year and the assessment year or even in the subsequent year, capital gains or 'capital losses' did not form part of the 'total income' of the assessee which could be brought to charge, and were, therefore, not required to be computed under the Act.

19. Before the insertion of sub-section (2A) in Section 22 by the amendment of April 1, 1952, an assessee was entitled to carry forward loss even if he had submitted no return for the year in which the loss was sustained. After the enactment of sub-section (2A), it is a condition precedent to the carry-forward and set-off of the loss, that the assessee must file a return either in response to a general notice under sub-section (1) of Section 22 or voluntarily, without any individual notice under sub-section (2) of that section. If he does not file return for the year in which the loss was incurred and get the loss computed by the Income-tax Officer, the right to carry forward the loss will also be lost. But if the loss is from a source or head of income not liable to tax or congenitally exempt from income-tax, neither the assessee is required to show the same in the return, nor is the Income-tax Officer under any obligations to compute or assess it, much less for the purpose of 'carry forward'. It is noteworthy that in the instant case, the assessee in his return had not shown any 'capital losses'. He had claimed this loss as a revenue loss. The Income-tax Officer could therefore, reject the assessee's claim to carry forward the loss, merely on the ground that it was not a 'revenue loss'. His further finding that it was a 'capital loss' was only incidental and, in fact, was not necessary.

20. From what has been said above, it follows as a necessary corollary, that during the period Section 12B did not make income under the head 'capital gains' chargeable, an assessee was neither required to show income under that head in his return, nor entitled to file a return showing 'capital losses' merely for the purpose of getting the same computed and carried forward. Sub-section (2A) of Section 22 would not give him such a right because the operation of that sub-section is, in terms, confined to (i) a loss which is sustained 'under the head 'profits and gains of business, profession or vocation'" and would ordinarily have been carried forward under sub-section (2) of Section 24, and (ii) to 'income' which falls within the definition of 'total income'. Both these conditions necessary for the application of the sub-section are lacking in the present case.

21. Not do we find any substance in the contention that under sub-section (2) read with sub-section (1) of Section 24, the assessee had an independent right to carry forward his capital loss, even if it could not be set off, owing to the non-taxability of capital gains, against future profits, if any, in the immediate subsequent years. Sub-section (2) of Section 24 expressly refers to loss 'in any business, profession or vocation'. It does not cover a "capital loss", or the minus income under the head 'capital gains' which at the relevant time, were not chargeable and did not enter into computation of the 'total income' of the assessee under the Act.

22. It may be remembered that the concept of 'carry forward of loss' does not stand in vacuo. It involves the notion of 'set-off'. Its sole purpose is to set-off the loss against the profits of a subsequent year. It presupposes the permissibility and possibility of the carried-forward loss being absorbed or set-off against the profits and gains, if any, of the subsequent year. Set off implies that the tax is eligible and the assessee wants to adjust the loss against profit to reduce the tax-demand. It follows that if such set-off is not permissible or possible, owing to the income or profits of the subsequent year being from a non-taxable source, there would be no point allowing the loss to be 'carried forward'. Conversely, if the loss arising in the previous year was under a head not chargeable to tax, it could not be allowed to be carried forward and absorbed against income in a subsequent year, from a taxable source.

23. Now let us test the claim of the assessee in the light of the above principles. The capital loss of Rs. 28,662 in the present case, was sustained in September, 1953, that is, in the previous year 1953-54. Let us assume that in the subsequent years 1955-56 and 1956-57 when the capital gains were not taxable, he made huge capital gains far exceeding this loss. Could he be obliged to show those capital gains in his returns ? Could the loss of the year 1953-54 be absorbed or set-off against such 'capital gains' of the subsequent years ? The answer is emphatically in the negative.

24. The cases cited by Shri Sen are not relevant. In all those cases, the heads of income under which the losses were sustained, were chargeable to tax. None of them was a case of 'capital loss' pertaining to the period, 1948 to 1957.

25. For the foregoing reasons, we are of the opinion that the High Court was in error in answering the question referred to it, in favour of the assessee. We would reverse that answer in favour of the Revenue.

26. In the result, the appeal is accepted with costs.

</html