

# BOMBAY HIGH COURT

Surat Peoples' Co-Operative Bank Ltd

Vs.

Commissioner of Income-Tax

Income-tax Ref. No. 16 of 1957

(Tendolkar and S.T. Desai, JJ.)

23.09.1957

## JUDGMENT

### **Tendolkar, J.**

1. The assessed in this case is the Surat People's Co-operative Bank Ltd., which is registered under the Bombay Co-operative Societies Act, 1925. Among the objects of the Bank is Object No. 5 "To undertake every kind of banking and shroffi business" and the assessee in the relevant year of account ending 30th June, 1949 was carrying on banking business. During the course of its banking business, the assessee purchased Government securities in the year of account and a profit of Rs. 53,229/- was earned by the assessee. The assessee claimed exemption from tax in respect of the said amount under an Explanation to F. D. (C. R.) Notification R. Dis. No. 291-I. T./25, dated 25th August, 1925, as amended by Notification No. 26, dated 25th June, 1927. The Notification is in the following terms :

"The following classes of income shall be exempt from the tax payable under the said Act, but shall be taken into account in determining the total income of an assessee for the purposes of the said Act :

1. \* \* \*

2. The profits of any Co-operative Society other than the Sanikatta Salt-owners Society in the Bombay Presidency for the time being registered under the Co-operative Societies Act, 1912 (2 of 1912) the Bombay Co-operative Societies Act, 1925 (Bombay Act 7 of 1925), or the Madras Co-operative Societies Act, 1932 (Madras Act 6 of 1932), or the dividends or other payments received by the Members of any such Society out of such profits.

Explanation : For this purpose the profits of a Co-operative Society shall not be deemed to include any income, profits or gains from :

(i) investments in (a) securities of the nature referred to in Section 8 of the Indian Income-tax Act, or (b) property of the nature referred to in Section 9 of that Act,

2. dividends, or

3. the 'other sources' referred to in Section 12 of the Indian Income-tax Act."

It was the contention of the assessee that under sub-Clause (2) of the Notification, the income of the assessee was exempt from tax and what was taken out from this provision by the explanation was merely "interest on securities" and not profits made by the dealer in securities. The Tribunal rejected this contention, and it is against the decision of the Tribunal that the present reference has been made. The question referred to us is :

"Whether the profit amounting to Rs. 53,229/- on the purchase and sale of Government Securities is exempt from tax under the Explanation to Notification R. Dis. No. 291-IT/25 dated 25-8-1925 as amended subsequently, under Section 60 of the Indian Income-tax Act?"

2. Now, turning to the Notification, it is clear that under sub-Clause (2), the profits of any co-operative society registered under the Bombay Co-operative Societies Act are exempt from tax, and since the assessee is a society registered under that Act, all its profits are exempt from tax. But to this subclause, there is an explanation; and the relevant part of the Explanation with which we are concerned on this Reference directly is sub-Clause (1). The explanation indicates that what is comprised in the explanation shall not be deemed to be profits of the society for the purpose of exemption from tax, in other words, it will be liable to tax, and the question is what is included in sub-Clause (1). The relevant words to construe are

"any income, profits or gains from- (1) investments in (a) securities of the nature referred to in Section 8 of the Indian Income-tax Act, or (b) property of the nature referred to in Section 9 of that Act." The contention of Mr. Joshi for the Income-tax Department is that what is liable to tax under this Explanation is income, profits or gains from securities held by the Society and such income, profits or gains do not merely include interest on securities but also include profits realised from purchases and sales of securities. On the other hand. Mr Kolah for the assessee contends that all that is included under the Explanation is "interest from securities" and not the profits made by dealing in securities. Now, in order to appreciate better these contentions, we may as well look at sub-Clause (2) of the Explanation. What is excluded from profits of a Co-operative Society which are exempt and therefore liable to tax in the hands of a co-operative society under that sub-clause is dividends and such dividends are taxable, whether the shares on which the dividends are earned are the investments of the co-operative society or its stock-in-trade. If they are dividends on shares which were its stock-in-trade, then having regard to the case *Commr. of Income-tax v. Ahmuty and Co. Ltd.*<sup>1</sup>, they would have been taxable as business income; while if they are dividends from shares, which are not its stock-in-trade, they would have been taxable under "other sources". That is why "dividends" form a separate head in the income, profits or gains which are excluded from the exemption, and are not included in Head No. 3 which relates to the "other sources" referred to in Section 12. Subsequent to the date of the Notification, however, the Income-tax Act has been amended by including dividends in Section 12 and a separate enumeration of 'dividends'

as a source of income, profits or gains which are taxable is no longer necessary in the Notification. But the point to note about dividends is that the language there used is not "investment in shares" but "dividends", while the language used in sub-Clause (1) is "investments in securities or property". There must be some reason

<sup>1</sup>1955-27 ITR 63

why the framers of the Notification made this distinction. It is true that the word "investment" in itself literally means nothing more or less than to lay out money; and, therefore, where a person purchases securities whether as his stock-in-trade or by way of capital investment, he is in either case investing in securities. But under Income-tax law it makes all the difference whether an assessee has purchased securities as an investment or a dealer. If he was an investor and he sold shares and made profits on such sale, this would be a case of capital appreciation and it may attract "capital gains" tax if applicable, but profits made are not income and are not liable to tax; whilst if he was a dealer in shares, the profits made by a sale of shares are liable to tax as income. Therefore, although in both the cases there is an investment in shares, under the Income-tax Law, there is all the difference between a person being an investor in shares and a dealer in shares; and it appears to us that the word "investment" in sub-Clause (1) is used in the sense of an investment which is in the nature of a capital investment and which is not an investment in securities or property which is its stock-in-trade. If there is investment in the popular sense in securities or property, which is its stock-in-trade, it is not investment in the sense in which that word is used in the Notification; and what attracts tax is the income, profits or gains of investments, which are investments in the sense that the securities or property is not held as the stock-in-trade of the Co-operative Society. This view also helps to explain why the framers of the Notification have not used the simple expression "Interest on securities" in sub-Clause (1), because if they did, the result would have been that income on securities whether or not the securities were capital investments or stock-in-trade would have equally attracted tax like dividends in sub-Clause (2); but the framers of the Notification obviously intended that a distinction should be made between these two kinds of securities.

3. Mr. Joshi has relied on a decision of the Punjab High Court in *Hoshiarpur Central Cooperative Bank Ltd. v. Commissioner of Income-tax, Simla*<sup>2</sup>, This decision appears to us to have no bearing on the issue which we have to determine. The question with which the Punjab High Court was concerned was whether profits flowing from a business carried on by a co-operative society which was outside the object of the Society earned an exemption. That is not the case before us, because as we have already pointed out it is one of the objects of the Society to undertake every kind of banking business and it is common ground that in the course of banking business it is essential to purchase securities. This was pointed out by their Lordships of the Privy Council in *Punjab Co-operative Bank Ltd. v. Commissioner of Income-tax, Punjab*<sup>3</sup>, where their Lordships pointed out that a Bank has always to keep easily realisable securities to meet any possible demand by depositors. This case is relied upon by Mr. Joshi in respect of certain observations made by their Lordships that a Banking Company has to make investments in securities. That no doubt is true as we have earlier pointed out in the normally accepted

meaning of the word "investment", but their Lordships were not there concerned with the distinction which we have already pointed out between an investor in securities and a dealer in securities. The issue before their Lordships was that the Bank had claimed that it had been dealing in shares and securities and their Lordships held that the dealings in securities were really part of the business of the Bank. Therefore, in our opinion, the word

<sup>2</sup>1953-24 ITR 346 : AIR 1954 Pun 2

<sup>3</sup>1940-8 ITR 635 : (AIR 1940 PC 230)

"investment" in sub-Clause (1) of the Explanation relates only to such securities as do not form part of the stock-in-trade of the co-operative society and as in the case before us they did form part of the stock-in-trade as it was a Banking company, the income, profits or gains made from the sale of these securities is not taxable.

4. Mr. Joshi has drawn our attention to the preamble and conditions for registration of a society under the Bombay Co-operative Societies Act and wished to urge that the activities that this society carries on by way of banking do not fall within the scope of that Act. The first answer to this contention is that a certificate of registration is by virtue of Section 11 of the Act conclusive evidence that all the requisite conditions have been satisfied; and the second answer is that if they are not, it may be open to the Income-tax authorities to get the registration cancelled and the question whether the conditions have or have not been satisfied has no relevance to the question referred to us, because all that we are concerned with determining is if there is a society registered under the Bombay Co-operative Societies Act, as the assessee undoubtedly is, it earns exemption by virtue of the Notification, which we have referred to.

5. Our answer to the question, therefore, will be : Is exempt.

6. Income-tax Commissioner to pay costs.

Reference answered accordingly.